WHITMAN
ASSET MANAGEMENT

Q2 Newsletter
10 JULY 20

As we enter the second half of 2020 the values of both our small cap strategies are down on the year but perhaps down less than many may have feared back in March. The UK Small Cap Growth strategy has fallen by 3.9%[1] over the first six months of the year, versus the benchmark which is down 16.6%[2] (The NSC plus AIM TR Index). By comparison, the AIM IHT strategy has fallen by 11.7%[1] over the first six months of the year, versus the benchmark which is down 8.3%[2] (NUMIS Alternative Markets TR Index).

Economic consensus is as varied as ever on the overall effects that COVID-19 is having and will have on economic activity. The International Monetary Fund has predicted that the Global Economy will shrink by 4.9%[3] in 2020 but rebound to grow at 5.4%[3] in 2021. While we believe inflation is likely to remain subdued for this year, given the amount of Central Bank liquidity injected into all major economies, combined with increased momentum for deglobalisation and trade protection, we think it seems likely there will be upward pressure on prices to follow.

Stock markets have certainly been firmly focused on the growth projections for next year with substantial rebounds since the lows at the end of March. In the UK, the FTSE Mid Cap 250 Index has increased by 33%[4] between its 19th March 2020 low and 30th June 2020. The FTSE AIM All Share Index is up by 50%[4] between its 18th March 2020 low and 30th June 2020. The latter has been significantly influenced by the dominance of a few stocks, including pure online retailers BooHoo and Asos.

The seismic changes being experienced by retailers provides a good example of the ways that investments can either benefit or suffer from the COVID-19 epidemic. There are other trends which may provide money making opportunities and current themes that we consider attractive include:

- Working from home
- Home entertainment
- The acceleration in digital technology into all aspects of life

Active small cap investors may be well placed to benefit from the changes taking place as a result of COVID-19. At a company level investors could latch onto compelling opportunities, unencumbered by legacy business models, redundant skill sets, onerous pension commitments and unnecessary property costs. A more subtle change that we think may benefit smaller companies is the more assertive role that Governments are destined to play in pressurising larger businesses to fulfil agendas which the Government sees as desirable. From our observations, these may be likely to include targeted regional investment, employment legislation, environmental legislation, and possibly even the direction of dividend policy, as has happened already with the major banks. We believe all of these are likely to become increasingly relevant and the Johnson led Government will be pushing at a largely open door to enact such corporate interference.

Our small cap portfolios have been largely fully invested over recent weeks in line with our optimism for companies which we think can trade well in the current environment. Turnover has been higher than usual and with over 40 AIM listed companies issuing new shares[5] to bolster their balance sheets over the last quarter, we have taken advantage of a few opportunities. We recently participated in a placing of shares in Marlowe plc across both strategies. Marlowe provides companies with critical asset maintenance services, including fire protection, water treatment and air hygiene. Their services are driven by stringent environmental and safety regulations providing an attractive and predictable revenue stream. The company has been consolidating the highly fragmented market and we believe they are on path to grow both organically and through acquisitions, with margins also set to increase.

Another company we recently added to both portfolios is Gamma Communications. Gamma provides companies with cloud based unified communication systems, enabling users to access business communications on any device, in any location. We consider these cloud-based solutions facilitating working from home even more important post COVID-19. The company benefits from 93% recurring revenues and has a presence in the UK, Spain, The Netherlands and recently Germany.

To summarise, despite the strong recent rebound in the sector we continue to believe the small cap sector and our chosen investments in particular are favourably placed to trade well through to a post COVID-19 world, both in absolute terms and relative to larger companies.

Source:

1. Whitman Asset Management Model Portfolios
2. Numis Indices
3. International Money Fund (https://www.imf.org/en/Publications/WEO/Issues/2020/06/24/WEOUpdateJune2020)
4. www.londonstockexchange.com/exchange/prices-and-markets/stocks/indices
5. Note: The FTSE index has been included for illustrative purposes and there is no direct correlation to the Whitman Asset Management model portfolio
6. Peel Hunt 26 June 2020

Important Information

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Risk Warnings

GENERAL AIM RISK WARNING

An AIM Portfolio should be regarded as a higher risk, long-term investment, suitable only for investors with financial security that is independent to any investment being made under these Terms. We strongly recommend that you seek professional advice before you ask us to manage your AIM Portfolio for you. The investments that will be held in the AIM Portfolio are likely to be smaller UK companies which should qualify for the maximum business relief after two years. Such investments will inevitably involve higher risk and may be difficult or even impossible to realise in a reasonable timescale or at an acceptable price. Investors and potential investors should be mindful of the need to appropriately diversify their assets and higher risk investments should not form a significant part of any portfolio.

PAST PERFORMANCE WARNING

Past Performance is no guide to future performance and there is no guarantee that your AIM Portfolio's objective will be achieved. We can make no guarantee of investment performance or the level of capital gains or income that will be generated by your AIM Portfolio. The value of Qualifying Investments and the income derived from them may go down as well as up and you may not get back the full amount invested.

LIQUIDITY RISK WARNING

Please note that Qualifying Investments can carry a higher degree of risk than investing in more liquid shares of larger companies. The share prices of AIM investments are generally more volatile than shares listed on the London Stock Exchange main market. There may be a wide spread between buying and selling prices for AIM- listed shares. If you have to sell these shares immediately you may not get back the full amount invested, due to the wide spread. The value of your investments may decline and there is a risk that this may outweigh any IHT saving. You should be aware that the Qualifying Investments in your AIM Portfolio may be classified under FCA Rules as 'not readily realisable' (these are investments in which the market is limited or could become so: they can be difficult to deal in or obtain reliable information about their value).

TAX LEGISLATION WARNING

Rates of tax, tax benefits and allowances are based on current legislation and HMRC practice. These may change from time to time and are not guaranteed. This investment may not be suitable for all investors. You are recommended to seek specialist independent tax and financial advice before deciding to subscribe to this AIM Service. This AIM Service has been designed with UK-resident taxpayers in mind. If you are not resident or ordinarily resident in the UK for tax purposes, it may not be appropriate or advantageous for you to subscribe to this AIM Service.

QUALIFYING INVESTMENTS WARNING

Qualifying Investment in which we invest may cease to qualify for inheritance tax exemption. In this case, the relief available on that particular investment will be lost. In some instances, investments in particular companies will be sold if we believe that the investment rationale outweighs the tax. If the investments lose their qualifying status then investors may not receive any tax benefits at all from making such investments. Qualifying investment status is subject to change without notice and tax benefits are not guaranteed.