

Smaller Companies, Bigger Opportunities

Goodbody Asset Management

Global Small/mid cap equities offer a compelling risk/reward proposition

For many equity investors, bigger often implies better. Indeed, from our own experience, it is clear the vast majority of domestic Irish investors are chronically underrepresented in small/mid cap stocks.

Skewed by familiarity bias, investors often position their equity exposure towards companies that they feel they 'know', frequently comprising large cap companies, including the usual household names such as Apple, Exxon Mobil, or Diageo. However, by doing so they risk missing an exciting and rewarding part of the broader equity market.

The evidence is unambiguous: global small/ mid cap equities consistently outperform their large cap peers over time. Since 2000, the segment has outpaced large cap equities by almost 70% or circa 2% per annum, according to analysis by Bloomberg*. While this higher return does come with higher levels of volatility, on a risk adjusted basis the segment still delivers superior results for investors. As such, in our view it warrants an allocation in an overall portfolio of global equities.

So why do the shares of smaller companies outperform over time?

The performance reflects the attributes of the companies themselves. Due to their size and stage of development, these companies tend to offer significant profit growth potential. They are often led by entrepreneurial and dynamic management teams. They are also frequently benefit from takeover activity. The latter point is especially relevant in the current environment of moderate global economic growth. Combined with the availability of historically low financing costs, this makes small/ medium sized companies increasingly attractive takeover candidates to their large cap peers.

As an active investment team with an established and successful track record of investing in smaller companies, we have consistently found the smaller companies segment a fertile hunting ground for investments that can materially outperform over time. It is a very large universe of stocks that is typically under-researched and frequently neglected by investors.

Globally, the universe of small/mid cap stocks is over three times larger than the large cap segment. Yet the average number of research analysts providing coverage on the space is just a third of that in the large cap segment. Combined, this implies a tremendous opportunity for active investors such as Goodbody Asset Management, with a structured and disciplined process, prepared to put in the hard work to find undiscovered opportunities.

Companies such as Kingspan fit the bill perfectly. Kingspan is a company which a market value currently of €6.3bn, just a quarter the size of the average global large cap and less than 1% of the size of Apple, the world's largest publicly listed company. Headquartered here in Ireland, Kingspan is a manufacturer of high-performance building insulation, deriving most of its revenues from international markets.

The business, managed by an owner operator family, is benefiting from long term structural growth tailwinds, as tighter energy efficiency and building regulations drive higher penetration of insulated panels and boards. Product innovation and R&D investment underpin an exciting future sales and cashflow growth outlook.

Kingspan has a quality growth profile that in our view is yet to be fully reflected in valuation and is an example of the type of smaller company investment opportunity that we feel is too big to ignore.

The Goodbody Smaller Companies Fund is an actively managed, concentrated global equity Fund that offers investment in a diversified portfolio of ~40 small/mid-sized growth companies. The Fund aims to outperform the MSCI World Small/Mid cap index by 2-3% per annum over the medium to long term.

*MSCI World Small/Mid cap index vs. MSCI World Index, total return, euro, 28/02/00 - 28/02/18.



Paul O'Brien, CFA
Head of Investment *Asset Management*

Warning: The value of your investment may go down as well as up.

Warning: This fund may be affected by changes in currency exchange rates.

Warning: If you invest in this fund you may lose some or all of the money you invest.

The Fund is a unit linked fund of the life company. The value of your life assurance policy is linked to the performance of the Fund. Please contact your financial adviser or New Ireland to make additional premiums. Please refer to your policy documentation for information on fees, charges and risks that apply to your investment.

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