Ennismore European Smaller Companies Fund

Investor Newsletter for the month of October 2019

Issued on 6 November 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 413m as at 31st October. Total assets under management by Ennismore Fund Management were GBP 1,002m. 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.

Performance as at 31 October 2019

	Share Class[2]				
	GBP A £	**GBP A €**	**GBP B**	**EUR A**	**EUR B**
NAV per Share[1]	**142.38**	**165.14**	**24.06**	**23.63**	**23.74**
Period	**% Change**				
October 19	**0.2**	**2.8**	**0.2**	**2.4**	**2.4**
September 19	0.6	2.9	0.6	2.4	2.4
August 19	0.6	1.2	0.6	1.1	1.1
July 19	0.6	-1.0	0.6	-0.7	-0.7
June 19	-0.7	-1.9	-0.7	-1.8	-1.7
May 19	2.2	-0.6	2.2	-0.1	-0.1
April 19	0.7	1.0	0.7	0.9	0.9
March 19	1.5	0.8	1.5	0.9	1.0
February 19	-0.2	1.7	-0.2	1.3	1.3
January 19	1.4	4.3	1.4	3.8	3.7
2019 to date	**7.2**	**11.6**	**7.2**	**10.6**	**10.7**
Annualised return[3]	**13.8**	**12.6**	**10.5**	**10.3**	**10.4**
Since launch[3]	**1350.7**	**1072.6**	**140.6**	**136.3**	**137.4**
	Discrete 12 Month Rolling Performance - % Change				
To 31 October 19	8.5	9.2	8.5	8.9	9.1
To 31 October 18	4.3	3.2	4.3	3.3	3.4
To 31 October 17	8.9	6.9	8.9	7.4	7.4
To 31 October 16	18.9	1.3	18.9	4.4	4.4
To 31 October 15	7.3	13.5	7.3	12.2	12.2

[1]Source: Administrator, Net Asset Value. [2]Source: Administrator, Net Asset Value, net income reinvested. [3]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. **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.

Top 5 Contributors and Detractors for October 2019

Contributors	**MTD (bp)**
German financial services company	81
UK technology company	44
UK healthcare company	44
Costain Group Plc	26
Secure Trust Bank Plc	18

Detractors	**MTD (bp)**
US auto company	-40
IQE Plc	-30
UK auto company	-22
Hong Kong real estate company	-19
U and I Group Plc	-19

Individual stock attributions relate to GBP A shares and are gross of fees and expenses (including financing/stock borrowing costs).

The Fund's NAV increased by 0.2% in October. Our long book was flat while the Fund's short exposure contributed 0.7%.

Nokian Renkaat Oyj – Finnish tyre manufacturer (0.9% NAV)

The pneumatic rubber car tyre is not the most cutting-edge product. Key innovations behind it – vulcanization to make the rubber weatherproof and an inner-tube to improve durability – have been in use for well over a century. There's no lack of competing manufacturers and only modest brand loyalty. About a quarter of the market is supplied by low-cost producers. As a whole, industry returns reflect this, with most players earning an average return on capital of about 15% (before tax). One producer stands out, though, with returns consistently closer to 25% since the early 2000s. That is the kind of anomaly we get very interested in, which is why we have followed Nokian's business for many years. Today its shares are trading at a multiple of less than 15 times average earnings over the last 5 years (the market cap is EUR 3.7bn, net earnings before goodwill amortisation a little over EUR 250m on average), with little debt (around EUR 400m net). If its return on capital is sustained close to historic levels, and if the top line continues to grow even modestly, we think the market is significantly undervaluing the business. We believe it's likely that the answer to both ifs is that they will, and have bought a position in Nokian shares.

There is no doubt Nokian earns a high return on its capital. That's only useful to us if we understand why this advantage probably won't be competed away over the coming years. Logically, the fact that it is has already been sustained for so long suggests that, unless something significantly changes in the industry, it is likely to continue for some time. That is hardly enough to give us confidence. The obvious thing that is different about Nokian is that it mostly focussed on a niche, winter tyres. But there's no reason why a niche should be more profitable than the mass market (and some reasons why it shouldn't, particularly economies of scale). Our research suggests that winter tyres are more profitable than summer tyres for most manufacturers. The cost of development and production is a little higher, but prices are higher still. We think this reflects how consumers value the product. The danger when a tyre doesn't perform on snow or ice is much higher than in normal driving conditions. Bluntly, a sub-standard winter tyre is more likely to kill you. That means drivers focus on quality when they buy, and are more willing to pay a premium for a well-known, specialist brand. We can't get reliable winter tyre margin data from other manufacturers, so we can't be sure how much of Nokian's advantage is due to the high share of winter tyres in its sales mix, but we don't think it is the whole story. The other thing that stands out to us is Nokian's distribution network. Whereas a large proportion of summer tyres are sold in bulk to go on new cars, winter tyres are always a secondary purchase (even in the Nordics where they are required by law). They also need to be stored for much of the year when they are not on the vehicle. In the Nordics, its main markets, Nokian has its own tyre reseller network (Vianor) that will do this for you. In Russia, its next largest market and home to most of its manufacturing capacity, it has national coverage through a network of third party resellers.

Overall demand for Nokian's tyres is driven by the number of cars in markets that experience severe winter conditions, adoption of winter tyre use in these markets, the type of cars people choose to own and how much they are driven. Combined we expect modest growth over the medium term, mostly from higher adoption in some markets where winter tyres are not currently mandatory (Russia and eastern Europe) and the more general trend to larger passenger vehicle sizes (which need bigger tyres). More specifically, Nokian is building a medium sized manufacturing plant in the USA which will mean it can serve parts of that market, particularly smaller resellers, more economically. The plant opens in January next year and will increase overall passenger tyre capacity by about 20%. At the macro level we assume car ownership broadly flattens out in developed markets.

Nokian is a high return on capital business. We think the reasons for that will persist for the foreseeable future. That doesn't necessarily make it a better investment than other tyre manufacturers, but we do think it is easier to forecast, primarily because its returns are less subject to capacity imbalances across the industry. That is, it is lower risk for us. We think a price to earnings ratio in the mid-teens is an attractive price to buy into a well run, shareholder focussed business. Nokian has paid out 90% of its free cash flow as dividends over the last 5 years, yielding close to 6%. We don't think that is under threat as capex is currently elevated while they build out the US plant. Earnings growth will be subdued in the short run while that capacity is ramped up, but we think it is sensible way to grow the business longer term without materially diluting its industry-leading returns. We expect total annual shareholder returns in the mid-teens from here.

Top Five Long Holdings as at 31 October 2019

	Company	Country	Sector	% of NAV
1	METRO	Germany	Consumer Staples	3.6
2	Sto	Germany	Materials	3.2
3	Costain	United Kingdom	Industrials	3.0
4	Jd Sports	United Kingdom	Consumer Discretionary	3.0
5	Vossloh	Germany	Industrials	3.0
				15.8

Exposures as at 31 October 2019

Longs %	Shorts %	Gross Exposure %	Net Exposure %
72.7 (72.2)	49.5 (45.7)	122.2 (117.9)	23.2 (26.5)

Figures in brackets refer to previous month end.

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

Country	Gross%	Net%
Austria	2.0	1.0
Finland	1.4	0.5
France	5.9	1.9
Germany	30.5	6.4
Hong Kong	1.3	-1.3
Ireland	3.5	3.5
Italy	5.5	3.5
Luxembourg	1.5	1.4
Netherlands	2.3	0.2
Norway	2.2	0.2
Sweden	2.4	0.0
Switzerland	5.0	-5.0
UK	44.9	13.7
US	9.9	-1.8
Other	3.9	-1.0

Market Cap	Gross%	Net%
>£2bn	41.4	6.9
£700m - £2bn	18.0	-5.9
£200m - £700m	39.8	6.2
<£200m	23.0	16.0

Positions	Oct	Sep
Long	80	76
Short	96	91
Longs Opened	5	5
Longs Closed	1	4
Shorts Opened	8	4
Shorts Closed	3	3

Sector	Gross%	Net%
Consumer Discretionary	35.7	6.1
Consumer Staples	5.3	3.1
Energy	0.5	0.3
Financials	9.8	9.5
Health Care	7.5	0.1
Industrials	19.1	8.7
Information Technology	31.3	-13.4
Materials	5.3	5.2
Real Estate	4.2	1.6
Telecommunication	3.5	2.0
Utilities	0.0	0.0
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.

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We hereby disclose that as at the date of first issue of the report to which this is an Appendix, we held positions in the companies discussed in that report and we are thus subject to conflicts of interest in respect of these companies. The analysis presented on these companies has not been prepared in accordance with legal requirements regarding the independence of investment research and as such is considered non-independent research, as defined by COBS 12.3.2R of the FCA Handbook and as a marketing communication.

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The examples of specific investments included herein are not representative of all of the companies purchased, sold or recommended for the Fund. The Fund's portfolio contains a much larger number of positions than the examples set forth herein and, accordingly, the examples are not intended to indicate the overall composition of the Fund's portfolio. It should not be assumed that investments in the companies identified will be profitable, that recommendations made in the future will be profitable or will equal the investment performance of those discussed herein, or are representative of investments that will be made in the future. There is also no guarantee that any of the positions are currently or will remain in the Fund. The information included in this document should not be considered a recommendation to purchase or sell any particular security or other financial instrument. All statements and expressions are the sole opinion of Ennismore and are subject to change without notice.

The list of winners and losers presented herein has been calculated by including those positions that contributed most significantly, either positively or negatively, to the performance of the Fund's portfolio during the period. This is not meant to be indicative of the performance of all positions contained in the portfolio. Past performance is not indicative of future results.

Additional Information for Recipients in Switzerland

The Fund has not been approved for distribution in or from Switzerland by the Swiss Financial Market Supervisory Authority. As a result, the Fund's shares may only be offered or distributed to qualified investors within the meaning of Swiss law. The Representative of the Fund in Switzerland is Bastions Partners Office SA with registered office at Route de Chêne 61A, 1208 Geneva, Switzerland. The Paying Agent in Switzerland is Banque Heritage, with registered office at Route de Chêne 61, 1208 Geneva, Switzerland. The place of performance and jurisdiction for Shares of the Fund distributed in or from Switzerland are at the registered office of the Representative.

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