Ennismore European Smaller Companies Fund

Investor Newsletter for the month of May 2019

Issued on 6 June 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 415m as at 31st May. Total assets under management by Ennismore Fund Management were GBP 894m. 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 31 May 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]	**140.47**	**158.88**	**23.73**	**22.85**	**22.94**			
Period			**% Change**				**% Change**	
May 19	**2.2**	**-0.6**	**2.2**	**-0.1**	**-0.1**	**-2.4**	**-5.1**	**-4.5**
April 19	0.7	1.0	0.7	0.9	0.9	4.3	4.3	4.1
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
2019 to date	**5.8**	**7.4**	**5.7**	**7.0**	**7.0**	**10.0**	**11.7**	**11.0**
Annualised return[5]	**14.0**	**12.7**	**10.9**	**10.4**	**10.5**	**9.4**	**8.1**	**4.0**
Since launch[5]	**1331.2**	**1028.2**	**137.3**	**128.5**	**129.4**	**519.8**	**386.7**	**123.0**
			Discrete 12 Month Rolling Performance - % Change					
To 31 May 19	11.3	10.4	11.3	10.2	10.3	-5.8	-6.5	-0.6
To 31 May 18	3.0	2.2	3.0	2.6	2.6	6.6	5.9	2.2
To 31 May 17	14.6	0.6	14.6	3.2	3.2	34.5	18.4	20.5
To 31 May 16	14.7	7.7	14.7	9.0	9.0	4.5	-2.1	-8.7
To 31 May 15	2.3	15.8	2.3	13.2	13.1	5.1	19.0	11.5

[1]Source: Administrator, Net Asset Value. [2]Source: Administrator, Net Asset Value, net income reinvested. [3]Source: Bloomberg, Euromoney (formerly HSBC) Smaller European Total Return Index. [4]Source: Bloomberg, MSCI Europe Index, local currencies, total return. [5]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 May 2019

Contributors	MTD (bp)
UK healthcare company	48
Sto SE & Co. KGaA	36
Chinese real estate company	31
US auto company	31
Renk AG	29

Detractors	MTD (bp)
Kongsberg Automotive Holding	-32
Vossloh AG	-29
Just Group Plc	-28
U and I Group Plc	-25
German financial services company	-23

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 2.2% in May. Our long book cost 0.7% while the Fund's short exposure contributed 3.4%.

Strabag – Austrian construction and building company (1.4% NAV)

Strabag is a leading European construction company with number one positions in its core countries of Germany and Austria that make up more than 60% of the business. In 2018, the company achieved an all-time high in revenues with EUR 15.2bn, an order backlog of EUR 16.9bn and operating profit of EUR 503m. The share price however does not reflect the positive development compared to when we last wrote about it three years ago. We think it is too cheap to ignore given a current market capitalisation of EUR 3.1bn, with net cash of EUR 1.2bn and an enterprise value of EUR 1.9bn. A construction company trading below four times its operating profit with a 15% discount to its conservative book value, could suggest that Strabag is a weak business in a structurally challenged market. We outline today why this is not the case but rather the opposite!

When Strabag went public in 2007, the market capitalisation was twice as high as today's, whereas the net profit after tax and minorities was only half of today's. Indeed, back then investors were hoping for huge profits stemming from the entry into the Russian market – today it is a tiny fraction of the total output with little risk. Last time we wrote about Strabag, it was not yet certain if the company would succeed with its 2013ff program with the goal to achieve a sustainable operating profit margin of 3%. While focussing on operational efficiency, risk management and prioritising profit before growth, Strabag's revenues increased by 16% from 2015 until 2018, while operating profit increased strongly by 78% from EUR 282m to EUR 503m. Even though the business is constrained by tight labour due to the high level of construction activity in its core markets as well as increasing prices for raw materials, this year the company is guiding for operating margins to be on par or better and a flat output given the high base set in 2018 as a result of the very favourable weather conditions. We think this is conservative guidance given the very good start to the year with output up 19% and a recent statement that new orders in its largest market Germany (48% of total output), allow for price increases that partially compensate cost inflation. We think it is paying off now that Strabag has access to its own raw materials as it serves as a hedge to price increases in a very tight construction market. This is a key competitive advantage, a barrier to entry for new players and crucial as the Bundesverkehrswegeplan 2030, a EUR 270bn investment plan for Germany's transportation infrastructure, provides a long-term structural demand, correcting the decade long underinvestment. It remains to be seen if Strabag can defend its operating margin level over a full business cycle; however, we are quite optimistic as the company continues to be very flexible regarding its cost base. The total number of employees has increased by only 3% since 2015, even though revenue has leapt by 16%. Cost overruns in large projects were another headwind of the past that burdened profitability – it seems that the intensive focus and improved risk management as well as the early adoption of the BIM (Building Information Modelling) processes mitigated these risks to some degree. That should help investors to become more confident in its earnings sustainability and lead to higher multiples. The increased medium-term guidance announced with this year's first quarter results should lend further support as Strabag now expects to increase the operating profit margin to 4% by 2022.

Although the business developed very favourably over the last few years, the valuation multiples contracted and we see that the low free float of only 13.5% is an obstacle to a more fundamental valuation. As of today, the stock continues to be tightly held by the former CEO Haselsteiner with 26.4%, Rasperia, Uniqa and Raiffeisen with 25.9%, 14.3% and 13.2% respectively and 6.7% held in treasury. Strabag's equity ratio increased to 31.4% and is high versus its peers' ratio and its own comfort zone of greater than 25%. We think Strabag could easily release EUR 900m and would still be better capitalized than its peers. We see a strong margin of safety at the current valuation and think that the shareholder structure will eventually change with a solution being found for the shareholding of Rasperia, whose owner Oleg Deripaska remains sanctioned by the US. In the meantime, we are rewarded by a well-covered dividend yield of 4.3%. Using an enterprise value to net operating profit multiple of 10x would give upside of more than 50%. Given the quality of the business, it should at least trade at its book value in the short term. Therefore, we see an upside of 25% for the next 12 months and substantially more once the shareholder syndicate has dissolved.

Top Five Long Holdings as at 31 May 2019

	Company	Country	Sector	% of NAV
1	Jd Sports	United Kingdom	Consumer Discretionary	4.7
2	METRO	Germany	Consumer Staples	4.6
3	Costain	United Kingdom	Industrials	3.8
4	Sto	Germany	Materials	3.2
5	Cello Health	United Kingdom	Consumer Discretionary	2.6
				18.9

Exposures as at 31 May 2019

Longs %	Shorts %	Gross Exposure %	Net Exposure %
72.2 (77.9)	44.9 (48.9)	117.1 (126.8)	27.3 (29.0)

Figures in brackets refer to previous month end.

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

Country	Gross%	Net%
Austria	2.2	0.8
Belgium	1.1	1.1
France	6.8	2.5
Germany	28.2	8.4
Hong Kong	1.5	-1.5
Ireland	1.4	1.2
Italy	4.6	2.4
Luxembourg	0.8	0.8
Netherlands	1.9	1.0
Norway	3.9	0.7
Sweden	2.7	-0.6
Switzerland	3.9	-3.9
UK	48.2	18.1
US	7.0	-2.3
Other	2.9	-1.4

Market Cap	Gross%	Net%
>£2bn	37.2	6.6
£700m - £2bn	14.5	-9.0
£200m - £700m	44.1	14.4
<£200m	21.3	15.3

Positions	May	Apr
Long	79	80
Short	92	91
Longs Opened	2	1
Longs Closed	3	1
Shorts Opened	4	9
Shorts Closed	3	4

Sector	Gross%	Net%
Consumer Discretionary	31.5	7.4
Consumer Staples	7.1	4.5
Energy	0.6	0.4
Financials	9.5	7.2
Health Care	6.8	-0.9
Industrials	17.6	8.1
Information Technology	29.6	-7.1
Materials	4.2	3.9
Real Estate	6.3	1.6
Telecommunication	3.9	2.2
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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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.

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