TB Saracen UK Alpha Fund

Quarterly Review – September 2020

FOR PROFESSIONAL INVESTORS ONLY-

Retail investors should consult their financial advisers

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Fund Manager

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	TB SUAF	MSCI UK All Cap (TR)	Relative
Q3 2020	-1.6%	-3.5%	+1.9%

Performance Summary

The third quarter of 2020 saw the fund continue to rebuild performance from the difficult period endured in Q1. July saw the fund outperforming the MSCI by some 1.6%, with this positive performance driven by strong returns from Premier Foods and DiscoverIE. This was followed by a broadly in-line performance in August when all of the main size indices in the UK rose in value, led by the Mid 250. During this period, we saw early signs of recovery in holdings such as Wood Group, Tyman and DFS Furniture. The quarter drew to a close with the fund posting a return for September of -1.2% compared to the UK index return of -1.7%. This meant that the relative return for Q3 overall was a fairly solid +1.9%, continuing the trend of regaining lost ground that began during Q2.

Cumulative Performance after all ongoing charges to 30th September 2020

	3 months	1 year	3 years	5 years
TB Saracen UK Alpha B Acc	-1.6%	-16.2%	-9.3%	15.6%
MSCI UK All Cap Index (TR)	-3.5%	-18.2%	-11.6%	15.8%
Sector Average	-1.0%	-12.8%	-8.0%	16.9%
Quartile Ranking	2	3	2	3

Source: Financial Express *Sector: IA Sector (UK All Companies)*

Market Overview

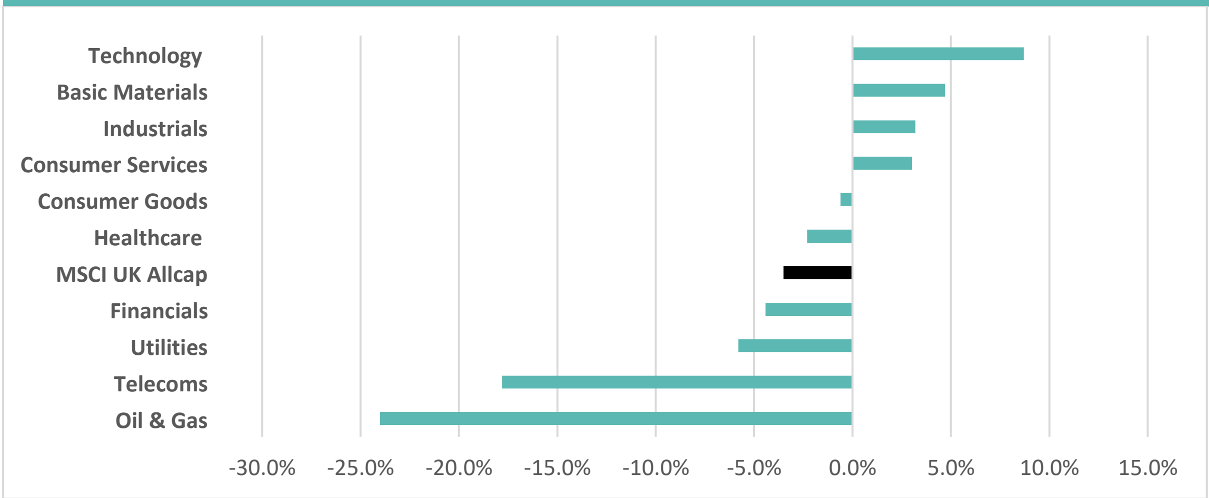
UK returns were dominated by the weakness in the FTSE100, with banks and oils in particular continuing their dramatic fall from grace. In addition, the UK indices continue to suffer from their very low exposure to the high performing technology sectors. By contrast, global equities continued to make progress, driven by the tech sector in the US and better economic trends emerging from Asia.

Looking at the UK market specifically, the small and midcap indices continued to make up some lost ground, with the AIM market in particular roaring ahead as investors focussed on emerging technology and healthcare names which are well represented there.

Total returns by capitalisation: 3 months to 30th September 2020	
FTSE100	-4.0%
FTSE Mid250	+1.8%
FTSE Smallcap	+1.2%

At a sector level, the oil sector continued its miserable form as BP joined Royal Dutch in slashing its dividend as well as their headcounts. Banks also remain friendless in a zero/negative interest rate environment where their dividend prospects remain uncertain. By contrast basic materials and industrials sectors in general benefitted from early signs of greater economic stability globally and a feeling that the worst may well have been seen. Having held up fairly well during the early stages of the crisis telecoms and utilities gave up ground again.

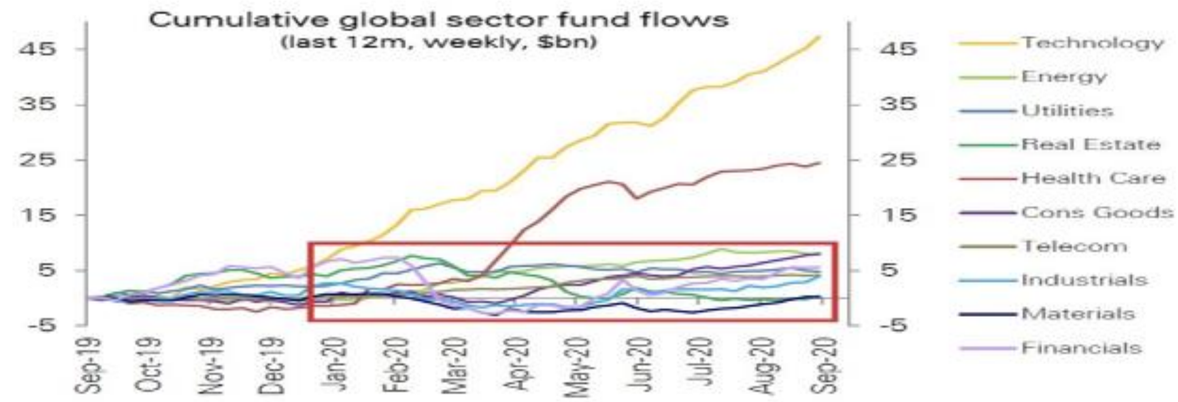
UK Sector Total Returns: 3 months to 30th September 2020



Source: Bloomberg

We continue to live in a world governed by extremities, with acute divergences between perceived winners and losers. Current stock markets exemplify this and more. The boom in the technology sector is widely documented and has become more extreme in a post-COVID world, closely followed by healthcare. Recent fund flow data shown below illustrate how this has become a self-fulfilling prophecy. IPO's such as Snowflake, a US cloud storage business, also reflect a mania of sorts with a market cap of $69bn and a multiple of 120x projected sales. Time will tell if this valuation is right.

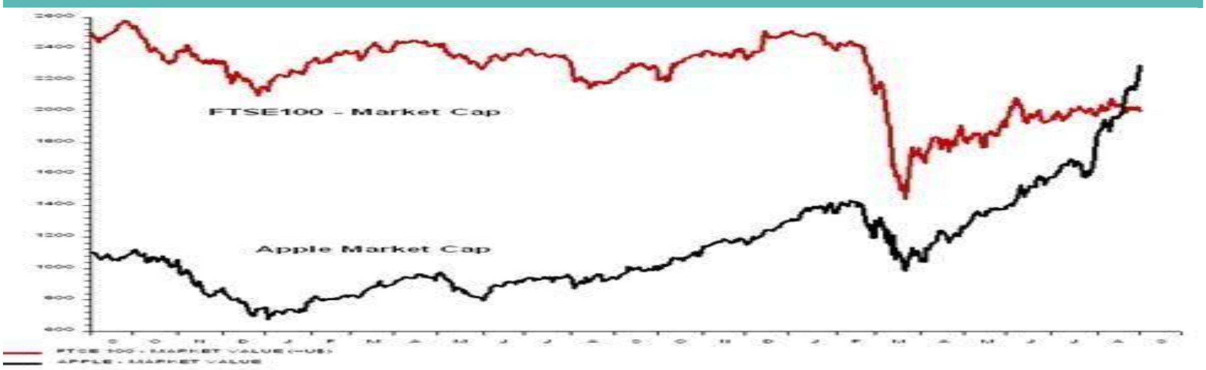
Global Sector Fund Flows



Source: Deutsche Bank Asset Allocation, EPFR, Haver Analytics, Data as of 16.9.20

Having become the first company to reach $1 trillion in value 42 years after it was founded, Apple took just two years to be the first to the $2 trillion mark, on 31 July 2020. This was larger than the individual market capitalisations of 470 of the companies in the S&P500. Even after a recent sell-off, Apple is still worth as much as the entire FTSE 100 index of leading UK businesses. This may reflect Apple's undoubted strengths and prospects but also highlights the fairly horrific decline in UK large companies of late. The non-UK earnings of the FTSE100 are more than 70% of the total, reflecting their global reach rather than their domicile. Therefore, poor UK economic prospects, Brexit and a bumbling Boris Johnson are not really the issues here. Whilst there are many structurally challenged sectors in this group it's hard to believe that the majority of this hundred are dead ducks.

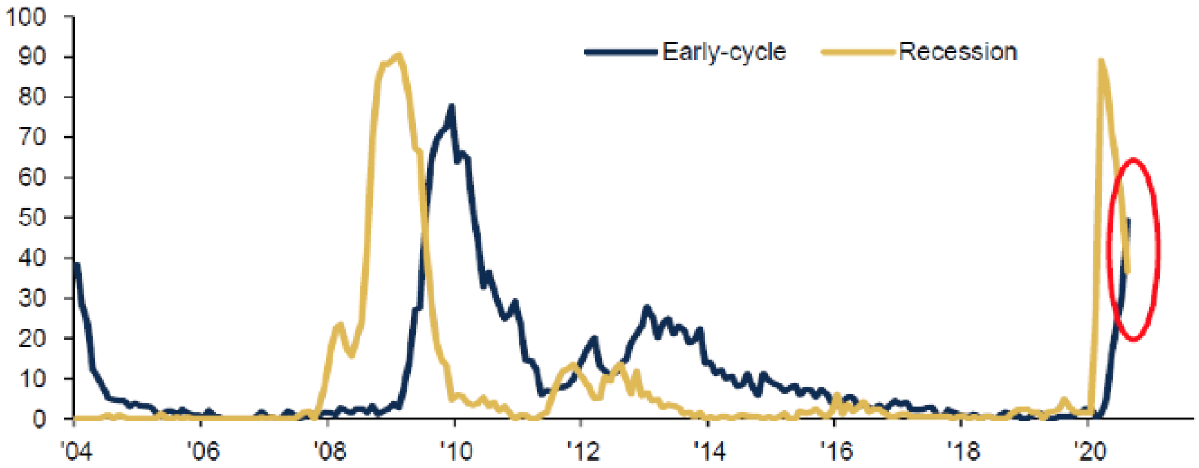
Apple Market Cap v FTSE 100 Market Cap



Source: Bloomberg

Investor sentiment has changed markedly since the onset of the COVID19 crisis in March. At that point the BOAML global survey had 90% of participants suggesting we were in a full-blown global recession. Six months later that figure has fallen to 37%, with almost half now saying we are in an early stage recovery. This was a pretty reliable barometer of market and economic recovery in 2009 also.

Global Recession Indicator



Source: Bank of America Global Fund Manager Survey

Global activity is now rebounding sharply from a low base. A second wave of infections is a clear and present danger but most governments are now better prepared to handle this.

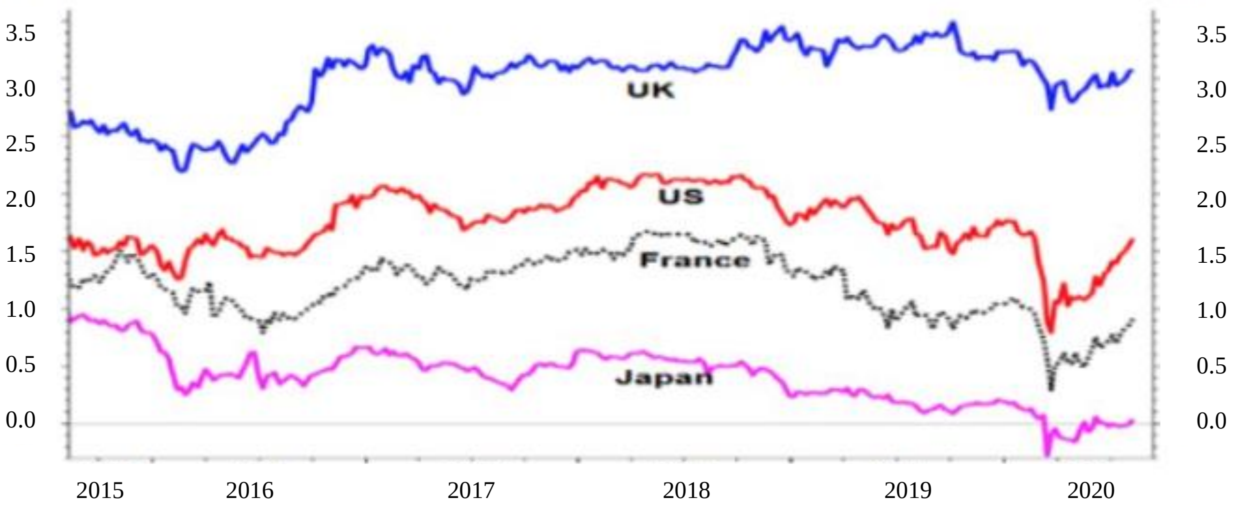
Closer to home, the short-term issues are considerable. A possible no-deal Brexit, the likelihood of a second wave of coronavirus infections causing further damaging lockdowns, low business and consumer confidence and a government which appears to be imploding under PM Johnson are all reasons to be wary.

Our previous concern that unemployment may rise over the 10% level in the UK as furlough unwinds and lockdown measures continue remains a risk. Similarly, a sharp fall in 2020 UK GDP of around 10% also still seems likely, particularly in the light of the 20% fall seen in Q2.

However, little of this is new news since our last report and more recently indicators such as PMI surveys, new home sales and retail spending have improved significantly from low bases.

As before interest rates and government bond yields remain effectively at zero, with concerns that the Bank of England will head into negative territory. Whilst neither short nor long rates are likely to change anytime soon, we would again highlight the considerable complacency around inflation. Any sustained uptick here would have considerable implications for market leadership we believe.

Implied Inflation Expectations Rising Globally



Source: Datastream

Portfolio Review

The portfolio has a 'multi cap' structure with high exposure to small and mid-cap companies, which make up 69% of the portfolio. The focussed nature of the portfolio means that the Fund has a high active share at 93%. This strategic positioning has been beneficial to our results over the years as well as offering considerable long-term flexibility.

Positive Contributors

There were a number of stocks whose performance contributed towards the outperformance of the Fund over the quarter, most notably amongst our smaller company investments.

The strongest performer in terms of contribution to return was **Premier Foods** (+32%) which continued to trade well during lockdown and has consistently issued positive trading updates.

Alpha FMC (+11%) also did a decent job for the fund as the management emphasised during market updates that the company was trading well and had made the transition to home working very successfully. Our holding in **Johnson Matthey** (+12%) repaid the faith we had in it with a robust return during the quarter helped by a growing appreciation of the group's underlying technologies. Also, in chemicals, **Synthomer** (+14%) reported no material disruption to its operations and ongoing strength in its nitrile gloves operations.

STV Group (+9%) has consistently outperformed both ITV and the BBC in Scotland throughout this crisis and has managed its way through the lockdown very successfully. Programme production has recommenced, and we expect further positive news from this very lowly valued holding in due course.

Tyman (+17%) also had a positive quarter after issuing an encouraging interim statement saying that its core markets were picking up well and debt levels reducing. **DiscoverIE** (+19%) issued a trading update at the tail end of July reassuring the market that their order book remains strong and that, given the global nature of their business, they are well insulated from any local secondary outbreaks of the virus. **Eurocell** (+11%) reported interims in early September stating that all of their sites were now fully reopened and that they had enjoyed better operational efficiencies since reopening.

In the retail sector **Halfords** (+19%) continued its strong run benefiting from the increase in bicycle sales as well as being able to keep the majority of its shops and garages open for the duration. **Palace Capital** began to improve (+12%), albeit from a low base. That there is value in companies like Palace in the property sector is beyond doubt though, in the current environment, it may take some time for that to be fully demonstrated given the challenges they and the broad real estate sector face.

Negative Contributors

Despite the portfolio holding up reasonably well during the quarter there are a number of holdings in the Fund which have yet to see a meaningful pick up in stock price performance.

Vistry (-20%) has been very disappointing in terms of its share price performance. This is despite very strong management action and rhetoric as well as impressive statements of confidence and some punchy forecasts going into 2021. The house building sector is doing well again and so is Vistry. It is our belief that the share price is being held back by the level of debt that the company is carrying post the Bovis/Linden Homes merger. We do not share this concern. Remaining with the housebuilding sector, **MJ Gleeson** (-9%) struggled a little as the market was a bit disappointed at the lack of strategic land sales and the slow initial recovery in house sales post COVID. However, management were at pains to point out that they were confident for 2021, with demanding targets remaining in place.

The financials sectors remain somewhat friendless and this impacted our returns over the quarter. **Standard Life Aberdeen** (-13%) suffered in the light of changes at the top of the company which have led to some uncertainty. In banks **Barclays** (-15%) fell during the quarter, but this was due to a sector malaise rather than anything company specific. Other stocks in the broad financials space that had a lacklustre period included **Premier Miton** (-9%), **U and I** (-31%), **Intermediate Capital** (-7%) and **Prudential** (-9%).

Clinigen (-13%) reported final results during the quarter which were marginally disappointing in terms of the impact that COVID had had on the business. The longer-term bull case remains undiminished however. **Equiniti** (-22%) had a difficult quarter mainly as a result of the fact that levels of corporate activity have remained low and low interest rates have impacted overall revenues.

Portfolio Activity

The fund has 33 investments which are spread across a variety of market capitalisations. As at 30th September 2020, the breakdown of the portfolio by size was 30% in large cap, 22% in midcap and 47% in small cap/other. The Fund is currently fully invested with only 1% cash.

Purchases

There were no new investments made during the quarter and all the portfolio activity was in terms of topping up some existing holdings or taking some profit in others.

We bought the retailer **DFS Furniture** last quarter. It is a business we knew well having held it in the past but we believed that it was oversold during Q2. Our faith in the business was repaid as during Q3 the company issued a better than expected trading statement to the market. However, the share price did not, we felt, react appropriately and so we were happy to top up further on our position.

We also invested in the transport business **National Express** last quarter and the share price had been a lacklustre and volatile performer since then. We felt sure that the ‘doom and gloom’ surrounding the company was massively overstated and added to our position. We are still confident that the company will make a strong recovery.

In a similar vein, we added to our holdings in both **Tyman** and **Vistry** who both announced results that beat market expectations, further building our confidence in these businesses.

Sales

We made no outright divestments during the quarter as we continue to believe in the robust nature of the portfolio and are happy to let the performance come through in due course. That said, we trimmed a few holdings as they had produced very good returns and we felt that the position sizes in the portfolio were creeping a little high in terms of the future risk/reward profile.

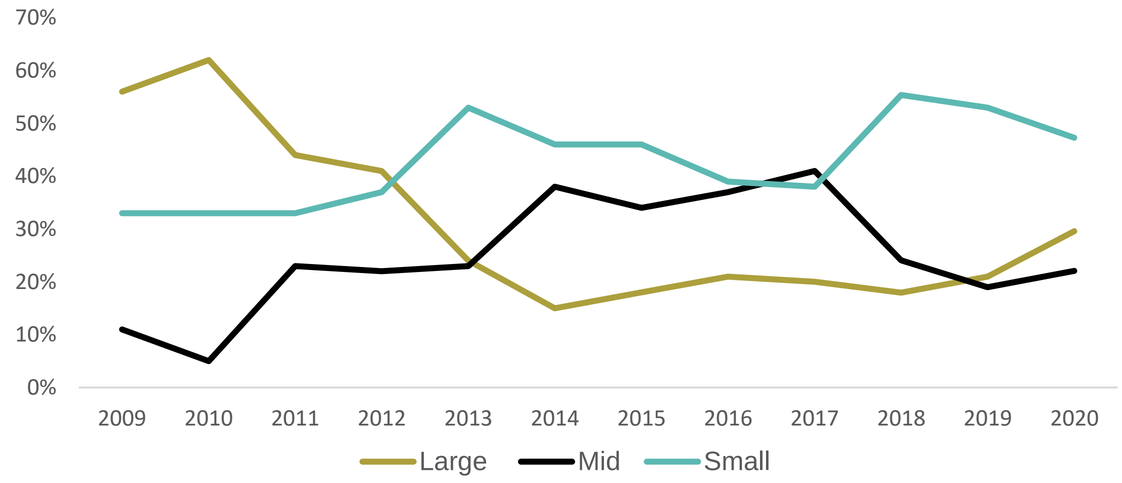
The stocks where we took advantage of some strong recovery in performance included **Premier Foods** which has been performing very well since we bought it. We also trimmed our position in **Alpha Financial Management Consultancy**, a long-time favourite of the fund as the stock continued to report strong trading during the COVID crisis. Likewise, we trimmed our large position in **Johnson Matthey** after some good recovery.

Portfolio Strategy & Themes

The continued outperformance of the portfolio during Q3 following a significant recovery in Q2 has been heartening and gratifying. We regularly comment on what we see as the underlying undervaluation inherent in the portfolio and make no apology for doing so again. It is this factor which we believe will drive a further recovery in performance after the COVID inspired set back we saw in Q1.

The Fund's flexible, multicap structure remains in place. Our overall exposure to small caps has drifted down a little as 2020 has unwound but remains around 50% of the Fund.

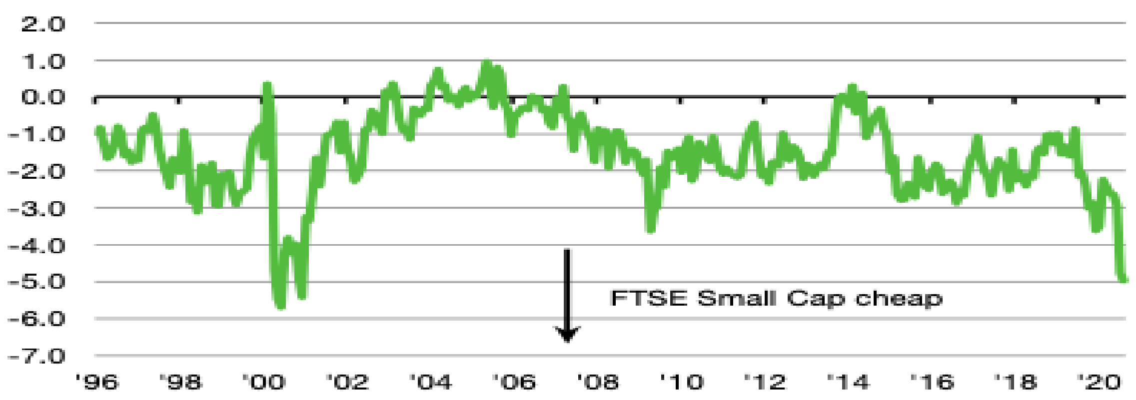
TB Saracen UK Alpha Fund – Historic Asset Mix by Size



Source: Saracen Fund Managers as of 30th September 2020

However, we remain very positive on the smaller end of the market where we believe that much better opportunities can be found and where forward valuations are generally much less demanding than those of mid and large cap stocks. The graphic below serves to reinforce this point and illustrates why the Alpha portfolio is positioned as it is in terms of market cap bias.

UK Small Cap Discount – Median Small Cap PE v FTSE 250

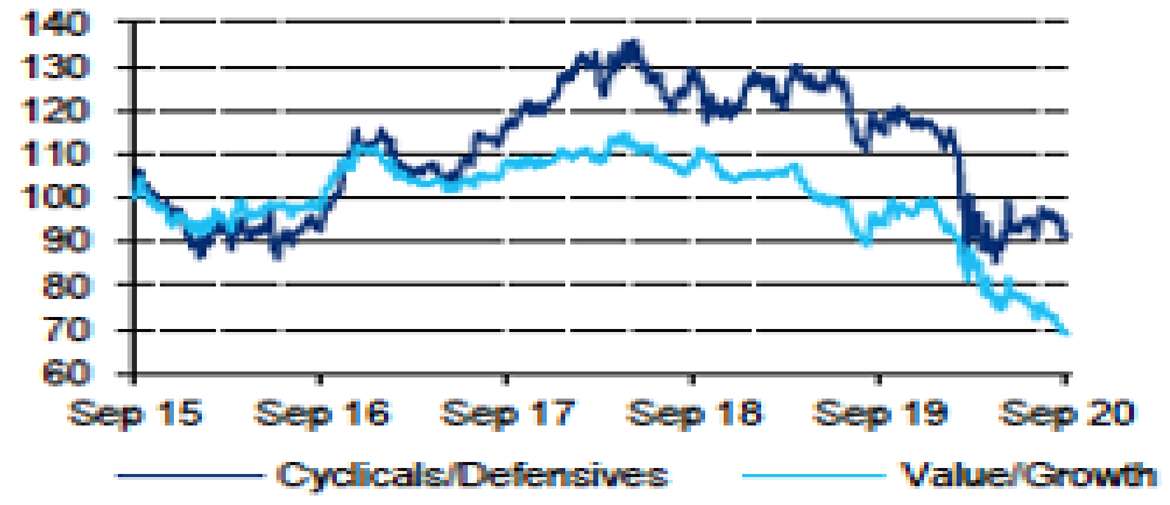


Source: Liberum, Datastream

Growth stocks, despite their high and growing ratings continue to outperform the broader market. As we have said before, the Alpha Fund is not a 'value' fund per se, but we are strongly of the opinion that valuation does actually matter when considering the relative merits of stocks and we are still reluctant to chase the heady multiples that characterise many a growth stock these days. We remain convinced that this is not a situation that can persist indefinitely and firmly believe that our approach will bear fruit again.

The chart below illustrates both the value and growth factor disconnect but also the disparity between cyclical and defensive stock performance.

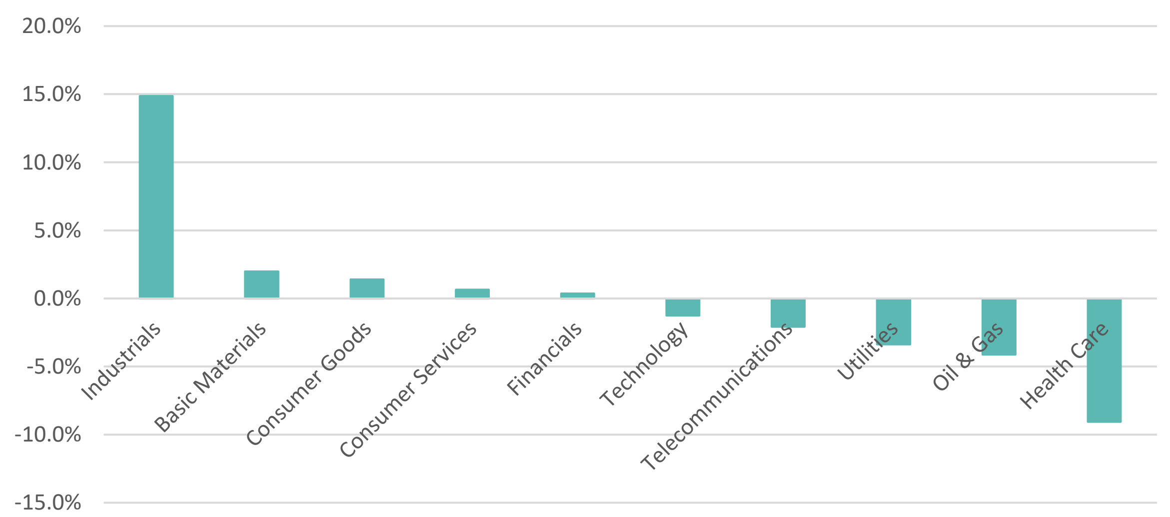
Cyclical Relative to Defensive & Value Relative to Growth



Source: Citi Research, MSCI, Factset

The sector chart below illustrates the relative positioning of the Alpha fund currently, with its very limited exposure to those normally defensive sectors and higher exposure to industrials and financials, which tend to be more domestically orientated and, in the case of the industrial companies that we hold, predominantly small and mid-cap stocks.

TB Saracen UK Alpha: Sector Active Weights



Source: Saracen Fund Managers as at 30th September 2020

Despite the obvious headwinds in terms of sector positioning the fund performed well through the quarter which, we believe, is testament to the underlying quality and valuations of companies within the portfolio and the fact that many of them have continued to trade unimpeded throughout the lockdown period.

The industrials holdings are always a mixed bag with limited correlation to each other, but we believe that our holdings are of a superior quality with positive long-term growth drivers which will stand the portfolio in good stead for some time to come.

Within the Financials sector we have seen some of the good performance in Q2 unwind as many businesses cope with the impact COVID has had on their profitability and margins. There has also been considerable 'top down' hostility to financial sectors in the light of very low interest rates and bond yields. On valuation grounds we see considerable upside in our property holdings but, we must acknowledge that they are not flavour of the month and some structural questions will be asked of them in terms of office and retail demand going forward.

We have very limited exposure to the oils sector, which has been in freefall for some time. We will never claim to have any particular insight into the direction of oil prices and it's clear that the sector now faces some potent structural challenges over the next few years. Having said that, the performance of this sector in total has been so poor that there may be some interesting opportunities affording themselves. We shall keep our eyes open to this.

Investment Approach

The TB Saracen UK Alpha Fund's investment objective is to achieve a long-term total return above the total return of the MSCI UK All Cap Index.

We have a focussed portfolio of 33 quoted UK companies making up a 'best ideas' fund with a very high active share, currently at 92%. We generally ignore index construction considerations and each position within the portfolio must be meaningful enough to make a difference to shareholder returns. Our approach is 'multi-cap' with significant investments in smaller and medium sized companies and correspondingly limited exposure to the largest companies found in most UK equity portfolios. Mid and small caps are currently 69% of the fund with large companies at 30% and cash 1%

We like to be patient shareholders in businesses and invest for the long-term. If the underlying business is performing as we expect and the valuation is palatable, we remain invested. Stock prices can be volatile in the short-term and we take advantage of this by adding to existing holdings if prices weaken and trimming large positions if valuations get out of kilter at any point. Valuation is key in every decision we make.

We spend very little time responding to what is in the news or analysing economic data. Most macro factors are unpredictable and volatile in our experience. Instead our time is spent searching for companies which the fund can invest in. These companies will fall into one of the following categories:

Core growth (41%* of portfolio assets)

We would expect the largest component of the fund's assets to be held in core growth companies, businesses which can deliver consistently strong compound earnings growth rates over a long-time period, allowing us to hold them for many years to come. The exposure to this segment has reduced from nearer 60% in early 2018 due to the scarcity value and high ratings being applied to growth companies, which led us to take profits in various holdings.

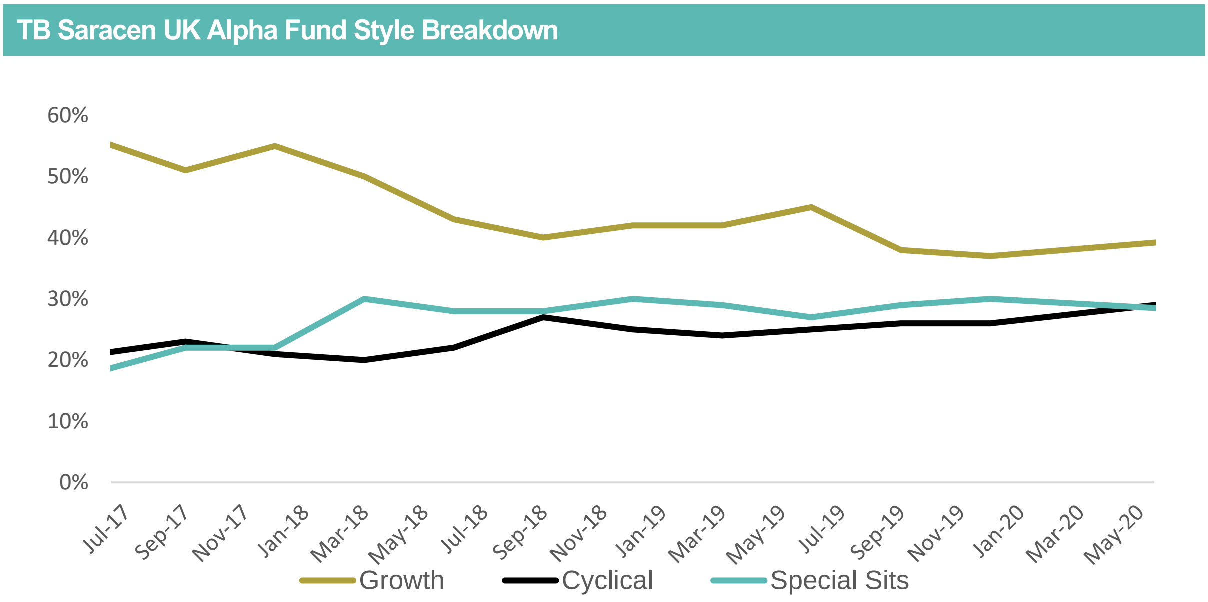
Special situations (28%* of portfolio assets)

The special situations investments are businesses where the long-term prospects may not be sparkling but where we see significant catalysts for change. These catalysts would include new management and takeover / breakup potential. During 2018, we saw takeover bids for four portfolio companies, but we only had one in 2019, IFG Group. Patience is often required with this approach, but it can be highly rewarding if executed well. This type of investment should be able to perform even in challenging stock market conditions.

Cyclical recovery (31%* of portfolio assets)

The final group are good quality, cyclical businesses where we recognise that economic conditions may not always be ideal, but the company has sufficient strength of management and balance sheet to justify an investment.

**asset mix shown as at 30th September 2020, source Saracen Fund Managers*

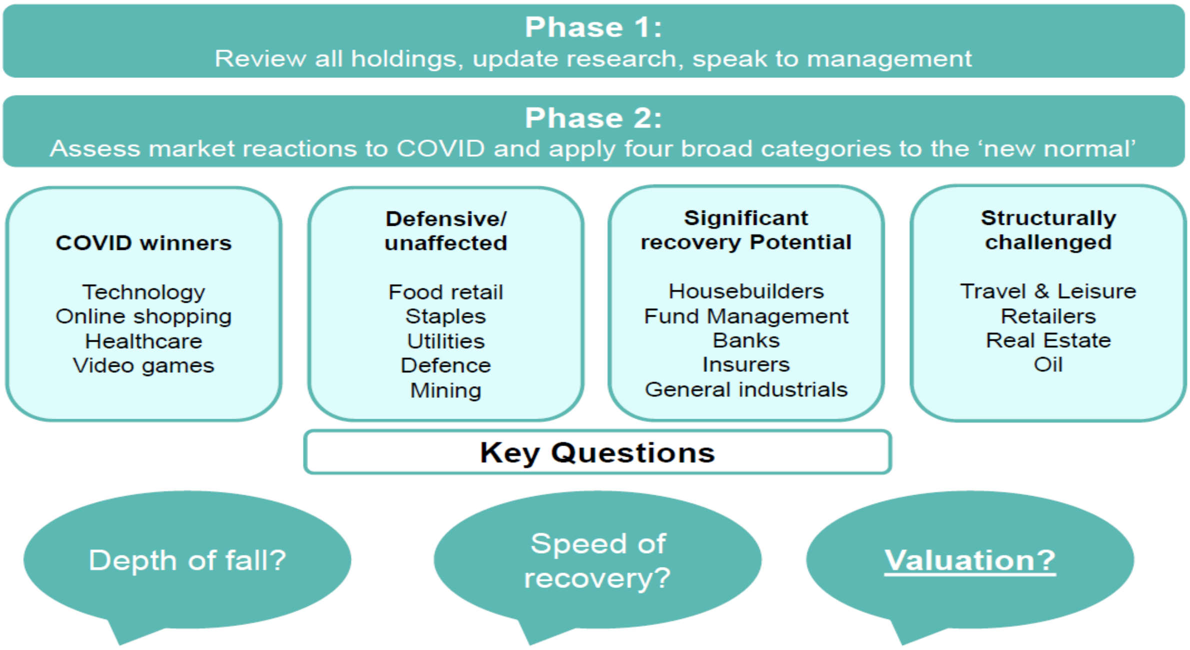


Source: Saracen Fund Managers 30th September 2020

With this structure in place the Fund is designed to be style agnostic and is able to take advantage of both 'value' and 'growth' opportunities when they arise. At this point in time there are far more potential investments emerging in the former category than the latter.

Outlook

Since the COVID pandemic took hold in March we have had to quickly reassess what has become a very different world for us as investors and most of the businesses we invest in. Often this has been done against a background of companies themselves having no clear view of events and timescales. The dangers of using short term extrapolations are currently very high. The schematic below attempts to outline the approach we have taken since.



If there has been a positive to come out of this crisis it is that we have enjoyed more frequent and better access to the management of the businesses in which we invest and we have been able to reassess our positions fairly quickly (phase 1 – ongoing).

In many ways making the broad categorisations of phase 2 was fairly straightforward – there have been a number of clear winners and losers throughout the pandemic. However, that is the easy part of the exercise and identifying a cosy consensus does not necessarily help us improve returns to investors. To us the following questions therefore remain key – how far has the share price fallen (or risen), how quickly will the business recover its earnings/cashflow and what are the implications for long term valuations? This latter point is crucial. Pretty soon 2020 will be over and there may well be brighter skies on the horizon.

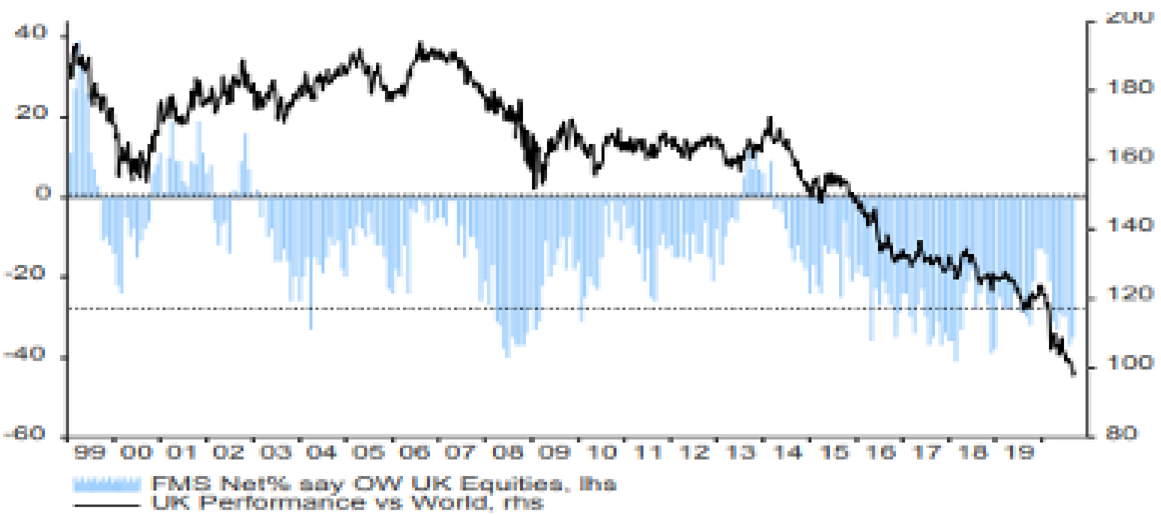
Taking all of the above into account we can broadly characterise the portfolio into three key earnings segments – 1) largely unaffected 2) recovery potential and 3) structurally challenged. The chart below is our assessment of all of our portfolio holdings, warts and all.

Largely unaffected	Recovery Potential		Structural ?
Alpha Financial Markets Consulting	Barclays	Kin & Carta	Melrose
Chemring	DFS Furniture	MJ Gleeson	National Express
Clinigen	Equiniti	Premier Miton	Palace Capital
DiscoverIE	Eurocell	Prudential	U&I Group
Intermediate Capital	Euromoney	Restore	
Imperial Brands	Halfords	Standard Life Aberdeen	
Marlowe	Inspecs	STV	
Mattioli Woods	Johnson Matthey	Tyman	
Premier Foods	(John) Wood	Vistry	
Rio Tinto			
Synthomer			
37% of Fund	**53% of Fund**		**10% of Fund**

More than half of the Fund by value we deem to have clear earnings (and share price!) recovery potential and this is the main part of the Fund where we have looked to add new ideas or increase our investments. These typically have very low valuations compared to their history, particularly when we look beyond the disruption seen in 2020. Readers could also rightly challenge the small proportion of the Fund held in structurally challenged areas. We shall remain vigilant and open minded with regard to these holdings but, in most cases, they could offer significant upside, albeit with higher levels of risk attached.

The relatively poor performance of the UK market can, to some extent, be explained by the reluctance of asset allocators to direct funds to the UK. This is for a variety of well-rehearsed reasons including further uncertainty over Brexit, the likelihood of a second wave of coronavirus infections causing further damaging lockdowns, low business and consumer confidence and worries over the potential for inflation to spike.

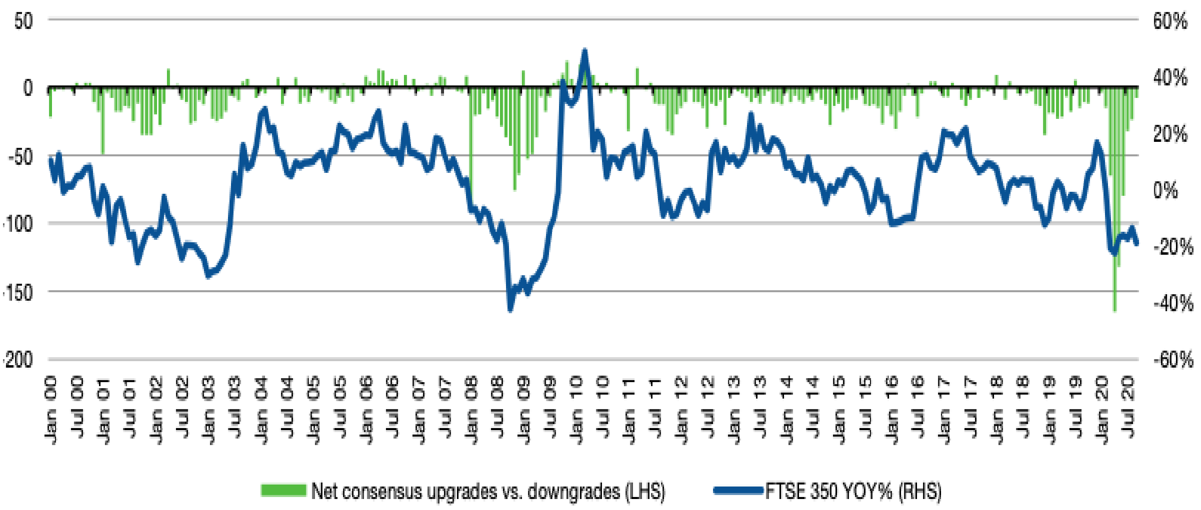
Net % Asset Allocators Who Say They Are Overweight UK Equities



Source: Bank of America Global Fund Manager Survey

We believe that the wave of downgrades that the market has endured since March does seem to be abating somewhat as shown below. However, if the second wave of COVID causes further lockdowns similar to those we have already seen across the country and further afield then we should expect that wave to pick up again.

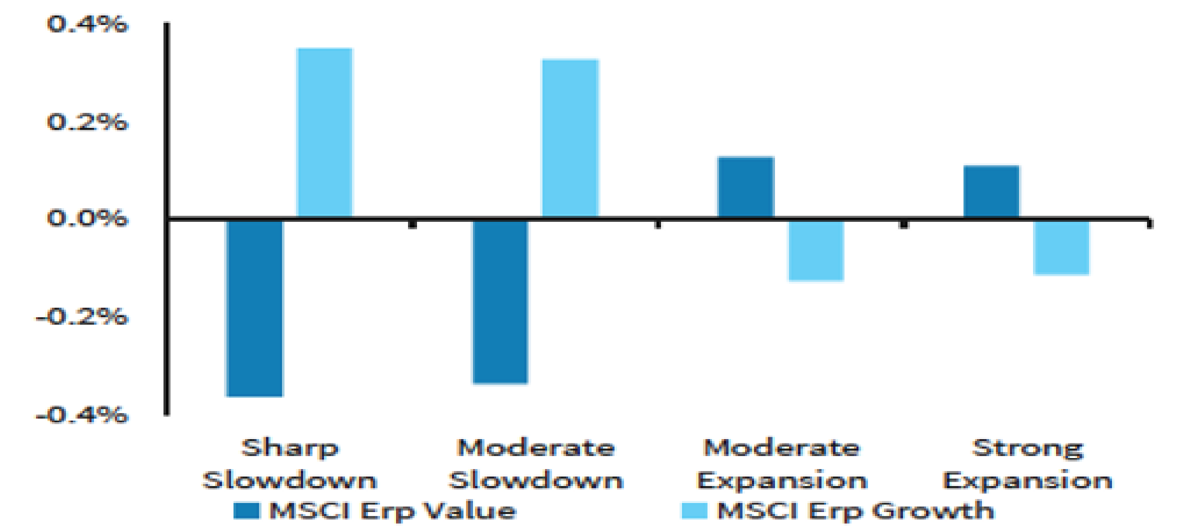
Number of stocks upgraded by more than 5% v stocks downgraded by more than 5%



Source: Liberum, Datastream (using FY2 estimates)

Not only do we believe that the portfolio is well placed for recovery in markets in a post-COVID world but we also believe that the portfolio is on the right side of the growth/value debate. The chart below shows that during any recovery or expansion phase of market not only does the value end of the market outperform but the growth end of the market underperforms. It is worth pointing out too that value proved to be a good hedge during the recent tech-led US sell off.

Value Outperforms and Growth Underperforms in Recovery/Expansion Phase



Source: Barclays Research

At Saracen we have long been advocates of taking the long view not only in terms of holding periods but also in terms of not putting too much weight on near term earnings. As many readers will know, we routinely forecast cash flows, balance sheets and income statements forward five years. That these forecasts will be incorrect is a given, but they are illustrative when seeking to assess longer term value and not focus overtly on near term multiples.

The earnings collapse in the first half of 2020 has led, not unnaturally, to a dramatic increase in trailing PE ratios, but for FTSE 250 and FTSE Small Cap these depressed earnings are expected to remain in place for 2020, creating artificially high 12-month forward PEs. We believe that it is important to look through this phase and focus on FY21, FY22 and beyond.

We have said before that we believe COVID 19 is a manageable event. We continue to spend a great deal of time at Saracen talking to the managements of the companies we hold and also to the managements of companies whose share prices have been hit hard and we believe may well be an interesting opportunity. Managements remain very keen to engage with investors and keep them up to date with how their businesses are faring in these unprecedented times. We mentioned last quarter that we were beginning to get a sense of the companies that are well positioned to be long term survivors of this pandemic and those that will struggle for some years to come. It is now becoming clear that many of our holdings are emerging from lockdown in much better shape than even the most optimistic of us might have hoped.

However, there are some industries where the forecast risks remain very high indeed, in particular the leisure and hospitality industries as well as travel and airline companies. As some wag once said, “It is difficult to make predictions, especially about the future.” As far as these industries are concerned our crystal ball is no better than anyone else’s at this stage.

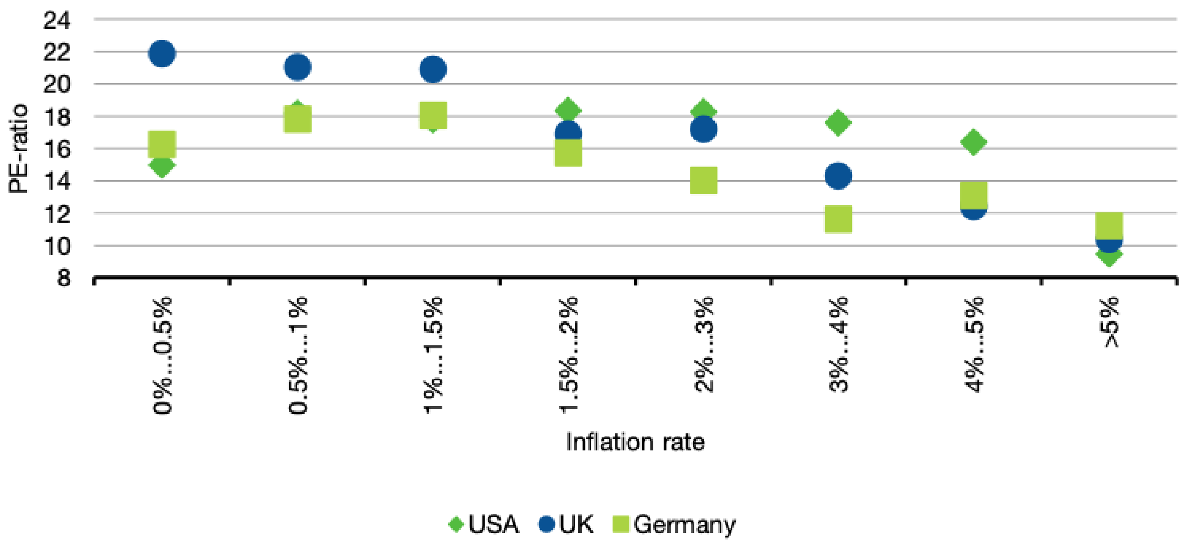
Other industries, though likely to survive, may have been changed forever. Sectors such as real estate and general retail face very real challenges and we are constantly hearing that the world has moved forward some five years in terms of digital adoption in the space of six months. There will be consequences, both good and bad, as a result of this.

There are reasons to be cheerful, however. Given that we have an environment of generally low inflation and low interest rates (which are likely to stay low) it does not seem ridiculous to say that we may see a significant re-rating of stock markets as we emerge from this crisis over the next 12-15 months or so. The immediate beneficiaries of this would be value stocks with extremely depressed earnings.

We are constantly being asked what the catalyst for performance of value stocks will be. It has always been a difficult question to answer but as things stand it seems likely that investors must have some confidence that the worst of the pandemic is over and there is a real prospect of being able to return to normal sometime in 2021.

We mentioned earlier in this piece that there are risks to the equity market if there was to be a sustained rise in inflation. The chart below shows that as long as inflation rates stay below 2% valuation multiples can stay at higher levels. Once inflation rises above 2% multiples tend to decline somewhat and go very much lower if inflation goes above 5%.

PE Ratios and Inflation



Source: Liberum, Datastream

They say that a week is a long time in politics and we have discovered during 2020 that a quarter can be a very long time in stock markets. Few could have foreseen the damage to global portfolios that would occur in March at the beginning of January.

It is interesting to speculate where we might be at the end of Q4 as we enter it. Much is due to happen in the course of the coming quarter and by December the US may have a new president, the UK Brexit deal should be done and dusted and we may have much clearer visibility on the timing of a COVID vaccine. All of these factors have the potential to significantly affect both the UK and overseas markets, to say nothing of any surprises that may well come along.

We thank you for your continued support during these times and, of course, hope that you and your families stay safe and well.

David Clark, Scott McKenzie
8th October 2020

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Past performance is not a guide to future performance. The value of investments and the income from them may go down as well as up and you may get back less than the amount invested. A full list of the risks applicable to this Fund can be found in the Prospectus. All fund performance figures calculated on a single price basis.

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Custodian – The Northern Trust Company, 50 Bank Street, Canary Wharf, London, E14 5NT

Depositary – NatWest Bank PLC, 135 Bishopsgate, London, EC2M 3UR

Regulatory Status:
FCA Recognised: Yes
Scheme Type: OEIC

Issue date – 8th October 2020