SHINING A LIGHT ON..... SLI UK AND GLOBAL SMALLER COMPANIES FUNDS

At a glance

In this review we look at two funds managed by Standard Life Investments (SLI). We have placed them together because the process behind the funds is the same as is the team. There is therefore some crossover with holdings.

The head of the team is Harry Nimmo who joined Standard Life over 30 years ago. He manages the UK Smaller Companies Fund which was launched in 1997, and took over the management of the UK Investment Trust in 2003. The team launched a European Smaller Companies Fund in 2007 and in 2012 a Global Fund was launched.

Although Harry is head of the team, the process in place means that the success or failure of the fund is not dependent on him. Alan Rowsell is the lead manager on the Global Fund and Andrew Paisley on the European Fund. This is as much about the team as it is any individual person.

In this update with Harry and Alan we touched on the process, performance and individual highlights within the funds.

Fund highlights?

The key to these funds is the matrix which is the propriety stock selection process they have developed. It is this that highlights potential opportunities and from this the managers can select those companies which they believe can grow into the large companies of the future. The types of factors in this process will include market share, barriers to entry and pricing power.

Examples of companies which the UK Fund no longer hold but held from a very early stage included Hargreaves Lansdown and ASOS. These companies have been replaced with the likes of Rightmove, Paddy Power and Poundland.

Harry and Alan both argue that this fund is about committing to invest for 5 years plus to get the best returns. Once they find good companies they will look to hold these for an extended period of time so investors benefit from earnings and dividend growth. At a point where there is little or no value to be gained those companies leave the portfolio.

Both funds have slightly outperformed the index in recent years and both managers explained that this is a reflection of ultra-low interest rates and low quality stocks performing strongly. Small cap is seen as high risk but this fund seeks out lower risk stocks, so they are looking for quality. So when poor quality does well this fund will lag.

Rising interest rates will be good for this fund because it is a sign that the economy is doing well and these companies tend to be beneficiaries of this. Their view is that in the short to medium term this will be positive for the fund but warn that the time to be nervous is when interest rates peak and the economy dips into a recession.

Before the update on the fund we covered three things – valuations, oil and accuracy of the matrix.

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They explained that valuations within the index are a bit more expensive than they have been although at this stage they do seem to be too concerned about this. Oil has been good news for small cap and this will benefit the fund. And finally the matrix works 70% of the time, which is a high measure of success.

On the fund updates:

Global Smaller Companies

Alan started by explaining that 2014 was difficult for the fund as there was a rotation from high quality stocks to low quality and the fund performance suffered as it didn't participate in this rotation. However, 2015 has been a stronger year for the fund.

They have reduced exposure to the US from 50% to 40% as there is more opportunities being identified in Asia, Japan and Europe. Areas of interest include India and online payment processors. To reflect this change the turnover in the fund has been slightly higher than normal.

The top ten holdings are not necessary the types of holdings you would expect to see in a global fund and therefore it may make a good blend with other funds. Two holdings he highlighted were Pigeon Corporation who are Japanese Baby Product Company. This he explains highlights a quality business with sustainable growth. It has a strong brand image which it has taken internationally to China and now Europe, US and other Asian states.

Teleperformance is a new company which they have added to the portfolio. It is a market leader in operating call centres, and gradually growing market share especially in the US. Alan believes outsourcing is on the up and this company will benefit from this.

UK Smaller Companies

Harry explained that this is a seasoned fund which has been through three bear cycles – Asia, Gulf War and Banking Crisis. Because of the quality aspect of the fund it tends to outperform during these periods.

Companies he likes included Shaftsbury which is a play on the vibrancy of the London Property Market, Dechra Pharmaceuticals (producing products for pets) and CVS Group which is a vet practice in the UK. He also highlighted Ted Baker who now generate a third of sales outside of the UK and are growing strongly, and as an old company, Greggs, who have re-invented themselves.

In summary the process is well established and has proven over time to deliver outperformance (although nothing is guaranteed). These funds should be seen as a long term hold and there will be short term periods of underperformance.

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Fund performance

Performance since launch vs the benchmark.

Standard Life UK Smaller Companies Fund

	2010	2011	2012	2013	2014	2015
SLI UK Smaller Companies Fund	48.60%	-8.90%	24.16%	39.10%	-7.69%	8.64%
FTSE All Share	14.51%	-3.46%	12.30%	20.81%	1.18%	7.84%

	1 year	3 years	5 years	10 years	Since
					launch*
SLI UK Smaller Companies Fund	4.79%	50.36%	109.48%	315.31%	1063.40%
FTSE All Share	7.48%	39.98%	59.95%	122.30%	240.36%

^{*3} January 1997

Standard Life Global Smaller Companies Fund

	2012*	2013	2014	2015
SLI Global Smaller Companies Fund	9.54%	38.94%	-1.65%	6.63%
iShares MSCI World Dist	3.85%	21.87%	10.53%	5.36%

	1 year	3 years	Since launch*
SLI Global Smaller Companies Fund	13.30%	49.47%	59.61%
iShares MSCI World Dist	16.48%	46.16%	47.38%

^{*19} January 2012

You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise. The total return reflects performance without sales charges or the effects of taxation, but is adjusted to reflect all on-going fund expenses and assumes reinvestment of dividends and capital gains. If adjusted for sales charges and the effects of taxation, the performance quoted would be reduced.

The source of information in this note has been provided by SLI and is correct as at May 2015. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase any fund mentioned. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision.