Ennismore European Smaller Companies Fund

Investor Newsletter for the month of June 2013

Issued on 5 July 2013

Fund Details

Daily dealing UCITS and Irish Central Bank regulated open-ended investment company with Financial Conduct Authority recognition, registered in Ireland and listed on the Irish Stock Exchange. The Fund size was GBP 237m as at 30th June. Total assets under management by Ennismore Fund Management were GBP 287m. Our funds are hard closed to new investment with the number of shares in issue capped and we have a waiting list of clients that want to invest as and when capacity becomes available through redemptions. If you would like to be included on this please call Eleanor Scott on +44 (0) 20 7368 4219 or email subs@ennismorefunds.com. Redemptions can be made through the Administrator in the usual way.

The Fund is managed as an absolute return fund with the objective of generating positive returns irrespective of market conditions rather than performing relative to any benchmark index. Index data is provided in the following table as a guide to general equity market conditions.

Performance as at 30 June 2013

	Share Class[2]					HSBC Index[3]		MSCI Index[4]
	GBP A £	GBP A €	GBP B	EUR A	EUR B	GBP	EUR	(local)
NAV per Share[1]	**76.50**	**89.27**	**12.92**	**12.74**	**12.81**			
Period	% Change					% Change		
June 13	**-0.9**	**-1.2**	**-0.8**	**-1.1**	**-1.1**	**-3.6**	**-3.8**	**-5.0**
May 13	1.8	0.9	1.8	1.1	1.1	4.2	3.2	2.5
April 13	-0.9	-1.1	-0.9	-1.0	-1.1	1.7	1.4	1.9
March 13	1.5	3.4	1.5	3.0	3.0	-1.8	0.2	0.9
February 13	2.7	2.1	2.7	2.2	2.2	3.5	2.8	0.9
January 13	6.5	0.9	6.5	2.0	2.0	9.7	4.2	5.1
2013 to date	**11.0**	**5.1**	**11.1**	**6.3**	**6.2**	**13.8**	**7.9**	**6.1**
Annualised return[5]	**15.3**	**13.7**	**11.0**	**10.6**	**10.8**	**8.6**	**7.1**	**2.7**
Since launch[5]	**679.4**	**533.9**	**29.2**	**27.4**	**28.1**	**229.8**	**167.4**	**47.4**

[1]Source: Administrator, Net Asset Value. [2]Source: Administrator, Net Asset Value, net income reinvested. [3]Source: Bloomberg, HSBC Smaller European Total Return Index. [4]Source: Bloomberg, MSCI Europe Index, local currencies, total return. [5]Since inception of GBP A share class on 27/01/99 to date , GBP B share class on 19/01/11 to date, EUR A and EUR B share classes on 31/01/11 to date. Note: All performance figures net of fees.

Comments below on performance refer to GBP NAV per share unless otherwise stated, exclude cash returns and are prior to expenses.

The Fund's NAV fell by 0.9% in June. Our long book cost 1.6% and the short book contributed 0.7%.

The main positive was Xing, contributing 0.7%. There was no significant news on the company. The main negative was social and mobile games developer Zynga, costing 0.5%. The share price fell 18% in June after the company reported lower than expected second quarter bookings and plans to cut nearly 20% of its staff. Since the end of the month the shares have recovered all of this decline after Zynga announced that Don Mattrick would take over as CEO from founder Mark Pincus. Mattrick previously ran the successful Xbox division of Microsoft and, before that, was head of development at console games manufacturer Electronic Arts. Home Retail also reduced NAV by 0.5%. The company reported first quarter sales that were slightly disappointing at its smaller brand, Homebase. The share price fell 14% in June and we took the opportunity to add a little to our position.

Portfolio Activity

Figures in brackets refer to previous month end; * = positions > 0.5% of NAV.

As at 30th June the Fund was invested in 79 (77)* stocks.

Lectra – French machinery manufacturer (0.7% NAV)

Lectra is the world's leading supplier of cutting machinery and design software for textiles, selling into the fashion (50% of sales), automotive (40%) and furniture (10%) industries. The software covers everything from design and collection management to production. The hardware automates the cutting process, typically cutting multiple layers of fabric at high speed with minimum wastage. Lectra is positioned at the high end, offering the highest performance machinery in terms of speed, accuracy and the number of layers that can be cut at one time, which translates into the highest level of cost savings and efficiency for customers. Overall market share is around 30% but is much higher in the more demanding segments – over 80% in airbags, for example. Their main competitor Gerber has 25% share with the rest of the market fragmented. Lectra has been spending 3-4 times more on R&D than Gerber in recent years, leading to a product that management believe is at least one generation ahead. This is backed up by our conversations with customers and we believe Lectra continues to win share at the high end. Technology leadership allows them to typically charge 10-30% more than competitors and still offer customer payback in under a year. In fact, management told us their internal analysis suggests that competitors could give away machines for free and still not offer as compelling a business case for high-end customers!

The business model is relatively resilient with more than 55% of revenue coming from recurring software licenses, hardware maintenance and spare parts and, we estimate, a further 10% of sales coming from replacement machines. New system sales are more cyclical due to the high capital cost, with a machine costing upwards of USD 100,000. Management (who own 40% of the share capital) are pragmatic about this and a key financial target is that gross profit on recurring sales must cover 75% of fixed overheads, which allowed the business to weather a 50% drop in new system sales in 2009 with only a small operating loss. The accounts are also conservative with R&D fully expensed and no debt. The business generates a high return on capital (averaging 25% pre-tax over the last 15 years), helped by demanding a 40% down payment from customers to fund work in progress.
Lectra's technological leadership should underpin future revenues as their customers increasingly need greater flexibility in production and speed to market, driven by consumer demand for fast fashion and customisation. This is true in automotive as well as in fashion. Management are currently investing in the sales force to capitalise on these trends and this will weigh on operating profit in 2013, as it did in 2012. We expect profit to be lower than the EUR 20m reported last year. Overall sales growth has proven challenging to come by in the past and we are reluctant to attribute any value to it until there is clear evidence that any pickup in new system sales can be sustained. In the absence of this we expect management will again take swift action to trim costs, as they did in 2007, and that the business will therefore be able to at least sustain the level of operating profit seen in recent years.
Lectra's current market cap is EUR 150m and it has EUR 25m of net cash. We estimate it generated free cash flow of over EUR 65m in the last three years, and more than EUR 75m in the last five despite the financial crisis severely constraining customers' capital investment in 2009. A reasonable proportion of these returns have been paid out as dividends with a current yield of over 4%. Valuing the business at 14 times our conservative estimate of sustainable net operating profit after tax, we believe the shares offer at least 50% upside and potentially much more in the longer term if growth plans are successful.

Top Five Holdings as at 30 June 2013

	Company	Country	Sector	% of NAV
1	Xing	Germany	Information Technology	6.2
2	Vib Vermoegen	Germany	Financials	4.9
3	Sto	Germany	Materials	4.3
4	Home Retail	United Kingdom	Consumer Discretionary	3.5
5	Oslo Bors	Norway	Financials	3.4
				22.3

Exposures as at 30 June 2013

Longs %	Shorts %	Gross Exposure %	Net Exposure %
93.6 (92.5)	28.9 (30.1)	122.5 (122.6)	64.7 (62.4)

Figures in brackets refer to previous month end.

Exposures by Country, Market Cap and Sector as % NAV as at 30 June 2013

Country	Gross%	Net%
Austria	1.6	1.6
Belgium	2.2	1.1
Bermuda	1.4	1.3
Denmark	3.3	0.4
France	5.2	4.8
Germany	31.5	26.3
Ireland	4.6	4.6
Italy	6.5	3.5
Norway	4.1	4.1
Spain	1.2	-1.2
Sweden	4.0	-1.9
Switzerland	8.0	-0.4
UK	38.8	17.2
US	7.5	0.7
Other	2.6	2.6

Market Cap	Gross%	Net%
>£2bn	1.4	-0.4
£700m - £2bn	31.4	3.9
£200m - £700m	48.3	27.5
<£200m	41.4	33.7

Sector	Gross%	Net%
Consumer Discretionary	34.2	17.5
Consumer Staples	0.8	-0.8
Energy	3.9	2.5
Financials	18.5	14.8
Health Care	4.2	1.0
Industrials	17.6	11.8
Information Technology	26.0	10.9
Materials	10.8	10.8
Telecommunication	4.5	-1.8
Utilities	2.0	-2.0
Other	0.0	0.0

Geographic analysis relates to country of incorporation or listing. This may not represent the underlying economic exposure of the operating business. Sector analysis is based on the Global Industry Classification Standard ("GICS"). Source: Bloomberg.

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