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Global Fundamental

Q4 2023

Liontrust Global Smaller Companies Fund

Tom Hosking
Co-Fund Manager

Hong Yi Chen
Co-Fund Manager

Q4 2023 review

- **Falling inflation was a key macro trend in Q4, spurring confidence in base rate cuts.**
- **Overweight in industrials and zero exposure to the energy sector contributed the most to relative performance; overweights in health care and consumer staples weighed.**
- **Heightened expectations for interest rate cuts boost holdings in housing sector.**

The Liontrust Global Smaller Companies Fund returned 9.6% over the quarter, outperforming its benchmark, the MSCI ACWI Small Cap Index, which returned 7.2%, and the average peer in the IA Global Sector, which returned 6.8% ('C' accumulation class, in sterling, net of fees).*

The key macro trend in Q4 was falling headline and core inflation around the world, which led to investors becoming more confident that leading central banks would cut interest rates significantly in 2024. US treasury yields fell from above 5% to less than 4% and this drove inflows to equities, providing stronger support for rate-sensitive stocks such as consumer discretionary, small and mid-cap and higher beta stocks.

The quarter had begun, however, with ongoing concerns that interest rates would remain higher for longer to tackle stubborn inflation. The S&P 500 officially corrected in October, breaching a level more than 10% below its high earlier in the year. Conflict in the Middle East also weighed on sentiment. Uncertainty over the future trajectory of interest rates was exacerbated by Q3 US GDP data showing surprisingly strong annualised growth of 4.9%. Yields on global government bonds rose amid a sell off, including a 16-year high for US treasury yields as questions were also raised over the US' credit quality and the extent of its debt issuance. But by November, the overall picture had changed to one of ebbing inflation and the tone of markets switched to risk-on into the end of the year.

We anticipate that inflation will continue falling provided the oil price does not spike up, giving leading central banks the scope to cut rates in 2024. The beneficiaries of this will be rate-sensitive stocks, including consumer discretionary and higher growth companies.

We are cautious about the global economy. The US has held up well post Covid, helped by the unwinding of the excessive savings that were built up. The pent-up demand resulting from the pandemic supply chain problems has also been supportive, with companies such as aircraft and car manufacturers ramping up production to meet the backlog of demand. This has now been largely converted, so the positive impact is dissipating. We continue to monitor the macro indicators and if the balance tips in one direction or the other we could change the direction of our portfolio. The fact that the European and UK economies are materially weaker than that of the US adds to our caution.

In Asia, Japan's balancing act between continuing to lift its economy out of decades-long deflation with ultra-loose monetary policy while preventing rising inflation from becoming a major problem took a turn in Q4 when it ended its seven-year policy of capping long-term interest rates at 1%. Japanese equities have rallied significantly in 2023, having benefited from relatively cheap valuations, a weakening currency, robust economic growth and loose monetary policy.

Elsewhere in the region, China's economic recovery post the pandemic has been disappointing. This has been a product of too much debt, over-reliance on capital infrastructure as a route to growth and a falling and aging population. State intervention can prevent a market bust, but it will also engender a slow decline. Although the government has announced new spending measures to boost the economy, doubts remain about its budgetary firepower. Significant bad debt at the local government level, and issues in its property sector, which accounts for around 25% of its economy, have yet to be resolved. Our exposure to China is limited to the discretionary growth sector, which we believe will do well even if one half of the Chinese economy flags.

From a sector perspective, our overweight in industrials and zero exposure to the energy sector contributed the most to relative performance, while our overweight in health care and consumer staples weighed the most. The rationale for our health care exposure is based on our caution regarding economic growth.

Positive stock attribution

The drivers of performance were both broad and diverse.

The most significant contributor to performance over Q4 2023 was **Installed Building Products** (IBP), one of the two dominant suppliers and installers of insulation in the US, particularly in new-build homes. IBP is sensitive to expectations for mortgage rates, so it reacted positively to markets becoming increasingly confident about base rate cuts. Moody's, the credit ratings agency, also upgraded its rating for IBP in December, adding that it expected the company to continue to perform well. Reduced interest rate expectations were also supportive of another of our leading performers, **LGI Homes**, the US housebuilder.

The second-leading contributor to performance was **Vertiv Holdings**, the provider of energy management systems for datacentres. After a tough year of post-Covid supply shortages, Vertiv is changing internally in enterprise resource planning and management, which is allowing it to benefit from the strong external changes to which it is exposed, as AI and datacentres grow.

Negative stock attribution

Calix, the telecommunications equipment provider, and **Maravai LifeSciences**, the vaccine, cell and gene therapy supplier to pharmaceutical companies, were the most significant detractors from returns. Calix has continued to suffer from a slowdown in telco capex, while Maravai has continued to see negative growth as customers digest inventory built up during the Covid pandemic.

Discrete years' performance (%) to previous quarter-end:

	Dec-23	Dec-22	Dec-21	Dec-20	Dec-19
Liontrust Global Smaller Companies C Acc GBP	20.8%	-27.1%	8.0%	48.0%	20.1%
MSCI ACWI Small Cap	10.2%	-8.4%	17.2%	12.7%	19.8%
IA Global	12.7%	-11.1%	17.7%	15.3%	21.9%
Quartile	1	4	4	1	3

*Source: FE Analytics, as at 31.12.23, primary share class, total return, net of fees and income reinvested.

For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance does not predict future returns. You may get back less than you originally invested. We recommend any fund is held long term (minimum period of 5 years). We recommend that you hold funds as part of a diversified portfolio of investments.

Overseas investments may carry a higher currency risk. They are valued by reference to their local currency which may move up or down when compared to the currency of the Fund.

The Fund may invest in emerging markets which carries a higher risk than investment in more developed countries. This may result in higher volatility and larger drops in the value of the fund over the short term.

The Fund may encounter liquidity constraints from time to time. The spread between the price you buy and sell shares will reflect the less liquid nature of the underlying holdings.

Outside of normal conditions, the Fund may hold higher levels of cash which may be deposited with several credit counterparties (e.g. international banks). A credit risk arises should one or more of these counterparties be unable to return the deposited cash.

Counterparty Risk: any derivative contract, including FX hedging, may be at risk if the counterparty fails.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

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