Results analysis: BlackRock Smaller Companies

BRSC has outperformed the index in a challenging period...

Update
15 May 2024

- **BlackRock Smaller Companies (BRSC) has released its financial results for the year ending 29/02/2024. Over a challenging period for the asset class, the trust has seen its NAV total return decline by 3.6% (debt at fair value). However, this represents an outperformance of BRSC's benchmark, the Deutsche Numis Smaller Companies plus AIM (excl. Investment Companies) Index, which declined by 5.8%.**

- **BRSC's share price total return outperformed the benchmark by 5%, (falling slightly over the year in absolute terms by 0.8%).**

- **NAV performance over the longer term remains strong with BRSC having outperformed the benchmark index cumulatively by 7.8% over the past five financial years and by 63.7% over the past 10 years.**

- **Total dividends increased to 42p per share over the year, representing a total dividend year-on-year increase of 5% on the previous financial year. There was a marginal decrease of 0.5% in BRSC's revenue return per share, however, the board has been able to take advantage of the investment trust structure utilising its substantial distributable reserves. Dividends have increased by 10.9% a year since 2003 - solidifying BRSC's 'Dividend Hero' status.**

- **Over the period, BRSC's shares traded at a discount of between 7.8% to 15.1%. During the financial year the board bought back 1.5 million shares, delivering an uplift to NAV per share of 0.3%. Subsequently, BRSC's discount has narrowed slightly to 12%, as at 13/05/2024.**

- **The trust's gearing increased over the financial year from 6.3% of net assets to 11.5%, reflecting the manager's optimism around the asset class and the favorable rate agreed on the long-term borrowing facility.**

- **Board Chairman Ronald Gould said: "Despite this challenging backdrop, it is comforting to note that many of our portfolio holdings continue to deliver against their objectives." He also noted ... "[The] company's portfolio is weighted towards companies with well capitalized balance sheets and entrepreneurial management teams that are able to rapidly adjust their businesses to the shifting market dynamics.**

As such we believe your company is well positioned and prepared to take advantage of the investment opportunities that lie ahead despite the uncertain market conditions."

Analysts:

Nicholas Todd
nicholas@keplerpartners.com

Kepler View

BlackRock Smaller Companies (BRSC) has a strong long term track record of generating alpha, reflecting the strength and consistency of the team's bottom-up approach, in our view. However, the past couple of years have proven to be a particularly challenging environment for UK small and mid-cap equities. A combination of uncertain macroeconomic conditions, particularly the higher level of interest rates, continues to have a negative impact in fund flows for the asset class, reflecting investors' negative sentiment towards the higher risk that is associated with investing at this end of the market cap spectrum. That said, optimism around future interest rate cuts, albeit to a lesser extent than was expected in Q4 last year, has seen BRSC's performance pick up in 2024, improving the outlook for the strategy.

Roland believes the focus on identifying high-quality companies that are cash generative and that have a competitive advantage, should uncover attractive opportunities to create long term value. He argues that corporates are operating with stronger balance sheets than the market is pricing in. Combined with factors such as low unemployment, and a rising level of consumer confidence, this gives him the assurance that the outlook for his holdings is for a sustained earnings recovery. Companies such as 4imprint act as a good case study to the team's investment philosophy; it remains a top contributor to performance and continues to convert profits into cash whilst investing in both their products and people to maintain market leadership and pricing power – characteristics that are particularly important in an inflationary and higher rate environment.

Even though many of the drivers of uncertainty and volatility may continue to impact UK smaller companies, Roland believes this is providing a range of high-quality and attractively valued opportunities in the UK small and mid-cap market. In part, this has been reflected through the positive contributions coming from private equity bids for Ten Entertainment Group, Ergomed, City Pub Company, and Numis over the course of the last financial year. That said, we would echo Roland's thoughts that whilst takeover activity is positive for overall performance, it forces the sale of businesses that could contribute to NAV growth over the longer term, meaning they must find suitable replacements. The consumer and industrials sectors remain core areas of interest for the team. Consumer cash flows are starting to improve following a couple of years of pressure, and the impacts of the inventory unwind suggest that market demand should be more closely correlated to industrial company revenues, with the structural drivers associated with re-shoring providing a multi-year tailwind for industrial companies.

In our view, Roland's "cautiously optimistic" increase in gearing and BRSC's current discount of 12.0%, which compares to a five-year average discount of c. 8%, may present an attractive long-term opportunity for investors and provide added fuel to the return potential should investors' attitudes to UK small and medium sized companies improve. In addition, BRSC's 2.8% dividend yield can provide a helpful contribution to total returns and is backed by a substantial revenue reserve.

Click here to read the FY report on RNS

Click here to read our latest research on BRSC

Click here to add BRSC to your watchlist

Disclaimer

This report has been issued by Kepler Partners LLP. **The analyst who has prepared this report is aware that Kepler Partners LLP has a relationship with the company covered in this report and/or a conflict of interest which may impair the objectivity of the research.**

Past performance is not a reliable indicator of future results. The value of investments can fall as well as rise and you may get back less than you invested when you decide to sell your investments. It is strongly recommended that if you are a private investor independent financial advice should be taken before making any investment or financial decision.

Kepler Partners is not authorised to make recommendations to retail clients. This report has been issued by Kepler Partners LLP, is based on factual information only, is solely for information purposes only and any views contained in it must not be construed as investment or tax advice or a recommendation to buy, sell or take any action in relation to any investment.

The information provided on this website is not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject Kepler Partners LLP to any registration requirement within such jurisdiction or country. In particular, this website is exclusively for non-US Persons. Persons who access this information are required to inform themselves and to comply with any such restrictions.

The information contained in this website is not intended to constitute, and should not be construed as, investment advice. No representation or warranty, express or implied, is given by any person as to the accuracy or completeness of the information and no responsibility or liability is accepted for the accuracy or sufficiency of any of the information, for any errors, omissions or misstatements, negligent or otherwise. Any views and opinions, whilst given in good faith, are subject to change without notice.

This is not an official confirmation of terms and is not a recommendation, offer or solicitation to buy or sell or take any action in relation to any investment mentioned herein. Any prices or quotations contained herein are indicative only.

Kepler Partners LLP (including its partners, employees and representatives) or a connected person may have positions in or options on the securities detailed in this report, and may buy, sell or offer to purchase or sell such securities from time to time, but will at all times be subject to restrictions imposed by the firm's internal rules. A copy of the firm's Conflict of Interest policy is available on request.

PLEASE SEE ALSO OUR TERMS AND CONDITIONS

Kepler Partners LLP is authorised and regulated by the Financial Conduct Authority (FRN 480590), registered in England and Wales at 70 Conduit Street , London W1S 2GF with registered number OC334771.