

# The case for UK smaller companies

January 2023

# Agenda

- Current opportunities in UK small caps
- Historic returns
- Valuations
- Inflation and small caps
- Why small caps for 2023
- Unicorn Asset Management

# UK Asset Management



## **Fraser Mackersie – Fund Manager**

- Joined Unicorn in 2008
- Manager of UK Income since 2013 and UK Ethical Income since launch in 2016
- Manager of the Unicorn UK Growth Fund since 2011



## **Simon Moon – Fund Manager**

- Joined Unicorn in 2008
- Manager of the Unicorn UK Smaller Companies Fund since 2013
- Manager of UK Income since 2013 and UK Ethical Income since launch in 2016



## **Alex Game – Fund Manager & ESG Officer**

- Joined Unicorn in 2014
- Manager of the Unicorn UK Growth since 2018 and UK Smaller Companies since 2021
- Manager of the Unicorn AIM IHT Service since 2016

# Why invest in UK smaller companies

The small cap effect:

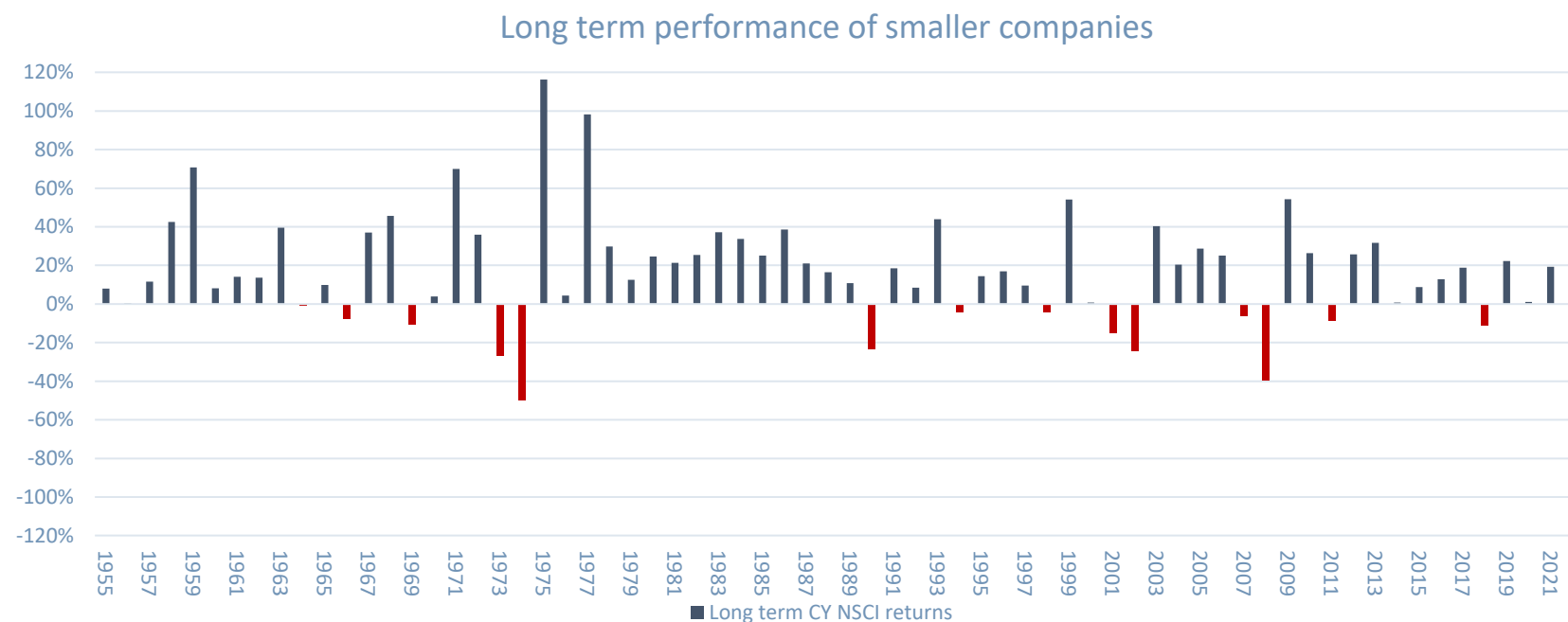
- Small and Nimble; more adaptable to changing economic conditions
- Growth opportunities – small companies are readily able to grow at faster rates
- Under-researched – limited market forecasts provide opportunities – more pricing anomalies

Current opportunity:

- Significantly underperformed large-caps in 2022
- Unloved and out of favour market since 2016
- Long-term outlook for UK smaller companies now highly compelling

**Smaller companies deliver superior returns over the long term**

# UK Smaller companies 1955 – 2022



C.A.G.R.

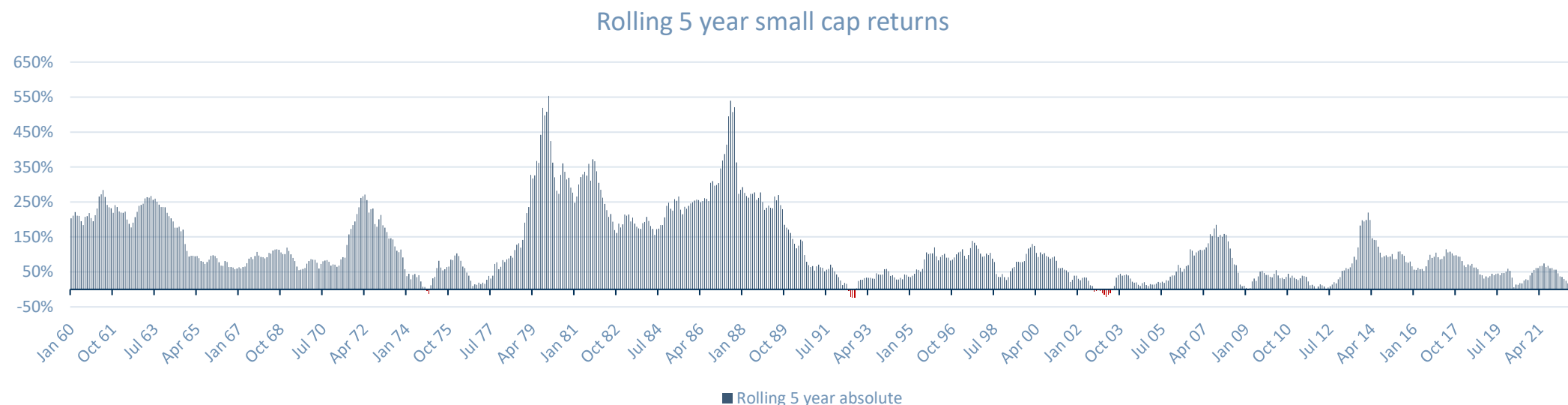
14%

Positive %

77%

Source: Unicorn Asset Management, Numis and ONS, 31<sup>st</sup> October 2022 , CAGR shows compound annual growth rate between 01/01/1955 and 30/10/2022, Positive % shows the number of positive calendar year returns delivered as a percentage of the total number of calendar year returns between 01/01/1955 and 31/10/2022 \* \*\*Past performance is not a guide to future performance, performance is based on returns net of fees. Your capital is at risk, the value of investments and the income from them may go down as well as up. Investors may not get back the amount of their original investment.

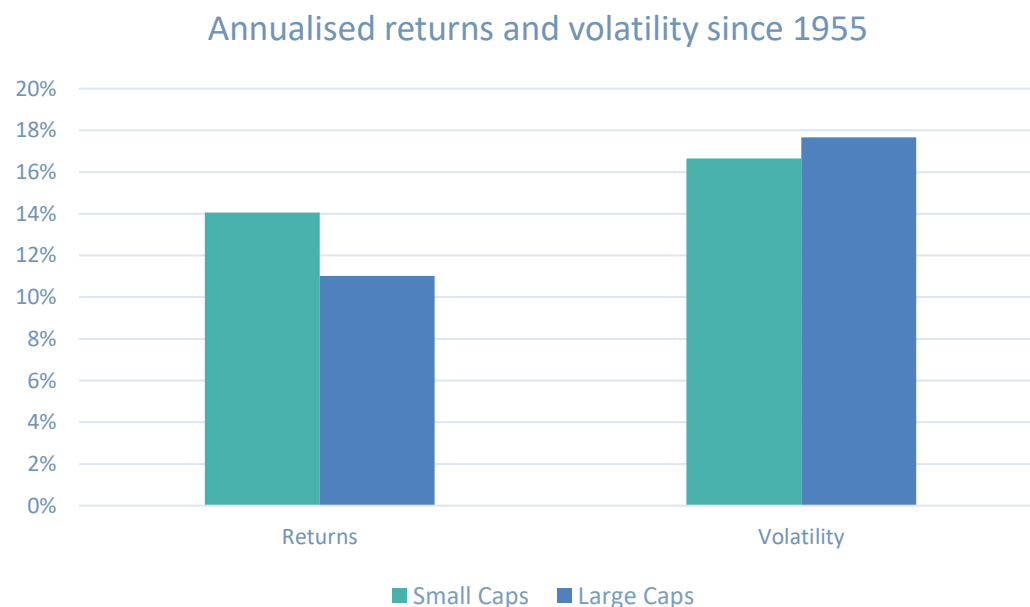
# Small caps deliver strong long term returns



	Rolling 1 year	Rolling 3 years	Rolling 5 years
Number of positive periods	804	675	740
% positive	77%	87%	98%
Average return	17%	60%	118%
Average positive return	26%	72%	121%
Average negative return	-13%	-17%	-11%

Source: Unicorn Asset Management and Numis 31 December 2022; \*Past performance is not a guide to future performance, performance is based on returns net of fees. Your capital is at risk, the value of investments and the income from them may go down as well as up. Investors may not get back the amount of their original investment.

# Small caps consistently outperform large caps over the long term



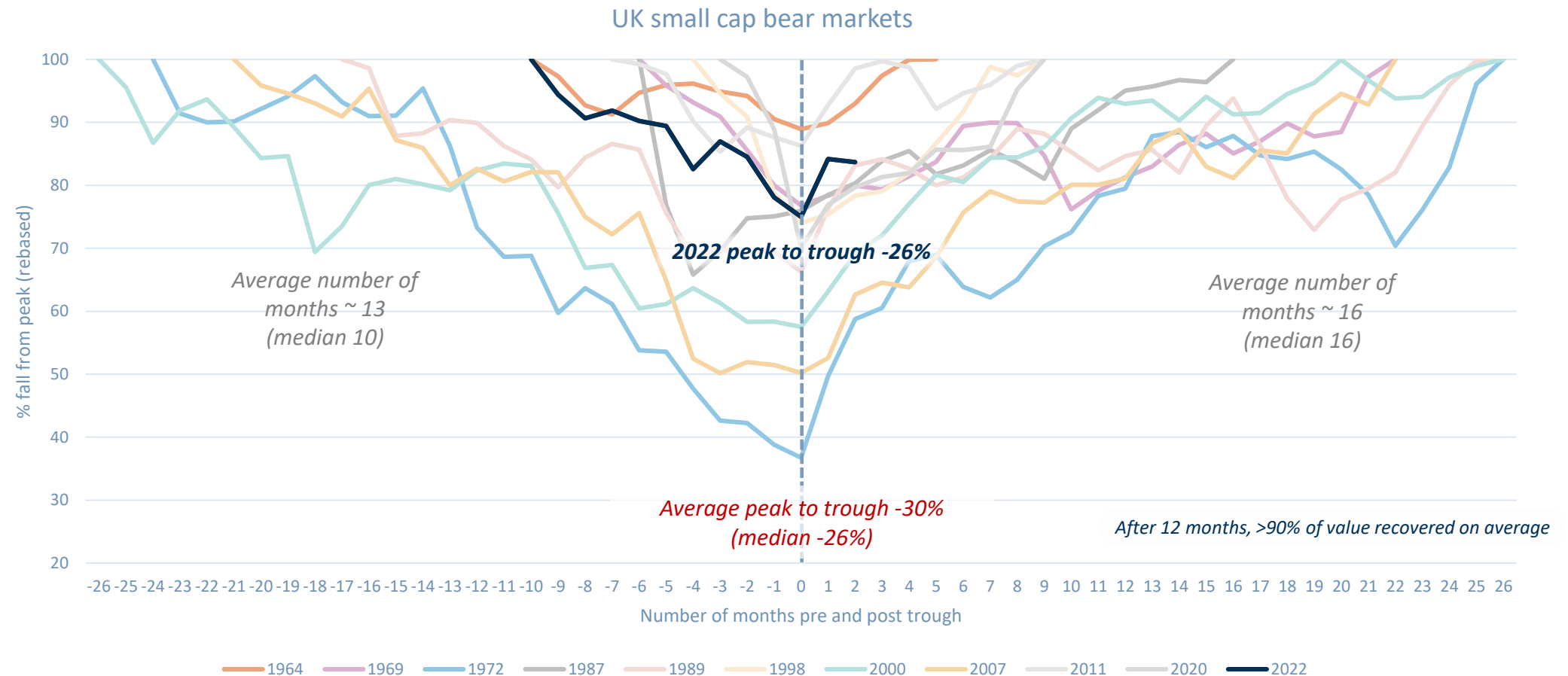
Small caps versus large	1 year	3 years p.a.	5 years p.a.
Periods outperformed	502	549	549
Total periods	804	780	756
<b>Periods outperformed (%)</b>	<b>62%</b>	<b>70%</b>	<b>73%</b>
Average small cap outperformance	12%	8%	6%
Average small cap underperformance	-9%	-6%	-4%

Source: Unicorn Asset Management and Numis 31 December 2022; \*Past performance is not a guide to future performance, performance is based on returns net of fees. Your capital is at risk, the value of investments and the income from them may go down as well as up. Investors may not get back the amount of their original investment.

# Valuations



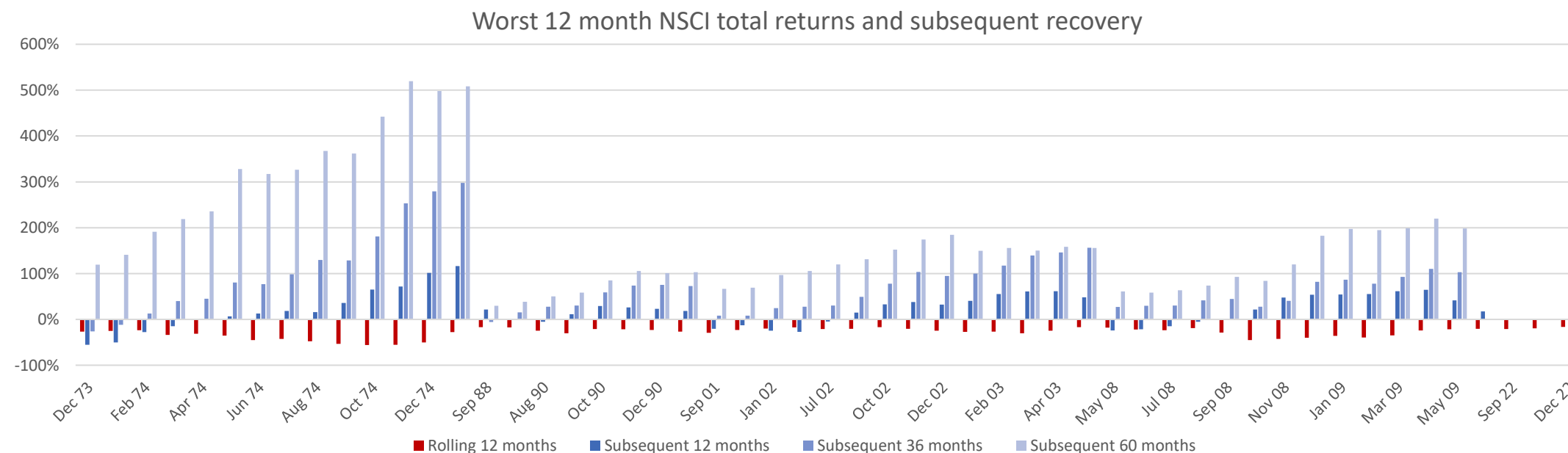
# Bear market analysis



Source: Unicorn Asset Management and Numis 31 December 2022; 2022 peak to trough shown from 4<sup>th</sup> January 2022 peak to 12<sup>th</sup> October 2022 trough. All other data shown on a monthly basis

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# 2022 was in top decile of worst 12 month returns for small caps

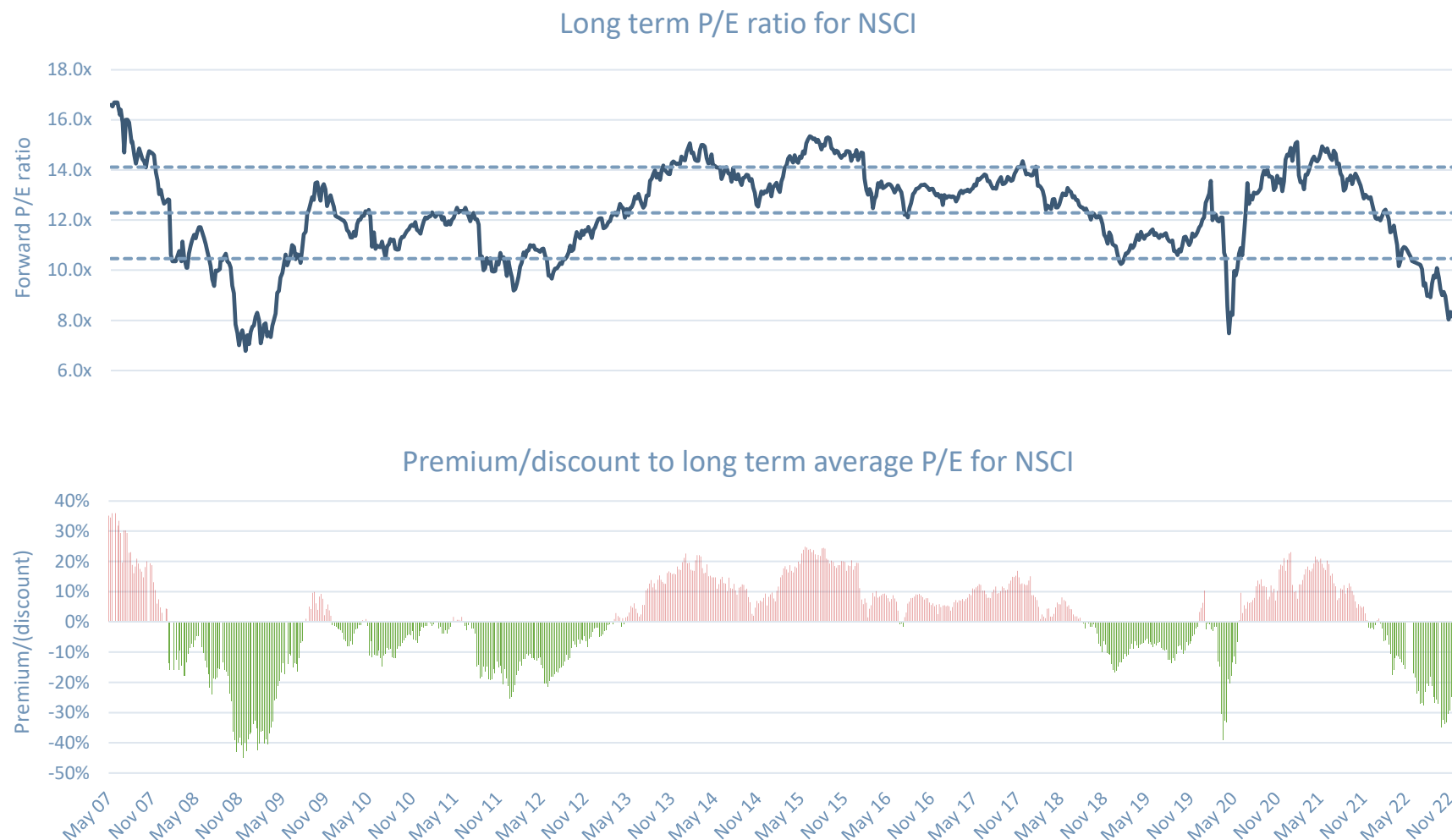


	Average	% positive
Rolling 12 months	-29%	--
Subsequent 12 months	+21%	70%
Subsequent 36 months	+78%	94%
Subsequent 60 months	+179%	100%

Excluding 1970s	Average	% positive
Rolling 12 months	-25%	--
Subsequent 12 months	+22%	69%
Subsequent 36 months	+64%	97%
Subsequent 60 months	+120%	100%

Source: Unicorn Asset Management and Numis 31 December 2022; \*Past performance is not a guide to future performance, performance is based on returns net of fees. Your capital is at risk, the value of investments and the income from them may go down as well as up. Investors may not get back the amount of their original investment.

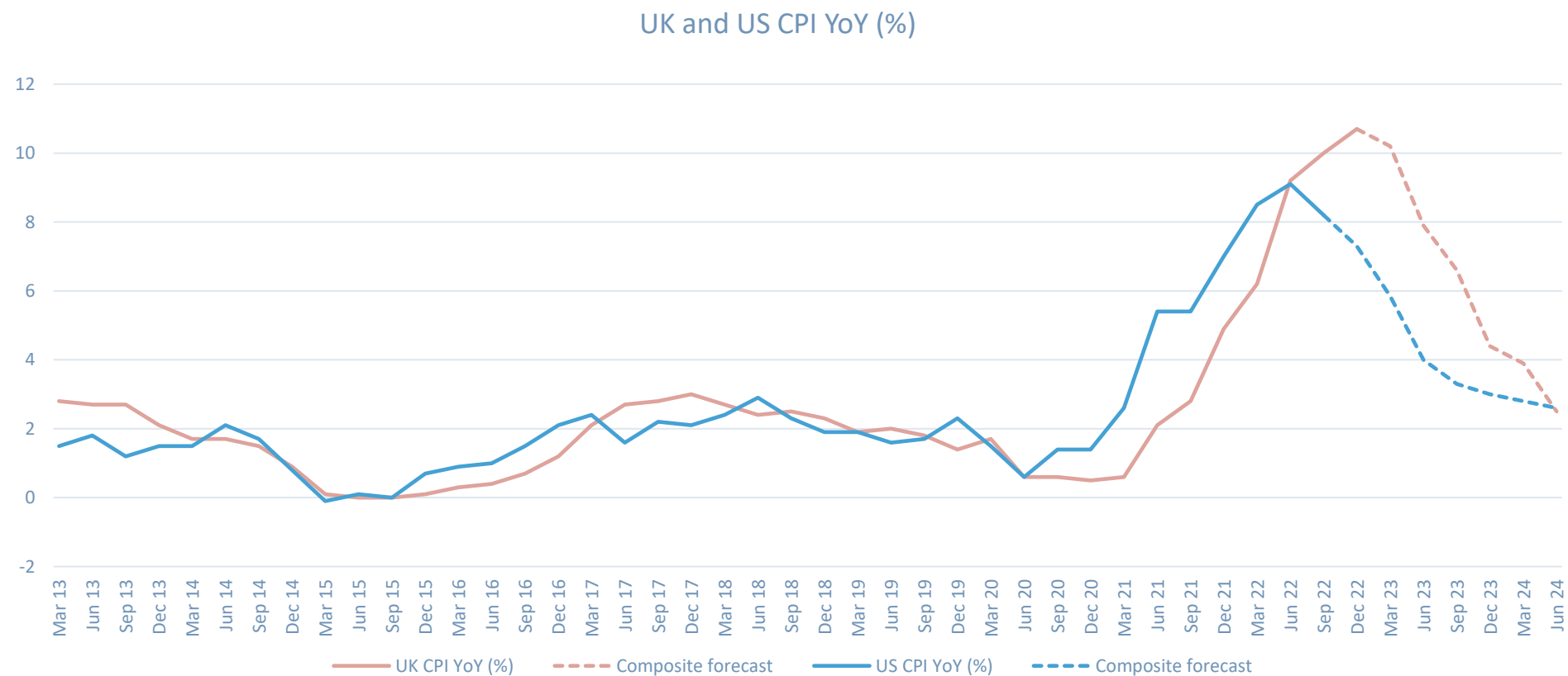
# Current valuations of smaller companies are compelling



Source: Unicorn Asset Management and Peel Hunt 19 December 2022; \*Past performance is not a guide to future performance, performance is based on returns net of fees. Your capital is at risk, the value of investments and the income from them may go down as well as up. Investors may not get back the amount of their original investment.

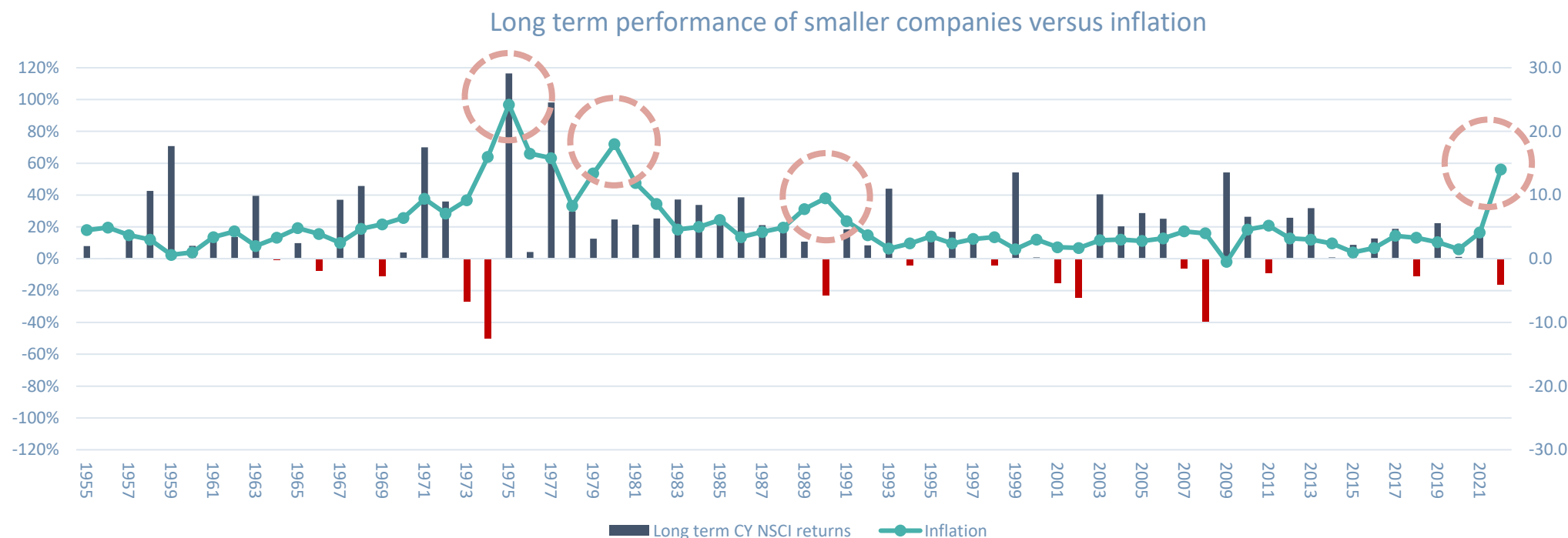
# Inflation and small caps

# Peak inflation



Source: Unicorn Asset Management and Bloomberg, 5<sup>th</sup> January 2023; composite forecasts show Bloomberg consensus

# Smaller companies and inflation



Peaks in inflation	Next 6 months	Next 1 year	Next 2 year	Next 3 year	Crisis
August 1975	36%	27%	106%	219%	OAPEC oil embargo
May 1980	19%	41%	54%	111%	1979 Energy crisis/industrial action
September 1990	21%	29%	13%	74%	Lawson boom

# Summary

- Merits of investing in small companies remain despite a challenging period
- 2022 was one of the worst years for UK small caps on record
- Trough valuations
- Extreme levels of inflation are now abating
- Markets are forward looking; economic data is backwards looking
- Conditions increasingly supportive for period of small-cap outperformance
- We have a strong track record of outperforming the attractive area of the market

# Unicorn Asset Management

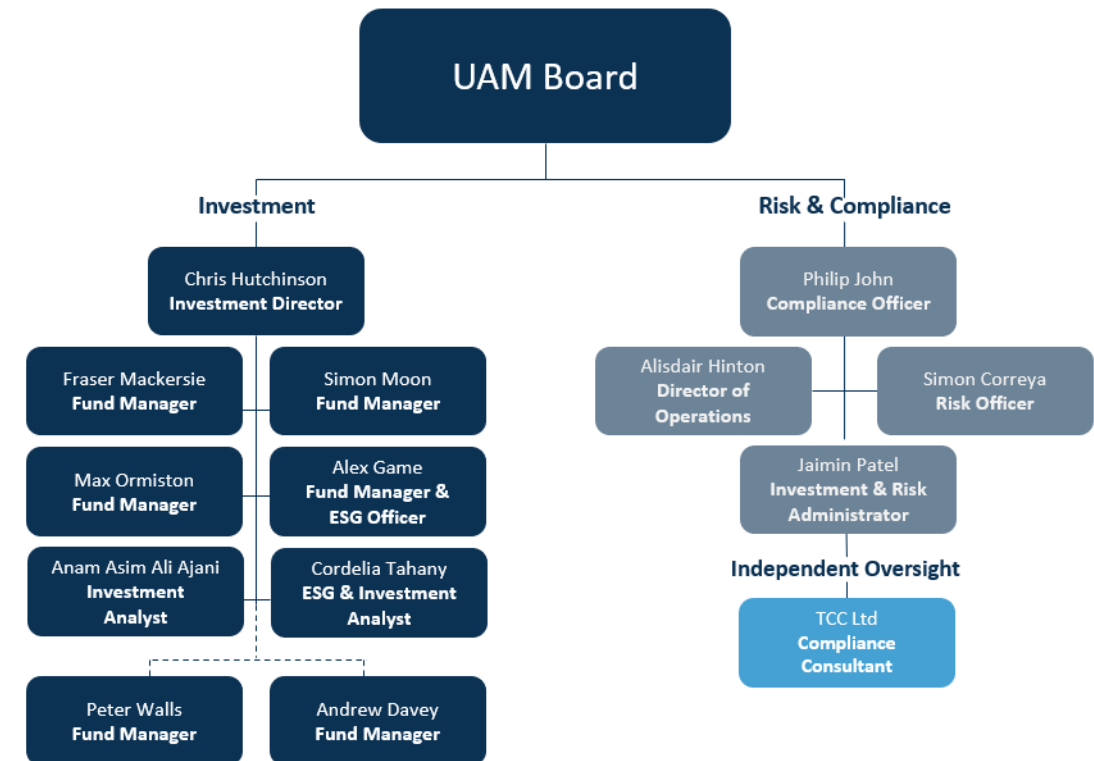


# Unicorn Asset Management

- **Specialist UK Equity investors** with c. £1.0bn AUM
- **Independent** manager founded in 2000
- **Well resourced** and experienced team
- Strategies covering **Income, Growth & Tax efficient AIM**

## Investment Philosophy

- **Structural bias to Small & Mid Caps**
- **Back quality** – best in class businesses with strong governance
- **Build high conviction portfolios** – from the bottom up
- **Responsibility & stewardship** – company engagement is key
- **Challenge & improve** – we can always be better

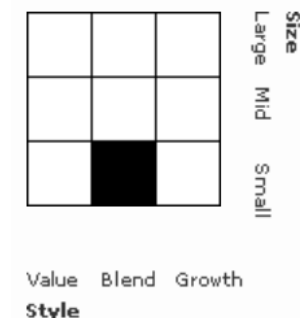


# UK Smaller Companies Fund

- Long term outperformance – top quartile 11/43 vs. sector since Simon Moon took over fund in 2013
- True smaller companies fund, average market cap ~£380m
- Long term approach, high conviction with 35-50 companies
- High quality, well capitalised businesses, with high growth prospects
- Disciplined approach to valuations – relative value investment process particularly relevant in current environment

	1yr	3yr	5yr	10yr	Since Manager Tenure*
<b>UK Smaller Companies</b>	<b>-16.2</b>	<b>-0.9</b>	<b>10.8</b>	<b>168.3</b>	<b>135.7</b>
NSCI (ex IC) + AIM	-21.9	-1.7	1.1	86.8	70.3
IA UK Smaller Companies	-25.2	-2.1	8.4	130.8	109.5
<b>Rank</b>	<b>8/50</b>	<b>19/49</b>	<b>17/47</b>	<b>10/43</b>	<b>11/43</b>
<b>Quartile</b>	<b>1</b>	<b>2</b>	<b>2</b>	<b>1</b>	<b>1</b>

\*\* Morningstar Style Box®  
Equity Style



Source: Unicorn Asset Management FE Analytics and Bloomberg, 30 December 2022; \*manager tenure started 31<sup>st</sup> March 2013. \*\*Morningstar 31/12/2022

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# UK Smaller Companies

Unicorn UK Smaller Fund	%
CY 2022 EPS growth	17%
CY 2023 EPS growth	10%
Return on invested capital	11%
Free cash flow yield	6%
Dividend yield	4%
Balance sheets	39% net cash



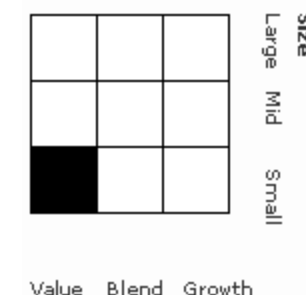
Source: Unicorn UK Smaller stats calculated on a simple average basis. CY2022 and CY2023 P/E and EPS growth figures calculated using consensus figures as at 30 December 2022; return on invested capital and balance sheet data latest reported and free cash flow yield shows blended forward 12 month figure based on consensus estimates; StyleAnalytics Fund vs Index (FTSE All Share ex IT), 3 December 2022  
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# UK Income Fund

- Long term outperformance – ranked 1/34 in IA Sector since launch in 2004
- Aims to provide an income in excess of the FTSE All Share and long term capital growth
- 35-50 Companies, multi cap approach
- 4.9% dividend yield – significant premium to FTSE All Share dividend yield

	1yr	3yr	5yr	10yr	Since Launch*
<b>UK Income</b>	<b>-11.7</b>	<b>-10.5</b>	<b>-0.5</b>	<b>92.3</b>	<b>393.8</b>
FTSE All Share Index (ex IT)	1.6	6.9	14.9	86.2	251.7
IA UK Equity Income	-1.7	3.9	11.6	85.5	227.1
<b>Rank</b>	<b>73/80</b>	<b>74/78</b>	<b>65/76</b>	<b>23/63</b>	<b>1/34</b>
<b>Quartile</b>	<b>4</b>	<b>4</b>	<b>4</b>	<b>2</b>	<b>1</b>

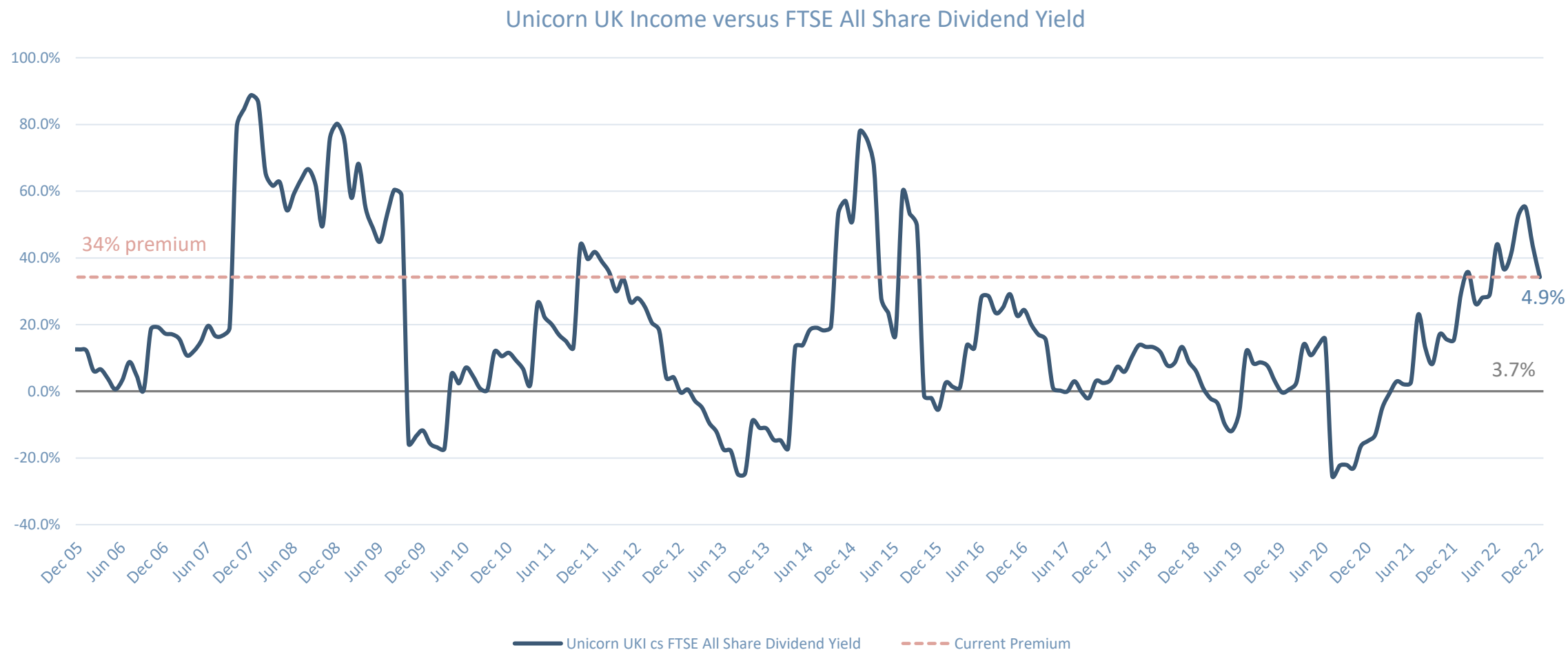
\*\* Morningstar Style Box\*  
Equity Style



Source: Unicorn Asset Management FE Analytics and Bloomberg, 30 December 2022; Since launch data from 24<sup>th</sup> May 2004. \*\*Morningstar 31/12/2022

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# UK Income dividend yield premium

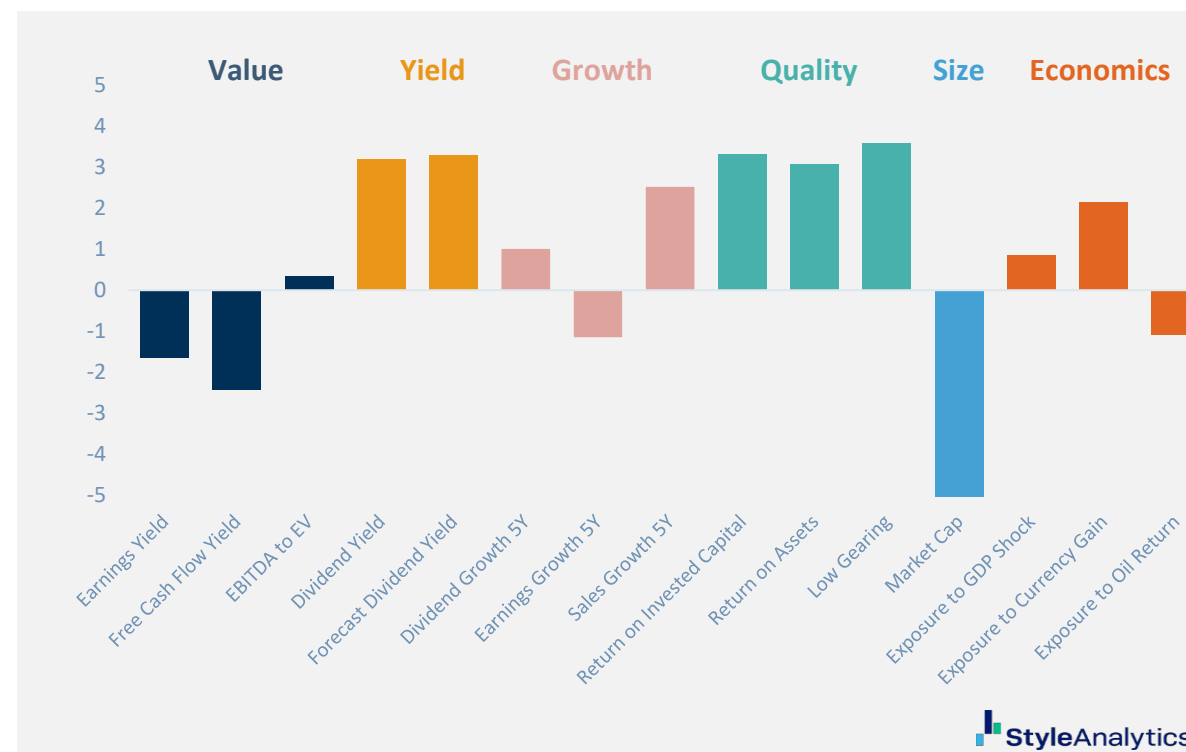


Source: Unicorn Asset Management and Bloomberg 30 December 2022

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# UK Income

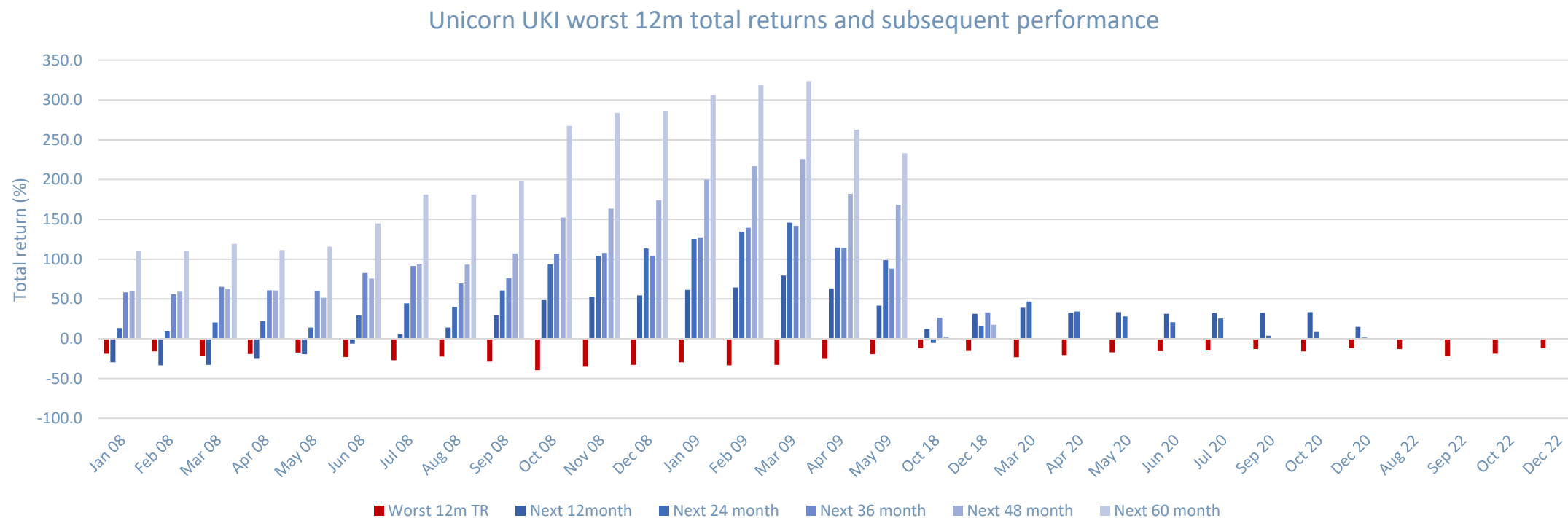
Unicorn UK Income Fund	
CY 2022 P/E ratio	15.3x
CY 2023 P/E ratio	13.4x
CY 2022 EPS growth	16%
CY 2023 EPS growth	7%
Return on invested capital	18%
Free cash flow yield	7%
Balance sheets	44% net cash



Source: Unicorn UK Income stats calculated on a simple average basis. CY2022 and CY2023 P/E and EPS growth figures calculated using consensus figures as at 30 December 2022; return on invested capital and balance sheet data latest reported and free cash flow yield shows blended forward 12 month figure based on consensus estimates; StyleAnalytics Fund vs Index (FTSE All Share ex IT), 30 December 2022

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# Last year in context



Total return	Average	% positive
Rolling 12 months	-22%	--
Subsequent 12 months	+25%	78%
Subsequent 36 months	+85%	100%
Subsequent 60 months	+209%	100%

Source: Unicorn Asset Management FE Analytics and Bloomberg, 30 December 2022

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# Appendix



# UK Growth portfolio metrics and performance

- Long term outperformance – **UK Growth Fund 4/104** in IA Sector since launch in 2001
- **Core holding for investors looking to diversify** their income outside the FTSE 100
- Portfolio biased towards high quality, **small and medium sized companies**
- **Long term approach** which aims to partner with businesses over an extended multi-year period
- **Excellent corporate access** allows us to **get to know companies** and the people who run them

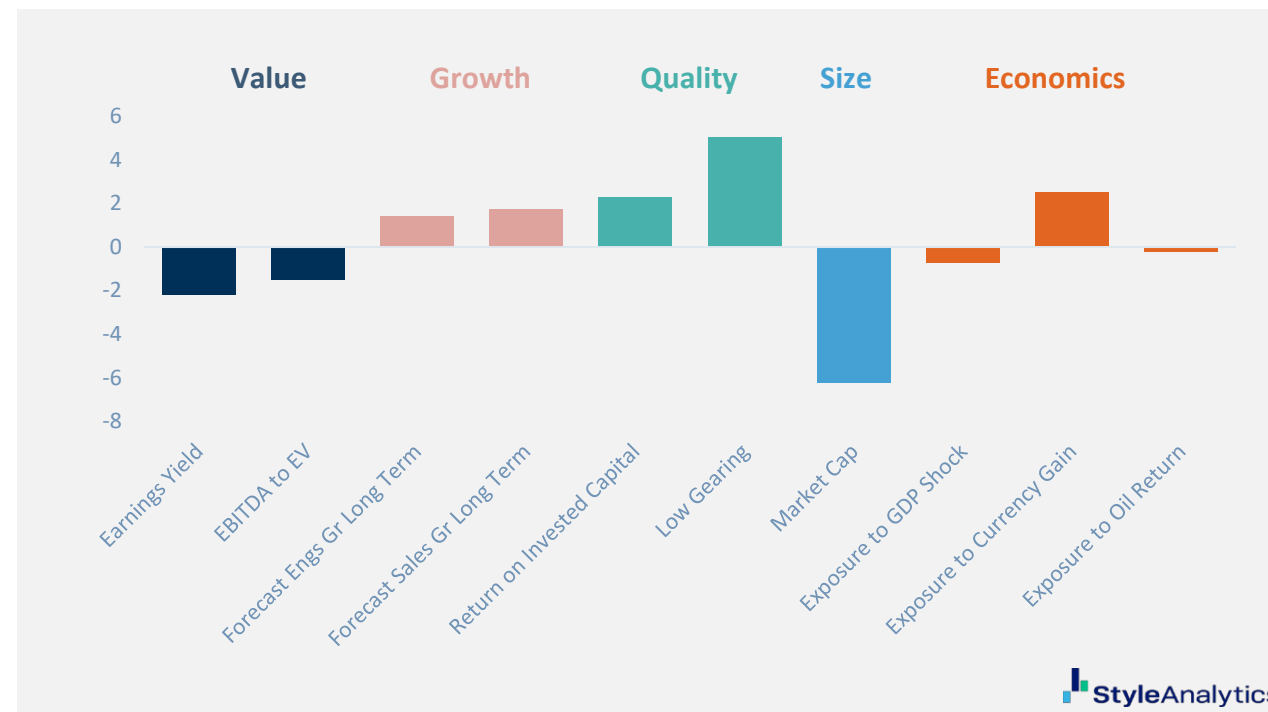
	1yr	3yr	5yr	10yr	Since Launch*
<b>UK Growth</b>	<b>-24.2</b>	<b>-10.3</b>	<b>0.2</b>	<b>132.0</b>	<b>604.0</b>
FTSE All Share Index (ex IT)	1.6	6.9	14.9	86.2	232.6
IA UK All Companies	-9.1	0.2	8.8	83.1	210.7
<b>Rank</b>	<b>228/253</b>	<b>202/243</b>	<b>193/233</b>	<b>19/200</b>	<b>4/104</b>
<b>Quartile</b>	<b>4</b>	<b>4</b>	<b>4</b>	<b>1</b>	<b>1</b>

Source: Unicorn Asset Management FE Analytics and Bloomberg, 30 December 2022; launch date 31 December 2001

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# UK Growth

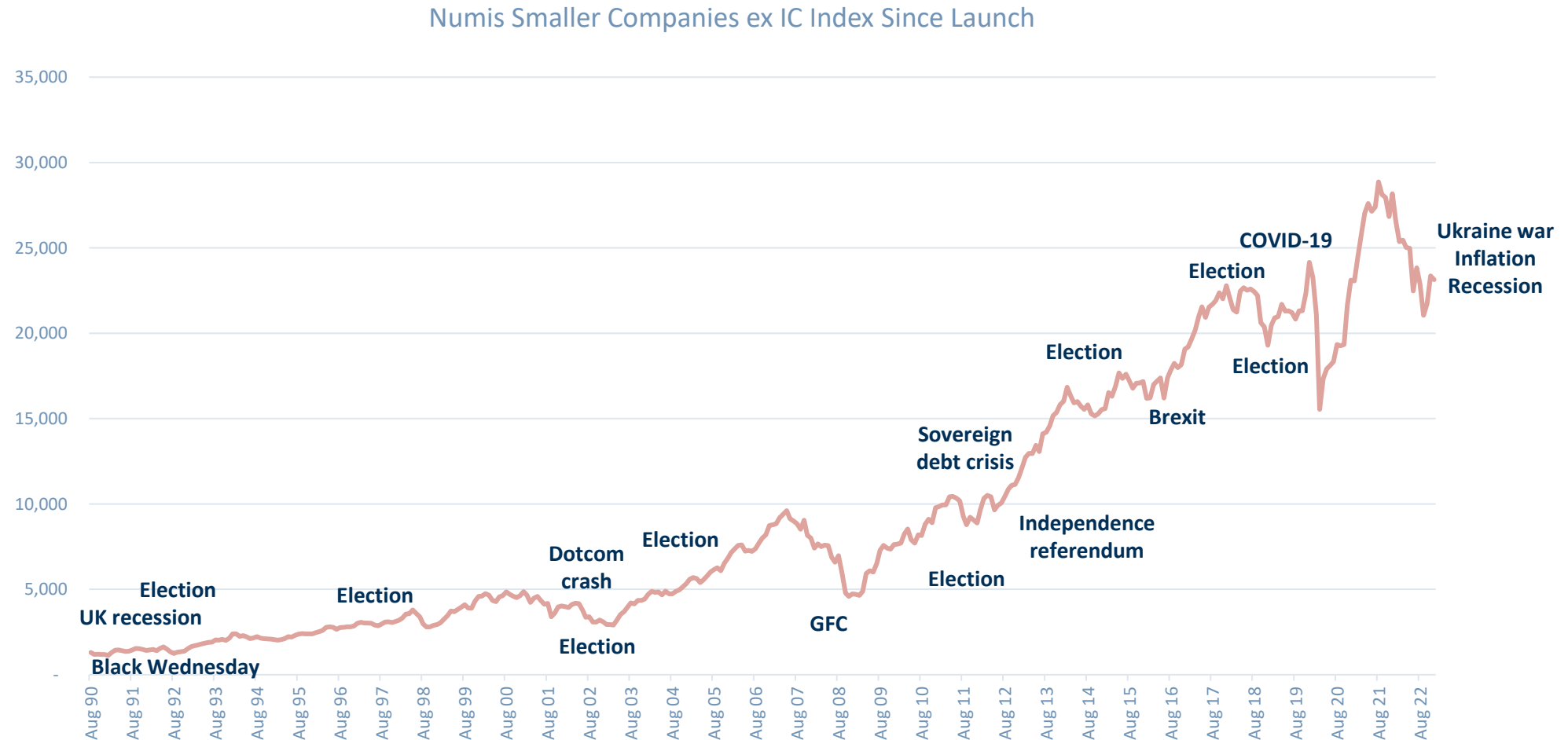
Unicorn UK Growth Fund	%
CY 2022 EPS growth	11%
CY 2023 EPS growth	13%
Return on invested capital	17%
Free cash flow yield	6%
Dividend yield	2.8%
Balance sheets	56% net cash



Source: Unicorn UK Growth stats calculated on a simple average basis. CY2022 and CY2023 P/E and EPS growth figures calculated using consensus figures as at 30 December 2022; return on invested capital and balance sheet data latest reported and free cash flow yield shows blended forward 12 month figure based on consensus estimates; StyleAnalytics Fund vs Index (FTSE All Share ex IT), 30 December 2022

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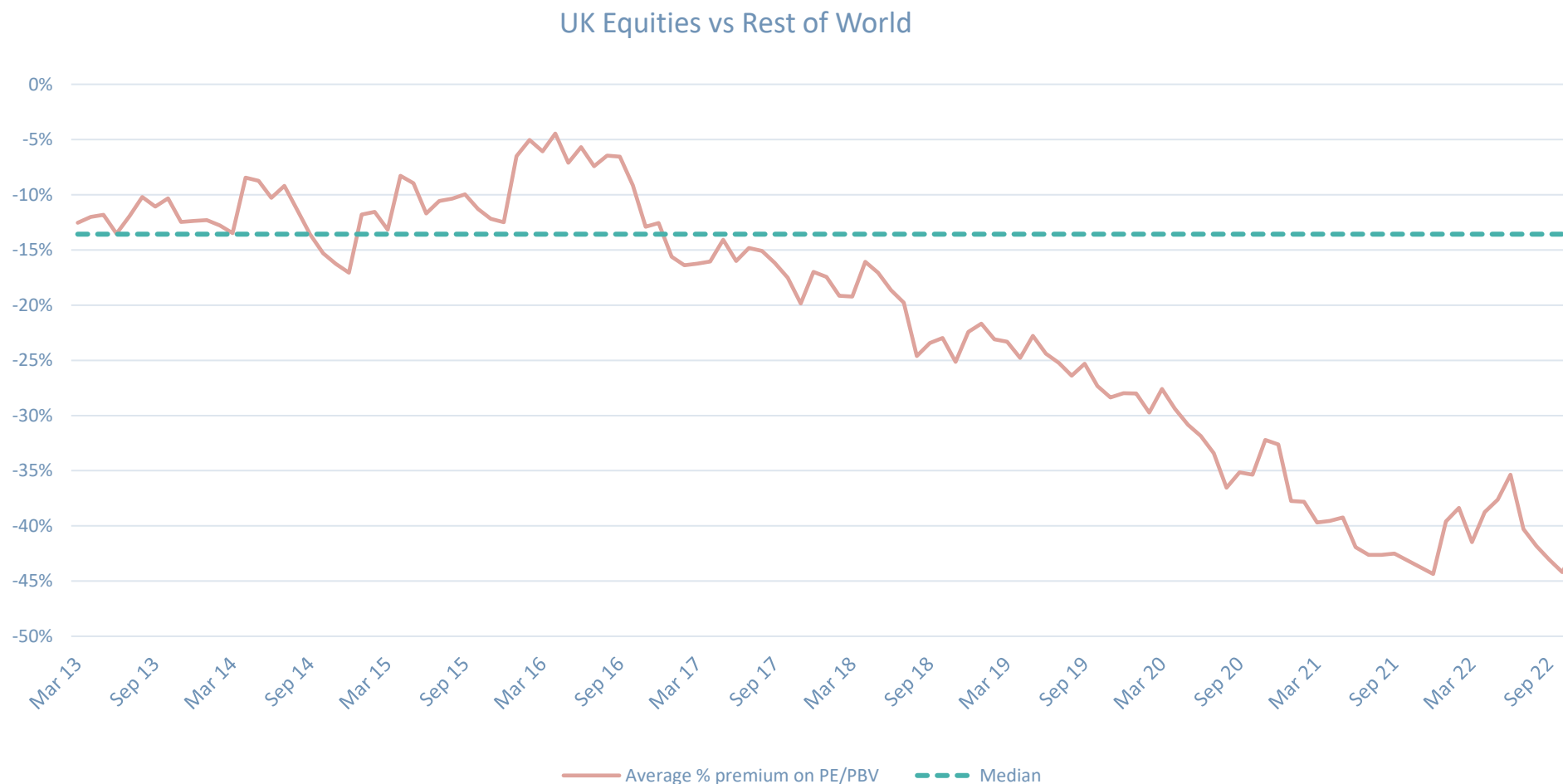
# There is always something to worry about



Source: Unicorn Asset Management and Bloomberg 30 December 2022

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# UK value opportunity



Source: Unicorn Asset Management and Bloomberg as at 30 December 2022. Valuations measured by price to book ratio of FTSE All Share versus MSCI World ex UK Indices

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# Responsible Investing

- Responsible investment framework applied across open ended fund range
- Our integrated approach to ESG, places responsibility for ESG analysis onto Unicorn's investment team and is a fundamental part of researching companies
- ESG assessment and monitoring conducted in house
- Engagement an integral part of the investment process
- Designated internal ESG Officer
- Signatories of United Nations Principles of Responsible Investment (UN PRI)
- Signatories of Net Zero Asset Managers Initiative (NZAMI)

*“It’s not just about the level of profits produced, it’s about the way in which a company generates it. This has always been our approach at Unicorn”*

## Regulatory notice

Investing in smaller companies, including AIM listed companies and unlisted companies, can carry greater risks than those associated with larger capitalized companies.

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