

LF Montanaro Global Select Fund**Quarterly Commentary – Q4 2021**

Market review

A “Santa Rally” capped off another good year for equity investors in 2021. This, despite the threat of the Omicron variant which worried financial markets in the lead-up to Christmas and led to heightened levels of price volatility. Investors across almost all geographic markets enjoyed positive equity returns for the year, with only the New Zealand and Hong Kong indices posting negative returns – New Zealand suffering from its extended covid lockdown and Hong Kong a victim of political instability. In Europe, almost every sector posted healthy returns, the leader being IT while the laggard was retail, the only area of the market to post negative returns for the year.

To some extent the strength of returns was surprising given the numerous issues that threatened the economic trajectory: supply chain bottlenecks; labour shortages; and rising inflation. Indeed, during the fourth quarter, inflationary pressures overwhelmed a strong earnings season, leading to the underperformance of SmallCap versus LargeCap.

Portfolio

During the quarter, the NAV of the sterling share class increased by 6.9%, an outperformance of 3.7% versus the MSCI World SMidCap Index. For the year, the NAV gains by 27%, a healthy outperformance of 9.5% versus the benchmark.

The strongest contribution during the quarter came from **Esker**, the French provider of cloud software solutions to make cash conversion more efficient, which rose following strong quarterly results. **MIPS**, the Swedish manufacturer of a brain protecting helmet insert, outperformed on good results and news that they are slowly gaining traction in the safety market. **Tyler Technologies**, the leading provider of software to the US public sector, gained in the run-up to its Q3 earnings which were strong.

The weakest contribution came from **Chemometec**, the Danish provider of instruments to enable the quality control of cell therapies, which underperformed alongside other high growth healthcare companies due to profit taking, despite reporting strong operating performance. **Paycom**, the US provider of payroll software for mid-sized businesses, underperformed on renewed fears of the impact of Covid-19 on employment rates as they charge on a per-employee basis. **Adyen**, the global leader in cross-border online payments processing, saw its shares derate following the market's pricing in of additional rate-hikes in 2022.

Outlook

There is a seasonality effect to markets and 2022 has started as it so often does, with the underperformance of Growth versus Value. The predominant reason for this has been a continuation of inflationary fears – indeed inflation in the US has reached a 40-year high. On this point we will only reiterate what we have said before: we are not economists and do not spend too much time worrying about the macro. We focus on the quality and growth opportunities of our individual companies and construct the Portfolio on a bottom-up basis.

That said, clients have recently been asking us about the potential impact of inflation and interest rates on the Fund, so here are a few thoughts. The first thing to note is that the SmallCap effect has held true throughout periods of both rising and falling interest rates and during all but galloping inflationary environments (>12%); so we are convinced that investing in Smallcap makes sense, no matter how the macro winds are blowing.

Secondly, the balance sheet strength of the companies in the Portfolio significantly reduces refinancing risk from rising interest rates. Our focus on Quality should mean that our companies are relatively well placed to deal with higher rates of interest. Indeed, one of the key attributes we look for when assessing Quality is pricing power – the ability to pass on cost increases to customers. While there is no doubt that inflation and supply chain disruptions are having some impact on operations, we feel that the companies in the Fund are relatively well placed to deal with these challenges.

We wish all of you a very Happy New Year and every success in 2022!

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