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# Monthly Monitor

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**February 2019**

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## Small Caps Equities – Appian Well Positioned for Growth

Appian has consistently viewed Small Cap Equities as a class that can outperform general equities over time. This is backed up by historic evidence which we discussed in our [White Paper two years ago](#). For example, \$1 invested in US Large cap stocks in 1955 would have grown to \$3,919 (including the benefit of dividends reinvested) by 2013 whereas a \$1 invested in Small Caps would have grown to \$29,400.

We set up the Appian Small Companies Opportunities Fund (ASCOF) in October 2012 to allow investors to invest in the Small Cap theme. Our investment process worked. We invested in well-managed businesses with strong cash generation and healthy balance sheets, bought at attractive valuations. They grew earnings and dividends, some made transformational deals, while others were taken over.

The Fund has delivered a positive return of 72% since inception (or 9% annualised, within our long-term target return range of 8-10% p.a), notwithstanding a challenging year in 2018. While Small Caps have outperformed historically, they have experienced periods of high volatility. These usually coincide with bouts of market stress, such as the 2007-09 period and more recently, 2018. Consequently, the pattern of returns over time from Small Caps can be very uneven as was seen in 2013 and 2015 when the Fund appreciated c.30% each year.

After a tough 2018 does our Small Cap investment process remain valid? There are some

parts of the market where we struggle to find attractive opportunities. For example, we currently own few US stocks in the Fund, partly because valuations are less attractive and partly because many US Small Caps carry relatively high levels of debt. But overall, we have been able to identify attractive opportunities and have built a portfolio of stocks with the following attractive characteristics:

- **Strong Quality**: The average cash return on capital of our companies is 12.2%, and our companies have strong balance sheets with little or no debt.

**Jungheinrich**, the German forklift producer is generating a cash return of 13.3% and is expected to be in a net cash position within a year.

- **Attractive Valuations**: the average P/E of the portfolio is 11.5x, lower than what it is has been for most of the Fund's existence.

**Strix**, the world's leading producer of kettle safety controls is a high-quality business, but has a P/E of just 10.2x.

- **Growing Companies**: This year, our Small Caps are expected to grow earnings by 9% on average and have delivered earnings growth of 19% p.a. on average over the past five years.

**Kingspan**, has delivered average annual earnings growth of 32% over the past five years, with a further 13% expected this year.

- **Robust Dividends**: The companies in the portfolio have an average dividend yield of 4.0%. Strong cash generation together with robust balance sheets within the Fund's companies reinforce the potential for good future growth in these dividends.

**Somero Enterprises**, yields 6% having increased its dividend six-fold over the last four years.

### **Conclusion**

The fundamentals of the stocks owned by the ASCOF are attractive in our view. We are available to meet with any who wish to discuss this in more detail. A portfolio of high-quality businesses, paying healthy dividends with good potential to grow, and trading on attractive valuations represent a solid platform from which good returns can be built over time.

**We are hosting a conference call on Thursday 14<sup>th</sup> February at 10am to discuss Small Caps and the ASCOF in more detail. Click on the link below for more details.**

## Conference call details



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## Appian Unit Fund Prices

4 February 2019

Appian Value Fund	<b>144.63</b>
Appian Equity Fund	<b>183.60</b>
Appian SCOF	<b>172.08</b>
Appian Liquidity Fund	<b>104.82</b>
Appian Ethical Value Fund	<b>101.52</b>
Appian Burlington Property Fund	<b>120.74</b>

For more detailed information on each of our funds click [here](#)

# Investment Team



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