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WS AMATI UK LISTED SMALLER COMPANIES FUND

Quarterly Review

March 2025

By
Scott McKenzie, Fund Manager

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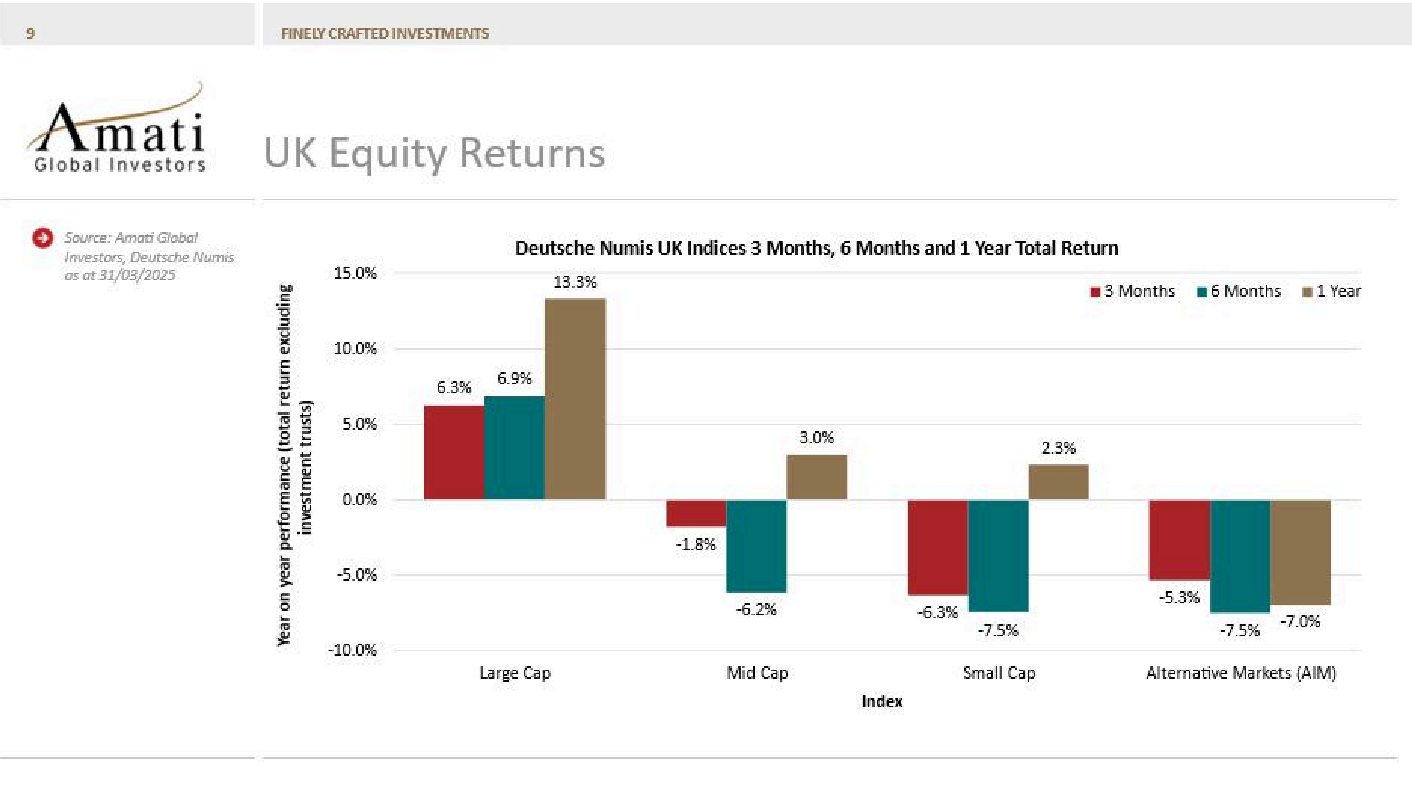
The first quarter of 2025 was a challenging one, with the Fund falling by -6.9% against a decline of -5.9% for the Deutsche Numis Smaller Companies plus AIM benchmark index.

It was a period when UK mid and small cap indices fared particularly badly compared to large cap. Whilst the Numis UK Large Cap index was up 6.3% over the period, the small cap, mid cap and AIM indices all went backwards again, with AIM in particular struggling as the changes to Inheritance Tax relief announced in the Budget last year continued to weigh heavily on many businesses.

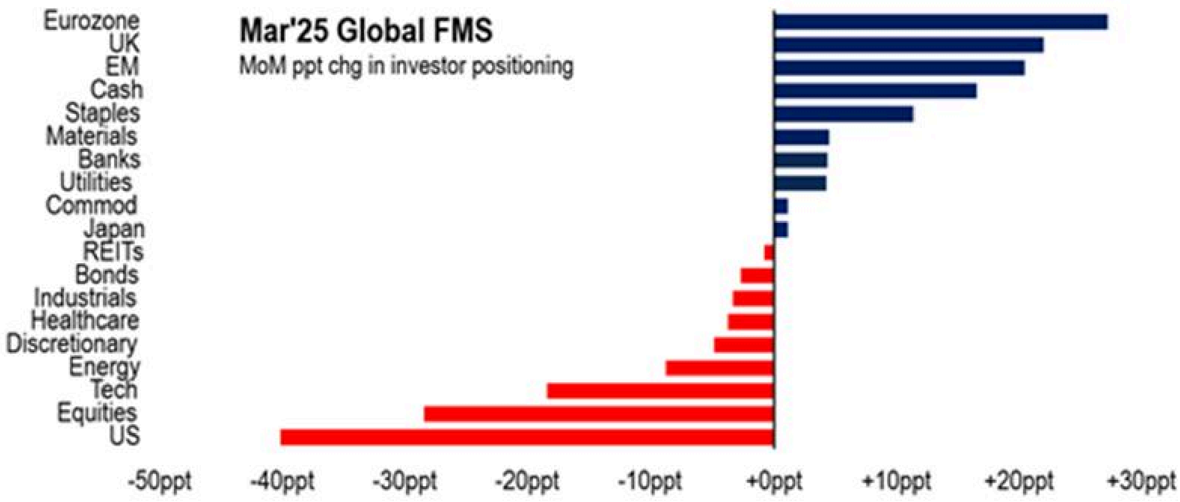


The quarter was dominated by geopolitical and economic events post the inauguration of President Trump in January, culminating in the US tariff announcements on April 2nd. Amongst many dramas to emerge from the White House recently, the uncertainty over the war in Ukraine and the direction of future US foreign policy also loomed large, resulting in upward reappraisals of European defence budgets, particularly in the UK and Germany. With President Trump's administration now weaponising its use of foreign and trade policy, no one can be sure where this move towards US protectionism and a radically different foreign policy will eventually lead us, but in the short term the outlook for global economic growth has undoubtedly deteriorated.

Against this dramatic change in outlook, global equity markets took fright, with US markets in particular falling sharply from what many observers had seen as elevated levels going into 2025. The S&P500 fell by over 6% during the quarter and the NASDAQ fared even worse, falling by 12%. Both indices are now in correction territory, having retreated by more than 10% since recent peaks. Therewas a notable move out of US equities and into the UK and European indices, with the FTSE100 rising by over 7% and the STOXX Europe Index up 8%. This represented the biggest quarterly swing in returns away from the US market in over twenty years, confirmed by the unprecedented change to fund manager allocations as recorded by the Bank of America survey below.

Chart 1: March FMS shows biggest drop in US equity allocation on record

Monthly change in FMS investor positioning

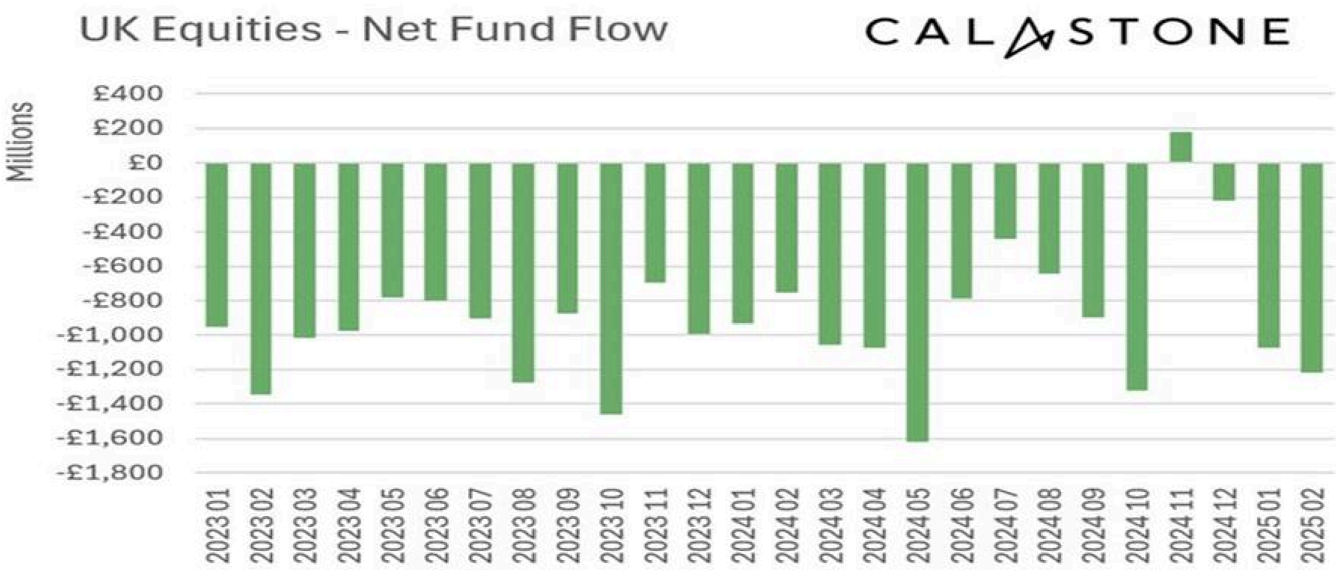


Source: BofA Global Fund Manager Survey

There were major moves in other asset classes, notably the safe haven of gold, where the price rose by 18% in the first quarter, reaching all-time highs. The US dollar also saw weakness, particularly against the Euro. The panic we saw in January over rising government bond yields began to dissipate in March, with US Treasury yields falling sharply in response to increased fears of economic slowdown. By contrast European yields rose from low levels in response to the new German government's plan for increased spending outwith normal debt constraints. Despite much press hyperbole, UK gilt yields were broadly unchanged over the quarter, having peaked at 4.9% in January before falling to 4.6%.

Turning to the UK, the main economic event was the Chancellor's Spring Statement, which was short on major policy changes but confirmed the bind that we are in both fiscally and with regard to growth, with the OBR cutting GDP forecasts for 2025 to only 1%. This forecast followed various GDP readings of close to zero in recent months. UK base rates continued to edge downwards slowly, and we saw a 0.25% cut in February. Although the UK government has limited room to manoeuvre, it is noteworthy that both corporate and household balance sheets are, overall, in much better shape. Adding a dash of confidence into this mix could have a swift and transformative effect, which is a far stronger starting point than most of our international peers.

Despite very attractive levels of valuation, UK retail funds still reported heavy outflows in the opening months of the year, as measured by the Calastone data, continuing the somewhat grim trend we have seen for several years now.



Against this difficult background any companies which delivered mild disappointment were poorly treated and those which had meaningful trading setbacks were savaged. The Fund was not immune to these shifts during the period. The weakest contributor to the Fund over the quarter was rail ticketing platform provider **Trainline**, where sentiment continues to be severely impacted by concerns over the setup of GB Railways by the government, which is scheduled for 2027. There was also a major disappointment from electronic prisoner tagging provider, **Big Technologies**, where the CEO and largest shareholder has been dismissed and results delayed as a result. The shares fell 44% in response. Other laggards included **Renew**, which issued a warning relating to its rail division in January, citing major problems at Network Rail. **Polar Capital** was weak in relation to the US market selloff and its large exposure to the tech sector. The 20% fall in **Gamma Communications** was somewhat frustrating given its recent strong progress in Germany. It has been de-rated mainly due to its intention to move from AIM to the main list on May 2nd, and we would expect to see a strong recovery in the shares after this transition period.

Turning to the positive contributors, our exposure to gold miners was the standout feature of the quarter, with **Greatland Gold** and **Hochschild Mining** rising by 90% and 25% respectively, in response to record gold prices and equity investors finally recognising their significant undervaluation relative to the commodity price. Greatland Gold made a particularly outsized contribution and has been an unexpected delight, rising by 150% since last year's fundraising on the AIM market. Most of the other positive contributions came from improvements in UK domestic businesses which were less impacted by sentiment regarding global trade. **Bytes Technology** rose by 15% after a positive trading update confirming that double digit growth rates were back on track. Both **Wickes** and **Victorian Plumbing** performed well, as they continue to take significant market share in an otherwise sluggish market for DIY spending. **Mortgage Advice Bureau** rose by 18% in response to the announcement of positive new medium term growth targets, targeting a doubling in shareholder value.

Having sold a number of sub scale positions of late we started to add various new holdings in February, including **ME Group**, the international supplier and maintainer of automated services equipment; and specialist fund manager, **Impax Asset Management**, which has not been immune from sector wide weakness but nowoffers a dividend yield of over 11% while maintaining an extremely strong balance sheet. Exposure to the Defence sector was increased via the inclusion of **Chemring Group**, a business ideally placed as European countries reinvest and seek to engage and support domestic supply chains. Finally, two software names were introduced to the fund: cybersecurity provider **GB Group** and outsourced IT provider, **Kainos Group**, the latter reintroduced to the portfolio as the share price failed to reflect the ongoing trend to outsourcing, not least from the UK government as it strives to increase efficiency.

In terms of sales, we cut our exposure to global manufacturing ahead of the Trump tariff announcements, selling the remaining positions in **DiscoverIE Group** and **XP Power**. The holding in buy-to-let lender **OSB Group** was exited after a rally in the share price. Smaller holdings in **Kooth** and **Watkin Jones** were also sold, the latter after a strong bounce from depressed levels.

The portfolio has become more focussed over the past year or so, with the number of holdings falling from 61 in early 2024 to 48 at the period end. As part of this process we have significantly reduced our exposure to smaller, less liquid companies and we believe that overall portfolio liquidity has improved as a result. The chart below confirms that our exposure to the very smallest businesses is now minimal and the weighted average market capitalisation for the portfolio has risen to £758m.

In early April markets have been negatively impacted further by the extraordinary events surrounding US President Trump's declaration of a trade war with the rest of the world in his "Liberation Day" speech. This speech will surely go down in history as one of the most weirdly dumb ever made by the leader of a major world economy. The Alice in Wonderland tone was set when the Head of State of the richest, most powerful country the world has ever seen started by claiming that his country has been "looted, pillaged, raped and plundered" for decades by the rest of the world's unfair trade practices. The so-called "reciprocal" tariffs Trump announced, based on the absurd idea that trade deficits are a tax on the US, have intervened in the global economy and caused a level of disarray in stock markets not seen since the pandemic. With such wild and fake cards being played, it is not possible to predict how this unfolds. But it does severely cloud the outlook for the global economy, and in turn, it will make life more difficult for some companies in the portfolio.

Unlike any former market crisis we have lived through, the severity of this one can be changed in minutes each time the US President changes his mind on tariffs. It is a purely voluntary crisis. This makes it exceptionally hard to deal with for investors, who can have no idea whether the game-show tariff announcements were just a moment of madness, or whether the tariff policy will stick in the long run, come hell or high water.

More importantly, perhaps, "Liberation Day" also marks a point at which America formally gave up on the idea of being the ultimate defender of liberal democracy, free trade and the rule of law. In this equation Trump has forsaken the trust which America's trading partners have placed in it over decades and is instead espousing a set of relationships based on fear and servitude. This is a perilous journey. However, given how much capital has flowed into the US economy from the UK and other large economies from around the world over the last few years, there is now the first glimmer of the prospect that these capital flows may begin to reverse, and if the UK can position itself as a natural home for these reverse flows, there is a prospect for some real benefits to emerge from the crisis.

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Risk Warning

Past performance is not a reliable guide to future performance. The value of your investment is not guaranteed and may go down as well as up and you may not get back the amount invested. This is because the share price is determined by the changing conditions in the markets in which the Fund invests. You should regard your investments as long-term. A dilution levy may be applied to the share price whenever the Fund is expanding or contracting. Should you buy when the Fund is expanding and sell when the Fund is contracting, this will have an adverse impact on the return from your investments.

This review does not provide you with all the facts you need to make an informed decision about investing in the fund. Before investing you should read the Prospectus and the Key Investor Information Document (KIID). The Prospectus sets out the main risks associated with the fund and the KIID shows you how costs and charges might affect your investment. If you are in any doubt as to how to proceed you should consult an authorised financial intermediary.

Fund documentation is available on request and can be downloaded from Waystone here or from our website.

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