

UK Smaller Companies Investment Trust (Capital Returns)

MONTANARO

Monthly Fact Sheet: July 2010

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.£900 million. 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

The NAV rose last month by 6% outperforming its benchmark by a further 3%. After the strong recent outperformance, this is pleasing. In 2010 the NAV has risen by 15% in marked contrast to the 2% fall by the SmallCap market.

After a weak May and June it was gratifying to see equity markets regain some lost ground. This was driven by a recovery in the Financials sector in anticipation of the announcement of the stress tests for the European Banks which only seven banks failed. The delayed introduction of Basel 3 does, however, mean that banks remain susceptible to further shocks or crises. Corporate activity remains high with further bids being seen.

GDP growth is expected in all European countries except Spain, Ireland and Greece and fears of a double dip recession are receding. However, the austerity measures put in place will affect some sectors - it looks increasingly likely that the Building and Construction sectors may suffer further reductions in order intake. Some evidence of changing spending patterns here has already been seen by companies such as Connaught whose shares have fallen 97% in the last 2 months. Avoiding the disasters is sometimes as important as backing the winners. The lack of job creation among many SMEs and the reduction in public spending may mean that the recovery remains relatively subdued. China continues to manage its growth for the longer term which will benefit those companies with exposure to the Far East.

With a high level of corporate activity it was not too surprising that the best performer this month was **Dana Petroleum**, the UK based Oil E&P company, which received a bid from the Korean National Oil Corporation lifting the shares by 50% over the month. This approach also helped the performance of **Premier Oil** which rose in sympathy. Double digit rises were also seen by companies such as **Croda** (specialty chemicals), **Dialight** (LED lighting), **Victrex** (specialty chemical) and **Renishaw** (measuring equipment)

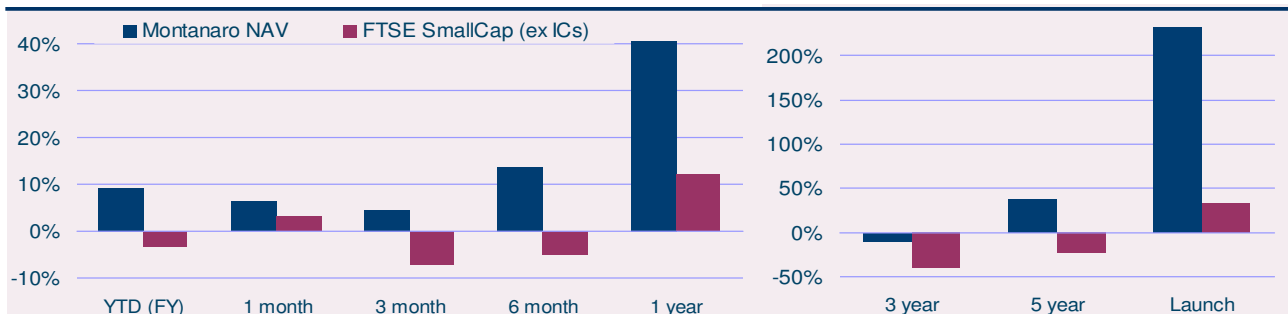
On the downside, **Ricardo** was weak after a broker downgrade. This was followed by a more positive update just after the month end as the company announced a significant increase in its order book. After a strong run in June **Immunodiagnostic Systems** (medical diagnostic testing) succumbed to some mild profit taking. **EDI**, the educational qualifications business, remained weak despite an investor day late in the month.

Companies are building up cash resources which should lead to a recovery in Capex spending and M&A. This will benefit the Industrials sector in particular but also the IT sector. With equity valuations remaining below historic averages and earnings growth still robust (plenty of upgrades still being announced), the outlook for the remainder of 2010 is still positive.

Fund Performance



Relative Performance



Y/E: March	YTD (FY)	1 month	3 month	6 month	1 year	3 year	5 year	Launch
Montanaro NAV	9.2%	6.2%	4.6%	13.6%	40.6%	-9.9%	38.3%	230.8%
FTSE SmallCap (ex ICs)	-3.4%	3.1%	-7.2%	-5.0%	12.1%	-40.2%	-23.5%	34.1%

Source: Montanaro, Bloomberg. NAV to NAV

Fund Analysis

	Fund	Index
NAV	326.2	2273.7
Share Price	265.5	na
Discount	-18.6%	na
Alpha (annual) *	8.2%	na
Beta *	0.71	1.00
Standard Deviation *	23.6%	30.9%
Sharpe Ratio *	-0.31	-0.68
P/E 11F _†	12.3	8.8
EPS Growth 11F _†	12.5%	12.8%
Dividend Yield 10F _†	2.7%	3.5%

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

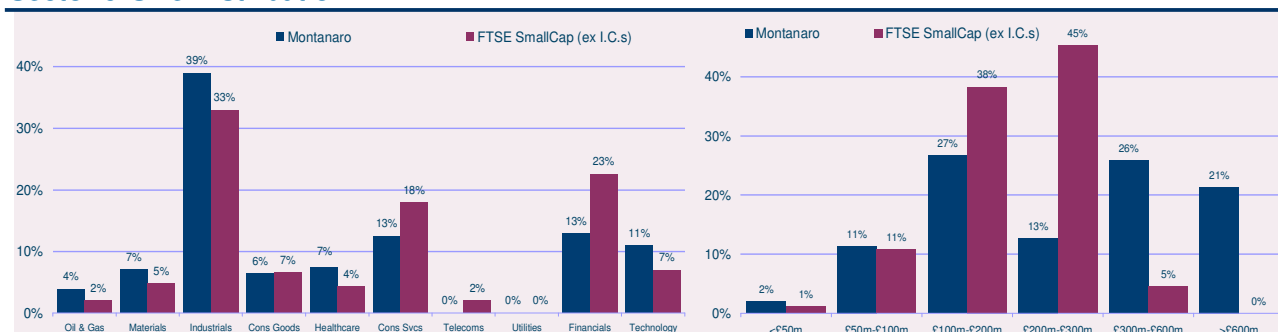
Fund Details

Launch Date	March 1995
Gross Assets	£125 million
Net Assets	£110 million
Net Gearing	7.7%
No. of holdings	58
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 Victrex	Chemicals	3.1%
2 Domino's Pizza	Travel & Leisure	2.9%
3 Domino Printing	Electronic & Electricals	2.9%
4 Dignity	General Retailers	2.8%
5 Dialight	Electronic & Electricals	2.7%
6 Devro	Food Producers	2.7%
7 James Fisher	Industrial Transportation	2.5%
8 Premier Oil	Oil & Gas Producers	2.5%
9 Barr (A.G.)	Beverages	2.4%
10 Croda	Chemicals	2.3%
TOTAL		26.8%

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%, high on high