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Economic Advantage

March 2024 review

Liontrust Special Situations Fund

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The Liontrust Special Situations Fund returned 2.3%* in March. The FTSE All-Share Index comparator benchmark returned 4.8% and the average return in the IA UK All Companies sector, also a comparator benchmark, was 3.9%.

The FTSE All-Share was one of a number of major stock indices globally to hit all-time highs in March as the latest forecasts from the US central bank painted a benign picture for the world's largest economy. Although the Federal Reserve left rates unchanged as expected, it still plans to cut by 75 basis points – three quarter-point reductions – over the course of 2024. At the start of 2024, investors had been forecasting a cut in March followed by three or four further reductions during the year. Together with a lift in the Fed's 2024 economic growth forecast to 2.1% from 1.4% previously, the prospects of a market-friendly 'soft landing' or even 'no landing' appear to have risen. At the same time, recessionary 'hard landing' fears associated with central banks' attempts to bring down inflation have eased.

March saw a number of investor updates from portfolio holdings, many of them providing full details of 2023 trading.

Full-year results from TP ICAP (+26%) were better than expected, with record adjusted operating profit of £300 million representing 9% growth over 2023. Overall revenue growth of 3% was driven by an 18% increase in its energy & commodities division. TP ICAP has been benefitting from high interest rates as well as elevated macroeconomic and geopolitical uncertainty, which serve to drive volatility higher and boost the inter-dealer broker's volumes. The company expects these supportive conditions to persist in 2024; it comments that trading in the first two months of the new year are in line with consensus forecasts for the full year. However, a much more significant driver of the share price bounce was the company's confirmation that it is exploring ways to unlock the value of its data and analytics division, Parameta Solutions, including via a potential IPO of a minority stake. TP ICAP commented that "Parameta's significant growth prospects, and the intrinsic value of the business, are not appropriately reflected in our share price".

Coats Group's (+19%) results were positively received, despite a 6% constant currency fall in revenues to $1.39 billion in 2023. The industrial threads and footwear component manufacturer expanded operating profit margin to its 17% target, allowing it to grow profits by 2% to $184 million. The company commented that widespread industry destocking impacted volumes in 2023, but it believes this trend is beginning to fade away as inventory levels normalise. Coats also states that, against this tough backdrop, it expanded market share by 200 basis points in both apparel (to c.25%) and footwear (to c.27%).

Likewise, **Savills** (+16%) shares responded well to evidence it is showing some resilience to tough market conditions. The real estate group's transactional advisory revenues – around a third of the total – dropped 17% in 2023 as high interest rates and uncertainty in the office sector limited transaction volumes. Leasing activity also softened as economic uncertainty led companies to delay committing to new contracts. However, its less transactional divisions – including consultancy and property management – grew revenue 7%, limiting the overall group revenue decline to 3% for the year (to £2.2 billion). Looking forward, Savills expects lower interest rates and sustainability considerations to drive transaction volumes. While it still expects the market to be characterised by significant economic uncertainty, it believes the worst is behind it following a 2023 which saw the lowest transaction volumes for a decade.

Business telecoms provider **Gamma Communications** (+11%) issued a robust set of 2023 results showing 8% growth in revenues to £522 million and a 10% rise in pre-tax profit to £71.5 million. While it saw some evidence of a softer economy last year, the company thinks there are signs of improvement so far this year with lower inflation reducing cost pressures.

Interim results from **YouGov** (-12%) gave a more mixed picture of trading. While the research data and analytics group said Q1 was slower than expected with sales cycles remaining long, momentum accelerated in Q2 and the company maintains full-year guidance. Underlying revenue growth was 2% across the six months while adjusted operating profits fell 4% on an underlying basis due to a 100 basis point contraction in margin. However, the integration of CPS (Consumer Panel Services) – the European household purchase data business purchased last year – has gone well and medium-term targets for the deal have been increased. The inclusion of CPS boosts revenue growth to 9% (to £143 million), while adjusted operating profit rose 23% to £27.9 million as the deal lifted group adjusted operating profit margins by 200 basis points. YouGov has lifted its CPS medium-term revenue target to £650 million (up from £500 million).

Keywords Studios (-9.2%), the provider of services to the video gaming sector, was able to report 17% constant currency revenue growth to €780 million in 2023 – including 9% organic growth – despite tough market conditions in which many developers shied away from risks associated from launching new games. As a result, Keywords' organic growth of 9% was slightly behind its medium-term guidance, but cost control efforts allowed it to achieve an adjusted operating margin of 15.6% - down from 16.6% in 2022 but ahead of its guidance. Despite the in-line update, the shares remain unloved in the short term; we have written before about the impact of wider AI-driven concerns around the business, and a second-half weighting to the current year forecasts is unhelpful even if partly driven, understandably, by the normalisation of US entertainment industry activity in the wake of strikes last year. We remain optimistic on a longer-term view, buoyed by Keywords' material outperformance of its wider market, its dominant market share and opportunities presented by investment in AI initiatives to help customers unlock efficiencies and productivity gains.

Having weakened in February due to a surprise decline in Q4 sales, shares in consumer goods group **Reckitt Benckiser** (-9.7%) lost more ground in March. Investors looked to price in the litigation risks relating to its Mead Johnson Nutrition subsidiary after a court in Illinois awarded $60 million in damages to the mother of a premature baby that developed a fatal bowel condition following use of its Enfamil formula. Reckitt plans to appeal the decision and has emphasised it believes there is no link between its products and necrotising enterocolitis.

Focusrite (-21%) develops hardware and software for the high-quality production of recorded and live sound. It commented in a disappointing half-year trading update that the challenging market conditions highlighted in January's AGM statement have continued in February and March. Retail weakness and industry-wide overstocking have created some weakness and volatility in demand, while its latest Scarlett Generation 4 higher-end products have been delayed due to engineering resource constraints. Revenues from these products are now not expected until the next financial year (ending August 2025). For the year to 31 August 2024, Focusrite now expects revenues of £155 million, around 14% below consensus, with EBITDA guidance cut around 25% to a £27 million to £30 million range.

Midwich Group (+23%) is a specialist on-trade audio-visual equipment distributor which the team believes possesses Economic Advantage in the form of its distribution network. Full-year results showed that it generated 7% sales growth to £1.29 billion in 2023, predominantly resulting from seven acquisitions completed during the year, with adjusted operating profit rising 17% to £59.6 million. Midwich described the market as highly challenging with lower demand for mainstream products. However, stronger sales of technical products allowed it still to achieve positive organic growth of 0.8%, while boosting gross profit margins by 150 basis points to 16.8%, and the company remains confident in its FY24 guidance and continuing above-market growth. Midwich raised £50 million via a share placing in June 2023 to support its acquisitive growth ambitions, and its full-year outlook noted that it retains a strong pipeline of potential targets.

Positive contributors included:

TP ICAP (+26%), Midwich Group (+23%), Coats Group (+19%), Savills (+16%) and Gamma Communications (+11%)

Negative contributors included:

Focusrite (-21%), Kainos Group (-13%), YouGov (-12%), Wood Group (-10%) and Reckitt Benckiser (-9.7%).

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

	Mar-24	Mar-23	Mar-22	Mar-21	Mar-20
Liontrust Special Situations I Inc	4.3%	0.1%	5.1%	31.1%	-11.0%
FTSE All Share	8.4%	2.9%	13.0%	26.7%	-18.5%
IA UK All Companies	7.6%	-1.9%	5.4%	38.0%	-19.2%
Quartile	4	3	3	3	1

*Source: Financial Express, as at 31.03.24, total return (net of fees and income reinvested), bid-to-bid, institutional class. **Source: Financial Express, as at 31.03.24, total return (net of fees and income reinvested), bid-to-bid, primary class.

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 this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.

This Fund may have a concentrated portfolio, i.e. hold a limited number of investments. If one of these investments falls in value this can have a greater impact on the Fund's value than if it held a larger number of investments.

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.

The Fund may invest in companies listed on the Alternative Investment Market (AIM) which is primarily for emerging or smaller companies. The rules are less demanding than those of the official List of the London Stock Exchange and therefore companies listed on AIM may carry a greater risk than a company with a full listing.

The Fund will invest in smaller companies and may invest a small proportion (less than 10%) of the Fund in unlisted securities. There may be liquidity constraints in these securities from time to time, i.e. in certain circumstances, the fund may not be able to sell a position for full value or at all in the short term. This may affect performance and could cause the fund to defer or suspend redemptions of its shares.

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.

Disclaimer