Rockwood Strategic (RKW LN)

Corporate Client

Investment Funds **Current price* 1415.0p**

Corporate

28 September 2022

Engaged Value Investing

Over the last three years, RKW has delivered exceptional NAV TR (+58%) as outcomes from its focused, active & recovery oriented investment strategy outweighed the wider macro-environment. We summarise the strategy as invest, transform and exit. A review of its portfolio highlights that investee's accounting for c35% of NAV look to be migrating into the strategy's third phase (exit) and management is guiding that their estimates of fair value suggests at least 60% upside. Whilst timing is uncertain, that c35% of the portfolio is at or close to exit mode suggests that there is an opportunity for significant idiosyncratic upside – in the meantime, we expect this potential to underpin the fund's NAV.

Strategy

RKW is a focused, value oriented, active UK microcap (mainly sub £100m mkt cap) investor. The strategy targets 2x money from individual investees over 3-5 years (15% IRR if held for five years). The fund is invested with a value and recovery mind-set. The manager, can and does, take significant stakes (>10%) in investees and seek board representation. RKW invests in companies where returns can be delivered, independent of the wider macro-environment as a result of operational, strategic or management change.

Performance

Over the three years to 31 August, the fund has returned 58% versus the Numis 1000 ex IC TR (N1000) +16.7% and the AIC UK Sm. Cos sector's return of 14.6%. RKW's NAV has been very strong (+3.8%) over the last year versus the N1000's return of -21.6%. One can easily attribute the recent performance to the maturity of key investees within the investment process. i.e. the upside from transformation (idiosyncratic risk) has outweighed the markets (systematic risk) general direction.

Portfolio

The portfolio is deliberately concentrated (up to 35 investees, top ten to account for at least 51% of NAV) to ensure that management has sufficient capacity to engage. The portfolio comprises seven core investees (Top 5 – 55% of NAV, single largest exposure c25% of NAV) and eight springboard/opportunity investments. We calculate the core investee's valuation multiple at 3.9x '23 est. EBITDA. At least two (c35%) investees are at or close to the third phase (exit) of RKW's strategy.

Manager

RKW is managed by Harwood Capital, an active smaller companies specialist. Harwood (£2.3bn AUM) is active in both the private and public markets including four investment trusts. RKW is differentiated from Harwood's other investment trusts by virtue of its focus on public markets and micro-cap investees. The lead portfolio manager, Richard Staveley started managing RKW in 2019 and since then he and the fund have moved to Harwood Capital.

Discount control, issuance and dividend

The board had taken the necessary authorities to repurchase shares and to issue new shares (at a premium to NAV). No shares have been repurchased since the fund reverted to an active investment policy. The board has expressed a desire to increase the fund's scale. The fund's board has adopted a policy of paying the minimum dividend permitted under the investment trust rules.

Valuation

Trading on a 10% discount versus an 11% average discount (12m and 3 years), RKW is trading in line with its history and tighter than the wider sector (13% current). The fund's rating may be attributable to its historic performance. As the market builds knowledge and confidence in the strategy and the trajectory of the investees, there is the potential for the discount to tighten further.

Key data

Yield (%)	Nil
Pub NAV (23 Sept)	1,575.5p
Discount (%)	10%
Market cap (£m)	36.0
Enterprise Value (£m)	36.0
Shares in issue (m)	2.5
Next Event:	01/12/2022 Interim results

	1m	3m	12m
Absolute %	1.4	3.3	-10.9
Rel. market %	8.5	4.2	-6.5

Share price chart

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Objective, Strategy and Portfolio

Rockwood Strategic (RKW) provides focused (up to 35 investees, currently 15), active, value oriented, UK microcap (mainly sub £100m mkt cap) stock specific equity exposure. The strategy targets 2x money from individual investees over 3-5 years (15% IRR if held for five years). The fund is invested with a value and recovery mindset and a focus on delivering a total, and not a relative, return that is independent of the wider macro-environment.

The portfolio manager, Richard Staveley, believes that value (as a strategy) will no longer be a terminal underperformer. He argues that the normalisation of interest rates has increased the value of tangible cash flows relative to the longer term (and less tangible) potential of growth investing. He also highlights that growth's dominance has culled the ranks of experienced value managers (such as the team at Harwood Capital) which has improved their competitive position.

The strategy is to invest in undervalued companies where RKW's management, led by Richard Staveley, has identified the potential to improve returns as a result of operational, strategic or management changes. Staveley estimates their universe at c1,000 companies, of which c300-400 are potentially credible investments and 50-60 (in addition to the portfolio) are actively monitored.

At its heart, RKW is a focused "recovery" style fund, where the concentrated approach allows de-risking via large stakes and active engagement rather than sit on the side-line and hope things get better, actually help drive, cajole and influence the speed and likelihood of recovery. This would be (a) a recovery in margins from depressed back to say "mean" (b) and in turn a recovery in valuation rating. The combination of the two drives the strong absolute return.

The portfolio comprises of up 10 core investees (c51-70% plus of the portfolio) plus a further 15-25 smaller positions (springboard and opportunity investments – split c50/50, 2-4% of NAV positions). Expanding on the smaller investments, Staveley highlighted that they enabled the fuller deployment of the fund's balance sheet and facilitated the establishment of core investments. Staveley categorises them as those whose potential (to become a core investee) is being evaluated (springboard investees) or more liquid opportunistic situations where the targeted return can be achieved but a large stake is not required to influence or generate change.

Once a core investee has been identified and a stake built, the team actively engages with the company to ensure the necessary changes occur. Activism is integral to their strategy. In their opinion, it is not enough to invest in a cheap company and hope that that the board/ management will make the necessary changes – proactive, constructive, engagement is required to ensure the change occurs. As part of the strategy, management can and does become directors of their investees. The Harwood team sits on four of their eight core investee's boards.

Key elements of each investment thesis include:

- How the Rockwood's management team will effectively engage with (influence the direction of) the investee; and
- The articulation of a take-private exit strategy (trade or private equity), including likely exit multiple and purchaser. The team expects c2/3rd's of their exits to occur via a corporate transaction and c1/3rd via the public market.

Discussing the exit process, Staveley noted that it could occur via bid (e.g. Augean -8.8x money multiple) or sale in the public market (e.g. RPS plc – 2.6x).

The team will not seek or target investments in privately held companies. However, they are permitted as part of a public-to-private transaction or as an investment in unlisted preferred equity or convertible debt in a public company.

Asked about how much AUM the strategy could handle, Staveley stated that they are comfortable up to £250m and would review the situation at this point.

Portfolio

The fund's current portfolio comprises seven Core investees and eight Springboard and Opportunity investees. Staveley expects the number of springboard and opportunities to grow overtime.

RKW's five largest investments (c55% of NAV) are summarised below; four of which fit the category of a core investment. The commonalties are as follows:

- An identifiable division with the potential for significant upside once the company's strategy has been appropriately re-focused; and/or
- A requirement for new management and/or the disposal of a problematic business line; and
- Sufficient influence to ensure that the necessary changes are made

Management teams often need encouragement and support to evolve a business, left to themselves the status quo can prevail. Staveley noted that they often need maximum influence during the exit process to ensure that all possibilities are fully considered.

In both examples where the manager has provided an estimate of upside (Crestchic and Centaur) they have chosen an exit multiple of 10x EV/EBITDA. Expanding he highlighted that these multiples reflect their expectation of what private equity or a trade buyer would pay for these businesses. A cursory review of the fund's largest holdings highlights a bias to Industrial and Media stocks. When challenged on this, Staveley highlighted that the investees' end markets were highly diversified. The industrials exposures range include the power market, parts distribution and hydraulics. Similarly, the Media exposures ranges from global advertising, B2B in the marketing and legal service sectors and financial services.

A review of the progress made by core investees (in the light of their 3-5yr time horizon) highlights that Crestchic (5+years, 25.4% of NAV) and Centaur (3 years, 9.3% of NAV) both look to be migrating to the third phase of RKW's strategy.

Figure 1: Top Holdings

Core Holdings	Board Rep.	Ticker	Age in 2023	Portfolio Wgt (%)	Rockwood Stake (%)	Total Harwood Stake (%)	EV/est23 EBITDA (x)
Crestchic (Northbridge)	Yes	LOAD	7 years	25.4	15.3	24.1	6.0
Flowtech Fluidpower	Yes	FLO	3 years	10.3	5.8	26.0	7.4
Centaur Media*	Yes	CAU	3 years	9.3	5.7	29.8	5.0
M&C Saatchi	No	SAA	2 years	7.5	1.6	1.6	3.8
Pressure Technologies*	No	PRES	4 years	7.4	13.8	13.8	9.0
Smoove (ULS Tech)	No	SMV		6.4	6.6	8.9	EV/S 1x
Van Elle Holdings	No	VANL		5.9	6.4	6.4	3.2
Bonhill	Yes	BONH		2.5	19.1	19.1	2.3
Total				**74.7**			**Wgt Av. 3.9x**

*Source: Rockwood Strategic, as of 31 Aug 2022. *Singer Capital Market is the broker to the company*

Top 5 Investees

Crestchic (LOAD, 25.4% of NAV), Mkt Cap £53m, 15.3% Stake (24.1% Harwood Group), position initiated in 2016

Crestchic specialises in power reliability, it manufactures, sells and hires load-banks on a global basis. Loadbanks are used to test generators and critical power supplies. Crestchic principle sectors include Data Centres, Energy Transition and Critical Infrastructure. The company is the largest manufacture and renter of loadbanks outside the USA. The Company is expanding its US business, it had distribution centre in Philadelphia and has recently opened one in Texas and is planning a third. In addition to the US market, the company is focused on expanding its better established European operations and is exploring the potential of the middle east. Following a recent (2021) decision to refocused on its core business (give the trends around electrification) cash generation has improved, the company has focused on growing its US and European businesses and its manufacturing facility been expanded by c50%.

The Manager expects demand to remain robust and EBITDA to continue to grow. FY21 EBITDA was reported at £5.1m (prior to the disposal of discontinued operations). Harwood is forecasting FY 22 and 23 EBITDA at £11m and £12m respectively and believes that the business should be valued at 10x EBITDA versus its current EV of c£75m; implying c60% upside from current valuations.

Discussing Crestchic's evolution since he started managing RKW in 2019, Staveley highlighted the appointment of Stephen Yapp in 2020 and RKW's Nick Mills (assistant fund manager) as NEDs, an evolution in the management of the company, the introduction of a suitable LTIP for the management team and exiting the oil services business.

Reflecting the modus operandi of the strategy (buy, fix and exit via either the private or public markets) and reflecting on the state of the company, we would characterise Crestchic as having exited the fix stage of RKW's process.

Flowtech Fluidpower (FLO, 10.3% of NAV), Mkt Cap £72m, 5.8% stake (26% Harwood Group), position initiated in 2020

Primarily distributes Fluidpower* components to a diverse range of customers with a strong bias to parts used for repair or maintenance reasons. **the use of fluids under pressure to generate, control, and transmit power (includes hydraulic and pneumatic systems).*

The company, an aggregator of fluid power specialists, is reporting subpar operating margins and has a stock-turn well below that targeted by management and achieved by peers. Staveley reports that management has recently established an ecommerce platform, is completing the integration of its acquisitions and is focused on improving margins and stock turn. Jamie Brooke, a member of RWK's Investment advisory group member, recently joined as NED. Flowtech's Chairman, Roger McDowell, was a NED at Augean Plc; a highly successful investment for RKW.

Flowtech is very much in the fix stage of the RKW process with at least 12 months until it migrates to the exit phase.

Centaur Media (CAU, 9.3% of NAV), Mkt Cap £66m, 5.7% stake (29.8% Harwood Group), position initiated in 2020

An international provider of business information, training and specialist consultancy. Its focus is on the paid provision of business intelligence, consultancy, training and lead generation.

New management was appointed in 2019 and adopted Margin Acceleration Plan 23 (MAP23) targeting 23% EBITDA margins & £45m of sales revenues by 2023. The company has been extensively restructured and digitised in the last few years with orientation to subscription based and premium content. A review of Centaur's management guidance (Interim results to 30 June 2022, published 20 July 2022) highlights an expectation that management will hit their MAP23 targets.

Reflecting on the state of the company and assuming Centaur hits its MAP23 targets, one could characterise Centaur as having exited the fix stage of RKW's process.

Singer Capital Market's is Centaur's broker and publishes research on the company. On 20th July 2022, SCM reiterated its Buy Rating with a headline of "*H1'22: Continues to deliver*" and a price target of 75p (current share price 44p, 26 September 2022)

M&C Saatchi (SAA, 7.5% of NAV), Mkt Cap £185m, 1.6% stake (1.6% Harwood Group), position initiated in late 2020

M&C Saatchi, the Global Advertising Company, had been in turmoil with the original Founders leaving, accounting errors and a poorly structured incentive scheme. The balance sheet has net cash and a new strategy to grow the business and improve margins has been unveiled. During COVID the business had no material client losses indicating the strength of their relationships. The fund invested in late 2020 when Management and Board changes started to take effect.

The investment in M&C Saatchi fits the team's Opportunistic category. The company was sufficiently undervalued that it offered the necessary 2x upside but because it had already initiated the changes required to deliver on its potential the fund didn't need to engender change.

Staveley observes that the progress through the fix stage has been disrupted by two bids (neither of which offer full value), they would be happy for the bids to fail and for the management team to complete its work.

Pressure Technologies (PRES, 7.4% of NAV), Mkt Cap £20.4m, 13.8% stake (13.8% Harwood Group), position initiated in early 2019

The company comprises two divisions Chesterfield Special Cylinders and Precision Machined Components (PMC). Chesterfield manufactures and services a range of end industries and customers including the Ministry of Defence and PMC manufactures high specification parts primarily for the oil & gas industry.

In 2020, the group undertook a series of management changes (new Chairman, new NED, new FD) and raised incremental capital to support the growth opportunity in hydrogen energy market.

The PMC division has suffered as result of COVID but should benefit from an improved oil & gas pricing environment resulting in higher activity levels. The Chesterfield business has a significant opportunity in the Hydrogen Economy; the business has the quality and specialist credentials. The end-market for Hydrogen storage, using their cylinders, could be significant with the potential for the company to become a key strategic supplier to the industry.

Staveley highlighted that there could be strategic value exiting the oil and gas industry in focusing the company on Chesterfield to capitalise on the secular growth offered by the energy transition.

Noticing that there still some strategic actions to be completed, one may conclude that Pressure Technologies is one step away from completing the fix stage of RKW's process.

Singer Capital Market's is Pressure Technologies' broker and publishes research on the company. On 27th September, SCM migrated its Rating from Buy to Hold with a headline of "*Return to profitability now expected in FY23*" and the price target was placed under review (current share price 35p, 11am, 27 September 2022)

Management Team & Manager

The fund's manager is Harwood Capital (£2.3bn AUM). Harwood specialises in active investment in smaller companies. See later, for additional information. On a day-to-day basis, the key personnel are Richard Staveley (Lead Fund Manager), Nicholas Mills (Assistant Fund Manager) and Christopher Mills (Advisory Company Member and CIO Harwood Capital LLP).

In addition, the team draws on a six strong (mainly external) team referred to as the Investment Advisory Group (IAG). The purpose of the IAG is to provide challenge to Staveley's investment thesis for core investments prior to investment. The team's job is to question not to decide, it is not an investment committee.

Figure 2: Harwood Investment Trusts

Fund	TNAV	Strategy
North Atlantic Smaller (NAS)	£750m	Investing in listed and unlisted smaller companies principally based in countries bordering the North Atlantic Ocean. NAS targets larger companies (up to £250m) than RKW and has greater exposure to private assets.
Oryx International Growth (OYX)	£225m	Small cap special situations and growth companies. The strategy targets listed and unquoted companies. Up to £250m mkt cap.
Odyssean (OIT)	£180m	A concentrated portfolio of well researched smaller companies, typically too small for inclusion in the FTSE 250. Constructive corporate engagement is a key part of Odyssean's approach. Up to £750m mkt cap.
Rockwood Strategic (RKW)	£40m	Valued oriented micro cap. Primarily up to £100m mkt cap.

Source: Harwood Capital

Asked about the potential for cross over and conflicts between the fund and Harwood's other strategies. Staveley highlighted that the Group provides substantive insights into the private SME markets without significant overlap and conflicts. The limited overlap (and conflicts) is a function of RKW's target market (sub £100m mkt cap) versus Oryx's and North Atlantic's £250m mkt cap ceiling and Odyssean's £750m ceiling.

That said, there are overlaps within the portfolio. Specifically, RKW's top three holdings are also owned by other clients of the Group.

Management team

Richard Staveley (Lead Fund Manager). Staveley has been managing UK Smaller company investments since 1999 and joined Gresham House plc in in 2019 to manage the fund. In May 2021, he left Gresham House and joined Harwood Capital in December 2021. Staveley sits on the boards of Bonhill Plc (BONH) and Centaur Plc (CAU).

Nicholas Mills (Assistant Fund Manager). Mills joined Harwood in 2019 after working at Gaballi Asset Management for 5 years. Mills currently sits on the board of Crestchic Plc (LOAD), Circassia Company Plc (CIR) and Hargreaves Services Plc (HSP).

Christopher Mills (Advisory Company Member and CIO Harwood Capital LLP). Mr Mills has been CEO and principal shareholder of Harwood since 2011. He is CEO of North Atlantic Smaller Companies Investment Trust (NAS LN) which he has managed since 1982 and Executive Director of Oryx International Growth (OIG) which he has managed since 1995. In addition, he is currently Chairman of EKF Diagnostics (EKF) and Renalytix AI (RENX).

Investment process

At the heart of Rockwood Strategic is a "value with a catalyst" mind-set. Success is defined as to a 2x money multiple over a three to five year period (a 15%plus IRR). The team is investing for a total return not a relative return.

The management team

- Seeks out proven businesses that have made a strategic error or require strategic change, or are performing poorly on an operational basis that has resulted in them being fundamentally undervalued by the stock market;
- Identifies the required changes, if they can bring sufficient influence to the situation to achieve change and what the upside potential could be; and
- Develops a thesis as to how they will exit their investment once their objectives have been achieved.

The actual process follows five stages:

- Idea generation, due diligence and expanded due diligence (3 stages);
- Engagement (1 stage); and
- Portfolio Management (including the exit, 1 stage).

The idea generation & due diligence segment is key. At this point in the process, the idea (which could already be a springboard investment, 2-4% portfolio weight) transitions to becoming a Core investment or gets sold.

"Core" investment status implies that the fund (and/or the wider Harwood group) has a sufficient equity stake to be influential and that Harwood will proactively engage with all stakeholders (management, the board and other shareholders).

The portfolio comprises of up 10 core investees (c51-70% plus of the portfolio) plus a further 15-25 smaller positions (springboard and opportunity investments – split c50/50, 2-4% of NAV positions). A springboard investment is designed to facilitate the team's engagement with the company's management and are often made a part of the due diligence process. An opportunistic investee (e.g. M&C Saatchi) offers the same return characteristics as the other allocations but does not require RKW to become activist because the board and management are already making the necessary changes.

Idea generation, due diligence

The investment process seeks to identify companies with proven businesses that have taken a strategic misstep. Their analysis is on estimating the investees value should its business be returned to its long term average margins and what steps are required for this to occur.

Staveley reports that their quant screens target metrics such as EV/Sales, price to book and historic (not current margins). He highlights traditional metrics such as p/e ratios are less useful as the types of companies targeted are often marginally profitable at the point of investment.

Engagement

The engagement process involves (where possible) meeting everyone; the board, management, suppliers/customers and shareholders. The purpose is to understand the stakeholders, their interests, any issues, their appetite for change and to clarify what change is required to transform the business. A review of RKW's portfolio highlights that necessary changes have included replacing management and/or exiting business lines.

As a non-control investor a key part of the strategy involves establishing if RKW can build a big enough coalition (shareholders, management and NEDs) to influence the direction of the business without creating a concert party. It is not unknown for RKW and/or Harwood to increase their stake to 29% towards the end of the 3-5 year investment period to assist in focusing management and the board on an exit strategy.

Portfolio Management

The portfolio management process combines active monitoring of the thesis and continued management engagement with regular site visits, client due diligence and engagement with the companies advisors. The team largely does not trade its position during this part of the process. At its heart, this element involves the continued building of their knowledge of and relationship with the investee, and the associated evolution of the investment thesis.

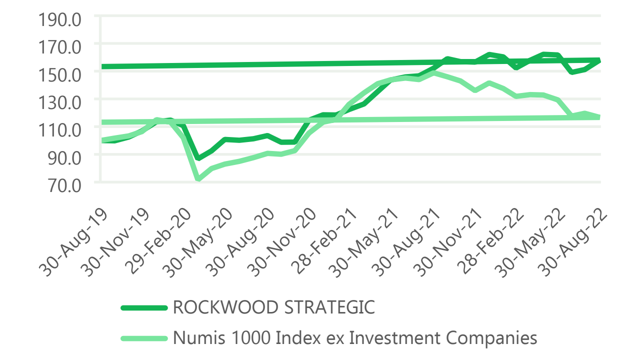
Performance

The fund has existed since 1999 and pursued a myriad of strategies. We have selected 1st September 2019, reflecting when Richard Staveley first started managing the fund. Discussing the 24 strong AIC UK Smaller Companies peer group with Staveley, we categorised:

- Six funds as pursuing activist & focused micro-cap investment strategies (e.g. Strategic Equity Capital (SEC), Odyssean (OIT) and Downing Strategic Microcap (DSM));
- Two funds as pursing diversified micro-cap strategies (River and Mercantile Smaller (RMMC) and Miton Micro Cap (MINI); and
- The balance (16 funds) as pursuing generalist, diversified, small cap investment strategies (e,g, BlackRock Smaller (BRSC), Aberforth Smaller (ASL) and JP Morgan UK Smaller (JMI)).

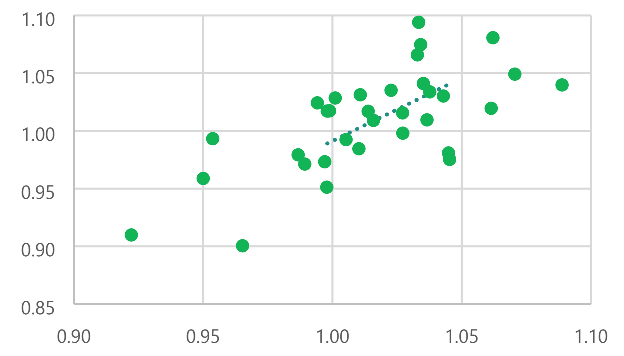
RKW has an absolute return objective and an idiosyncratic risk and return profile. In light of this, we have elected to compare its performance against the NUMIS Smaller Co 1000 (ex IC) index (N1000) over the long term (min 3 years) and against its total return objective (> 2x money from each investee over 3-5 years). We regard the N1000 index as an appropriate proxy for a more vanilla approach (systematic risk) to UK small cap investment.

Figure 3: Investment Performance



Source: Company data, Singer Capital Markets calculations as of 31 August 2022

Figure 4: Regression Analysis



Source: Singer Capital Markets. Monthly returns. Calculations as of 31 August 2019-2022

An analysis of RKW's performance against the N1000 over the three years to 31 August 2022 highlights significant out performance (NAV TR +58% versus the N1000's 17% return). Surprisingly, RKW and the N1000 have similar statistical characteristics; 20% volatility versus 25%, 20% downside deviation versus 26%, a 1.1 beta and a 0.8 RSQ. RKW's recent performance has shown a significant divergence from the N1000. Given this, we would expect a short-term statistical analysis to exhibit a greater degree of divergence from the N1000.

The vast bulk of RKW's outperformance has been driven by the robustness of its NAV since August 2021 and particularly during 2022 YTD. Discussing the performance, Staveley highlighted that it had been underpinned by the performance of exited core investees such as RPS Group (2.6x mm), National World (2.9x mm) and Augean (8.8x mm). More recently, Crestchic has driven returns.

We attribute this performance to the increasing maturity of some of the fund's key exposures; resulting in the fund's NAV being driven by idiosyncratic rather than systematic considerations.

Figure 5: UK Smaller Companies IT Performance - NAV TR

Fund	1 YR	3YR
AIC Small Cap Sector	-25.9	14.6
Numis 1000 ex IC TR Index	-21.6	16.7
Rockwood Strategic	3.8	58.0
Strategic Equity Capital	-9.0	27.1
Odyssean IT	-0.4	61.9
Downing MicroCap	-16.8	11.2
Oryx International Growth	-23.7	45.2
Miton MicroCap	-26.3	47.0
R&M MicroCap	-40.4	2.0
Aberforth Smaller Companies	-20.5	13.4
abrdn UK Smaller Co	-34.8	8.6
Blackrock Smaller Co	-30.1	13.8
Henderson Smaller Co	-32.7	11.4
JPMorgan UK Smaller Cap	-32.4	26.6

Source: AIC, Singer Capital Markets as of 31 August 2022

Reflecting the concentrated nature of the portfolio and its activist approach, we expect RKW's performance to be lumpy and diverge significantly from the wider market especially over the short term. In the long term, we define success as delivering 2x money over 5 years or less (the manager's specific target for investees) and outperforming the UK Smaller Companies index (an alternative small cap investment strategy). 2x money over 5 years, translates into a 15% IRR.

Over 1 and 3 years (Figure 5), RKW has outperformed the UK Smaller Companies index and RKW is ranked first over one year and second (to Odyssean) over three years. Given that its 3 year NAV TR (+58%) annualises at 16.5%pa, we view RKW as being on track to double its money over a 3-5 year period.

Corporate

Rockwood Strategic was incorporated in 1999, began its life as a tech vehicle (Newmedia Spark PLC) and has since undergone several repositioning's. On 25th April 2022, shareholders approved the adoption of active investment policy and on 4 May the company changed its name to Rockwood Strategic plc.

Rockwood is not an investment trust. It is the director's intention to apply for investment trust status from 1 April 2023.

The company has 2,541,046 ordinary shares in issue.

Issuance Strategy, Discount Control & Life

In the event that the fund trades at a premium to NAV the company may issue new ordinary shares. The board would like to increase the scale of the company.

The board has shareholder authority to repurchase up to 14.99% of the fund's issued capital. The authority maybe employed with a view to increasing NAV or assisting in controlling the discount to NAV. However, in the light of the concert party (owning 29.9% of issued capital) it is the board's and manger's view that for the foreseeable future any discount will be addressed through marketing, promotion and sustained investment performance driving excess buyers over sellers.

The fund has neither a fixed life or provisions for a continuation resolution.

Dividend & Policy

In the year ending 31 March 2022, the company did not pay a final dividend stating that the company would use capital to compound NAV.

The company's policy is to pay-out at least 85% of portfolio income net of expenses as dividends, retaining capital for re-investment. This is the minimum pay-out ratio to comply with the requirements of the Investment Trust rules.

Gearing and Policy

As of 31 March 2022, the company was not levered and did not have a borrowing facility. The company's policy is to restrict gearing to no more than 20% of gross assets, calculated at the time of drawdown of the relevant borrowings.

Management's current intention is not to lever the company.

Manager, Contract & Fees

Harwood Capital was appointed manager of the fund in October 2021. As a result of the change of investment strategy in April (from realisation to investment), Richard Staveley will act as lead fund manager, advised by Christopher Mills (founder of Harwood Capital)

Harwood Capital Management Group ("HCMG") has £2.3 billion of assets under management invested in public and private equities and managers three other investment trusts (North Atlantic Smaller Cos (NAS), Oryx Intl Growth (OIG LN) and Odyssean (OIT)). Harwood takes an active interest in the running of the companies in which they are invested. The aim is to add substantial value by enhancing the businesses.

Management Agreement

Harwood's appointment as investment manager is subject to a minimum term of one year, expiring on 5 November 2022. The agreement it terminable on not less than six months notice. As part of the agreement, Richard Staveley and Christopher Mills are deemed key individuals under the agreement. In each case a replacement key individual may be nominated.

Until the company's NAV is equal to or greater than £60m the management fee shall be £120,000 (inc VAT). Once the threshold has been passed the fee rises to 1% of NAV assets per annum.

In addition, the manager is entitled to a performance fee equal to 10 per cent. of outperformance over the higher of a 6% pa total return hurdle and the high watermark. The 6% pa compounding weekly and the performance fee will be calculated annually.

Provided that the Company's average NAV is at or below £100 million, performance fees in any performance fee period are capped at 3 per cent. of the Company's average NAV for the relevant performance fee period. In such instance, performance fees in excess of the 3 per cent. cap will not be paid and will instead be deferred into the next performance fee period.

If the average NAV exceeds £100 million, the performance fee shall be further limited such that the combined investment management and performance fees shall not exceed 3 per cent. of the Company's average NAV. In such instance, performance fees in excess of the cap will not be deferred and will not become payable at any future date.

We estimate the fund's ongoing expenses at c1.5% pa (pre-performance fees).

Board

The fund's board comprises Noel Lamb (Chairman), Kenneth Lever (Chair of the Audit Committee and Paul Dudley (NED). All three directors are independent NEDs.

Major shareholders & Concert party

Rockwood and Harwood have entered into a relationship agreement. Items covered by the agreement includes restrictions on Harwood's voting rights. On almost all matters to be approved by Shareholders, Harwood has restricted its voting rights in respect of any shareholding it has in excess of 10%. Harwood retains its full voting rights in matters related to a change in going concern status, tender offers and investment policy or investment strategy changes.

Harwood together with Richard Staveley, the lead fund manager, own 29.9% of the company and are considered to be acting in concert.

Figure 6: Major shareholders

Shareholder	% Held
Harwood Capital	28.9
James Sharp & Co	7.2
Unicorn Asset Management	5.4
River & Mercantile Asset Management	4.9
Smith & Williamson Investment Management	4.3
Investec Wealth & investment	3.9
Local Pension Partnership	2.5
Premier Miton	2.5
Total	59.6
Company data as of 31 March 2022	

Source: Company data, Singer Capital Markets estimates

Important disclosures

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Recommendation/Target price

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