DW | Dowgate Wealth
A tailored approach

SVS Dowgate Wealth UK Small Cap Growth Fund Quarterly Commentary: 30 June 2023

15 Fetter Lane, London, EC4A 1BW
Phone: +44 (0)20 3416 9143
Email: funds@dowgate.co.uk

PERFORMANCE

The portfolio was down 2.5% over the quarter, which was in line with our benchmark. The most significant detractor in our portfolio was **Franchise Brands,** which raised money in a difficult market at a reasonable discount to the price to do a significant acquisition. **Franchise Brands** is an international multi-brand franchisor, focused on building market leading businesses; their focus is currently on B2B reactive and planned services. The Co-Founder and Exec Chair is Stephen Hemsley, who took Domino's from private ownership to a market capitalisation of £1.5bn. He retired from Domino's in 2019 after 21 years with the business to focus exclusively on **Franchise Brands.**

Ashtead Technologies was the best performer in the quarter; **Ashtead** is a subsea equipment rental, advanced technologies and solutions provider for the global offshore energy sector. The business is seeing some significant demand for it's products and services in the context of the large investment happening in offshore windfarms, and this remains a really nice way of playing the sector.

INVESTMENT OUTLOOK

So far in 2023, markets have been mixed, but with more vital signs than last year. Although consumers and policymakers remain understandably worried about inflation, markets are more concerned with the implications of elevated interest rates on financial stability and corporate solvency. The widely anticipated recession is proving elusive as most output and employment measures are far more resilient than expected. However, rapid rate rises also increase the risk of excessive policy tightening, and the fear of recession lurks.

After the dramas of Silicon Valley Bank and First Republic, immediate concerns over global financial stability have subsided, reflected in the 10% fall in the dollar price of gold. But, worries over the viability of highly indebted Thames Water remind us that the uncertain trajectory of interest rates requires vigilance regarding indebtedness. We are reminded that the consequences of monetary tightening are long and variable.

The market's base case outlook is for an economic slowdown. Negative forward indicators include downward-sloping yield curves, declining energy and industrial material prices, falling producer prices and a faltering Chinese recovery. As a result, most large investors remain cautiously positioned with lower-than-normal risk asset exposure and higher-than-normal cash holdings, meaning illiquid risk assets such as UK mid and small-caps remain attractively valued.

Although policy rates continued to rise in 2023, financial conditions eased somewhat as the Federal Reserve provided monetary assistance to its regional banks, and the US Treasury wound down its General Account in the run-up to June's debt ceiling negotiations. A softening stance from Beijing has also boosted liquidity in recent weeks. The POBC has lowered some rates and eased reserve requirements to avert issues in its residential property sector and attempts to re-ignite the stalling Chinese recovery.

This extra liquidity has helped fuel the search for enhanced returns from generative AI, which burst into mainstream consciousness following the rapid adoption of Chat GPT—a trend captured by Nvidia, becoming the world's first trillion-dollar semiconductor company. As a result, NASDAQ, the S&P 500, and Japan's previously unloved stock market were all up comfortably by double-digit percentages in the period. However, currency movements mitigated returns for UK investors as the US$ (-7%) and the Yen (-15%) weakened against stronger Sterling.

It was disappointing, but unsurprising, that investors didn't view UK equities as a safe haven in this period. Although various bodies including the OECD, IMF and OBR, have upgraded assessments of the UK's economy, the UK market has remained sluggish. The FTSE 100 was down 2% in Q2, the FTSE 250 was down by 3%, the AIM 100 was down 9%, and the AIM All share by 14%. While disappointing, returns were broadly flat in dollar terms. Specific concerns about the UK's ability to contain inflation and suffer higher rates and ongoing worries about London as a viable listing venue continue to mitigate against global investors allocating to UK equities.

One feature has been the diminished impact of PE-backed bids in Q2, as the first quarter flurry of PE bids faded. EQT's substantial offer for Dechra was revised down but looks like completing, while offers for Wood Group and THG failed to materialise. Offers for Medica should complete. However, higher interest rates negatively impact PE returns, and the recent spike in UK rates may have tempered PE appetite. Meanwhile, the unexpected £450m offer for Lookers from Canada's Alpha Auto and AB Foods' offer for National Milk Records indicate that UK assets remain attractive but unpredictable targets for corporate buyers.

As the debate rages regarding London's suitability to attract

capital, two high-profile IPOs were announced. Turkey-based commodity chemicals supplier WE Soda soon withdrew, citing disappointing valuation feedback without mentioning the well-documented governance concerns. However, the smaller, but more exciting, CAB Payments progressed to an agreed valuation, which should reflect well on peer Alpha International Group, which we own.

The equity recovery has been narrowly focused on AI, US large tech and Japan. However, as the quarter progressed, evidence increased that this recovery is starting to include a broader range of stocks. With Japan rerating, the UK looks increasingly isolated as the final value play among developed equity markets. Many less liquid, smaller UK companies now look incredibly cheap; this area remains our preferred investment hunting ground, and we look forward to today's value becoming tomorrow's accepted recovery and momentum plays. We are conscious that the timing of such a sentiment transition is unknowable, the end of rate increases and therefore falling CPI should be positive catalysts.

Mark Chadwick
Lead Fund Manager
Mark.Chadwick@dowgate.co.uk
+44 (0) 20 3416 9145

DISCLAIMERS

This document has been prepared by Dowgate Wealth Limited ("DGW"). Dowgate Wealth Ltd, registered in England number 12221221, is authorised and regulated by the Financial Conduct Authority and is a member of the London Stock Exchange. Registered address: 15 Fetter Lane, London, EC4A 1BW. All data has been sourced by DGW.

Investors should carefully consider the investment objectives and risks as well as charges and expenses of the fund before investing. The prospectus contains this and other information about the fund. If you're unsure of the suitability of an investment please seek advice. Tax rules can change and the value of any benefits depends on your personal circumstances. The value of investments, and any income from them, can fall as well as rise so you could get back less than you invest. Past performance is not a reliable indicator of current or future performance.

We believe the information provided here is reliable but should not be assumed to be accurate or complete.

All information accurate as at 30 June 2023

The Key Investor Information Documents (KIID's) and the Prospectuses for all funds are available, in English, free of charge and can be obtained directly using the contact details in this document. They can also be downloaded from:

https://dowgatewealth.co.uk/fund-management

An investor must always read these before investing.