Ennismore European Smaller Companies Fund

Investor Newsletter for the month of February 2014

Issued on 11 March 2014

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 273m as at 28th February. Total assets under management by Ennismore Fund Management were GBP 333m. 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 28 February 2014

	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]	**88.61**	**107.51**	**14.97**	**15.26**	**15.32**			
Period	% Change					% Change		
February 14	**0.5**	**0.0**	**0.5**	**0.1**	**0.1**	**7.0**	**6.4**	**4.8**
January 14	1.1	2.5	1.1	2.2	2.2	0.0	1.4	-2.2
December 13	2.3	2.2	2.4	2.3	2.3	1.6	1.4	1.0
November 13	1.2	3.1	1.2	2.8	2.7	-0.1	2.0	0.5
October 13	4.2	2.9	4.2	3.2	3.2	6.1	4.7	4.4
September 13	1.6	3.6	1.6	3.2	3.2	3.6	5.7	3.6
2014 to date	**1.6**	**2.5**	**1.6**	**2.3**	**2.3**	**7.0**	**7.9**	**2.5**
Annualised return[5]	**15.7**	**14.4**	**13.9**	**14.7**	**14.9**	**10.0**	**8.7**	**3.7**
Since launch[5]	**802.8**	**663.4**	**49.7**	**52.6**	**53.2**	**320.1**	**253.5**	**73.1**

[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 increased by 0.5% in February. Our long book contributed 3.5% while the Fund's short exposure cost 2.6%.

In what was a very strong month for equity markets most of our long positions contributed positively and the largest attributions came from several of our larger positions. Xing and Oslo Bors VPS added 0.4% each to NAV, Vib Vermoegen, Sto and Home Retail 0.3%. Xing and Oslo Bors both reported strong Q4 trading and higher than expected dividend payments, with Oslo Bors shares still trading on a double digit yield.

Most of the Fund's short positions lost money in February with no significant positive attributions.

Portfolio Activity

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

As at 28th February the Fund was invested in 78 (70)* stocks.

Home Retail – UK general merchandise retailer (3.7% NAV)

Home Retail owns Argos, the largest general merchandise retailer in the UK, and the second largest home improvement chain, Homebase. Both businesses have struggled along with the UK consumer and when we bought into it in early 2012 the Argos business was generally written off by the investment community as unable to compete in a world with online retail. It was in fact the most heavily shorted UK-listed stock at the time. We do not often invest in companies that are so well followed but it seemed obvious to us that the short case was fundamentally wrong. A return to positive sales growth over the last year has come as disposable incomes in the UK have finally started to rise (a little), a pretty clear sign that its problems have in fact been mostly cyclical. With unemployment also falling and housing market transactions up very strongly the outlook for trading at both Argos and Homebase is the most positive it has been for nearly a decade.

There were always several obvious reasons why online competition is not an insurmountable challenge for Argos. Firstly it is already one of the largest online retailers in the UK with nearly 45% of sales made online. Crucially, though, not much more than 10% of sales are ordered online for home delivery and this has not changed much over the last ten years, other than that people now order online rather than over the phone (for what it is worth this is about the same level of pure online sales as AO World, an online only electricals retailer that recently had its IPO in London and now has as large a market cap as the whole of Home Retail Group). Instead most of Argos's online sales are collected in store by the customer, 40% within 4 hours and all of them by the next day. Argos is, as it has always been, a convenience retailer (the stores are little more than warehouses with collection points for customers, which also makes them more efficient than retailers with large display areas) with 95% of the UK population less than 10 miles from a store. Aside from convenience and speed, the product range is also mostly unsuitable for home delivery. About 80% of the items they sell cost less than

GBP 30 but are too big to go through the letterbox, which means they are not economic to deliver to home as this costs around five pounds (plus the opportunity cost of someone making sure they are in to take delivery). These products amount to about half of their sales by value but, we estimate, more like 75% of their gross profit. The main area where Argos is exposed to online competition is in consumer electronics, which accounts for about a third of sales and has been their worst performing category. Importantly the gross margin here is low at only around 15%-20%, compared to an average of over 35% across the other categories they sell (homewares, furniture, toys, jewellery and leisure equipment are the main ones). Even here though, Argos is differentiated by its consumer credit offer and by convenience, as its great success in selling tablet computers shows. Finally Argos will continue to benefit from other less diversified retailers exiting the high street, with electricals specialist Comet shutting all its outlets at the end of 2012. Having faced more competition for several years from supermarket chains adding non-food space this trend appears to have largely run its course. Even sales growth at online specialist Amazon is now modest, and may well be in single digits in 2014. Far from being structurally doomed, Argos could in fact be able to increase its market share in future, allowing revenues to increase ahead of a recovery in consumer spending.

Home Retail has a current market capitalisation of GBP 1,600m. This buys you a significant net cash position – over GBP 300m at the end of March this year – and a completely self-financed customer credit book of around GBP 470m. Argos's operating profit for the year to March 2014 will be around GBP 100m. Homebase, the number two home improvement chain, will only add a little more to this but it is well positioned to benefit from the very strong recovery in housing transactions that is now evidently underway in the UK (transactions had been running at half their long term average for over five years). With a gross margin of 50% Homebase is highly operationally leveraged and could quickly return to making GBP 50m plus a year (in the five years before the financial crisis it averaged GBP 85m). For Home Retail as a whole we believe operating profit of around GBP 200m a year is achievable in the next two to three years and that the business is therefore still significantly undervalued by the market. We expect the share price to increase by at least 30% in 2014.

Top Five Holdings as at 28 February 2014

	Company	Country	Sector	% of NAV
1	Vib Vermoegen	Germany	Financials	4.7
2	Jd Sports	United Kingdom	Consumer Discretionary	4.3
3	Sto	Germany	Materials	4.3
4	Oslo Bors	Norway	Financials	4.1
5	Xing	Germany	Information Technology	3.7
				21.1

Exposures as at 28 February 2014

Longs %	Shorts %	Gross Exposure %	Net Exposure %
74.8 (74.9)	34.2 (30.8)	109.0 (105.6)	40.6 (44.1)

Figures in brackets refer to previous month end.

Exposures by Country, Market Cap and Sector as % NAV as at 28 February 2014

Country	Gross%	Net%
Austria	1.0	1.0
Belgium	2.0	0.6
Bermuda	1.8	0.8
Canada	2.5	-2.2
France	4.6	3.7
Germany	29.9	21.2
Italy	5.3	1.7
Jersey	1.2	-1.2
Norway	6.1	6.1
Poland	0.9	-0.9
Sweden	2.3	-0.7
Switzerland	5.4	-2.7
UK	37.1	12.9
US	5.0	-0.2
Other	3.9	0.5

Market Cap	Gross%	Net%
>£2bn	7.9	-0.3
£700m - £2bn	30.8	5.1
£200m - £700m	40.3	11.5
<£200m	30.0	24.3

Sector	Gross%	Net%
Consumer Discretionary	37.2	17.5
Consumer Staples	2.4	-0.2
Energy	1.0	-1.0
Financials	14.0	9.8
Health Care	3.1	1.2
Industrials	14.2	2.5
Information Technology	24.5	4.5
Materials	7.8	7.8
Telecommunication	3.4	-0.1
Utilities	1.4	-1.4
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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