

Ennismore European Smaller Companies Fund

Investor Newsletter for the month of March 2019

Issued on 4 April 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 406m as at 29th March. Total assets under management by Ennismore Fund Management were GBP 835m. 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 29 March 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	136.42	158.31	23.05	22.67	22.75			
Period	% Change					% Change		
March 19	1.5	0.8	1.5	0.9	1.0	1.0	0.7	2.0
February 19	-0.2	1.7	-0.2	1.3	1.3	1.3	3.1	3.6
January 19	1.4	4.3	1.4	3.8	3.7	5.6	8.7	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
2019 to date	2.7	7.0	2.7	6.1	6.1	8.1	12.9	11.6
Annualised return ⁵	13.9	12.7	10.7	10.5	10.6	9.4	8.2	4.1
Since launch ⁵	1290.0	1024.1	130.5	126.7	127.5	509.3	391.7	124.3
	Discrete 12 Month Rolling Performance - % Change							
To 31 March 19	9.8	11.8	9.9	11.1	11.1	-2.3	-0.1	4.3
To 31 March 18	4.6	2.1	4.6	2.8	2.8	9.9	6.6	2.0
To 31 March 17	10.0	2.0	10.0	3.5	3.5	26.0	16.8	19.6
To 31 March 16	20.8	10.2	20.8	11.3	11.3	6.6	-2.6	-10.6
To 31 March 15	-2.1	11.9	-2.0	10.0	10.0	0.7	15.1	14.7

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 1.5% in March. Our long and short books contributed 0.5% and 1.4% respectively. The biggest contributor was our long position in JD Sports, which added 0.6%. IFG Group and Inmarsat, which were both subject to takeover offers, added 0.5% and 0.4% respectively. On the short side, IQE was the biggest contributor, adding 0.5% as the company announced weaker guidance for 2019. In addition, a short position in a UK healthcare company added 0.4%.

The biggest detractors were our long positions in Costain Group and Just Group which both cost 0.4%, the latter of which announced an equity placing.

RENK AG - German industrial components manufacturer (2.3% NAV)

RENK is a global manufacturer of gear units, bearings and transmissions, selling into a wide range of end industries including shipbuilding, defence, aviation, rail and power generation. We wrote about the company approximately four years ago and think it is an ideal time to give an update post the positive results for 2018 and recent strategic changes in the majority shareholders.

As of now, RENK continues to be an overlooked European small-cap that is highly regarded within its industry and entirely neglected within ours due to the absence of any sell-side coverage. Admittedly, the challenges stemming from the shift to renewable energy have had a greater impact than we expected during our initial investment. Despite these headwinds however, RENK has been able to successfully keep profits broadly stable which we see as testament to the company's quality.

In our view, there are several factors that serve as good examples with which to demonstrate the high quality of the business. Firstly, RENK is a very innovative company that rigorously protects its proprietary intellectual property; we experienced this first hand, when we were asked to cover the cameras on our mobile devices during a site visit. The internal knowledge and safeguarding thereof, serves as an economic moat and are key to explaining the recurring double-digit operating margins and high returns on invested capital, which are currently around 20% post-tax. In addition to robust and consistent margins, the company benefits from strong market presence, exceeding a 60% share in certain product areas. Lastly, RENK has a very compelling corporate culture, reflected in its high staff retention with an average length of service of 16 years. RENK's business quality has led to an extremely solid balance sheet with no intangibles,

minor financial debt with net cash of EUR 186m and a tangibles book value covering 70% of the current market capitalisation.

At the most recent results, revenues increased 7% to EUR 502m and operating profit was stable at EUR 60m. Order intake increased significantly by 21.8% to EUR 529m. The results differed by segment: Vehicle Transmissions performed strongly, generating circa 35% of total revenues and more than half of the operating profit, whereas Special Gears disappointed with a slight increase in revenues to EUR 171m and a decrease in operating profit to EUR 5m. For 2019, RENK is guiding for further growth in orders, revenues above EUR 500m and a stable operating profit. We would expect the outcome to be in line with their indications.

As mentioned above, we should also consider the implications of the recent changes to the majority shareholder of the company. RENK had belonged to the German industrial giant MAN SE, an 87% owned subsidiary of Volkswagen AG, for 95 years until it was sold at the end of 2018 to another Volkswagen AG wholly owned subsidiary, Volkswagen Klassik GmbH. Even though there were no apparent synergies between MAN and RENK, the emotional ties forged over a 95-year relationship appeared strong, unlike perhaps at Volkswagen AG. Volkswagen AG has clearly demonstrated to the market it is looking to release capital through the albeit postponed IPO of its wholly owned truck business, Traton. The disposal of RENK of which it owns 76%, would also fit naturally within this rationalisation strategy. As Volkswagen aims at refocusing its core business we don't see it as the optimal owner for RENK and don't expect that it will remain so in the long term. Although it is not the core part of our investment thesis, if the business was disposed of in a corporate transaction, the valuation paid for this asset could be materially higher than those used in our base assumptions.

Based on the current market capitalisation of EUR 665m, its net cash position and owning 3% treasury shares, RENK's enterprise value is valued at less than 11 times operating profit after tax. They also generate a modest, but sustainable, dividend yield of more than 2%. We believe the current valuation is too cheap for a high-quality business that has constantly returned double digit margins throughout the cycle and healthy returns on invested capital. Valuing the company on a modest 15 times net operating profit after tax would give an upside of circa 30% by the end of 2019.

Top Five Long Holdings as at 29 March 2019

Company	Country	Sector	% of NAV
1 Jd Sports	United Kingdom	Consumer Discretionary	7.7
2 METRO	Germany	Consumer Staples	4.7
3 Costain	United Kingdom	Industrials	3.8
4 Oslo Bors	Norway	Financials	3.4
5 Sto	Germany	Materials	2.7
			22.3

Exposures as at 29 March 2019

Longs %	Shorts %	Gross Exposure %	Net Exposure %
80.5 (82.5)	45.6 (48.8)	126.1 (131.3)	34.9 (33.7)

Figures in brackets refer to previous month end.

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 29 March 2019

Country	Gross%	Net%	Market Cap	Gross%	Net%	Sector	Gross%	Net%
Austria	2.2	0.5	>£2bn	43.3	6.2	Consumer Discretionary	36.8	9.9
Belgium	1.0	1.0	£700m - £2bn	11.8	-5.0	Consumer Staples	7.3	4.8
France	6.1	1.7	£200m - £700m	54.0	20.6	Energy	0.6	0.4
Germany	28.3	9.0	<£200m	17.0	13.1	Financials	12.3	10.7
Hong Kong	1.8	-1.8				Health Care	6.9	-0.8
Ireland	1.6	1.4				Industrials	18.9	8.9
Italy	4.6	2.3				Information Technology	28.5	-6.3
Luxembourg	0.8	0.8				Materials	4.0	2.9
Netherlands	3.1	1.0				Real Estate	7.4	1.9
Norway	7.3	6.0				Telecommunication	3.4	2.5
Sweden	3.1	-0.8				Utilities	0.0	0.0
Switzerland	3.9	-3.9				Other	0.0	0.0
UK	52.7	22.1						
US	7.5	-3.1						
Other	2.1	-1.3						

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

For further information please contact: Eleanor Scott, Ennismore Fund Management +44 (0) 20 7368 4219 subs@ennismorefunds.com
 For dealing please contact: Northern Trust International Fund Administration +353 (0) 1 434 5103 Ennismore_TA_Queries@ntrs.com
 Services (Ireland) Ltd

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