

Ennismore European Smaller Companies Fund

Investor Newsletter for the month of May 2017

Issued on 6 June 2017

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 382m as at 31st May. Total assets under management by Ennismore Fund Management were GBP 630m. 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 31 May 2017

	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	122.59	140.74	20.71	20.21	20.27			
Period	% Change					% Change		
May 17	2.2	-1.2	2.2	-0.6	-0.6	5.5	1.9	2.6
April 17	1.0	2.7	1.0	2.4	2.4	3.1	4.5	1.5
March 17	0.9	0.7	0.9	0.8	0.7	2.3	2.5	3.5
February 17	-0.2	0.4	-0.2	0.3	0.3	2.5	3.0	2.8
January 17	1.2	0.6	1.2	0.7	0.7	1.8	1.4	-0.3
December 16	1.9	1.4	2.0	1.6	1.5	6.0	5.2	5.8
2017 to date	5.2	3.1	5.2	3.5	3.5	16.2	13.9	10.4
Annualised return ⁵	14.8	13.4	12.1	11.8	11.8	10.4	9.1	4.4
Since launch ⁵	1149.0	899.4	107.1	102.1	102.7	517.1	391.6	119.5
Discrete 12 Month Rolling Performance - % Change								
To 31 May 17	14.6	0.6	14.6	3.2	3.2	34.5	18.4	20.5
To 31 May 16	14.7	7.7	14.7	9.0	9.0	4.5	-2.1	-8.7
To 31 May 15	2.3	15.8	2.3	13.2	13.1	5.1	19.0	11.5
To 31 May 14	18.1	24.1	18.2	23.2	23.1	22.0	28.2	15.2
To 31 May 13	21.4	14.1	21.3	15.5	15.4	40.9	32.2	31.7

¹Source: Administrator, Net Asset Value. ²Source: Administrator, Net Asset Value, net income reinvested. ³Source: Bloomberg, Euromoney (formerly HSBC) Smaller European Total Return Index. ⁴Source: Bloomberg, MSCI Europe Index, local currencies, total return. ⁵Since 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. **Past performance is not a guide to future returns.**

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 2.2% in May. Our long book contributed 4.6% while the Fund's short exposure cost 2.1%. Cegedim contributed 0.4% to NAV following a strong Q1 update in April. Henry Boot also added 0.4% after its trading update announced 2017 results would be ahead of expectations. Our short position in a German software company cost 0.5% of NAV.

KSB - German manufacturer of pumps and valves (1.9% of NAV)

KSB was founded in 1871 and is a leading producer of pumps and valves which it sells through a well-established global sales and service network. The company has strong positions in the energy, industrial and water sectors and with revenues of EUR 2.2bn, is a top five global player in a fragmented market. The current operating environment however is tough as KSB faces a slump in the oil & gas industry and the "Energiewende" - Germany's nuclear exit. In response to this the company launched its largest restructuring program in its history in 2016, aiming to save costs of EUR 200m annually by 2019. We are confident this will deliver value - the 2016 results and our discussions with management demonstrate the company is making progress. KSB has a complex shareholding structure with around 40% of the equity and more than 80% of the voting shares held by the founding family which has meant it is overlooked by the market. Even so, we were astonished to find a business that traded on a 20% discount to a conservative book value when we invested in early 2017. The price is the major attraction in this unexciting but high quality business and we think the potential for operating profit to double by 2019 means further upside is warranted.

KSB is a high quality business. There is limited competition from Asian players in their core business and barriers to entry are high, particularly in the energy segment where given the critical role pumps play in conventional and nuclear power plants, customers are typically unwilling to make compromises on product quality or reliability. Customer concentration is low and KSB is not dependent on any single customer. New business in conventional and nuclear power plants is limited to emerging markets, but globally we think the long term outlook for the water and industry segment remains strong.

2016 was a very difficult year for KSB with revenues down 7.2% to EUR 2,166m and operating profit down 16.2% to EUR 88.2m. Despite overcapacity within the industry resulting in a highly competitive backdrop KSB actually increased its underlying operating profit thanks to the initial benefits of the cost savings program. After adjusting for EUR 50m

restructuring costs, operating profit increased and margins reached 6.3%. Peers have historic margins averaging well above KSB's target of 8%, a goal which we believe is not overly ambitious. Last time the company initiated a cost cutting program operating margins increased from below 4% in 2004 to 10.5% in 2008, so we are optimistic for improvements from current levels. Structurally KSB will always have lower margins compared to peers given the ownership structure and the involvement of the founding family as customer satisfaction is prioritised over efficient capital allocation. However, this results in a strong reputation amongst customers and commitment to invest for the longer term. This is evident in Brazil where despite business with their largest client becoming negligible and competitors exiting the market, KSB has remained and kept key personnel – even though it means senior managers are driving forklift trucks for the time being.

KSB currently has a market capitalisation of around EUR 770m with net cash of EUR 260m and pension liabilities of EUR 590m. The balance sheet is conservative and reveals some reserves in real estate and its holding in the listed Indian subsidiary which we cautiously estimate are worth around EUR 150m. Enterprise value fully accounting for the pension liabilities is just eight times last year's operating results adjusted for restructuring costs. The dividend yield is 1.4% currently but is set to potentially double in line with operating profits as this is the sole income source for the family foundation. Although the proposed change of the legal structure to a KGaA (Kommanditgesellschaft auf Aktien) at this year's annual general meeting is somewhat negative from a corporate governance perspective, we think at ten times this year's underlying operating profit – which we estimate will be more than EUR 150m – is a sensible valuation considering the shareholder structure. Therefore we see upside of around 25% for the next twelve months and substantially more if the company can achieve its 8% margin target going forward, generating profits of EUR 200m.

Top Five Holdings as at 31 May 2017

Company	Country	Sector	% of NAV
1 Jd Sports	United Kingdom	Consumer Discretionary	6.0
2 Vib Vermoegen	Germany	Real Estate	3.9
3 Conviviality	United Kingdom	Consumer Staples	3.5
4 Oslo Bors	Norway	Financials	3.1
5 Cello Group	United Kingdom	Consumer Discretionary	2.8
			19.3

Exposures as at 31 May 2017

Longs %	Shorts %	Gross Exposure %	Net Exposure %
83.7 (84.6)	46.4 (46.3)	130.1 (130.9)	37.3 (38.3)

Figures in brackets refer to previous month end.

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 31 May 2017

Country	Gross%	Net%	Market Cap	Gross%	Net%	Sector	Gross%	Net%
Australia	1.3	0.7	>£2bn	36.2	0.8	Consumer Discretionary	35.9	17.3
Austria	2.8	0.7	£700m - £2bn	29.2	0.3	Consumer Staples	11.0	-2.4
Belgium	1.7	-0.1	£200m - £700m	48.2	20.7	Energy	0.2	-0.2
Canada	1.3	0.5	<£200m	16.5	15.5	Financials	6.8	1.7
France	6.5	6.4				Health Care	6.2	3.3
Germany	30.5	8.9				Industrials	19.8	7.5
Italy	3.7	3.0				Information Technology	25.8	0.2
Netherlands	3.8	-2.7				Materials	5.1	3.7
Norway	6.0	6.0				Real Estate	11.8	7.3
Spain	1.9	-1.9				Telecommunication	6.6	-0.2
Sweden	1.3	-0.4				Utilities	0.9	-0.9
Switzerland	5.8	-5.3				Other	0.0	0.0
UK	51.8	24.2						
US	9.5	-3.6						
Other	2.2	0.9						

Geographic analysis relates to country of incorporation or listing. This may not represent the underlying economic exposure of the operating business.

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