Ennismore European Smaller Companies Fund

Investor Newsletter for the month of September 2014

Issued on 14 October 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 282m as at 30th September. Total assets under management by Ennismore Fund Management were GBP 347m. 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 September 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]	**90.34**	**115.94**	**15.26**	**16.29**	**16.36**			
Period	**% Change**					**% Change**		
September 14	**-0.2**	**1.6**	**-0.2**	**1.3**	**1.3**	**-3.7**	**-1.9**	**-0.2**
August 14	1.1	1.0	1.1	1.0	1.1	1.2	1.2	1.8
July 14	0.2	1.2	0.1	1.0	0.9	-3.8	-2.9	-1.8
June 14	-2.0	-0.4	-1.9	-0.7	-0.7	-2.1	-0.5	-0.9
May 14	-1.4	-0.5	-1.4	-0.7	-0.7	1.0	2.0	2.2
April 14	1.5	2.1	1.4	2.0	2.0	-1.4	-0.9	1.8
March 14	2.9	2.6	2.9	2.6	2.7	-0.2	-0.2	-0.7
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
2014 to date	**3.6**	**10.6**	**3.6**	**9.3**	**9.3**	**-2.4**	**4.4**	**4.7**
Annualised return[5]	**15.2**	**14.4**	**12.1**	**14.2**	**14.4**	**9.0**	**8.2**	**3.7**
Since launch[5]	**820.5**	**723.3**	**52.6**	**62.9**	**63.6**	**283.4**	**241.9**	**76.8**

[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 was down by 0.2% in September. The long book cost 1.0%, the Fund's short exposure contributed 1.4%. On the long side JD Sports was the main positive with a 0.4% contribution after reporting continued strong trading. The main negative was Home Retail, which cost the Fund 0.3%. The company reported slightly weak (but still positive) like-for-like sales at Argos for the last quarter. There were no significant contributions either way from the short book.

ASOS – UK apparel retailer (1.7% NAV)

ASOS is a leading online fashion retailer selling branded and own brand clothing. The company has grown revenue from less than GBP 15m ten years ago to almost a billion pounds in the year ended this August. All of this growth has been organic. This is a remarkable achievement and, to be honest, ASOS has consistently surprised us. What started out as a niche site for young women is now a broad fashion retailer. Many of the twenty somethings who were shopping on the site ten years ago are still using it in their thirties, and this cohort effect could underpin growth for a very long time. You can see this in the UK business which already has sales of around GBP 400m and was still able to grow 30% last year. ASOS has replicated this success in several other countries in northern Europe and in Australia – the majority of revenue now comes from outside the UK - and has the potential to do so in many more.

In the past we were sceptical that online fashion retail could deliver a good return on capital with the physical barrier to entry of bricks and mortar gone. We underestimated the benefits scale has brought to what is effectively a department store business model, albeit one focussed purely on fashion so far. ASOS is now so big in many markets that it is hard for brands to justify not being on it. The product offering continues to be broadened significantly (not just more brands but also the amount of their range they make available), which is another driver of sales growth. A key part of what ASOS offers consumers is delivery, with both lower cost (orders over GBP 15 are free) and more convenience – in the UK orders made by midnight can be had the next day. Here again scale matters. Even the ASOS website itself is a competitive advantage, with content as sophisticated as any fashion magazine, making it a destination for consumers and a great way of recruiting new customers for the company without having to spend on expensive TV advertising. To compete against ASOS, where it is established, is no longer easy. In the UK, for example, its main peers are Next and Littlewoods, which already had large catalogue businesses to convert to online. For a new entrant it would be much harder. Replicating the number and depth of supplier relationships (c.1,000 brands), carrying and turning (profitably) GBP 150m of inventory and attracting a large customer base is not easy or cheap. We know this because German copy-cat Zalando, which

recently listed, has burnt over EUR 400m in the last three years to establish itself as a competitor in Europe. By comparison ASOS generated cash over the same period, with a pre-tax return on capital employed of around 30%.
ASOS will deliver to pretty much anywhere in the world and made 60% of its sales outside of the UK last year. Entering new markets requires little fixed capital as they can be serviced from the UK until sales reach a material level that can support local infrastructure. However this does mean that international growth will not be particularly profitable until real scale is achieved, with market share being built by competitive pricing and a superior service. We believe focussing on revenue growth remains the right strategy for ASOS to follow and are confident that they can deliver good profitability in markets where they achieve significant scale. Two things give us this confidence. One is that all of ASOS's investment so far has been funded from its own cashflow; the company has not needed to raise any capital since it first listed (and unlike many of its tech peers has resisted the temptation to do so). The other is that ASOS is already profitable in its most mature markets – management do not disclose profitability by territory but we assume most of its c.GBP 45m operating profit comes from these markets, which implies a margin of close to 10%.
The ASOS share price peaked at over GBP 70 in February. Three profit warnings later we have bought our position at GBP 20, which values the company at around GBP 1.65bn. That is less than one and a half times forecast sales for this year. Lower than expected profit in the short term is the result of investment in some new markets and using pricing to take market share. We think this is exactly the right strategy for ASOS in fashion retail, as it has been for Amazon in most other categories. ASOS has the potential to grow sales many times over in the coming years and we would expect a good level of profitability to follow as it has in its core markets. We do not see the share price returning to its peak any time soon but we believe it could easily double over the next year as the company delivers stronger revenue growth than the market is now expecting.

Top Five Holdings as at 30 September 2014

	Company	Country	Sector	% of NAV
1	Jd Sports	United Kingdom	Consumer Discretionary	5.0
2	Vib Vermoegen	Germany	Financials	4.7
3	Oslo Bors	Norway	Financials	4.4
4	Home Retail	United Kingdom	Consumer Discretionary	4.0
5	Sto	Germany	Materials	3.6
				21.7

Exposures as at 30 September 2014

Longs %	Shorts %	Gross Exposure %	Net Exposure %
70.7 (70.7)	29.5 (31.9)	100.2 (102.6)	41.2 (38.8)

Figures in brackets refer to previous month end.

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 30 September 2014

Country	Gross%	Net%
Belgium	1.4	1.4
Bermuda	1.0	1.0
Denmark	0.7	0.4
France	6.1	5.4
Germany	22.7	7.4
Italy	3.0	0.2
Jersey	1.0	-1.0
Norway	6.7	6.7
Poland	1.3	-1.3
Spain	0.9	0.5
Sweden	2.6	-2.0
Switzerland	3.8	-2.0
UK	43.3	23.6
US	3.5	0.5
Other	2.2	0.4

Market Cap	Gross%	Net%
>£2bn	9.6	-0.8
£700m - £2bn	31.4	10.9
£200m - £700m	35.2	12.8
<£200m	24.0	18.3

Positions	Sep	Aug
Long	76	74
Short	60	57
Longs Opened	4	0
Longs Closed	2	3
Shorts Opened	6	9
Shorts Closed	3	4

Sector	Gross%	Net%
Consumer Discretionary	38.4	24.4
Consumer Staples	3.3	2.5
Energy	0.0	0.0
Financials	14.9	7.4
Health Care	5.7	1.3
Industrials	11.4	3.3
Information Technology	17.9	-1.5
Materials	5.0	5.0
Telecommunication	2.3	0.1
Utilities	1.3	-1.3
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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