

UK Smaller Companies Investment Trust (Capital Returns)

MONTANARO

★★★★ – Morningstar Rating™
(as at 31/12/11)

Monthly Fact Sheet: December 2011

Montanaro, an independent specialist fund manager, was established in 1991 to research and invest in UK and Continental European quoted Small/MidCap companies with particular expertise in “smaller” companies. Funds under management are c.£1.1 billion. The UK Investment Trust invests in quoted UK companies with a market capitalisation lower than the largest constituent of the Hoare Govett Smaller Companies Index (the smallest 10% of the UK stock market) focused on “smaller” companies.

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 Trust ended the calendar year c.12% ahead of its benchmark and ahead of both the HGSC and 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.

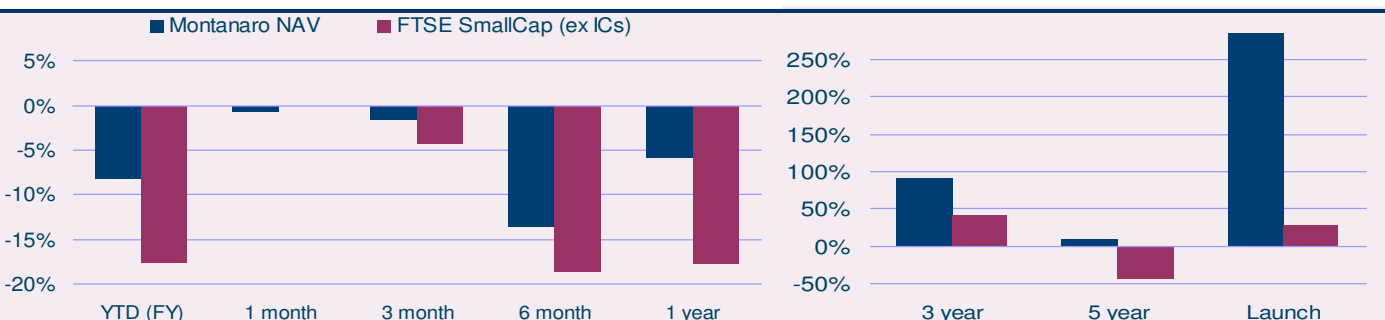
In stark contrast to last year, investor portfolios are positioned defensively with larger cash allocations, a reflection of the prevailing gloom in Europe. UK SmallCap is currently trading on multiples well below historical averages, which should limit the downside risk. Under-owned and under-loved,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

Performance



Relative Performance



Y/E: March	YTD (FY)	1 month	3 month	6 month	1 year	3 year	5 year	Launch
Montanaro NAV	-8.1%	-0.7%	-1.5%	-13.7%	-5.9%	91.2%	9.7%	285.8%
FTSE SmallCap (ex ICs)	-17.7%	0.0%	-4.4%	-18.6%	-17.7%	42.0%	-43.6%	27.7%

Source: Montanaro, Bloomberg. NAV to NAV

Analysis

	Fund	Index
NAV	380.4	2164.5
Share Price	300.5	na
Discount	-21.0%	na
Alpha (annual) *	14.4%	na
Beta *	0.61	1.00
Standard Deviation *	16.7%	24.8%
Sharpe Ratio *	1.41	0.47
P/E 12F _†	13.1	7.2
EPS Growth 12F _†	13.1%	4.6%
Dividend Yield 12F _†	2.7%	3.9%

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

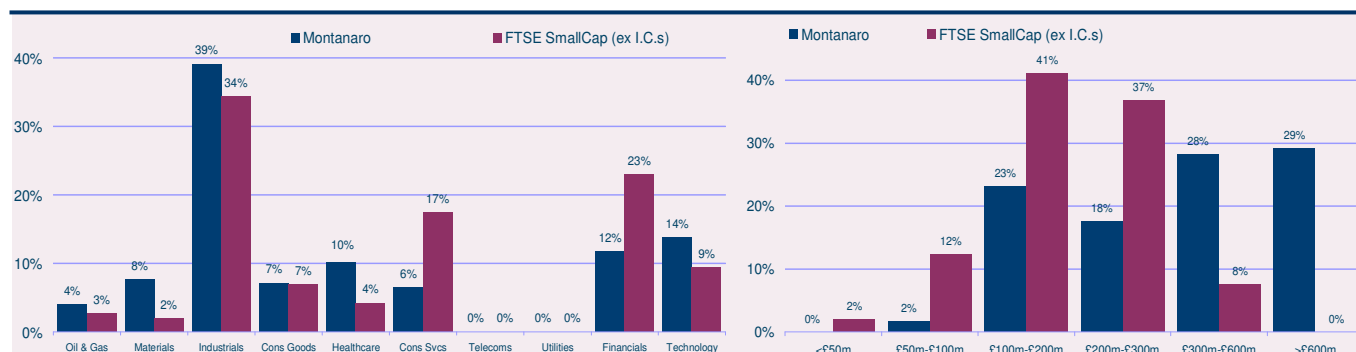
Details

Launch Date	March 1995
Gross Assets	£144 million
Net Assets	£129 million
Net Gearing	11.2%
No. of holdings	50
Mgmt Fee	1% p.a.
Perf Fee	See below*
Legal Status	UK closed-end Investment Trust
Listing	London Stock Exchange
Valuation	Daily
Annual dividend	June

Top Ten Holdings

Name	Sector	% of net portfolio
1 NCC Group	IT Services	3.8%
2 Fenner	Machinery	3.3%
3 Oxford Instruments	Electronic Equipment, Instruments & Components	3.3%
4 Victrex	Chemicals	3.0%
5 Devro	Food Products	2.9%
6 SDL	Software	2.9%
7 Domino Printing Sciences	Electronic Equipment, Instruments & Components	2.8%
8 Genus	Biotechnology	2.8%
9 Latchways	Commercial Services & Supplies	2.7%
10 Dialight	Electronic Equipment, Instruments & Components	2.7%
TOTAL		30.2%

Sector & Size Distribution



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*Performance Fee is calculated at 0.1% of each 1%, or part thereof, outperformance of FTSE SmallCap Index plus 2%, capped at 0.5%, with a hurdle of 421.65p

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