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Economic Advantage

March 2024 review

Liontrust UK Smaller Companies Fund





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The Liontrust UK Smaller Companies Fund returned 2.5%* in March. The FTSE Small Cap (excluding investment trusts) Index comparator benchmark returned 2.7% and the average return of funds in the IA UK Smaller Companies sector, also a comparator benchmark, was 3.1%.

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 tine, recessionary 'hard landing' fears associated with central banks' attempts to bring down inflation have eased.

March's largest riser in the Fund was **Mattioli Woods** (+39%), which recommended an 804p a share takeover offer from Pollen Street Capital, the European private equity firm specialising in financial services. The deal values Mattioli Woods at around £432m and represents a premium of around a third to its prior 'undisturbed' share price.

On numerous occasions over the last couple of years, we've highlighted the extent to which takeover activity has picked up as a result of depressed valuations, particularly lower down the market cap scale. While M&A activity is always a double-edged sword, at the very least it does help to crystallise in investors' minds the level of latent value within share prices at current levels and provides an influx of capital to redeploy across other holdings.

Staying with the theme of corporate activity, two of the Fund's other large risers made key investments during the month. Delivered wholesale goods business **Kitwave Group** (+22%) announced the purchase of Total Foodservice Solutions, a catering supplies group operating in the north of England. Net of a £4 million cash balance, the purchase price was £17 million; Total Foodservice generated £2 million of profit before tax in the year to 20 April 2023. Meanwhile fintech provider Fintel (+14%) acquired stakes in Mortgage Brain, a provider of software to over 15,000 mortgage intermediaries, and ifaDASH, a customer relationship management solution helping IFAs meet their regulatory requirements. Fintel also released 2023 results showing growth in adjusted revenues and earnings as increased penetration of fintech software compensates for volume weakness in the UK housing market.

Contract wins were responsible for the sharp rise in defence and security technology mini-conglomerate Cohort's (+25%) shares. Its Systems Engineering and Assessment (SEA) business has been awarded a contract with the Royal Navy worth at least £135 million over more than a decade to supply its trainable decoy launcher system. Earlier in the month, Cohort's Chess Dynamics unit was also awarded a £15.7 million contract to supply surveillance systems for Royal Australian Navy frigates.

Turning to updates on trading, Focusrite (-21%) weakened after commenting in a half-year trading update that the challenging market conditions highlighted in January's AGM statement have continued in February and March. Focusrite develops hardware and software for the high-quality production of recorded and live sound. 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.

Interim results from YouGov (-12%) gave a 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 margins. 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).

Bioventix (-9.2%) slid on the release of interim results. The company develops high-affinity monoclonal antibodies for applications in clinical diagnostics. In the six months to 31 December, revenues rose 13% to £6.7 million as the core business performed well, with good sales of its vitamin D antibody and strong demand from China. However, sales relating to troponin antibodies were a little below its expectations, which Bioventix attributes to operational difficulties at its partner customers. It still expects troponin sales to meet growth expectations in the longer term. March's share price weakness nonetheless represented only a partial reversal of the strong mid-teen percentage gains posted by the shares since November, which have been driven by excitement around Bioventix's co-development of assays relating to the early detection of the "Tau" blood biomarker associated with the onset of Alzheimer's disease. Recent advances in the development of treatments for Alzheimer's have increased focus on the importance of early testing and detection, given that such treatments have shown success in significantly slowing the progress of the disease, but not reversing it.

Midwich Group (+23%), a specialist on-trade audio-visual equipment distributor which the team believes possesses Economic Advantage in the form of its distribution network, continued to demonstrate its resilience in the face of tricky market conditions 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. Echoing Focusrite's comments, 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:

Mattioli Woods (+39%), Cohort (+25%), Midwich Group (+23%), Kitwave Group (+22%) and Fintel (+14%).

Negative contributors included:

Focusrite (-21%), Kainos Group (-13%), YouGov (-12%), AB Dynamics (-9.4%) and Bioventix (-9.2%).

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

	Mar-24	Mar-23	Mar-22	Mar-21	Mar-20
Liontrust UK Smaller Companies I Inc	3.8%	-14.7%	2.6%	56.7%	-5.8%
FTSE Small Cap ex ITs	11.0%	-12.9%	5.5%	74.9%	-24.4%
IA UK Smaller Companies	5.0%	-16.6%	-1.7%	65.7%	-17.9%
Quartile	3	2	1	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.

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.

As the Fund is primarily exposed to smaller companies there may be liquidity constraints 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. In addition the spread between the price you buy and sell units 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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