Gresham House
Specialist asset management

LF Gresham House UK Micro Cap Fund

Factsheet commentary - January 2022

Overview

January continued recent themes, with an increasing level of market volatility driven by negative sentiment surrounding inflationary pressures, expectations of ongoing rate rises, geopolitical tensions over Ukraine and an impending cost of living squeeze in the UK. Weaker markets were exacerbated by a sharp rotation from growth to value stocks and as a result of a major sell-off in global technology stocks.

We have been anticipating increasing market and stock level volatility for some time and we believe our portfolio is well set up to deliver resilient relative performance due to its focus on high-quality and moderately valued growth stocks with more limited cyclical exposure than the wider equity market.

Despite the increased volatility and weaker sentiment, we continue to believe that the longer-term opportunity in UK smaller companies - which is underpinned by the continuing discounted valuations applied to the UK and to smaller companies in particular - remains material, providing some downside protection in more challenging market conditions.

We believe current market conditions are supportive of finding attractive investment opportunities for those prepared to take a longer-term view. We remain selective and disciplined in our approach, seeking high-quality companies with attractive long-term capital growth characteristics at sensible valuations.

Performance

The LF Gresham House UK Micro Cap Fund (the Fund) delivered a return of -5.0% during the month, outperforming the IA UK Smaller Companies sector which decreased by 7.7% and the NSCI + AIM (ex IC) index which decreased by 6.4%.

Key contributions came from **Ten Entertainment** (+9%), after a strong trading update; **Anexo Group** (+10%), after a positive trading update exceeding expectations; and **Diaceutics** (+6%), after a positive trading statement indicating revenues were ahead of expectations.

The largest detractors to performance were **Kape Technologies** (-17%), which fell as part of the wider technology sector de-rating despite announcing that its results would be ahead of expectations; **Access Intelligence** (-24%), after a trading update cutting revenue expectations relating to its recent acquisition; and **Accrol** (-43%), after reporting in its trading update that inflationary pressures continue to impact input costs, reducing margins.

Portfolio activity

The Fund made a number of follow-on investments into core holdings including **Diaceutics**, and **Angling Direct.**

Outlook

Our medium-term view remains that the economic recovery in the UK should continue to support earnings growth and share prices. However, we continue to expect volatility in the short term, driven by an inherently uncertain environment for market estimates.

We are still seeing aftershocks from the pandemic, such as the currently elevated level of inflation across a number of areas and both global and domestic supply chain disruption impacting at the company level. We also anticipate a rising number of profit warnings in coming months. This in turn is likely to aggravate share price volatility forindividual stocks.

We believe stock-level volatility across the market, while creating some challenges, will provide an attractive environment in which we can unearth good long-term investment opportunities at attractive valuations. The economic environment and lingering Covid-19 discontinuity will provide agile smaller businesses with strong management teams the opportunity to take market share and build strong long-term franchises.

We continue to believe that our fundamentals-focused investment style has the potential to outperform over the long term. The Fund will maintain its focus on building a high-conviction portfolio of less cyclical, high-quality, niche growth businesses which we believe can deliver strong returns through themarket cycle regardless of the performance of the wider economy.

Important information