

TRANSCRIPT: EPISODE 140

6 July 2021 (pre-recorded 28 June 2021)

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[INTRODUCTION]

**Chris Salih (CS):** Hello and welcome to the Investing on the go podcast. I'm Chris Salih and today we're joined by Simon Moon, manager of the Elite Rated Unicorn UK Smaller Companies fund. Thank you for joining us today, Simon.

**Simon Moon (SM):** You're welcome, thanks for having me.

[INTERVIEW]

[0:18]

**CS:** Let's start obviously, UK small caps clearly, they've had a great start to the year best performing asset class, second to energy funds. Could you maybe just give us a snapshot of why they've done so well and whether you think this will continue?

**SM:** Yeah, absolutely. Small companies tend to perform best in this part of the economic cycle, they're hit harder, generally, in times of extreme economic volatility, as we saw about a year and about 15, 16 months ago. But they tend to recover at a much sharper rate as well. So that would be seen by looking out a year or two ahead and small cap economic growth is probably the 20% for 2022 compare to 5% on the FTSE 100. That's obviously a pretty appreciable difference.

The UK economy is favorable versus many other developed nations – if you look at the success of the vaccine roll out, the makeup of the economy and the surface that nature, many parts of it. This would be further boosted by the Brexit resolution we saw six, seven months ago. You know, that removed significant uncertainty, that we had overhanging the UK economy for years. I think you sort of combine this with, with sterling strengthening and it's still a long, a long way below, below its long-term average, but it's, you know, getting stronger as well. And I just think you combine that with a really attractive valuation makeup of the UK small cap market as well, that you, you end up with a pretty compelling case, so you can keep moving forward. You know, small companies tend to be the drivers of economic growth and tend to be the biggest beneficiaries. But in my opinion, you know, absolutely on a tangent of recovery at the moment.

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**CS:** Merger and acquisitions obviously been picking up lately, is that a good or bad thing for smaller company investment? You know, obviously there's a chance to make big sort of gains, but obviously there's probably potential dangers as well?

**SM:** Well. Yeah. You know Chris, that's a really good question. It's a double-edged sword. You know, it's always a moment of excitement to see one of your companies you hold receive a bit of approach and you may see another sort of coming from the wings as well. But you know, you're potentially you know going to miss out on future years growth from what would be a very good company, but it's no surprise as to see well-run market leaders the focus of trade buyers and PE buyers as well. Yeah, it does affect the improving out the attract evaluations I just mentioned, you know, combined with that low level of sterling and comparable long term average. It occasionally is disappointing to lose, you know, a high quality UK plc, but there's still plenty of other opportunities out there. And when you run a conviction fund like this is you can reallocate that capital to any one of the number of very good companies that are on sort of your subs bench.

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**CS:** Obviously with a portfolio like this, we want to talk about the stocks. I mean, they're the underlying drivers. So let's go into a bit detail in some of your top 10. Let's start with Alpha FX, which is a payment and collection company. Are they starting to think about cryptocurrencies, obviously that's a big buzzword at the moment, maybe just talk us through that please.

**SM:** Yeah, of course. So Alpha FX, they're a payment and collection company, they're also primary element of their business is hedging transactions for small and medium sized businesses. So basically, they react to whatever their companies are transacting in. So they're not really talking about crypto yet, but that the company Alpha FX itself is very client centric. You know and if that's what the clients start using, then they'll start using crypto as part of their hedging mechanism as well. And they will build it into their infrastructure but there's still plenty to go for in traditional currencies, long established currencies, in my opinion. The company can focus by growing the service offering, which they're doing, grown geographically and expanding with existing clients all of which they've got a very good track record of doing.

And just probably as an aside to the strength of this company and what it's achieved in the last few years you know, it IPO'd only about four or five years ago, only about four years ago I think, at less than £2 and it's now over £16 today, it really has done incredibly well on earnings growth, and when you look at the earnings growth, it's very attractively valued on a price earnings growth (PEG) ratio. So I think loads more it can do, when cryptocurrencies become an important element of their client's needs, I'm sure they will build into their infrastructure.

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**CS:** Let's turn to another one now, Braemar Shipping Services is obviously another interesting one in the top 10. We have supply chain issues around the world and the now infamous blocking of the Suez Canal. How is that still impacting that company or has, how much has it impacted a company like that?

**SM:** Well, important to recognize that Braemar is a ship broker, it doesn't own or operate ships, so you got it look at it from that perspective and there are lots of challenges in terms of the global shipping industry, but when you look at the supply chain issues as a result of the blocking of the Suez Canal, and actually it's a positive for Braemar, as that sort of friction puts upward pressure on rates, and is very well placed to benefit from that, obviously, you know, the higher the rates the higher the commission. As an aside, it's sort of in a period of growth at the moment. So it's got a new chief exec, called James Gundy, who used to be the guy that operated the main division of ship broking - and he's now the chief was say my whole company, which is really put the focus on where it needs to be. And again, I'll mention valuation, as I probably will a few times in this, I do think a lot of small companies in the UK, very attractively valued. And yeah, these guys are sitting there at 12 times PE on a forward year. Recently they reinstated their dividends, you know, which really underpins and underlines their confidence in the underlying cash flows of the business.

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**CS:** And Severfield is a steel company that helped build the likes of the Shard and the Olympic stadium amongst other things. Will the new working from home or the new flexible working sort of dynamic around the world, will it have an impact on a company like that, or will they simply provide steel, for different buildings? Maybe talk us through that as well.

**SM:** Yeah absolutely. So Severfield, they're genuine market leader in the UK, and you just mentioned the Shard and Olympic stadium there, they really are involved in so many landmark projects, and the Shard sort of demonstrates, commercial offices do form an part of the companies' order book but, importantly, the companies very well exposed to two very attractive areas of growth such as you know, logistics and distribution hubs, data centers, and you could sort of - if you did subscribe to the theory that office development might diminish - but then the flip side of that home working coin is more people are shopping online. More people will need distributed data and distributing goods as well. So there'll be a beneficiary to that trend as well.

I don't necessarily buy into the theory that the pandemic will bring the end of the traditional office. I just think maybe working habits will change. But I still anticipate office will be an aspect of people's ordinary work, maybe not five days a week, but in some way, shape or form. And again, valuation, you know, they're on a 4% yield 11 times PE. To get any market leader but one that's so specialists and structural steel on that valuation is pretty eye watering.

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And I get it, if I will just talk a bit about something that is less well-known about the company, you know, you think structural steel, you wouldn't automatically think about anything ESG, but the company's doing great work in reducing its environmental footprint. It was listed in the FT's inaugural climate leaders list by reducing emissions by over 20%. Yeah, small companies can be leaders in ESG, but tend not to have whole divisions and departments of people reporting it to ratings agencies. So it's less well known about, but the company is starting to talk about things like that more readily in a more formalized basis, and it's really encouraging to see them communicate that message and do more good work over the next 12 to 18 months.

[9:23]

**CS:** And just lastly, on ESG, could you maybe give us a bit more of an insight on that and how that role plays in smaller companies? Are you finding more companies that are working, you know, that's filtered down into their businesses as well?

**SM:** Yeah, that's a great question. So traditionally small companies might have been doing excellent things in terms of environment, social considerations, governance. But they tended not to, and I'll use quotation marks – “play the game” – that some other more corporate, larger companies might do. And because of this I suppose, lack of disclosure, they may well be rated more harshly by rating agencies. What we're doing is we get to know our companies as well as we possibly can, so that really ticks the governance box in our sort of information finding process. But we see what they're doing in terms of environment and social aspects, and we're encouraging them to more formally represent that as part of their annual reporting structure, and it's really pleasing to see many of them take that advice on board, and because of that, they're getting better ratings agencies by the numerous ESG ratings that have popped up in the last 10 years.

**CS:** That's great Simon. Thank you very much for joining us today.

**SM:** Thank you.

**CS:** And if you'd like to learn more about the Unicorn UK Smaller Companies fund, please visit [fundcalibre.com](http://fundcalibre.com) and while you're there, remember to subscribe to the Investing on the go podcast.