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Q2 2024 review

Liontrust UK Growth Fund

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The Liontrust UK Growth Fund returned 2.4%* in Q2. The FTSE All-Share Index comparator benchmark returned 3.7% and the average return in the IA UK All Companies sector, also a comparator benchmark, was 3.8%.

Although expectations for interest rate cuts in 2024 continued to moderate on both sides of the Atlantic, investors took heart from a building picture of economic and corporate resilience.

The quarter's UK inflation releases saw March and April's readings come in higher than expected at 3.2% and 2.3% respectively, but the May data – released in June – finally showed inflation easing to an annual pace of 2.0%, in line with the Bank of England's target. Meanwhile, economic growth, while muted, has turned positive, with the 0.6% expansion registered during the first quarter of 2024 the fastest growth in two years.

Encouragingly, sentiment towards UK equities appears to be on an improving trajectory – one which was bolstered by the prospect of a general election on July 4. With polls pointing towards a strong Labour majority, investors were ready to price more political certainty into share prices. The prospect of a stable majority government should provide a supportive market backdrop and allow investors to look towards the likelihood of upcoming policy catalysts for the UK stockmarket.

After the significant underperformance of UK small caps in recent years, there were some signs of an improving trend in Q2: the FTSE Small Cap (ex-ITs) index return of 9.3% outstripping the FTSE 100's 3.8% rise, though the FTSE AIM All-Share still lagged with a 3.5% return.

Despite this improvement in sentiment towards UK equities, valuations of UK listed companies remain substantially lower than their long run average and their global peers. As the fund managers have highlighted on several occasions in recent months, these low valuations mean many UK companies have proven susceptible to takeover approaches from private equity or corporate acquirers keen to exploit the opportunity.

Q2 was a particularly busy period in terms of Fund holdings being targeted by potential acquirers.

The Fund's largest riser was Keywords Studios (+78%), a support services provider to the video gaming industry, which was added to the portfolio only a few months ago as a new position. Its shares almost doubled after confirming it was in discussions with Swedish private equity group EQT regarding a possible 2550p cash offer, having rejected four lower offers in recent months.

Perhaps the highest profile takeover approach on the UK market was for Hargreaves Lansdown (+54%). It announced it had rejected two takeover proposals from a private equity consortium, but later received an improved proposal of 1140p a share, leading it to engage with the bidder and provide due diligence access.

The third confirmed takeover target in the portfolio was engineer Wood Group (+56%). It disclosed that it had rejected three successive takeover proposals from Dubai-based group Sidara at 205p, 212p and 220p a share, before agreeing to enter discussions over a fourth and final offer at 230p. In 2023, Wood Group received five takeover proposals from private equity group Apollo, rejecting the first four but agreeing to enter discussions following the final cash proposal of 240p before Apollo dropped its interest.

Elsewhere among the Fund's major risers, specialist media group Future (+71%) saw its shares rebound following the release of interim results. Future shares had previously sold off heavily over the course of 2022 and 2023, hit by broader weakness in the advertising market, the announcement of increased investment costs to stimulate medium-term growth and also lingering concerns over the potential impact of generative AI on its business model. While reporting a 2% organic revenue decline to £391 million in the six months to 31 March, Future noted that Q2 saw a return to organic growth, with revenues rising 3%. This stabilisation in revenues gives Future confidence in maintaining its prior full-year guidance. Longer term, the group expects its recent investments to accelerate organic revenue growth into the mid-single digit range.

AstraZeneca (+16%) was also a large contributor to Fund performance in the quarter. The pharmaceutical group released Q1 results which beat expectations for both revenues and earnings. In constant currency terms, revenues were up 19% year-on-year, driven by a 26% expansion in oncology sales and 23% rise in its cardiovascular, renal and metabolism unit, with the *Farxiga* diabetes treatment leading the way with 45% growth. The company maintained full-year guidance for "low double-digit to low teens percentage" growth in revenues and earnings, but the strength of Q1 trends has led some analysts to expect upgrades later in the year.

Most of our fund commentaries see a spread of short-term 'winners' and 'losers' as portfolio holdings experience the inevitable short-term successes or headwinds in their pursuit of the longer-term capital growth potential for which we hold them. Q2 was no exception, with YouGov (-59%) one of a handful of portfolio disappointments to consider alongside the areas of strength already mentioned.

Shares in YouGov were punished after the company issued an unscheduled profit warning. When reporting interim results in March, the research data and analytics group had noted Q1 was slower than expected with sales cycles remaining long, but that momentum had accelerated in Q2, giving it confidence in meetings its prior full-year sales guidance. Since then, YouGov has experienced weaker performance than anticipated, with a slowdown in the Data Products division affecting revenue and having an outsized impact on profits given the higher margin profile of the business. Fast turnaround research services also declined, while – although the recently-acquired Consumer Panel Services business is said to be performing well – some revenues have shifted into next year due to alignment of revenue recognition policies. Notwithstanding the broader attractions of YouGov's business (an extensive and high-quality global panel and proprietary datasets), it will take time to rebuild market confidence.

A trading update from precision measurement specialist Spectris (-15%) also downgraded guidance, albeit more moderately. Its Q2 update noted that rollout of its enterprise and resource planning system has completed but caused more operational disruption than anticipated – shifting around £15 million of sales into the second half of the year. The company has also seen demand weakness in China and in the pharmaceuticals and electric vehicles markets. Spectris now expects full-year operating profit to be at or marginally below the lower end of the analyst consensus forecast range.

Elsewhere in the portfolio, Next 15 Group (-14%) slid in the wake of a trading update. The data-driven marketing and digital transformation consultancy commented that the macro environment remains tough, with political uncertainty leading to some delays on government contracts. It also flagged that spending across large US technology clients remains soft. However, Next 15 has maintained guidance ahead as it approaches the second half of its financial year (running to 31 January) – a period which historically captures a larger proportion of business each year.

Finally on the quarterly detractors, Indivior (-27%) issued Q1 results showing 12% growth in net revenues to $284 million, once again driven by its *Sublocade* opioid addiction treatment, which rose 36% year-on-year, though only 2% quarter-on-quarter. Growth of *Sublocade* during the quarter was impacted by a number of factors which the company described as transitory, including Medicaid patient disenrollments, abnormal trade destocking and a cyberattack on the largest US medical claims processor. It maintained 2024 guidance, anticipating a resolution of these items as the year progresses: revenues of $1.24 billion to $1.33 billion, up 18% at the midpoint.

The portfolio position in Reckitt Benckiser was sold following Q1's unexpected litigation blow, in which a court in Illinois awarded $60 million in damages to the mother of a premature baby that developed a fatal bowel condition following use of its Enfamil formula. The company has made too many missteps in recent years and the acquisition of Mead Johnson, the infant milk business, has destroyed value. The litigation ruling was our catalyst to sell as the financial risks could potentially be quite meaningful but are unlikely to crystallise for some time. In the meantime, we can reallocate the capital to plenty of other Fund holdings which are at attractive valuations and do not suffer from such an uncertain outlook.

Having already looked to take advantage of currently depressed small cap valuations by initiating a position in Keywords Studios in recent months, the Fund added another new position in Auction Technology Group. ATG is a leading operator of online auction marketplaces and services across two key sectors: Industrial & Commercial and Art & Antiques. It is a business which truly exploits the power of network effects, with an increasing audience of bidders participating in auctions driving higher prices for auctioneers and greater volumes of items listed on the company's marketplaces While ATG, like its peers, has seen some softness in activity due to prevailing economic conditions, this has provided the Fund with the opportunity to take a small starting position, taking a longer term view of the business' potential.

Positive contributors included:

Keywords Studios (+78%), Future (+71%), John Wood Group (+56%), Hargreaves Lansdown (+54%) and AstraZeneca (+16%).

Negative contributors included:

YouGov (-59%), Indivior (-27%), Diageo (-15%), Spirax Group (-15%) and Spectris (-15%).

Discrete years' performance** (%) to previous quarter-end:

	Jun-24	Jun-23	Jun-22	Jun-21	Jun-20
Liontrust UK Growth I Inc	11.8%	5.4%	1.7%	18.0%	-10.2%
FTSE All Share	13.0%	7.9%	1.6%	21.5%	-13.0%
IA UK All Companies	12.6%	6.2%	-8.5%	27.7%	-11.0%
Quartile	3	3	1	4	2

*Source: Financial Express, as at 30.06.24, total return (net of fees and income reinvested), bid-to-bid, institutional class. **Source: Financial Express, as at 30.06.24, total return (net of fees and income reinvested), bid-to-bid, primary class.

For a comprehensive list of common financial words and terms, see our glossary at: https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance does not predict future returns. You may get back less than you originally invested. We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.

The Fund may encounter liquidity constraints from time to time. The spread between the price you buy and sell shares will reflect the less liquid nature of the underlying holdings.

The Fund may invest in companies listed on the Alternative Investment Market (AIM) which is primarily for emerging or smaller companies. The rules are less demanding than those of the official List of the London Stock Exchange and therefore companies listed on AIM may carry a greater risk than a company with a full listing.

Outside of normal conditions, the Fund may hold higher levels of cash which may be deposited with several credit counterparties (e.g. international banks). A credit risk arises should one or more of these counterparties be unable to return the deposited cash.

Counterparty Risk: any derivative contract, including FX hedging, may be at risk if the counterparty fails.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

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