

Fund Manager: Richard Penny

TM CRUX UK Core Fund

“ The Fund performed broadly in-line with its performance comparator over Q1 2023. ”

Over the period under review, the TM CRUX UK Core Fund (B Accumulation GBP) returned -2.0% against its performance comparator the IA UK All Companies Sector return of +2.6%.

During Q1 2023, the UK market continued to move away from the October lows, following Trussonomics and the accompanying LDI crisis, amid signs that the UK economy was holding up better than expected and growing hopes that the US Federal Reserve might be in a position to 'pivot' to cutting interest rates in the second half of 2023. The market recovery ended abruptly in early March amid fears of a global banking crisis, fuelled by the collapse of Silicon Valley Bank in the US. Since mid-March markets have displayed green shoots, with investors increasingly comfortable that a global banking crisis is likely to be avoided.

The Fund performed broadly in-line with its performance comparator over Q1 2023 until fears of a global banking crisis materialised at the beginning of March, after which the mid and small-caps within the portfolio underperformed. At a stock level, the main contributors were the larger positions in cyclical, including JD Sports Fashion, Whitbread and St James's Place.

The portfolio's best performer over the period was JD Sports Fashion, which rose c.41% to 178p as at 31 March 2023. Shares bottomed at 89p in mid-October, having fallen from a peak of over 230p in November 2021, as investors priced in aggressive earnings downgrades which failed to materialise amid ongoing resilience of consumers. Similarly, Whitbread was another strong performer returning 16% and contributing c.0.8% to Fund performance. Whitbread has a strong balance sheet and asset backing and continues to see some recovery from depressed levels of Covid trading. FD Technologies was a strong performing small-cap amid signs of encouraging progress in regards to the KX Insights partnership with Microsoft. Shares were up 26% during the quarter and contributing c.0.8% to Fund performance.

Important Information

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“ The fund performing in-line with a strongly recovering market was encouraging, given the fund’s focus on capital preservation, as well as the outperformance of the fund over the course of 2022 during which the defensive qualities of the fund

The key detractor from performance over the period was WANdisco, a Sheffield based technology company, which reported ‘significant, sophisticated and potentially fraudulent irregularities with regard to received purchase orders and related revenue and bookings, as represented by one senior sales employee’. The shares had been purchased for the Fund at a low price and had performed strongly until the unprecedented and sophisticated fraud was uncovered. Although it is incredibly disappointing that the entirety of the profits made by the Fund will not be realised, start to finish the fund will have made a small profit (due to trimming the position on the way up) even in the unlikely event of no value remaining in the shares on resumption of trading.

Despite the extremely disappointing WANdisco experience, fraud (especially at this scale) remains very rare in the stock market. We remain firm believers in the small-cap premium and the potential for small companies’ share prices to go up many multiples on the way out of a recessionary environment, as was demonstrated by the Fund’s outperformance on the way out of the pandemic, and by Richard Penny’s previous Funds during the 1998, 2003 and 2008 recoveries. Although there has been significant selling of small and mid-cap UK companies by institutions under liquidity pressures, other participants have been buyers. Companies are repurchasing their own shares at substantial levels, which is testimony to the strength of corporate balance sheets. Elsewhere, the level of director purchasing and takeover approaches for UK companies speaks to the long-term value that the “stock market” cannot see.

Looking ahead, the fund should benefit from a weak sterling given its overweight in overseas companies, as well as rising interest rates, given its overweight in financials. Once there are greater signs of economic recovery, we will look to pivot some of the large cap exposure into more domestic mid cap exposure. Although there has been significant selling of small/mid-cap UK companies by institutions under liquidity pressures, other participants have been buyers. Companies are repurchasing their own shares at substantial levels, which is testimony to the strength of corporate balance sheets.

In terms of transactions, we replaced British American Tobacco with Imperial Brands during the period, as the latter has a more attractive valuation, similar yield, less debt and a more sensible capital allocation policy. We initiated a position in Legal & General following record results, confirmation of a solid balance sheet, and an attractive valuation and dividend yield. Made Tech floated at 140p in October 2021 and fell c.85% to c.22p in December 2022 despite just one earnings downgrade during the period. We took the opportunity to purchase the shares following a positive update and new contract wins announced, having met with management several weeks earlier and being impressed with the significant potential that remains in the business.

Important Information

Please note: Due to rounding the figures in the holdings breakdown may not add up to 100%. Unless otherwise indicated all figures are sourced from Financial Express, Datastream, State Street and CRUX Asset Management Ltd. Third party data is believed to be reliable, but its completeness and accuracy is not guaranteed.

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Headlines for the UK economy remain negative and have been for some time. Paradoxically although the temptation is to sell any asset listed on the UK stock market, there are three specific reasons why this is not the case. Firstly, the majority of revenues on the UK stock market are generated overseas, thus the UK economy is not the UK stock market. Secondly, many of the UK earners in impacted sectors have already declined significantly. Whilst 2023 will see deteriorations in underlying profit, we believe many of these businesses are now valued too low for their long-term earning power.

Thirdly, notwithstanding general economic headwinds, a focussed fund should be able to find the companies that are overly discounted or can outperform in difficult market conditions. In 2020, distressed market conditions brought about the low prices that facilitated the Fund's subsequent significant outperformance from larger cyclical businesses and disruptive small and mid-cap companies. We believe current depressed conditions offer a strong opportunity to buy well-run sensibly financed businesses for the long term.

Source of performance data: FE, 31.12.22-31.03.23, B Accumulation GBP share class, Bid-Bid basis, net income re-invested GBP

Attribution Stock Level Q1 2023

Top 5 Contributors (%)	Bottom 5 Contributors (%)
JD Sports Fashion 1.6%	British American Tobacco -0.4%
FD Technologies 0.8%	HeiQ -0.4%
Whitbread 0.8%	IQE -0.5%
Inspecs 0.5%	Glencore -0.8%
Grafton 0.5%	WANdisco -2.6%

Source: Stat Pro as at 31.03.23