

Montanaro, an independent specialist fund manager, was established in 1991 to research and invest in UK and Continental European quoted SmallCap companies. Funds under management are currently c. £1.1 billion. The Focus Fund mainly invests in UK quoted small companies below £1 billion in size. A limited number of collective investments may also be held. The objective is long-term capital appreciation of at least 10% p.a.

Monthly Review

In a difficult market environment marked by events that will make their way into our history books – the Arab Spring, Japan’s deadly tsunami, two European bailouts, the loss by the US of its perennial AAA rating - we are pleased to report that the Fund ended the year 13% ahead of its benchmark and 2% ahead of the All Share.

The strongest contributor in December was **NCC**, the UK’s leading provider of escrow and assurance testing solutions, which climbed 26% as the company continued to benefit from good demand for its anti-hacking and website testing business. **SDL**, a software company that offers multilingual content services and web content management, reached an agreement for a cash offer for all Alterian shares. **Renishaw**, the UK-based producer of high specification sensors used in precision engineering applications, saw investors return following a less strong November.

On the downside, **Domino’s Pizza** declined on tough like-for-like comparables in Q4, coupled with decreasing consumer confidence and an unusually warm winter. Management subsequently confirmed that full year profits would meet consensus. **Latchways**, which specializes in the provision of fall safety equipment to construction, oil service and energy markets, experienced some profit-taking following a good set of interim results. Shares in **Ocean Wilsons**, a port operator in Brazil, fell following a quarterly loss owing to currency fluctuations, announced in November.

In December we visited the offices of **Brooks MacDonald**, a discretionary private client wealth manager. Growth has been phenomenal since listing in 2005, with AuM and profits having grown by 39% and 45% CAGR respectively over this period. We decided to visit their offices to judge whether or not they have the infrastructure in place to deal with this pace of growth.

We were given a walk through their “front to back” IT system, Figaro, and were updated on their current project which is to bring in house the

remaining 15% of their back office functions which are still outsourced. This project will increase capacity levels considerably.

The visit strengthened the investment case. We feel comfortable that the company can handle further inflows and expect growth to continue. Management has been investing in the business steadily over the years, at the expense of margins. However, when investment slows we should see considerable margin expansion.

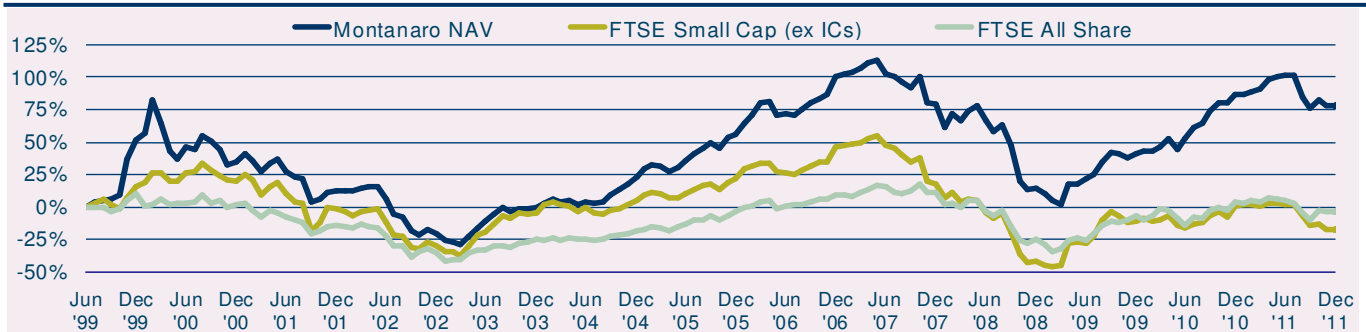
As we enter 2012, two of last year’s themes will inevitably continue to dominate market sentiment: the EMU’s transition from a currency to a fiscal union; and the tug-of-war between monetary deflation and fiscal consolidation. Elections in the US, China and France will also be important milestones. German-led austerity may well tip Europe’s economy into a mild recession. Politicians everywhere are in the driving seat and as investors we are at their mercy perhaps to a greater degree than ever before. 2012 will be a volatile year.

However, companies are sitting on large cash piles which will need to find a home. We see room for M&A activity to gain steam as large firms start looking at external growth to offset slowing earnings growth.

In stark contrast to last year, investor portfolios are positioned defensively with larger cash allocations, a reflection of the prevailing gloom in Europe. UK SmallCap is currently trading on multiples well below historical averages, which should limit the downside risk. Under-owned and under-loved, UK SmallCap could well surprise on the upside this year.

The context of high uncertainty should translate into further outperformance of the “quality growth” theme - companies offering secure earnings growth and good visibility. Balance sheet strength is also crucial at a time when bank lending may be restricted. Montanaro are well positioned to take advantage of a scramble for the highest quality “blue-chip” small companies. We wish all our investors a Happy New Year!

Fund Performance



Relative Performance



Fund Performance

Y/E: December	YTD (FY)	1 month	3 month	6 month	1 year	3 year	5 year	Launch
Montanaro NAV	-4.8%	-0.2%	1.1%	-11.8%	-4.8%	55.1%	-11.3%	78.0%
FTSE SmallCap (ex IC)	-17.7%	0.0%	-4.4%	-18.6%	-17.7%	42.0%	-43.6%	-17.4%

Source: Montanaro, Bloomberg. NAV to NAV

Fund Analysis

	Fund	Index
Latest Price / NAV	1540.3	2164.5
Alpha (annual) *	8.3%	na
Beta *	0.52	1.00
Standard Deviation *	15.2%	24.8%
Sharpe Ratio *	0.99	0.47
Tracking error *	14.3%	na
P/E 12F _†	13.2	7.2
EPS Growth 12F _†	13.8%	4.6%
Dividend Yield 12F _†	2.6%	3.9%

* risk statistics over three years † Source: Factset consensus estimates

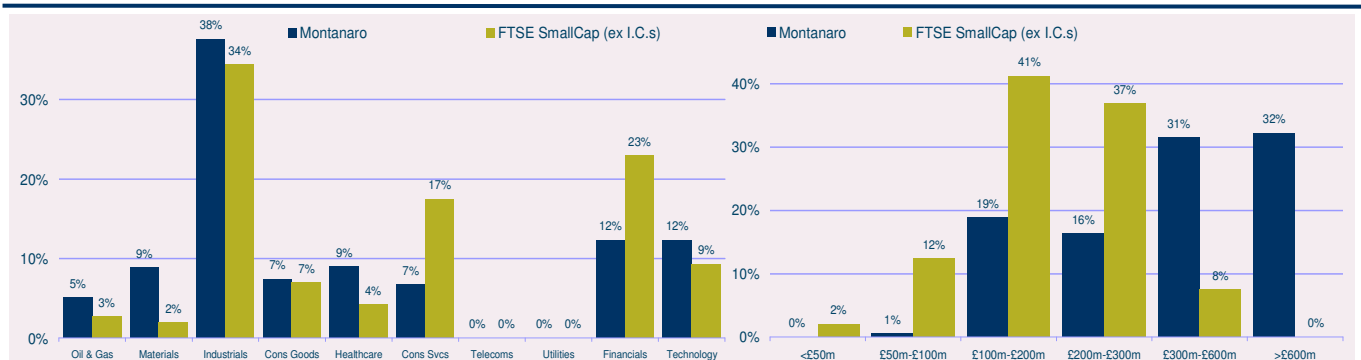
Fund Details

Launch Date	June 1999
Fund Size	£23 million
No. of holdings	42
Mgmt Fee	Annual 1.5%
Perf Fee	See below*
Legal Status	Offshore (Cayman) Unit Trust
Valuation	Each Friday
Offering memo	March 1997

Top Ten Holdings

Name	Sector	% of portfolio
1 NCC Group	IT Services	4.9%
2 Dignity	Diversified Consumer Services	3.6%
3 Oxford Instruments	Electronic Equipment, Instruments & Components	3.6%
4 Croda International	Chemicals	3.1%
5 Victrex	Chemicals	3.1%
6 Dialight	Electronic Equipment, Instruments & Components	3.0%
7 Devro	Food Products	3.0%
8 Renishaw	Electronic Equipment, Instruments & Components	3.0%
9 Genus	Biotechnology	3.0%
10 SDL	Software	2.9%
TOTAL		33.1%

Sector & Size Distribution



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* Performance fee is calculated at 20% of the returns over a hurdle rate of 10%