

Montanaro UK Smaller Companies Investment Trust

Quarterly Commentary – Q1 2020

Before turning to investment matters, it is important to update you on how we are faring amid the Covid-19 pandemic. The team are working remotely and are thankfully all well. To a large extent, it is business as usual: our Analysts are speaking to the companies in which we invest; liquidity has not been a problem; and our operations are running smoothly. We have also just added to the team with the hire of a specialist Healthcare Analyst. We are fortunate that during the quarter we experienced net inflows and all Montanaro Funds outperformed their respective benchmarks. Our Quality investment style has again served us well in turbulent markets.

The first quarter of 2020 will enter the history books: the Bull Market came to a shocking close to its 11th anniversary, as the S&P 500 recorded its second fastest 10% drop from peak since the Great Depression; the FTSE-100 suffered its worst one-day crash since Black Monday in 1987; the FTSE-250 fell for ten consecutive days, its worst run since 1998; UK SmallCap posted its second largest quarterly decline (-26%) since 1955; the European STOXX 600 Index experienced its worst ever one day fall (-11%); the oil price fell to levels not seen since 2002; and weekly jobless claims in the US exceeded 6.6 million (the highest weekly figure reached during the Great Financial Crisis of 2008 was less than 700,000). As financial markets saw large movements, the rest of the world halted: planes were grounded; shops, schools and factories closed; and by the end of March some 4 billion people had been instructed to stay at home. This was a true “Black Swan” event and one without precedent.

At the end of March, “MUSCIT” passed its “Silver Anniversary”. When we launched the Trust in March 1995, it was one of 27 UK SmallCap Trusts. Today, there are just seven left. It has been quite a journey and we thank all of our shareholders for their many years of support.

During the first quarter of 2020, the NAV of the Trust declined by 26%. While it is always disappointing to report a negative number, this was an outperformance of 10% versus the benchmark index. The result was that over the Financial Year to 31st March, the NAV outperformed by over 17%.

The strongest contribution during the quarter came from **Cranswick**, the leading supplier of fresh pork meat products, which rose after growing pork exports into China where the pig herd has been decimated by Asian Swine Fever. **Hilton Foods**, the leading meat packer, gained after reporting full year results ahead of expectations.

IntegraFin, the online investment platform for IFAs, benefited despite difficult markets, as management expect to see a continuation in net inflows from recently acquired advisers.

The weakest contribution came from **RPS**, the global engineering consultancy, which come under pressure due to expectations of revenue declines and little in the way of balance sheet headroom. **Cineworld**, the leading cinema operator in the UK and US, suffered as cinemas closed across their markets. **4imprint**, the supplier of promotional merchandise, declined because of potential supply chain disruptions and promotional merchandise budget declines from its core US customer base.

The financial conditions stemming from the coronavirus most threaten businesses with structural weaknesses. Despite our Quality approach to investing – we invest in businesses with strong balance sheets who have a greater chance of weathering economic storms – we are taking nothing for granted.

We are speaking to our companies to understand how the crisis is changing their operating conditions and how it has impacted staff. We are also asking management about balance sheet stability, the availability of credit facilities and the potential for future funding requirements. Finally, we are trying to assess what opportunities may emerge from the darkness of the pandemic.

Amid glimmers that Europe is beginning to see the benefits of social distancing measures, we wish all of our investors and their loved ones well. Please remain safe and take care during this difficult time.

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