

Ennismore European Smaller Companies Fund

Investor Newsletter for the month of January 2019

Issued on 6 February 2019

Fund Details

Daily dealing UCITS and Irish Central Bank regulated open-ended investment company with Financial Conduct Authority recognition and registered in Ireland. The Fund size was GBP 399m as at 31st January. Total assets under management by Ennismore Fund Management were GBP 804m. Our smaller companies 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 January 2019

	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	134.69	154.41	22.76	22.17	22.24			
Period	% Change					% Change		
January 19	1.4	4.3	1.4	3.8	3.7	5.6	8.8	5.6
December 18	0.2	-1.0	0.2	-0.7	-0.7	-5.3	-6.4	-5.3
November 18	2.3	2.2	2.3	2.2	2.3	-2.3	-2.5	-0.9
October 18	-1.0	-0.6	-1.0	-0.7	-0.7	-7.5	-7.0	-5.4
September 18	0.3	0.8	0.3	0.7	0.7	-1.8	-1.2	0.3
August 18	1.1	0.8	1.1	0.8	0.8	0.1	-0.3	-2.4
2019 to date	1.4	4.3	1.4	3.8	3.7	5.6	8.8	5.6
Annualised return ⁵	14.0	12.7	10.8	10.5	10.5	9.3	8.1	3.8
Since launch ⁵	1272.3	996.5	127.6	121.7	122.4	495.3	373.8	112.3
Discrete 12 Month Rolling Performance - % Change								
To 31 January 19	7.6	8.1	7.7	7.7	7.7	-8.8	-8.6	-6.6
To 31 January 18	6.1	4.1	6.1	4.7	4.7	20.8	18.4	14.7
To 31 January 17	13.4	0.7	13.4	3.2	3.1	28.1	13.8	12.4
To 31 January 16	12.9	11.2	12.8	11.1	11.1	6.8	5.3	-4.0
To 31 January 15	4.5	14.1	4.6	12.5	12.5	0.6	9.8	11.2

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 1.4% in January. Our long book contributed 5.6% while the Fund's short exposure cost 3.2%. The biggest contributor to NAV for the month was our long position in JD Sports, which added 1.8% after publishing a strong Christmas trading update, followed by Costain and Cegedim adding 0.9% and 0.4% respectively.

Secure Trust Bank - UK specialist lender (1.1% NAV)

Secure Trust Bank is a GBP 260m market capitalised, conservatively managed, specialist UK lender. The company is very shareholder return focussed and dynamically managed, being wary of the available returns adjusted for default risk. This ability to assess risk, enables them to act quickly and stop lending into a segment if they feel returns are no longer satisfactory and has enabled them to build and maintain a relatively small but well diversified loan book. The decision in the last couple of years to pull out of two different areas - subprime lending for motor purchases and specialist residential mortgages - bears testament to this. A further example of the management's strong focus on creating shareholder value is the sale of the Everyday Loans Group in 2016 at two times book value, leading to an equity gain of around GBP 120m having paid GBP 1 for the business four years previously. This has helped them to generate more than GBP 250m of accumulated net profit over the last 7 years.

As of the end of June, the company had a loan book of around GBP 1.8bn across various sub segments, generating an overall revenue margin of about 8.5%, which compares favourably to a provision rate of less than 2%. We feel the business is over resourced for a specialist lender, perhaps being prepared for a substantially bigger loan book over time. This generates a current cost to income ratio of over 55% which we would expect to improve in the medium term. Given the risks for this type of business however, we would definitely prefer an over resourced to an under resourced company.

Real estate finance and retail finance, which grew 30% in first half of their fiscal year, are two main areas of lending and account for around two thirds of the loan book. Real estate lending focusses especially on the institutional buy to let market as well as lending into the residential house building sector. Retail finance lends to consumers via retailers in areas

such as jewellery, sport season tickets, furniture and bicycles, typically on 12-month interest free type deals, receiving a fee from the retailer plus any future interest. The other main area of focus is for used car financing (15% of total lending) which, as already mentioned, was pivoted away from subprime consumer categories.

Going forward, we expect Secure Trust Bank to grow further in niche sub segments within the consumer finance area as well as focussing more on higher quality customers within the motor area. Recent hires with experience in the car lending market as well as investments made into their digital platform will assist here and we believe this could have a material impact on profits in the medium term.

Clearly the cloud of Brexit is currently a worry for all UK lenders, but we do feel that the management at Secure Trust Bank will create value over the coming number of years whatever the outcome. More than 90% of its funding comes from retail deposits which we prefer in terms of funding uncertainty in a worst-case Brexit scenario.

The business generates a return on equity of over 13% which means that they may slowly absorb capital as they are growing their loan book at a double-digit rate alongside paying out a growing healthy dividend. Although we don't expect it, if further capital was needed going forward then given the company's historic value creation, we expect them to be well supported.

Overall, we see the stock as having strong tangible equity backing on our forecasts of around GBP 240m by the end of 2019, with earnings growing close to 20%. This after paying out a dividend yield of 6%. Over time we expect the business to leverage their well invested cost base by further value accretive lending, giving good quality earnings momentum and an increasing return on equity. Putting the business on a multiple of 1.4 times tangible book for 2020 gives a total return of over 60% over the next two years.

Top Five Long Holdings as at 31 January 2019

Company	Country	Sector	% of NAV
1 Jd Sports	United Kingdom	Consumer Discretionary	7.2
2 METRO	Germany	Consumer Staples	4.9
3 Costain	United Kingdom	Industrials	4.4
4 Oslo Bors	Norway	Financials	3.4
5 Sto	Germany	Materials	2.9
			22.8

Exposures as at 31 January 2019

Longs %	Shorts %	Gross Exposure %	Net Exposure %
82.4 (74.8)	43.3 (36.2)	125.7 (111.0)	39.1 (38.6)

Figures in brackets refer to previous month end.

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 31 January 2019

Country	Gross%	Net%	Market Cap	Gross%	Net%	Sector	Gross%	Net%
Austria	2.1	0.9	>£2bn	43.4	8.3	Consumer Discretionary	37.5	9.5
Belgium	1.5	0.8	£700m - £2bn	11.7	-4.3	Consumer Staples	8.2	4.5
France	5.3	2.1	£200m - £700m	49.7	20.9	Energy	0.6	0.4
Germany	30.6	9.4	<£200m	20.9	14.2	Financials	13.5	10.3
Hong Kong	1.7	-1.7				Health Care	5.1	1.2
Ireland	1.6	1.3				Industrials	19.0	10.3
Italy	4.6	2.8				Information Technology	27.0	-4.4
Luxembourg	1.1	1.1				Materials	4.2	3.1
Netherlands	2.8	0.8				Real Estate	8.1	2.6
Norway	6.7	6.3				Telecommunication	2.5	1.6
Sweden	2.3	-0.1				Utilities	0.0	0.0
Switzerland	4.0	-4.0				Other	0.0	0.0
UK	52.6	23.1						
US	7.0	-2.6						
Other	1.8	-1.1						

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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