MONTANARO
ASSET MANAGEMENT

MUSCIT

Montanaro UK Smaller Companies Investment Trust

Quarterly review – Q2 2026

Key points:

1) Political risk resurfaced as **Sir Keir Starmer resigned on 22 June**, paving the way for a new Prime Minister over the summer, likely Andy Burnham.
2) AIM's long decline continued, falling to its fewest constituents since 2001 after April's further halving of Business Property Relief, even as the wider **SmallCap discount to LargeCap remains close to its most stretched levels in two decades**.
3) **MUSCIT's NAV demonstrated resilience**, delivering outperformance of over 4% relative to the benchmark.

With a pace of regularity that we should really be used to by now, the UK political landscape shifted again when Sir Keir Starmer resigned as Prime Minister on 22 June following heavy losses in the local elections. This left ten-year gilt yields elevated well above international peers and the prospect of a new government led by Andy Burnham being installed over the summer.

Against this backdrop, SmallCap delivered a two-speed quarter. April and May saw the best month for the Numis SmallCap (ex-Investment Trusts) index in over a year. This momentum reversed sharply in June when the index fell back due to macroeconomic worries, while AIM was hit hard by the further halving of Business Property Relief that took effect from April. Remarkably, AIM now has the fewest constituents since 2001.

The quarter's defining story was the extraordinary rally in semiconductors and AI-related equities, which left Growth comfortably ahead of Value globally even as the pattern partially reversed in June, when Quality and Value briefly reasserted themselves as technology wobbled. SmallCap, with its more modest exposure to that theme, moved to a different rhythm, shaped instead by company results, takeover activity and the political and rate backdrop described above.

Performance & Portfolio

MUSCIT's NAV increased by 13.6%, compared to the benchmark return of 9.3%. Since the beginning of the calendar year, MUSCIT has outperformed by 6%.

The **strongest contributors** during the quarter were:

- **Luceco –** the designer and manufacturer of LED lighting and electrical wiring accessories rose as it upgraded full-year profit guidance on accelerating EV-charger demand and broad-based core product growth over the quarter.
- **XP Power –** the designer and manufacturer of power converters for industrial, healthcare and technology equipment, gained strongly on tangible signs of order-book recovery, with first-quarter order intake up sharply year-on-year.
- **Beauty Tech Group –** the owner of the CurrentBody, ZIIP Beauty and Tria at-home beauty-device brands, continued to see strong momentum, doubling from its October IPO price as investor appetite for the at-home beauty-device category strengthened.

The **weakest contributors** during the quarter were:

- **ME Group International** – the operator of self-service photo booths and laundry kiosks declined over the quarter after cutting full-year profit guidance on a French consumer slowdown that hit its Photo and Wash divisions through the period.
- **Cerillion** – the British provider of billing and customer-management software for telecoms operators weakened as the stock de-rated alongside global software peers on AI-disruption fears, even as the underlying business remained on track with record order intake following its £42.5m Omantel contract win.

- **Boku** – the listed mobile payments and carrier-billing network, softened over the quarter despite delivering H1 revenue and EBITDA growth ahead of expectations, as the shares continued to de-rate after a period of sharp prior outperformance.

Manager's comments

This was a strong quarter in both absolute and relative terms for MUSCIT. At a sector level, Industrials led relative returns by some distance, while Technology was the laggard, as the same AI-disruption worries that hit software globally caught up with a small number of our holdings. Meanwhile, the takeover of Tate & Lyle, a stock we do not own, cost us in relative terms, a reminder that M&A can hurt as well as help on a relative basis.

We continue to manage a high-conviction Portfolio, now at 57 holdings against a target range of 55 to 60, with roughly two-thirds of overall risk stock-specific rather than factor-driven, which enables our stock picking to be the key driver of performance. We welcomed four new holdings to the Portfolio during the quarter. **Gooch & Housego**, the precision optics manufacturer, is benefiting from record aerospace and defence demand alongside a cyclically recovering semiconductor market. **Avon Technologies** is riding a similar wave of strong global defence demand, with operational execution translating into accelerating profit margins. **Bioventix**, considerably the smallest of the four, offers an attractive Alzheimer's diagnostic royalty stream growing alongside a highly resilient core antibody portfolio. **Sabre Insurance** rounds out the new additions, a high-quality insurer operating in an attractively niche corner of the market.

On the other side of the ledger, we exited two property names, **LMP** and **Workspace**, both REITs that combine low earnings growth with too much rate sensitivity for our taste in the current environment. We also sold out of **Telecom Plus**, where competitive pressures were becoming harder to ignore, and exited **Pinewood Technologies** as we were concerned about execution risk and the same rising software competitive threat that has weighed on **Cerillion** and others this quarter; though we have higher conviction in the competitive moat of the latter. **Animal Care**, meanwhile, left the Portfolio the easy way: via a takeover bid at a premium of 36% though we had hoped to be able to build this position further having recently initiated

If one holding deserves a closer look this quarter it is **Beauty Tech Group**. Last October we participated in the IPO of the owner of the CurrentBody, ZIIP Beauty and Tria at-home beauty-device brands. It has repaid our conviction handsomely: the shares have more than doubled from their offer price and the company has raised its earnings and sales expectations twice since listing. The investment case rests on a straightforward observation, borne out again this quarter, that consumers are increasingly willing to spend on professional-grade beauty devices for use at home rather than in a salon or clinic, a category that continues to grow faster than beauty retail as a whole. It is precisely the kind of structural, well-managed growth story we look for and we are pleased to have been early.

Outlook

SmallCap valuations remain historically depressed relative to LargeCap, a consequence of five consecutive years in which SmallCap, Quality and Growth as investment styles have all been unfashionable. We saw a reminder within the quarter itself of how quickly this can turn. We remain Quality Growth investors by design and see little value in departing from that discipline simply because it has been out of favour.

Corporate buyers continue to see value where public markets do not: the takeover bids of Animal Care and non-holding Tate & Lyle this quarter, on top of a run of similar approaches over the past two years, is as good a signal as any that current valuations are not sustainable indefinitely. Domestic political uncertainty is a near-term risk to sentiment, but it does not change the underlying earnings power of the businesses we own, over half of which hold net cash.

As a brief aside, the policy backdrop for SmallCap is worth watching. In a widely discussed speech, “Field of Dreams”, the former Bank of England Chief Economist Andy Haldane set out what he termed the UK's capital paradox: UK households hold around £9 trillion in financial assets, yet under 5% of this is invested in UK companies, with pension fund allocation to UK equities having fallen from over half in 2000 to under 5% today, a shift he estimated at c. £2.5 trillion of divestment. He noted that the UK is now the only major pension system without a domestic home bias. Will we finally see regulation that encourages investment in our domestic companies, many of whom are global leaders?

The four companies we added this quarter, spanning aerospace and defence, diagnostics and niche insurance, are exactly the sort of well-run, structurally growing businesses that MUSCIT exists to own. We remain confident that patient, high-conviction ownership of quality smaller companies will be rewarded once sentiment turns, even if the timing, as ever, is not ours to call.

Charles Montanaro
July 2026

Montanaro Asset Management Ltd | 53 Threadneedle Street | London EC2R 8AR

T: +44 20 7448 8600 www.montanaro.co.uk