UNIPLAN
A BETTER ALTERNATIVE

"I'm not going to say I told you so. But I did."
-***Nouriel Roubini***

Mean Reversion As Anticipated

After an historically difficult Q4, with our benchmarks down over 22%, we penned our yearend report in January with an observation about rolling returns and mean-reversion within the micro cap sector. The key thought is reprinted below:

> *"As what would be mathematically expected given mean reversion, each period of either return acceleration or deceleration is followed by the opposite with the average rolling 12 month expected return being 15.7%...micro caps are currently experiencing a relatively deep and lengthy deceleration of returns. Although there could be more downside, **one would expect mean-reversion to begin to emerge at some point in the near future and appears to be reversing given the January rebound as of this writing"**.*

The complete Flash Report with the supporting statistical analysis can be found on our website at: https://uniplanic.com/micro-cap-flash-2018-q4/.

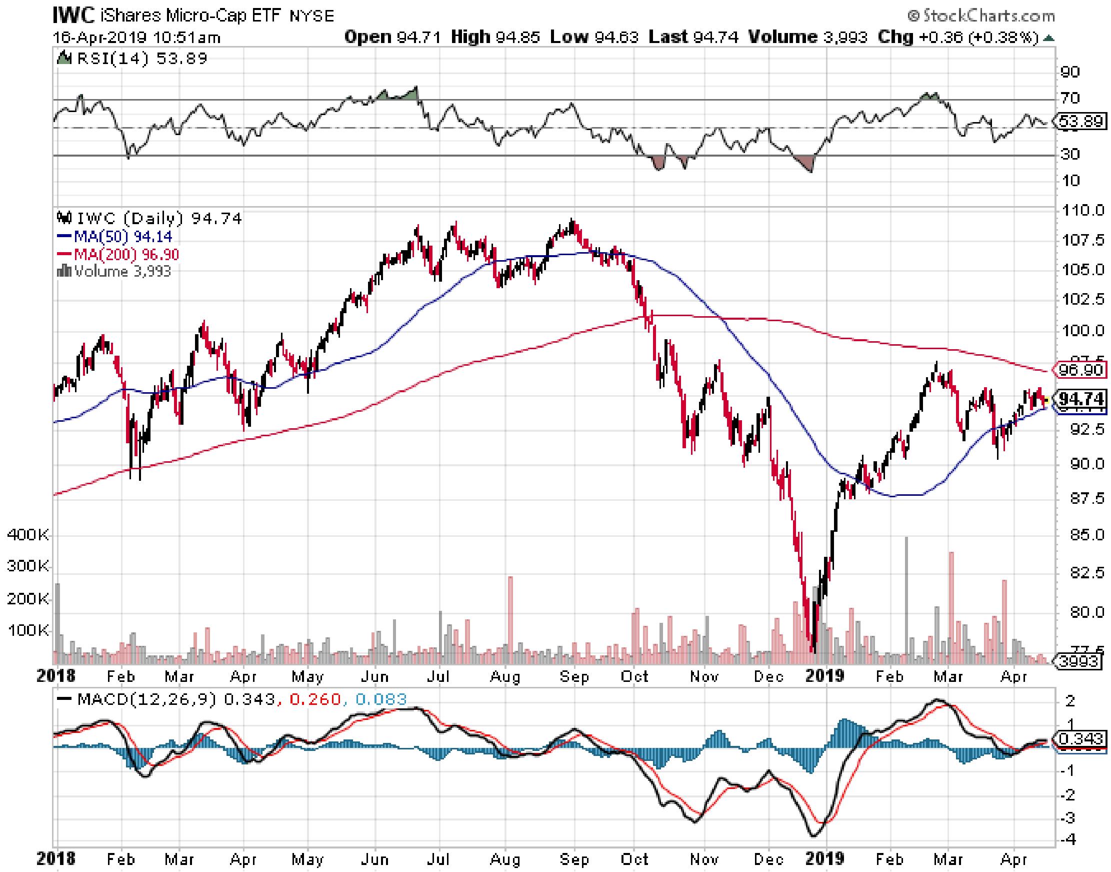
Summary for 2019 Q1 –

For the year-to-date period ended March 31, 2019, the ***preliminary estimated*** investment results for the Uniplan micro cap portfolio are as follows:

	QTD	YTD
Uniplan Micro Gross	21.67%	21.67%
Uniplan Micro Net	21.04%	21.04%
Russell Micro	13.10%	13.10%
Wilshire Micro	15.18%	15.18%

Beginning in June of 2018, micro cap stocks moved sideways into the fall and peaked in September. Then they began a steady and relentless decline right into late December. The impact of tax selling and the shadow of overall market volatility which put many market participants into a "risk-off" mode late last year were certainly contributors to the decline. By early January micro caps had gained about 5%YTD;

Investors were hopeful the downward slide had ended. Then an unprecedented change in Fed Policy sent the US equity markets into a strong rally that has continued to date.



Source: StockCharts.com

The catalyst for the astonishing market turnaround, of course, was Federal Reserve Chairman Powell's remarks at a press conference on January 4, 2019. On that day, in a stunning about-face, he announced the Fed's willingness to show restraint in moving interest rates higher. Immediately, the markets were off to the races based on these more dovish comments. The prevailing outlook concerning fears of three to four rate hikes in 2019, shifted suddenly to active discussions of rate *cuts*. By the quarter's end, the Russell Microcap Index was up 13.1%; the Wilshire Microcap Index gained 15.2%.

It is important to note that when a rebound begins, it lasts on average for seven months and the returns on average are +31%. So, if January was the start of the recovery, and the track record of past rebounds for small caps repeats itself, the rally has some duration remaining. We continue to find interesting businesses at attractive valuations despite the recent rally.

A Quarter of Adversity = Opportunity for Patient Investors

Due to liquidity constraints and the effects of information flow, being a patient long term investor is an important factor in micro cap investing. For that investor micro cap stocks offer better return opportunities than any domestic equity class. In looking back at the history of micro cap securities they are often punctuated with periods of extreme volatility. It's easy to argue that we are in one of those periods of volatility. As such, we often look to those periods as a guide when we reposition and evolve the portfolio.

During Q1 we made some adjustments in positions and holdings given the window of opportunity and increased trading volume in the market. Key among them was reducing our exposure to financial stocks which was modest to begin with. But given the reversal in Fed policy and the subsequent flattening of the yield curve the change seemed prudent. In addition, we sold two positions which had not met the investment thesis which we had anticipated.

Risk management is also a part of the micro cap portfolio management process and to that end we trimmed the size of two positions which had done very well and thus had become a higher-than-desirable percentage of the portfolio. The first, Innovative Industrial Properties, (IIPR-NYSE) an owner of industrial real estate focused on the growing operations of medical marijuana producers, gained +81% during the quarter prompting us to lower our exposure.

Source: StockCharts.com

The second position reduction was a medical testing company, Neogenomics (NEO-NASDAQ). The stock had moved up about +150% over the trailing twelve months with a very strong move during the first quarter. The position had grown to around 5% and as a risk mitigation measure, we trimmed the size back to a 3% position.

Source: StockCharts.com

With proceeds from the changes we initiated eight new positions in the portfolio which we had been watching for some time. These stocks formerly were at prices higher than we were willing to pay or had not met certain threshold events that we deemed important in the evolution of their business plan. So, for the Uniplan Micro Cap portfolio it was a busy and exciting quarter.

Requiem for the Sell Side; Less Efficiency = More Opportunity

Over the years we have argued that investing in micro cap stocks can offer excess returns because of the inefficient information flow regarding the thousands of small companies which populate this space. Do your homework, be mindful of valuation and actively manage risk; this is the road to adding alpha in a micro cap portfolio. This thesis in part, is supported by the fact that very few micro cap companies have meaningful sell side research coverage. As a result, doing primary source research can often lead to gaining insights and finding opportunities long before the investing public learns about these facts.

Is there anything that a portfolio manager can learn about Alphabet (Google) that the 80+ analysts who cover the company don't already know? Highly unlikely. But is it possible to learn valuable insights about a $500 million market cap company that has no analyst coverage? Yes. Not only is it possible, but it often takes months for the broader market to discover these companies, usually as those insights translate into higher earnings or important milestones which naturally attract the attention of investors.

Beginning in 2018, the micro cap market became less efficient as the sell-side investment research world continued to shrink with the implementation of something called MiFID II in the Eurozone. The rules, known as Markets in Financial Instruments Directive Part 2, requires investment managers to pay for investment research in hard dollars (cash) which they had heretofore been receiving at no cost in exchange for directed brokerage activity. The regulatory mandate is intended to ensure that asset managers are obtaining value for client monies spent on brokerage commissions and research information.

The unintended consequences of regulation like this are manifold, but it certainly seems that the world of sell-side research, which was already shrinking, will get even smaller. MiFID II has become another cost and compliance burden with the largest investment management firms, who have the biggest amount of research dollars to spend, are changing the landscape of the sell-side research world. The outcome of this paradigm has been large sell side firms providing research covering large companies which are what large money management firms tend to buy and sell. The net result is that mid-tier firms, who produce comparable research on a few big names while extending coverage to smaller companies, are quickly becoming obsolete. The best analysts are leaving as margins and pay are squeezed and the coverage universe of most firms is shrinking. The net result is that fewer analysts than ever cover small and micro cap companies. This continues to drive less efficiency which equals more opportunity for adding value in the micro cap segment of the public securities market.

"China Resistant"

As rumors, headlines, leaks and a few actual events gave hope that lasting trade agreements had at last been reached, the fact remains: nations have yet to make substantial progress between themselves so trade and tariff issues remain unresolved. The markets surge at the faintest ray of hope only to fall back in a few days when it is revealed that no agreements have been reached. Again, this lack of international cooperation has caused increased market volatility, decreased investor sentiment and damaged the valuations of many global companies.

It is likely that the global trade situation will remain a potential irritant to the markets and may continue to cause uncertainty for the outlook of US global companies. The most impacted is the chief trading partner of the US which is, of course, China. But does that mean most US-domiciled small cap stocks will necessarily be affected? Perhaps. But more importantly for our clients: will the names in the Uniplan Microcap Portfolio be affected?

To answer that question, we decided to look more closely at each of the names in the portfolio. When the portfolio is put under the microscope, you will find that 86% of the aggregate sales of the Uniplan holdings are within the United States. Further, there are just four companies in the portfolio that source some content from China. We spoke to the managements of each of these four companies and found that none use China as a sole source for parts or materials and each has alternative sourcing as a backup should normal supply channels be interrupted. So, the answer to the second question is that the Uniplan micro cap portfolio holdings should not be materially impacted by trade disruptions with China. Thus, we characterize the portfolio as "China resistant".

In addition, small business confidence continues to remain strong due to a combination of 2018 tax cuts, the current Administration's economic policies and the reduction of regulations. These factors coupled with the availability of capital cause us to believe the outlook is positive for business in general and micro caps in particular.

Conclusion

Using past cycles as a guide, it appears that small cap stocks still have significant gains ahead despite the broader market's rise since early January. Part of the recent increase has been a reversion to the mean which Uniplan anticipated. Research has shown that this return premium is the result of the limited liquidity in smaller companies and the lack of research or analyst coverage on many of these companies. We see opportunity in finding companies that have little coverage, those names where we can add value by doing thorough research, versus larger firms covered by dozens of analysts. Stated differently, we see benefits in taking advantage of the inherent market inefficiencies available in small caps, inefficiencies that large institutional investors cannot exploit. In addition, Uniplan's investments have very little overlap with China; almost 90% of collective revenues are made domestically. Given this picture, we believe micro cap stocks should be part of most well-diversified portfolios.

Richard Imperiale
Chief Investment Officer

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The Uniplan Micro Cap Portfolio is a low-turnover high-conviction micro cap strategy designed to offer investors a quality alternative to private equity having a similar unlevered return while providing daily liquidity. The Uniplan core investment thesis is focused on companies trading at a low multiple of cash flow or EBITDA, those with little or no debt and meaningful insider holdings. We search for smart money activity which we define as insider buying which is found in 13G/13D filings. A cash dividend and an identifiable macro or company-specific catalyst are preferred.

Important Information: 1. Uniplan Investment Counsel is a boutique investment firm, with roots dating back to 1984, that manages a variety of portfolios primarily for US clients. Uniplan maintains a complete list and description of composites that is available upon request. 2. The composite was created August 1, 1999. Performance is calculated in US dollars utilizing a time-weighted total rate of return. Total return for the composite is represented by the asset-weighted returns of the portfolios within the composite. Trade-date valuation is used. 3. Performance is net of all transaction costs and net performance is net of transaction costs and (maximum allowable total) investment management fee, but before any custodial fees (that may be incurred separately by the client). 4. The benchmark for the composite is the Wilshire US Micro Cap Index that represents a float-adjusted, market capitalization-weighted portfolio of all stocks below the 2,500th rank by market capitalization in the Wilshire 5000 at March 31 and December 31 of each year. The index is used to measure small stocks and is adjusted to reflect the reinvestment of dividends, when applicable. It is not possible to invest directly in an index. The index figures do not reflect any deduction for fees, expenses or taxes. 5. The dispersion of annual returns is measured by the standard deviation of asset-weighted portfolio returns represented within the composite for the full year. The standard deviation of the annual returns for the period August 1, 1999 to March 31, 2019 is 18.19% for the composite and 24.89% for the Wilshire Micro Cap Index. 6. The composite does not have a minimum size criterion for composite membership. All fee-paying discretionary accounts with similar investment objectives are included. Leverage is not used in this composite as a means to generate higher returns. There may be non-fee paying portfolios in the composite. Individual account holdings may vary depending on numerous factors including the size of an account, cash flows, and account restrictions. 7. There have been no changes in the personnel responsible for the management of this composite. 8. The composite contains both traditional and wrap fee portfolios. Uniplan has a flexible and negotiable fee schedule reflecting the differences in size, composition and servicing needs of clients' accounts. A complete description of investment advisory fees is contained in Uniplan's Form ADV and is available upon request. 9. Uniplan Investment Counsel does not claim GIPS Compliance. Individual account performance may vary from the results shown because of differences in inception date, restrictions and other factors. 10. Investors should understand that micro cap stocks are subject to a higher degree of risk than other equity investments due to the small size of the companies and the limited trading volume inherent in micro cap stocks. 11. This information is not an offer to buy or sell a security nor does it constitute investment advice or an offer to provide investment advisory or other services. All information is subject to correction or change. **Past performance is no guarantee of future results. Investment involves a risk of loss.**

All investments carry a certain degree of risk, including possible loss of principal. It is important to review your investment objectives; risk tolerance and liquidity needs before choosing an investment style. Value style investing presents the risk that the holdings or securities may never reach their full market value because the market fails to recognize what the portfolio management team considers the true business value or because the portfolio management team has misjudged those values. In addition, value style investing may fall out of favor and underperform growth or other style investing during given periods.

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