Ennismore European Smaller Companies Fund

Investor Newsletter for the month of February 2022

Issued on 7 March 2022

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 334m as at 28th February. Total assets under management by Ennismore Fund Management were GBP 560m. The fund continues to limit capacity by capping the maximum number of units in issue, there is currently a small amount of capacity available due to the natural rate of investor turnover. If you would like to invest when capacity is available through redemptions please contact Adam Sullivan on +44 (0) 20 7368 4224 or email subs@ennismorefunds.com.

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 28 February 2022

	Share Class[2]				
	GBP A £	**GBP A €**	**GBP B**	**EUR A**	**EUR B**
NAV per Share[1]	**154.27**	**184.28**	**26.07**	**26.25**	**26.37**
Period	**% Change**				
February 22	**-2.6**	**-2.7**	**-2.5**	**-2.6**	**-2.6**
January 22	1.1	1.6	1.1	1.5	1.5
December 21	1.5	2.9	1.5	2.6	2.7
November 21	1.8	1.0	1.8	1.2	1.2
October 21	-1.8	0.0	-1.8	-0.4	-0.4
September 21	-0.1	-0.3	-0.1	-0.3	-0.2
2022 to date	**-1.5**	**-1.2**	**-1.5**	**-1.2**	**-1.2**
Annualised return[3]	**12.7**	**11.8**	**9.0**	**9.1**	**9.1**
Since launch[3]	**1471.8**	**1208.6**	**160.7**	**162.5**	**163.7**
	Discrete 12 Month Rolling Performance - % Change				
To 28 February 22	18.2	22.6	18.2	22.4	22.5
To 28 February 21	-3.1	-4.0	-3.1	-4.0	-4.1
To 29 February 20	0.2	-0.2	0.2	-0.5	-0.4
To 28 February 19	8.3	11.9	8.2	11.1	11.1
To 28 February 18	5.5	1.8	5.5	2.5	2.5

[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.

The Fund's NAV decreased by 2.6% in February. Our long book cost 4.9% while the Fund's short exposure contributed 2.3%. Our long position in Studio Retail, very disappointingly, cost the fund 1.4% as the shares were abruptly suspended as they announced they would be appointing administrators. They were not able to persuade their lenders to increase the working capital facility, which was in sharp contrast to what was expected from conversations with the management. It is very hard to understand the rationale on why the request was declined given the company's historic profitability and we also find it surprising that there was no plan to raise equity if there was a significant risk with respect to the lenders' decision.

Top 5 Contributors and Detractors for February 2022

Contributors	**MTD (bp)**
Swedish software company	38
US food manufacturer	37
Dutch online retailer	33
UK online retailer	24
UK online retailer	22

Detractors	**MTD (bp)**
Studio Retail Group Plc	-141
Norwegian energy machinery supplier	-72
STO SE & Co KGaA	-66
Synairgen Plc	-60
UP Global Sourcing Holdings Plc	-29

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

Fielmann AG – German optical retailer (1.4% NAV)

Fielmann is a leading optical retailer in Europe with a dominant position in Germany, Switzerland and Austria. Established in 1972, it continues to be a family-owned business with the founder holding 72% of the shares and has built a strong high quality business in an industry that is profiting from long term positive demographic and structural trends. Moreover, the pandemic accelerated these trends as people now spend more time than ever looking at screens. The company's extensive scale and vertical integration are strong moats enabling it to consistently achieve industry leading operating margins. Ennismore has enjoyed watching from the sidelines as Fielmann achieved a bond like status over the years. Due in part to the aforementioned points, we think there is a great opportunity now to get involved as the stock has derated for various reasons, trading around average levels seen in 2014. Its profits are still depressed from the pandemic, but the reasons for the derating to ease are visible. We expect Fielmann to return to higher growth rates for revenues and profits. Assuming normalized operating margins, the shares trade on fifteen times operating profit, which we find attractive with no financial debt, and net cash of around EUR 200m. With a return to higher sustainable growth and an outlook for this year that foresees double digit revenue and profit expansion the shares have solid upside potential and the dividend yield of 3% and positive director dealings over the last year lend further support.

With a market cap of EUR 4.1bn, Fielmann is certainly not a stock that is undiscovered or under-covered but, despite this, it ticks many of the boxes we like for our investments. The business is benefiting from very strong scale effects. Within its largest market Germany, which accounts for around 70% of total revenue, every second pair of glasses is sold by Fielmann even though it makes up only 5% of all shops within Germany, implying unmatched productivity. Furthermore, even though Fielmann has a 51% market share by volume, it has only 22% by value, which is testament to their low-price strategy. Similar ratios apply for the much smaller markets in Switzerland and Austria. Low price does not mean low quality, because its key performance indicator has always been customer satisfaction. The success of their strategy can be seen financially with the increase in gross margin averaging now 80% up from mid 60% 20 years ago. It is the company's scale, but also, the vertical integration of their supply chain which enables industry leading margins. Though Fielmann buys frames and lenses from external partners, it has the full value chain in-house and cuts out the wholesale margin to give better prices to their customers. One bottleneck of growth has been, and still is, the supply of trained opticians. In this area, Fielmann is vertically integrated as well, possessing its own academy which supplies more than 40% of all apprentices in Germany. This all leads to a very robust business model and superior financials. Fielmann consistently averages high pre-tax return on capital in the 20s, generates substantial free cash flows which enable it to pay out attractive dividends (apart from 2020), while still supporting growth. Given its size in Germany, growth is maturing. However, the positive trends of an increasingly elderly population and a younger generations' screen exposure many times higher than previous generations, provides for good growth. Higher growth will also come from international markets like Italy and Poland, acquisitions like the purchase of the number three optical chain in Spain, Optica del Penedes, and the rollout of hearing aid sales studios within its retail outlet. Hearing aids are a natural add on as they do not need any additional marketing, given the target group is already a customer. Currently at 6% of total revenues, it will approach 10% of total revenues in the mid-term and continue to be a growth driver. Therefore, we expect Fielmann, post crisis, to grow more in the high single digits vs. low to mid-single digits seen in recent years.

We believe there are many reasons for the derating and underperformance of the shares. Revenue growth did come down and with cost inflation, mostly wages, this led to operating profits flatlining in the years 2017 and 2018. This is being addressed. Progress can be seen by the acceleration of the store rollouts by 45 stores per year and can also be seen by their focus on organic and external growth in international markets and a focus on increasing the hearing aid business. Another drag for the shares has been the looming risk from new online retail players, due to the disruption it has brought to other industries. The last decade has shown that online sales are not working for corrective lenses and pure online optical retailers are turning to the high street. Fielmann is spending a lot on R&D to find good solutions to take parts of the customer journey online but only if it can guarantee its high-quality standards are upheld. We think the threat from online competition has eased and Fielmann is focusing on innovation that will improve customer satisfaction. Furthermore, a generational leadership change may also have hampered shareholder conviction, given the son of the founder is the youngest acting CEO for a large, listed company in Germany. Even though Marc Fielmann is just 32 years old, we think he has been well prepared to head Fielmann and has navigated the choppy waters of the pandemic successfully, earning him respect from senior management and investors alike. We see it as a big win for the company to be headed by a millennial. Especially for a traditional brand acting in a much more dynamic environment. Lastly, there were also fears that Fielmann could significantly decrease its dividend payments given increased investments in omnichannel capabilities and its ramped-up store roll out. With the announcement of the latest dividend with a pay-out ratio above 80% leading to a 3% yield, we think Fielmann proves that its business model continues to be very cash generative with investments likely to have peaked last year.

With its new emphasis Fielmann should return to a healthy growth path and the preliminary numbers show a first indication of this. In 2021 almost all markets exceeded the pre-crisis sales level with only Austria being impacted by more severe lockdown, leading to revenues of EUR 1,225m in Germany and EUR 455m in International in which we estimate organic growth of 8% and 16% respectively. The hearing aid business was up 15% to EUR 93m with only circa one third of its 913 stores containing hearing aid studios. Operating profit of EUR 210m was still burdened by the pandemic, and growth investments in the second half coincided with lockdowns, as well as a non-cash impairment of EUR 15m for software development. This year will still be impacted by restriction measures and growth investments, but we expect both revenue and profits to increase at circa double-digit growth rates. For 2023, when hopefully the pandemic becomes a memory of the past, Fielmann should gradually return to its historic operating profit margins above 16% and we expect revenues of EUR 2bn and an underlying operating profit of EUR 320m. Applying the average multiple of enterprise value to operating profit of 17.5 times over the last ten pre-crisis years results in an upside of more than 30% over the next twelve months.

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Top Five Long Holdings as at 28 February 2022

Company	Country	Sector	% of NAV
STO SE & Co KGaA	Germany	Materials	8.3
IG Group Holdings Plc	United Kingdom	Financials	3.5
UP Global Sourcing Holdings Plc	United Kingdom	Consumer Discretionary	3.3
Vossloh AG	Germany	Industrials	3.1
D4t4 Solutions Plc	United Kingdom	Information Technology	2.5
			20.7

Exposures as at 28 February 2022

Longs%	Shorts%	Gross Exposure%	Net Exposure%
67.2(67.0)	34.5(32.9)	101.7(99.9)	32.7(34.1)

Figures in brackets refer to previous month end. All calculations are subject to the impact of rounding

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 28 February 2022

Country	Gross%	Net%
Australia	0.6	-0.6
Austria	3.0	3.0
Belgium	2.5	1.8
Finland	0.7	-0.1
France	3.4	2.9
Germany	22.2	17.2
Italy	2.0	1.4
Netherlands	2.4	2.4
Norway	5.5	-3.0
Other	0.7	0.1
Spain	0.6	0.6
Sweden	9.3	-3.1
Switzerland	5.8	0.9
United Kingdom	37.2	12.1
United States	5.7	-2.8

Market Cap	Gross%	Net%
>£2bn	17.7	0.3
£700m - £2bn	26.0	4.8
£200m - £700m	39.2	11.0
<£200m	18.7	16.6

Positions	Feb	Jan
Long	68	65
Short	75	70
Longs Opened	3	4
Longs Closed	0	4
Shorts Opened	14	6
Shorts Closed	9	8

Sector	Gross%	Net%
Communication Services	3.5	0.6
Consumer Discretionary	28.4	1.9
Consumer Staples	5.1	-0.9
Energy	0.0	0.0
Financials	6.8	6.2
Health Care	4.4	1.1
Industrials	24.2	10.0
Information Technology	15.5	2.4
Materials	11.2	9.7
Real Estate	2.2	1.9
Utilities	0.4	-0.4
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.

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