

MONTANARO

ASSET MANAGEMENT

UK Smaller Companies Investment Trust (“MUSCIT”)

AGM Presentation

25 July 2019



Montanaro Asset Management Ltd

53 Threadneedle Street, London EC2R 8AR

www.montanaro.co.uk enquiries@montanaro.co.uk Tel: +44 (0)20 7448 8600

Follow us on **Twitter:** [@MontanaroAM](https://twitter.com/MontanaroAM) **Blog:** <http://www.montanaro.co.uk/blog>

We are different

1. It is our business
2. One big family - no big egos
3. Conservative (no loss-makers, no unquoteds, no derivatives, no stock lending)
4. We invest in our own funds
5. Long-term investors
6. We avoid brokers
7. Small & MidCap are all that we do

What is a “Montanaro” company?

1. Simple business **we can understand**
2. **Profitable**
3. **Niche business** in a growth market
4. **Market leader**
5. Business with **high operating margins** and a **high return on capital**
6. **Good management** we trust

“Quality Growth” investment approach

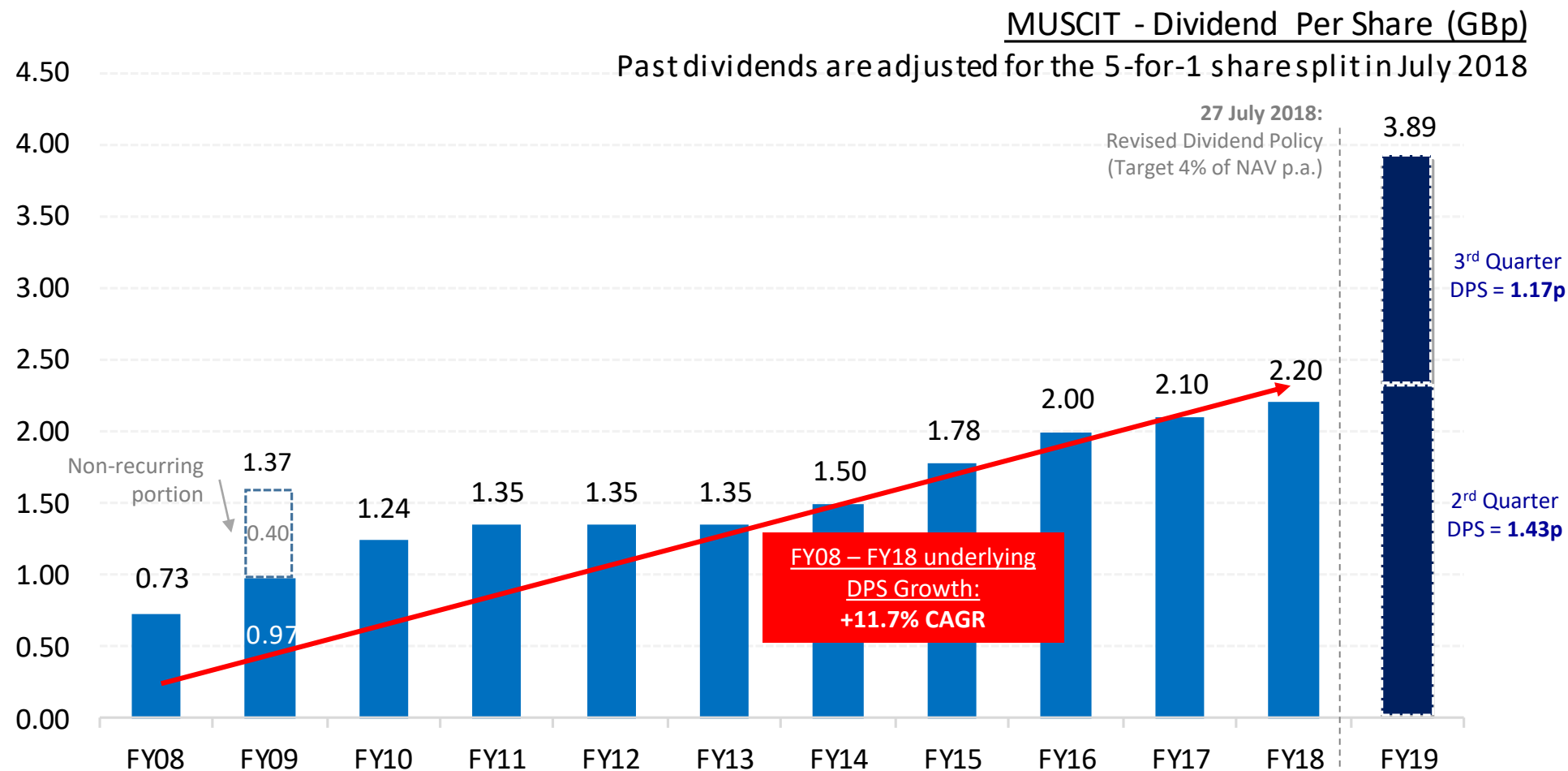
Our Top 20 holdings

Company	Country	%	Company	Country	%
Marshalls	UK	4.0%	Brewin Dolphin Holdings	UK	2.7%
Entertainment One	UK	3.9%	Restore	UK	2.6%
4Imprint Group	UK	3.8%	Porvair	UK	2.5%
Big Yellow Group	UK	3.7%	GB Group	UK	2.4%
First Derivatives	UK	3.5%	XP Power	UK	2.4%
Hilton Food Group	UK	3.5%	Diploma	UK	2.3%
Integratin	UK	3.3%	Equiniti Group	UK	2.3%
Polypipe Group	UK	3.2%	FDM Group	UK	2.2%
Ideagen	UK	3.1%	Consort Medical	UK	2.2%
James Fisher & Sons	UK	2.9%	Cineworld Group	UK	2.2%
Top 10		35.0%	Top 11 - 20		24.0%

Current Portfolio

- 47 holdings (14 AIM = 27% by value)
- 23% have net cash
- Further growth forecast (2019e): Sales +6%; EPS +3%; Dividends +4%
- Price / Earnings ratio 18.9x

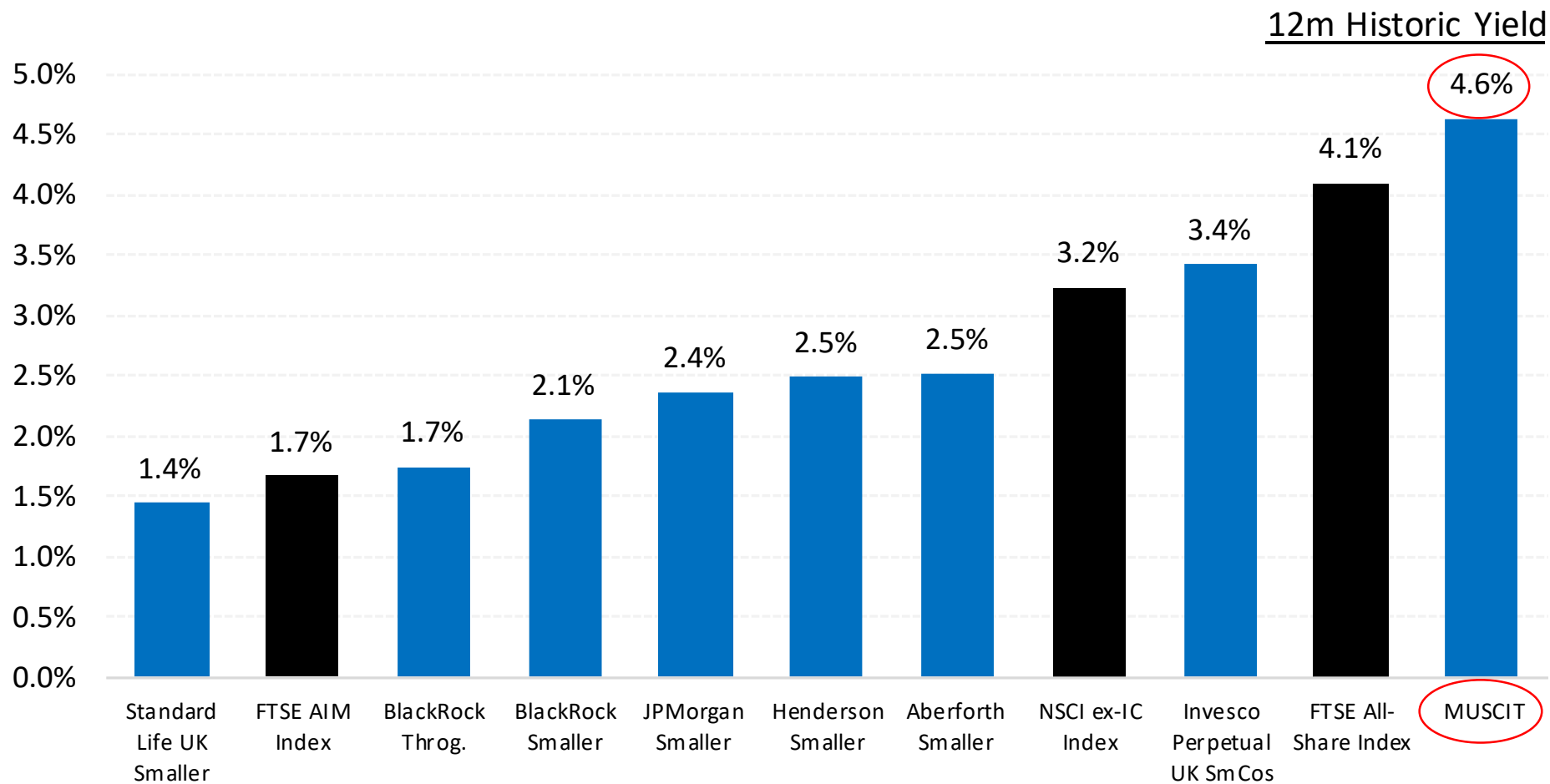
MUSCIT started paying quarterly dividends in 2018



Source: Montanaro. Financial Year end is 31 March.

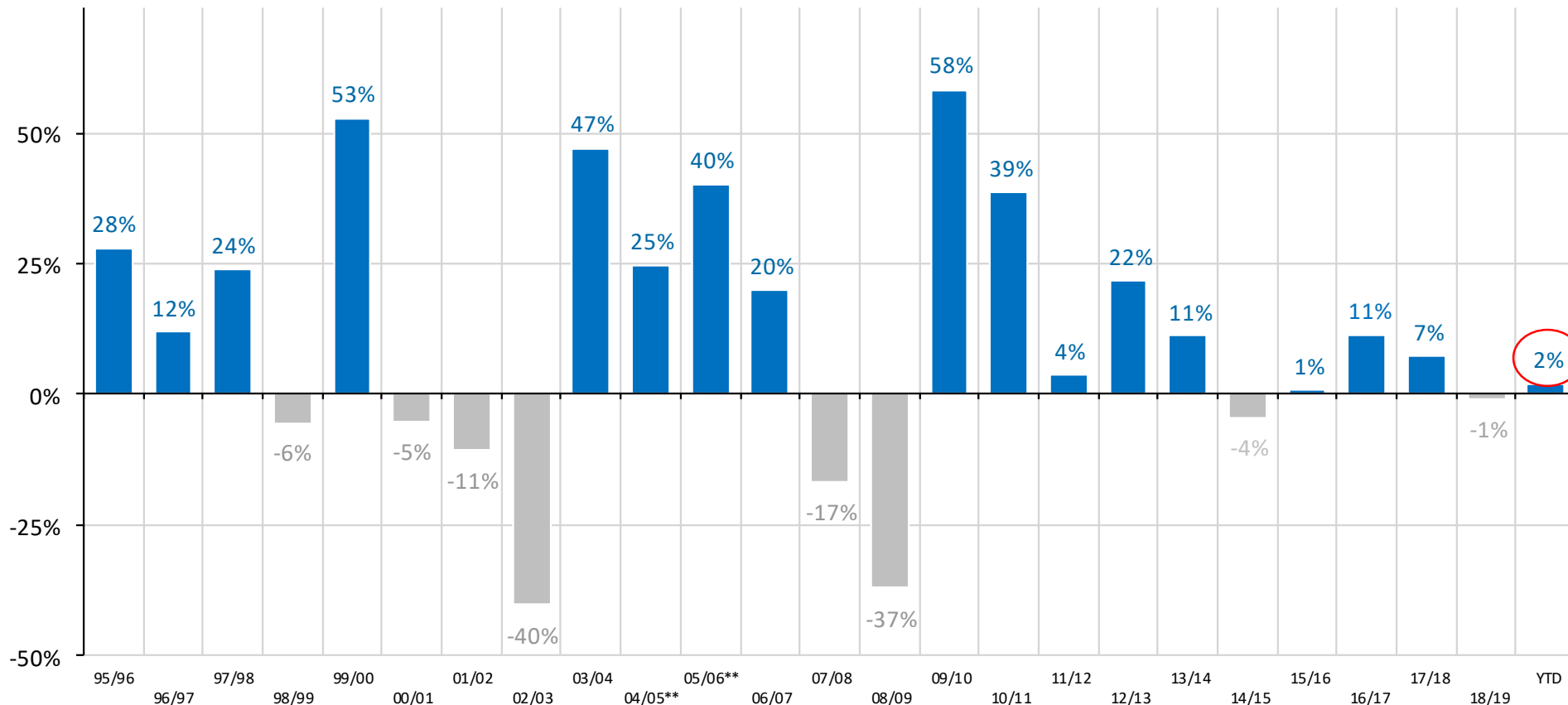
Note: On 27 July 2018 the Board announced a change of Dividend Policy. With effect from 30 September 2018, MUSCIT began paying quarterly dividends equivalent to 1% of the NAV (or roughly 4% per annum). The first quarterly dividend was paid on 23 November 2018 and the second will be paid on 22 February 2019.

MUSCIT now offers the highest yield within its peer group



Source: Montanaro. Numis. As at 4 July 2019.

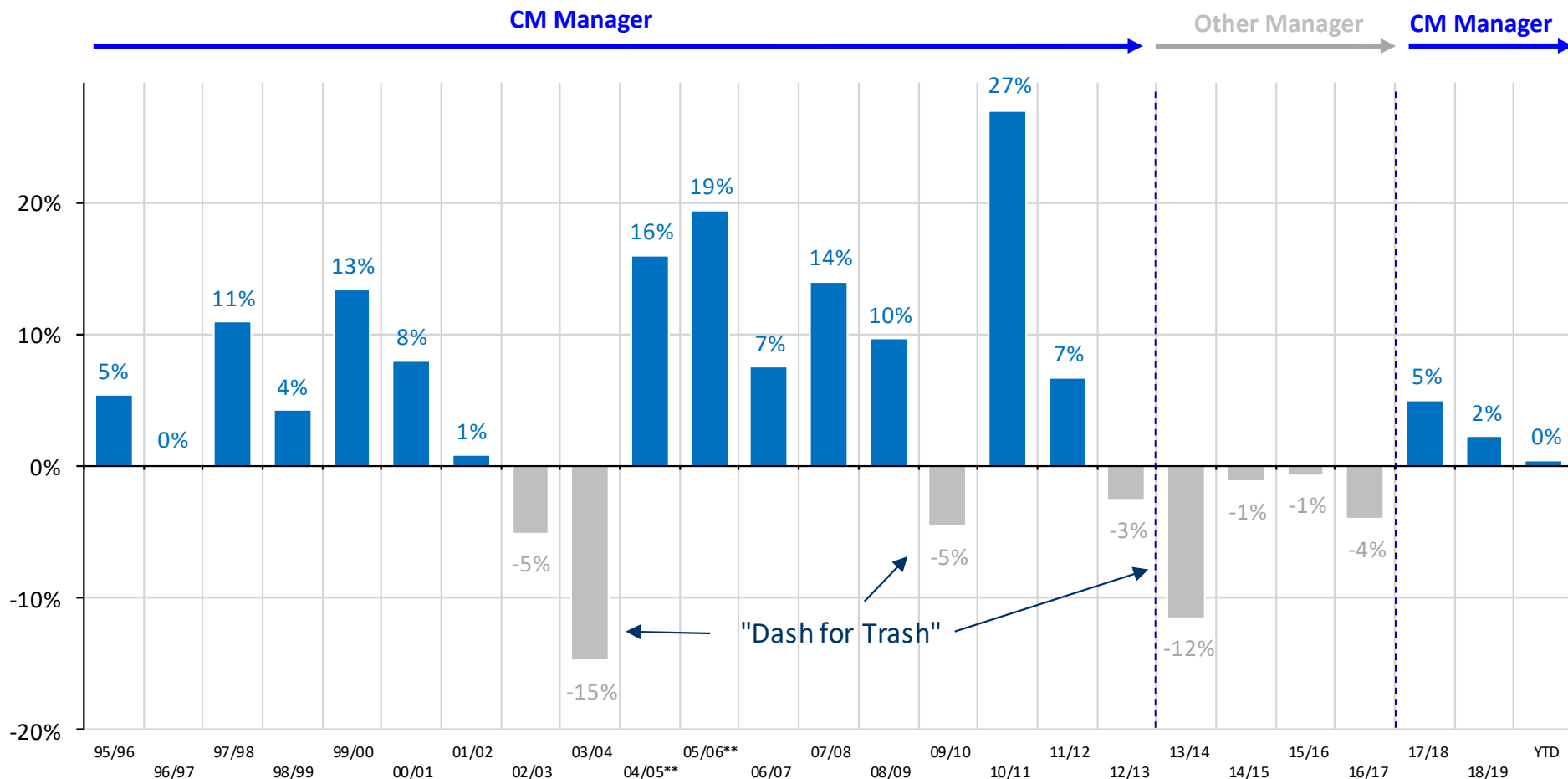
Absolute returns (by Financial Year) - 2019 YTD +15%



Source: Montanaro.

Note: Years 1-3 undiluted NAV, years 4-5 diluted NAV and years onwards basic NAV as no longer any warrants in issue. The FTSE All-Share index is shown for comparison only.

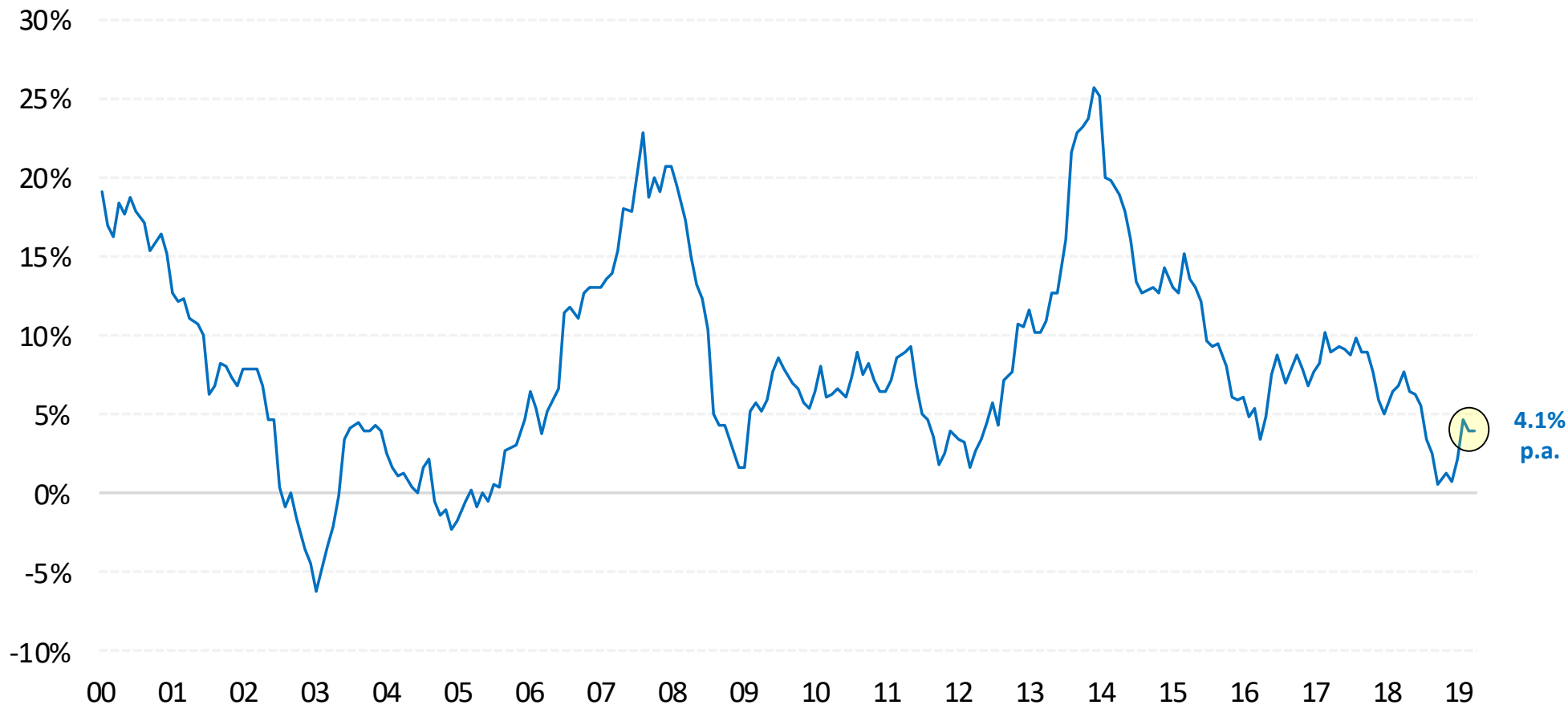
Relative returns – back to the “old” MUSCIT



Source: Montanaro. The benchmark for the UK Trust changed from the FTSE SmallCap Index (ex-IC) to the Numis Smaller Companies Index (ex-IC) effective 1 April 2013.
Note: Years 1-3 undiluted NAV, years 4-5 diluted NAV and years onwards basic NAV as no longer any warrants in issue

Over almost all 5-year periods MUSCIT produced positive returns

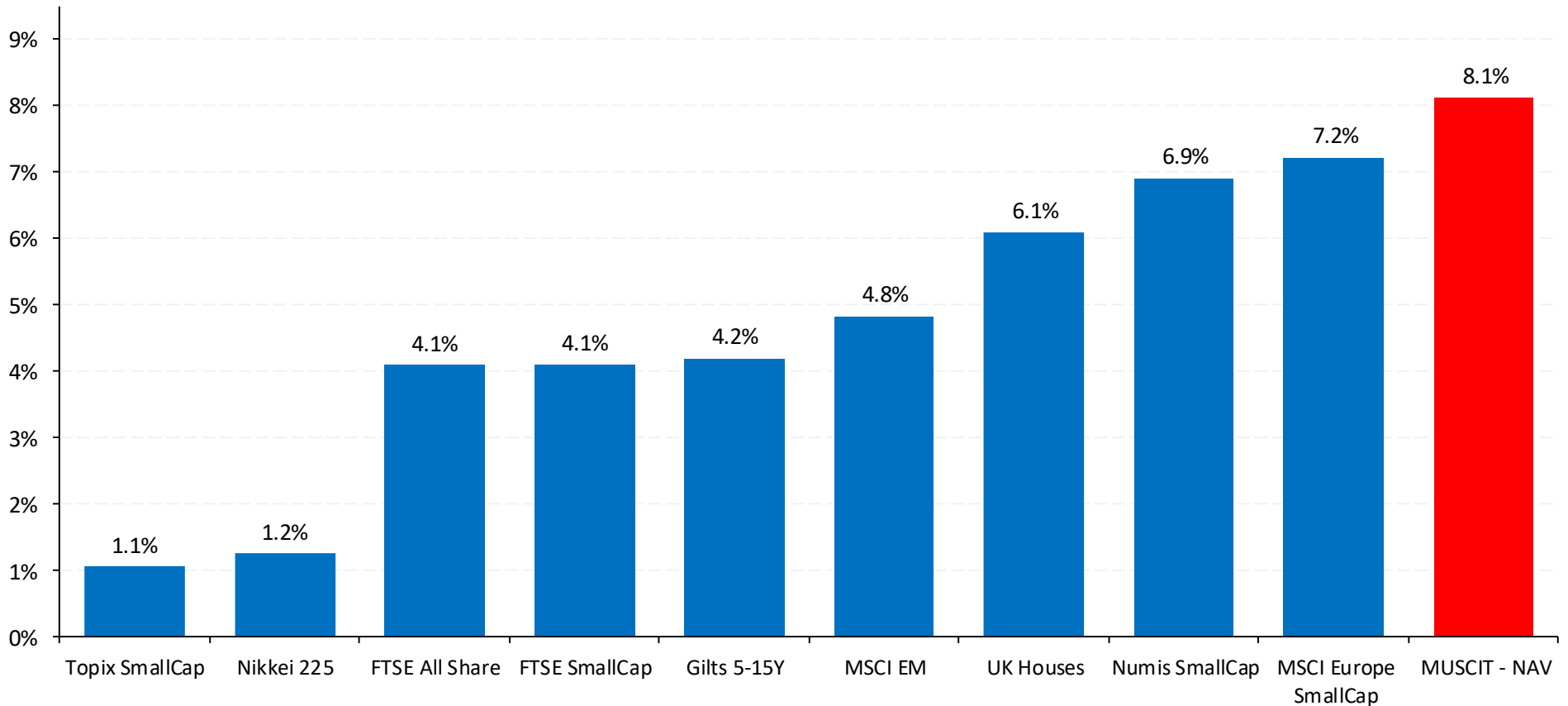
MUSCIT - 5-year rolling NAV return (annualised)



Source: Montanaro, Bloomberg.

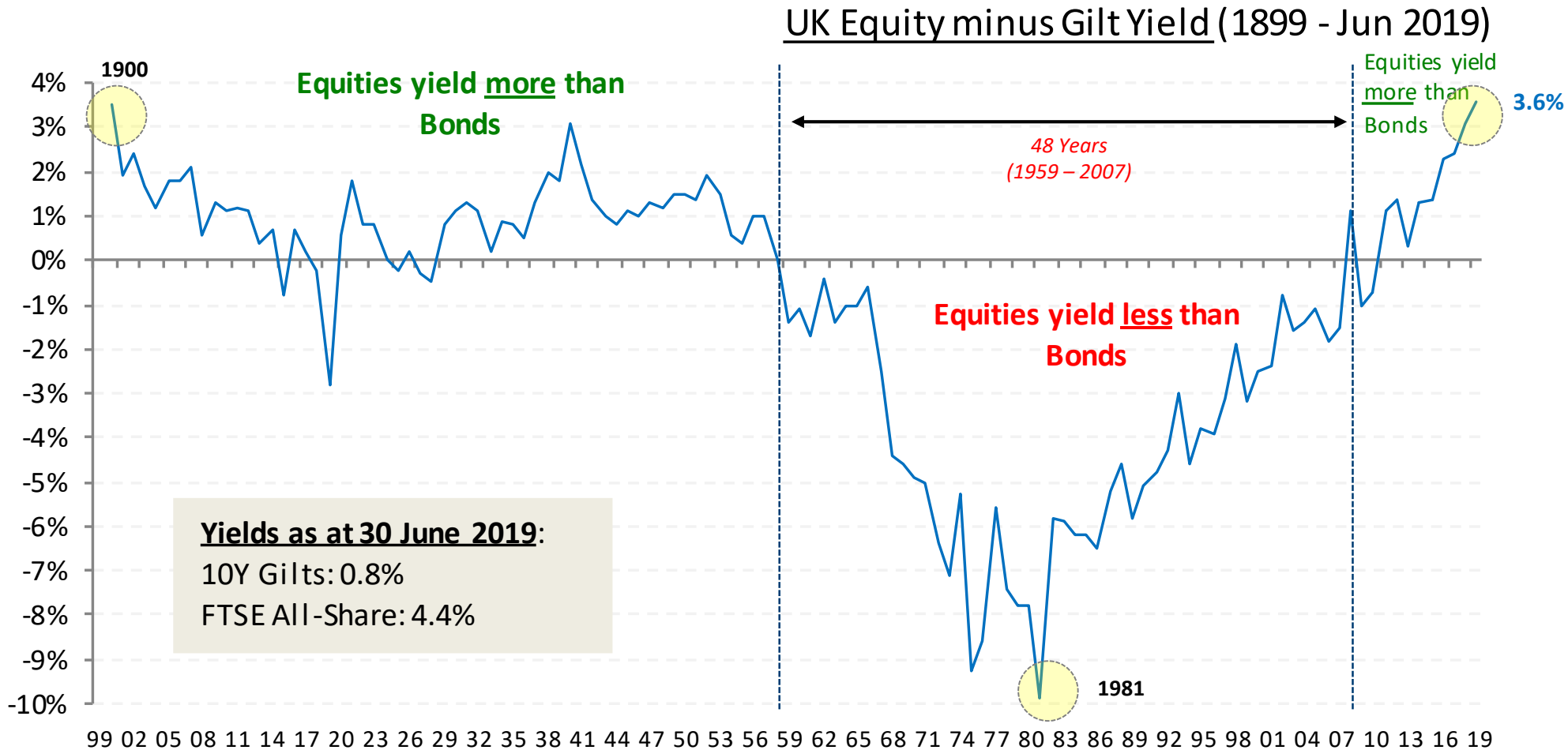
A good investment over the past 24 years (TR after fees: +9.5% p.a.)

Absolute Capital Returns p.a. since Trust inception (Mar 1995 - Jun 2019, all returns in GBP)



Source: Montanaro, Bloomberg.

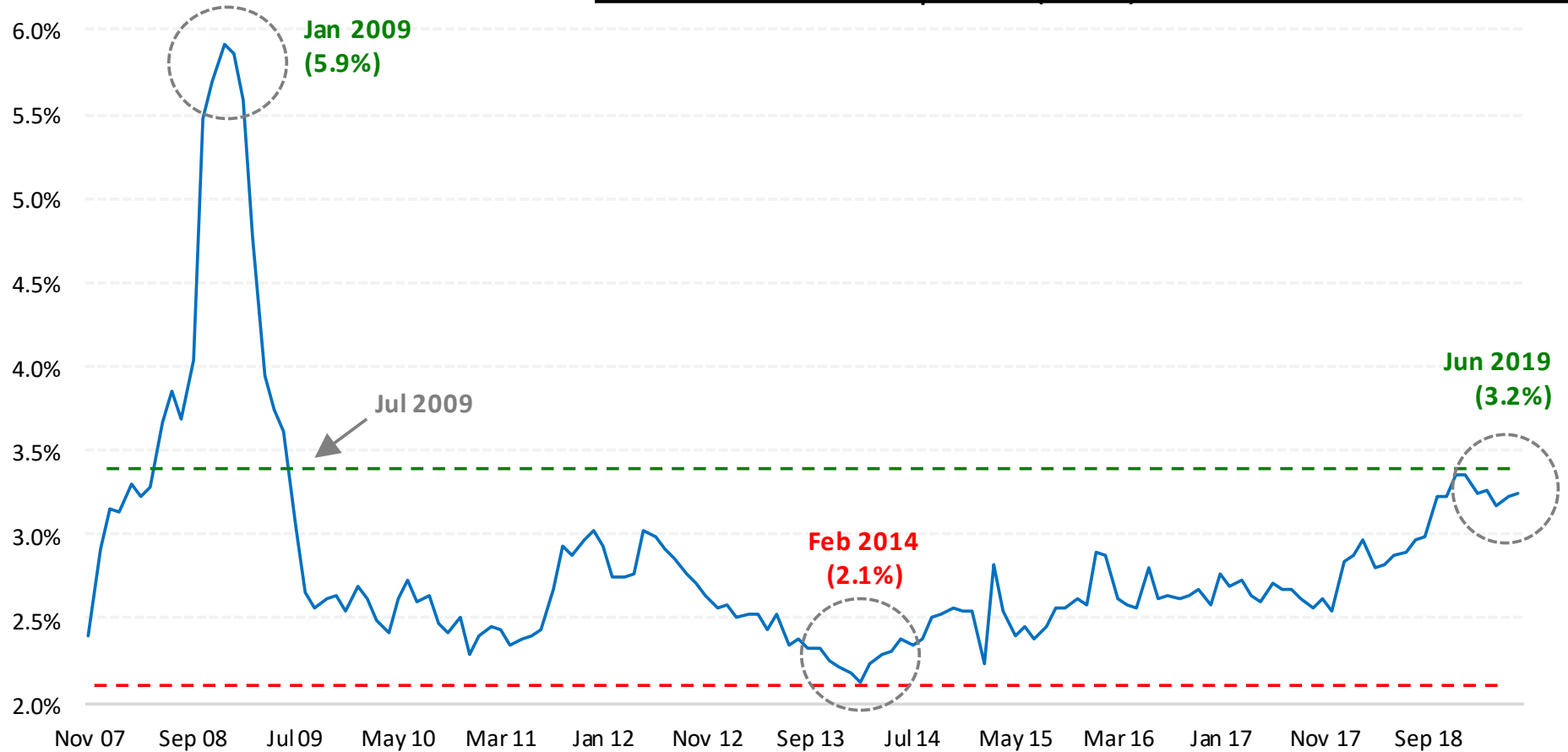
Outlook: UK equities yield 360bp more than bonds – highest since 1900



Source: Montanaro, Barclays Equity-Gilt Study, Numis, Bloomberg.

... and the yield on UK SmallCap is close to a 10-year high

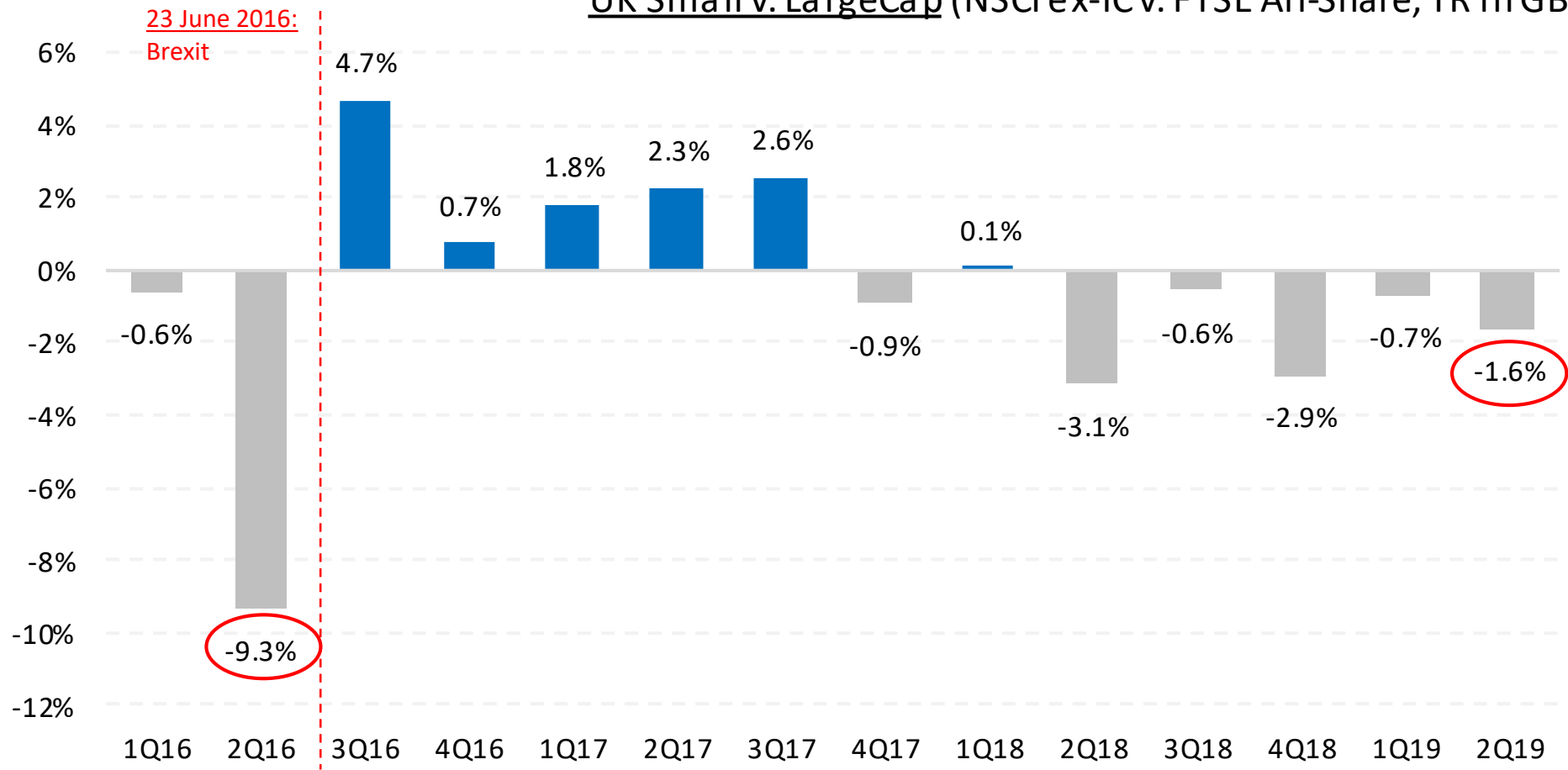
Numis Smaller Companies (ex-IC) - 12m Trail. Dividend Yield



Source: Montanaro, Numis.

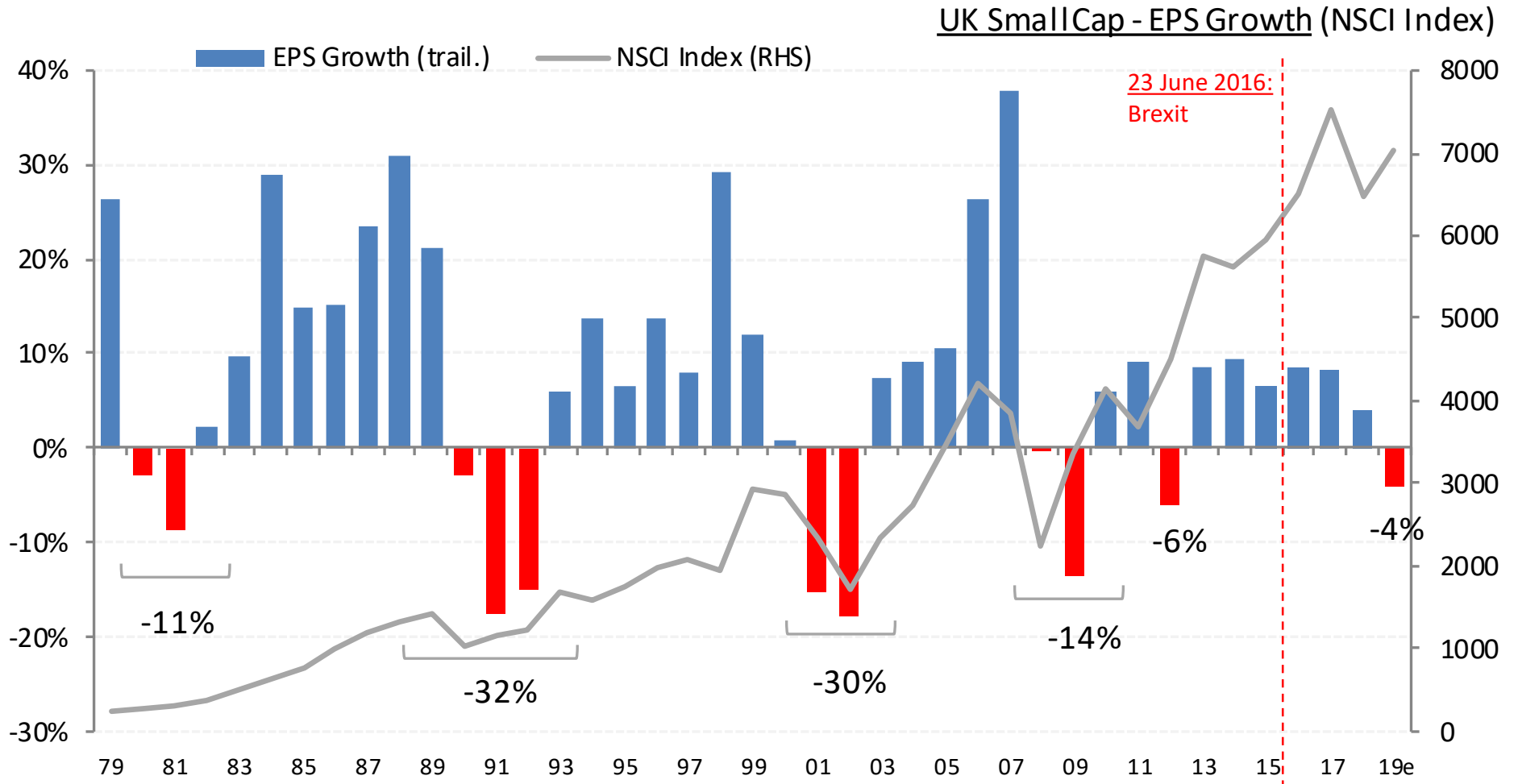
Brexit has been a drag on UK SmallCap performance (more domestic)

UK Small v. LargeCap (NSCI ex-IC v. FTSE All-Share, TR in GBP)



Source: Montanaro, Bloomberg.

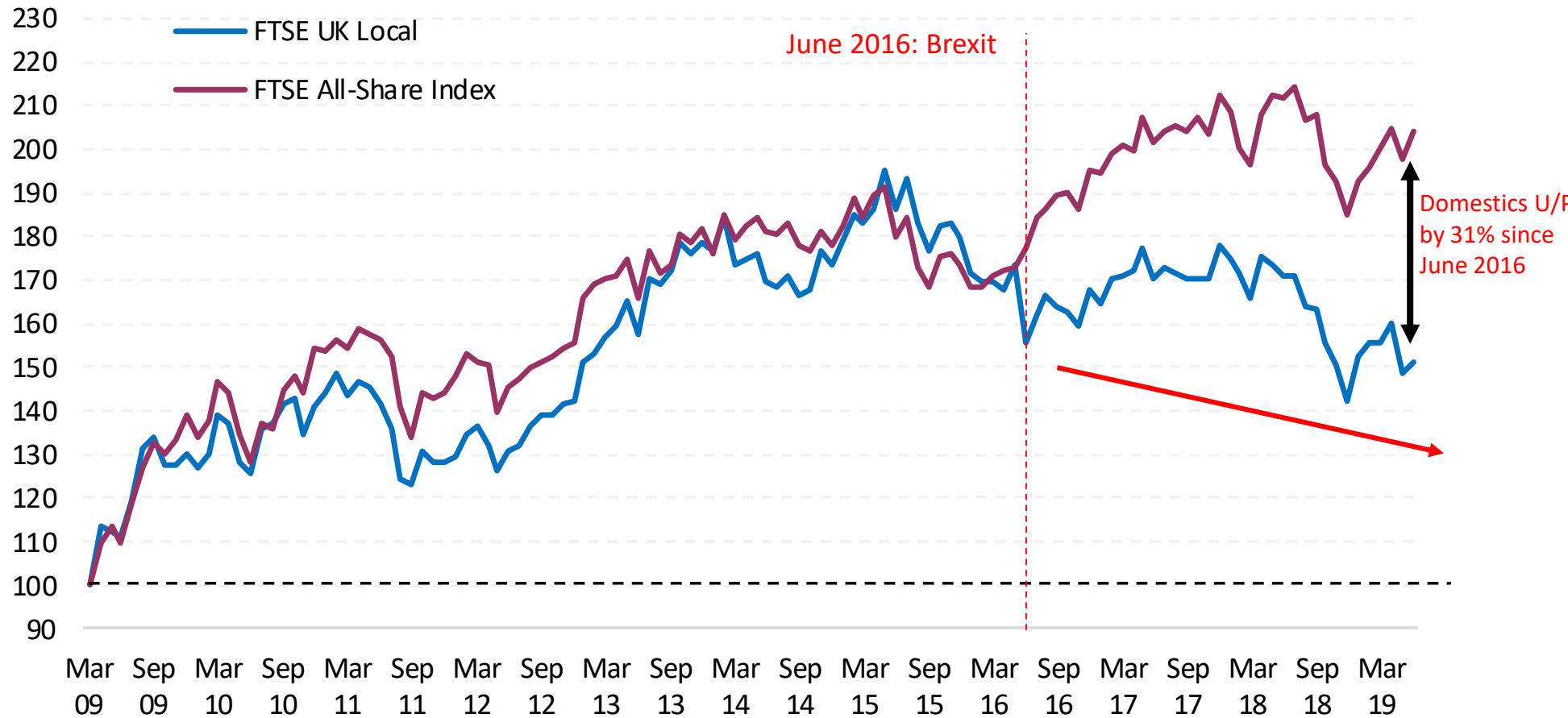
... and a drag on EPS growth



Source: Montanaro, Numis, Bloomberg.

The “Buy the *UK exporters* / *Sell the UK domestics*” trade will end

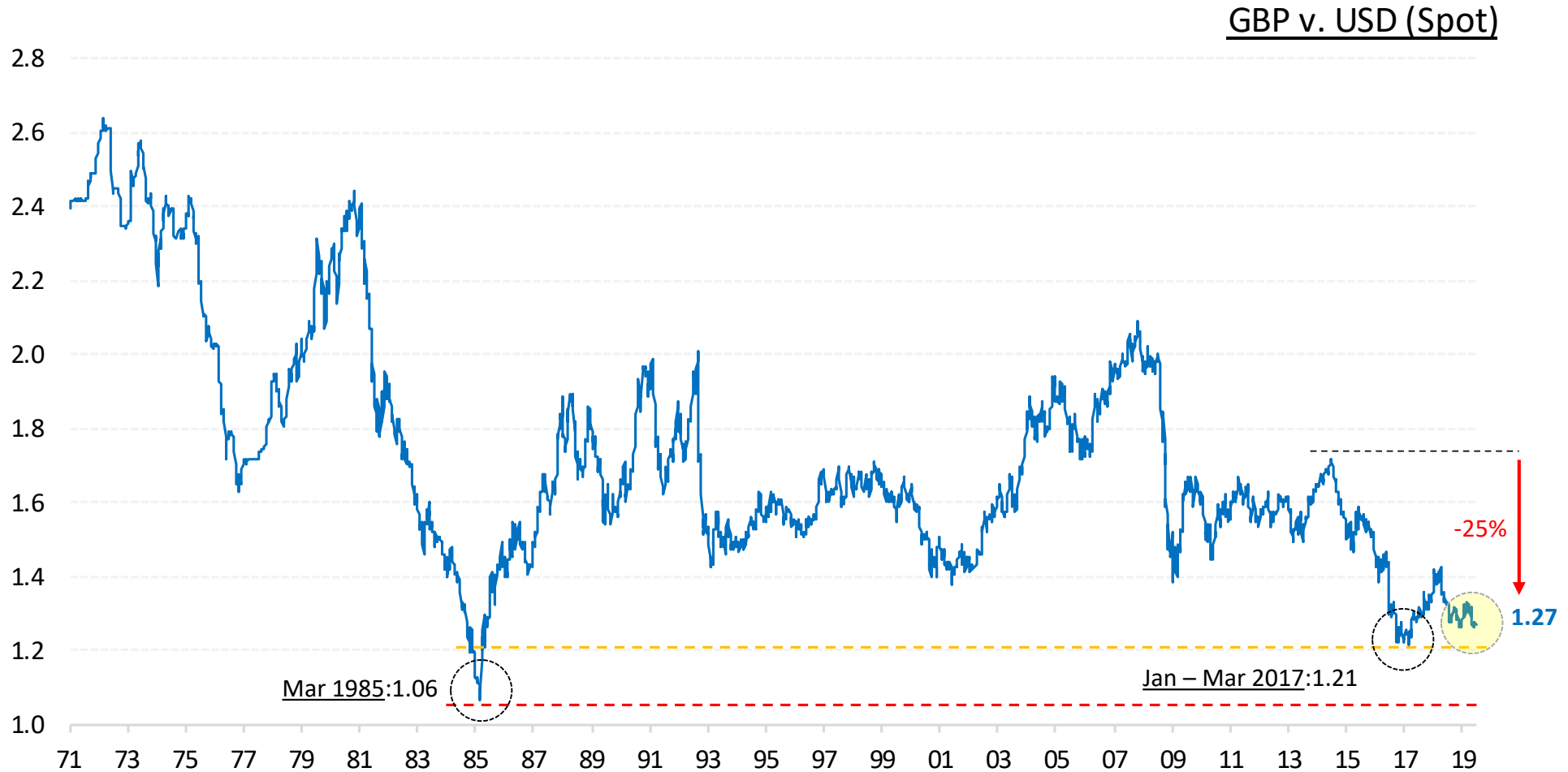
UK - FTSE Local index v. FTSE All-Share index (rebased)



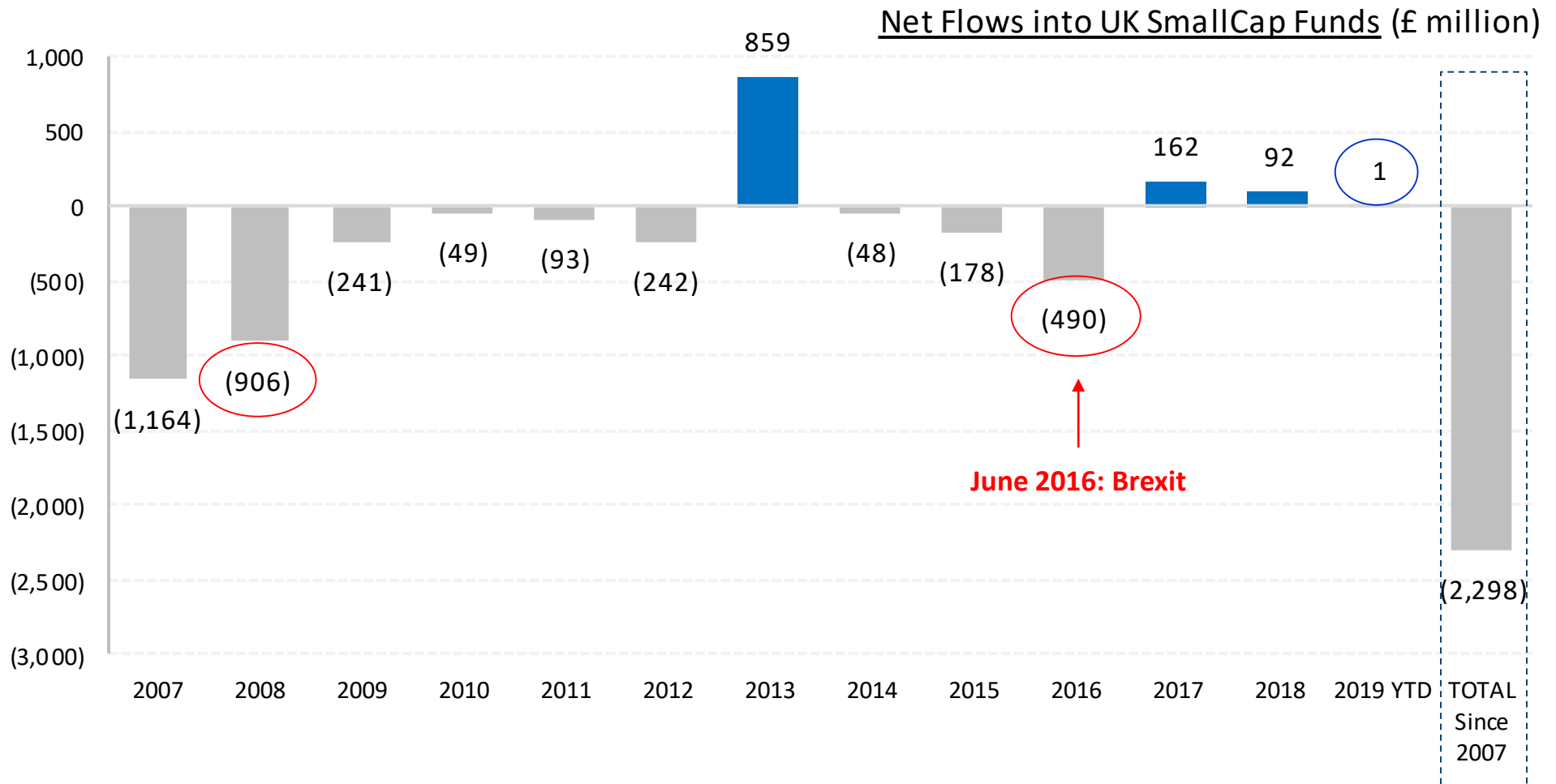
Source: Montanaro, Bloomberg.

The FTSE UK Local Index includes UK-listed companies with > 70% of sales to the UK.

... as Sterling nears its 30-year lows (again) v. the USD (5% downside)

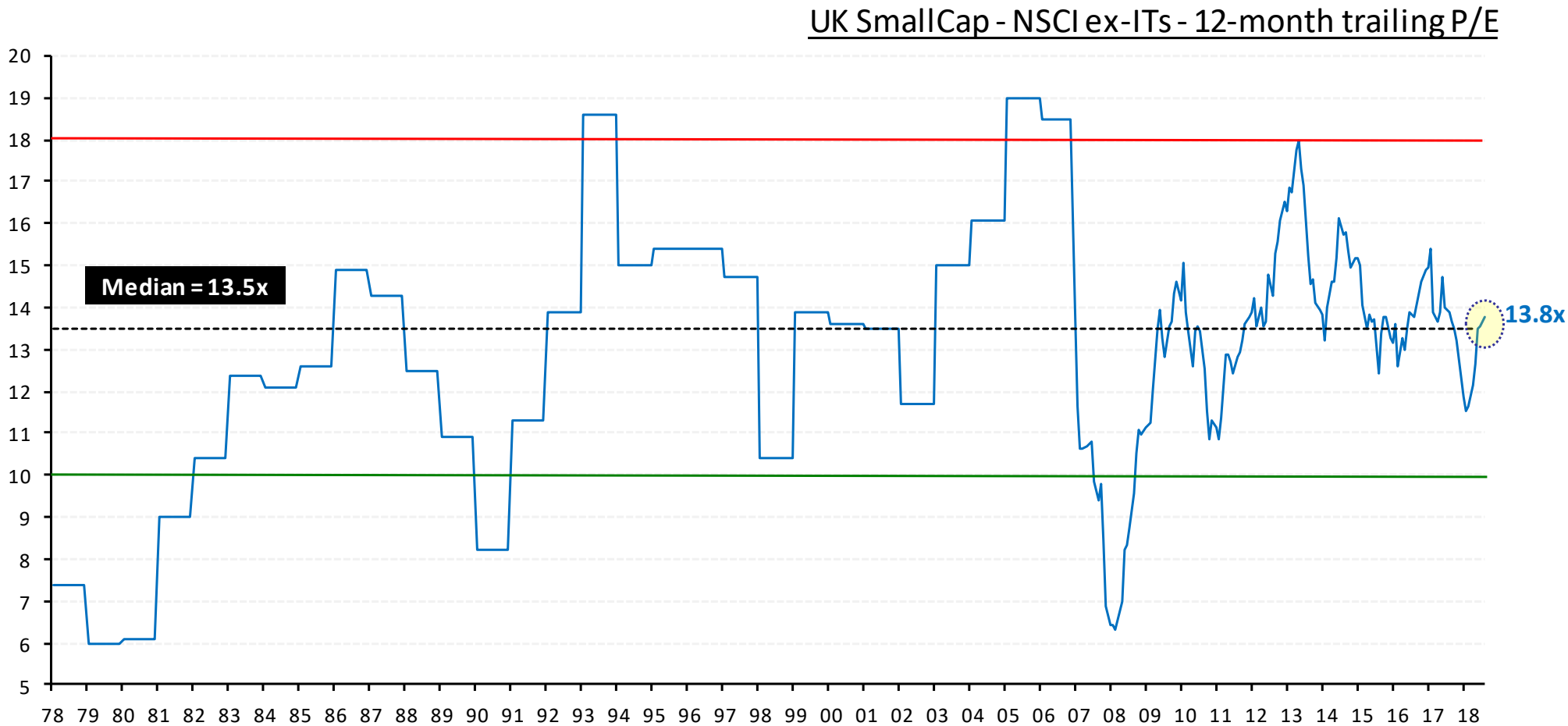


Two years after Brexit UK SmallCap is heavily under-owned



Source: Montanaro, Investment Association.
Data to 31 October 2018.

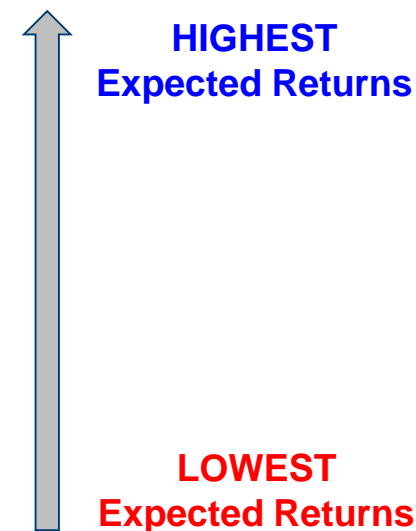
... which means SmallCap valuations are inexpensive



UK SmallCap offers plenty of upside over the medium-term

Estimated Total Returns over the next 7 years *:

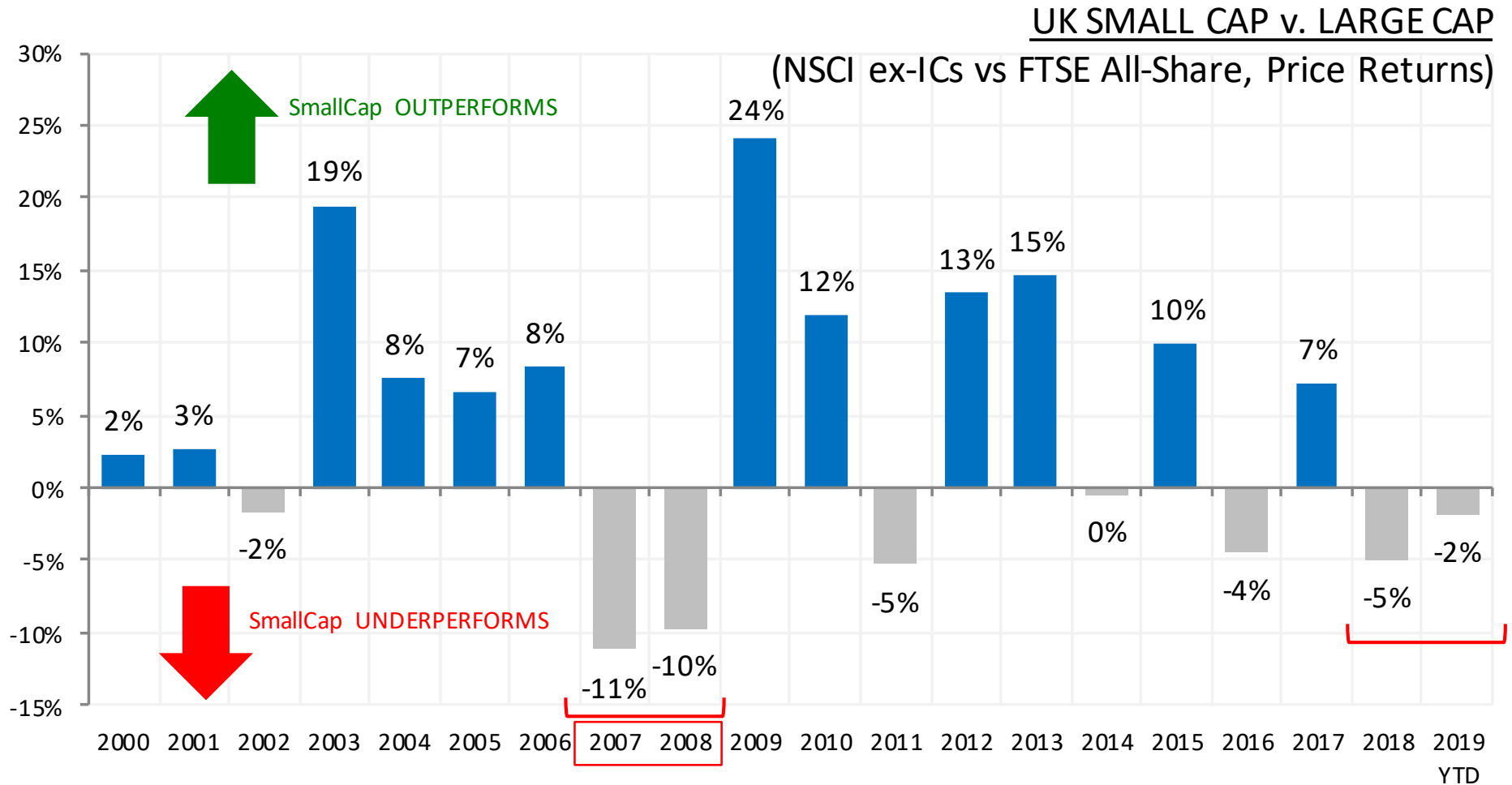
<i>(per annum)</i>	Dividends	EPS Growth	PE Change	Total Return
Numis SmallCap (ex.IT)	2.9%	5.7%	0.7%	+9.5%
MSCI Europe SmallCap	2.9%	5.0%	-0.1%	+7.9%
FTSE All-Share	3.8%	1.7%	0.4%	+5.9%
MSCI Europe MidCap	3.0%	3.4%	-1.7%	+4.6%
MSCI Europe	3.4%	1.5%	-0.9%	+4.0%
MSCI Europe LargeCap	3.5%	1.0%	-0.7%	+3.7%
S&P 500	2.2%	-0.3%	-1.9%	-0.3%
Small v. Large (Pan-Europe)				+4.2%
Small v. Large (UK)				+3.6%



Source: Montanaro model, based on data sourced from Bloomberg.

* Estimated Returns are calculated by Montanaro based on four components which are assumed to mean-revert by nature: 1) sales growth, 2) dividend yield, 3) profit margin change and 4) PE ratio re-rating. P/E ratios exclude loss-makers.

It would be unusual for SmallCap to underperform 2 years in a row



Source: Montanaro, Bloomberg.

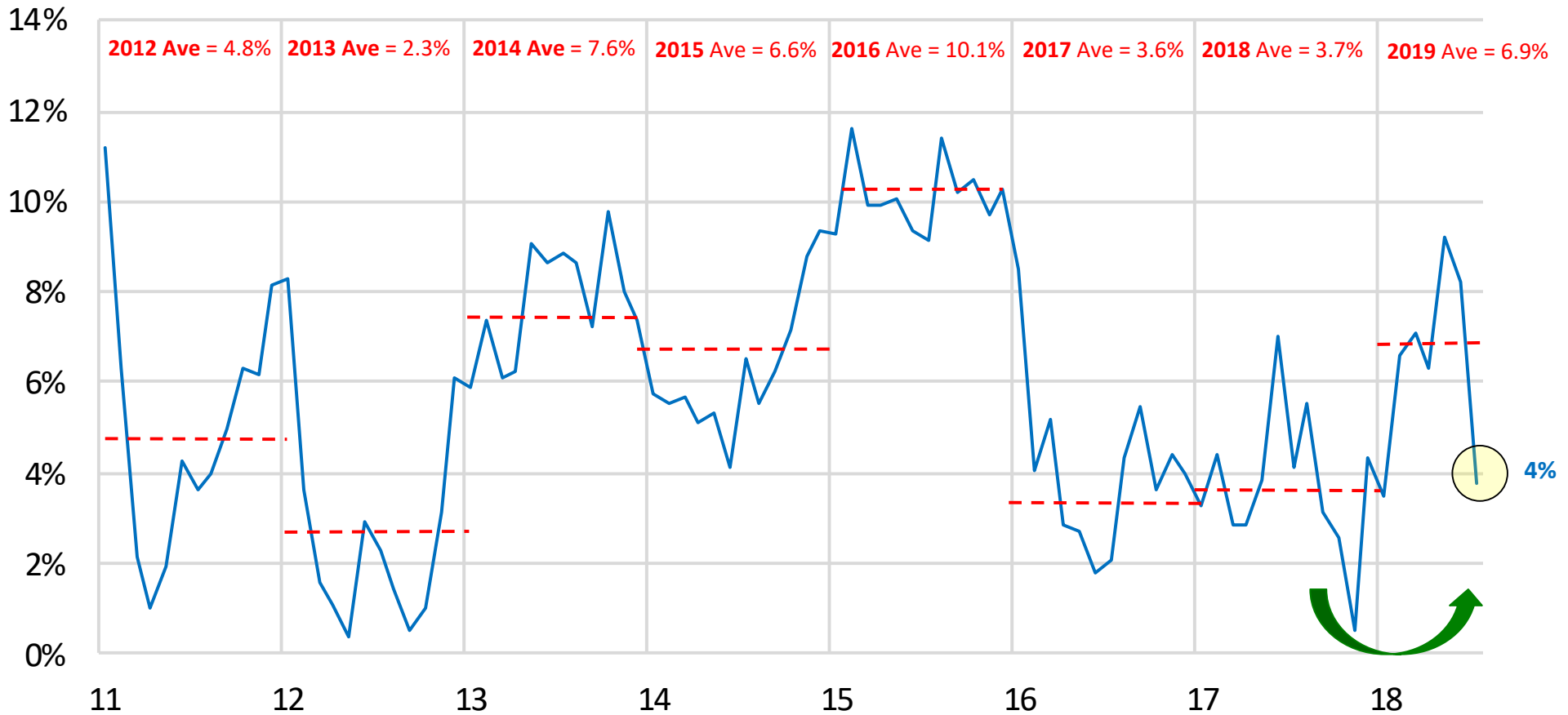
We are getting ready for the 4th quarter which is typically strong

Numis UK Smaller Companies ex-IC Index (£)	Q1	Q2	Q3	Q4
2000	1.3%	(3.4%)	2.4%	(2.3%)
2001	(9.0%)	1.8%	(22.6%)	17.9%
2002	1.7%	(9.0%)	(19.8%)	(0.1%)
2003	(6.6%)	25.3%	11.6%	6.1%
2004	8.4%	0.6%	(1.1%)	8.7%
2005	5.0%	1.7%	7.7%	8.1%
2006	10.1%	(4.6%)	5.4%	12.7%
2007	4.9%	(1.3%)	(7.3%)	(6.3%)
2008	(6.8%)	(9.6%)	(14.2%)	(21.2%)
2009	2.7%	21.7%	25.0%	(0.1%)
2010	7.8%	(7.5%)	13.4%	10.7%
2011	1.2%	3.0%	(15.7%)	0.5%
2012	17.7%	(6.6%)	8.7%	5.6%
2013	11.8%	(0.3%)	10.9%	7.7%
2014	3.0%	(4.8%)	(3.6%)	0.9%
2015	4.5%	5.3%	(3.9%)	1.6%
2016	(1.4%)	(5.6%)	11.8%	3.8%
2017	5.4%	2.5%	4.0%	3.4%
2018	(7.2%)	4.9%	(2.1%)	(13.8%)
2019	8.2%	0.3%		
MEDIAN	3.8%	0.0%	2.4%	3.4%
AVERAGE	3.1%	0.7%	0.5%	2.3%
% POSITIVE	75%	50%	53%	68%

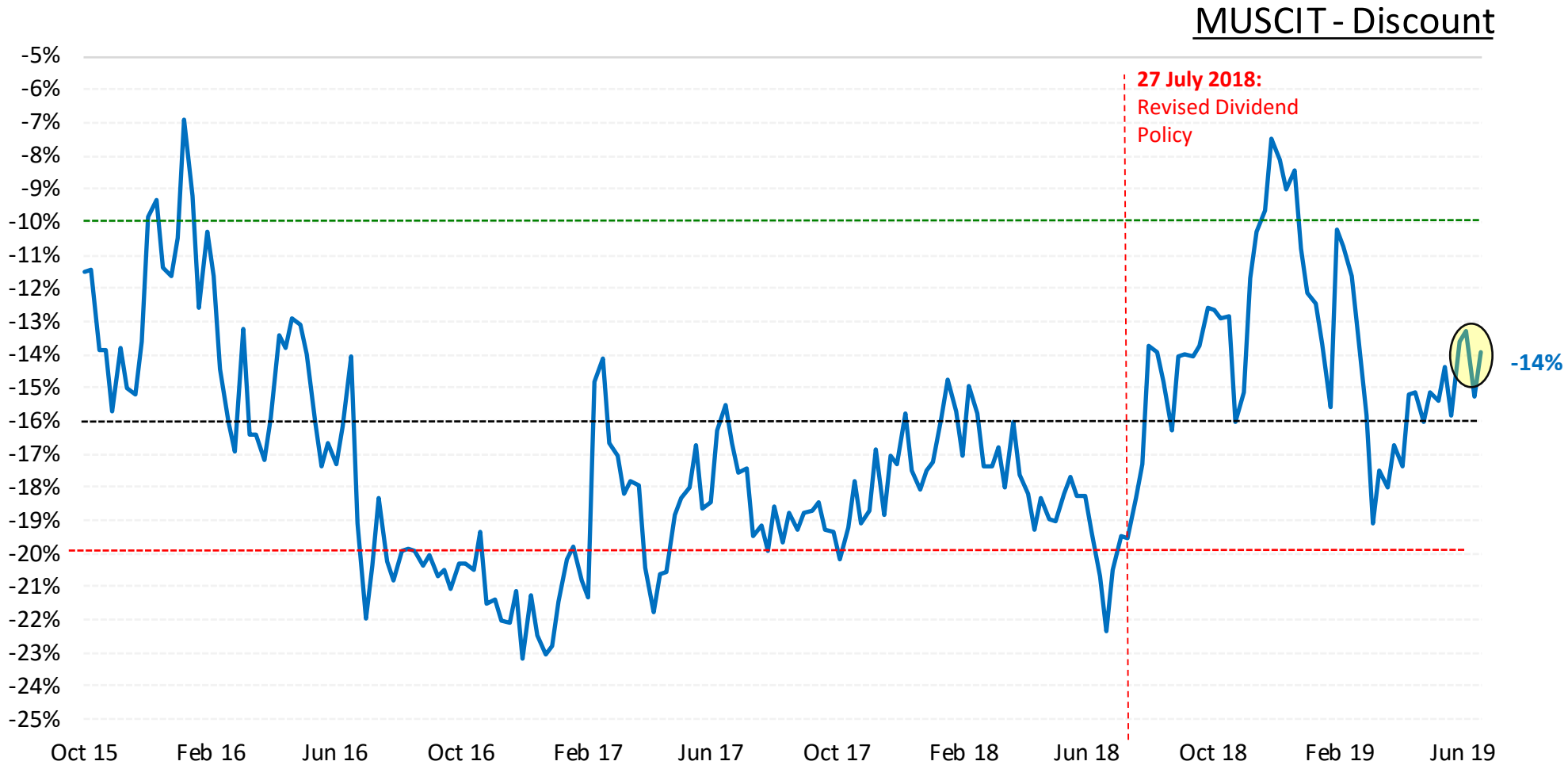
Source: Montanaro, Bloomberg.

... so we are keeping some dry powder for the Santa rally

MUSCIT Gearing (Annual)



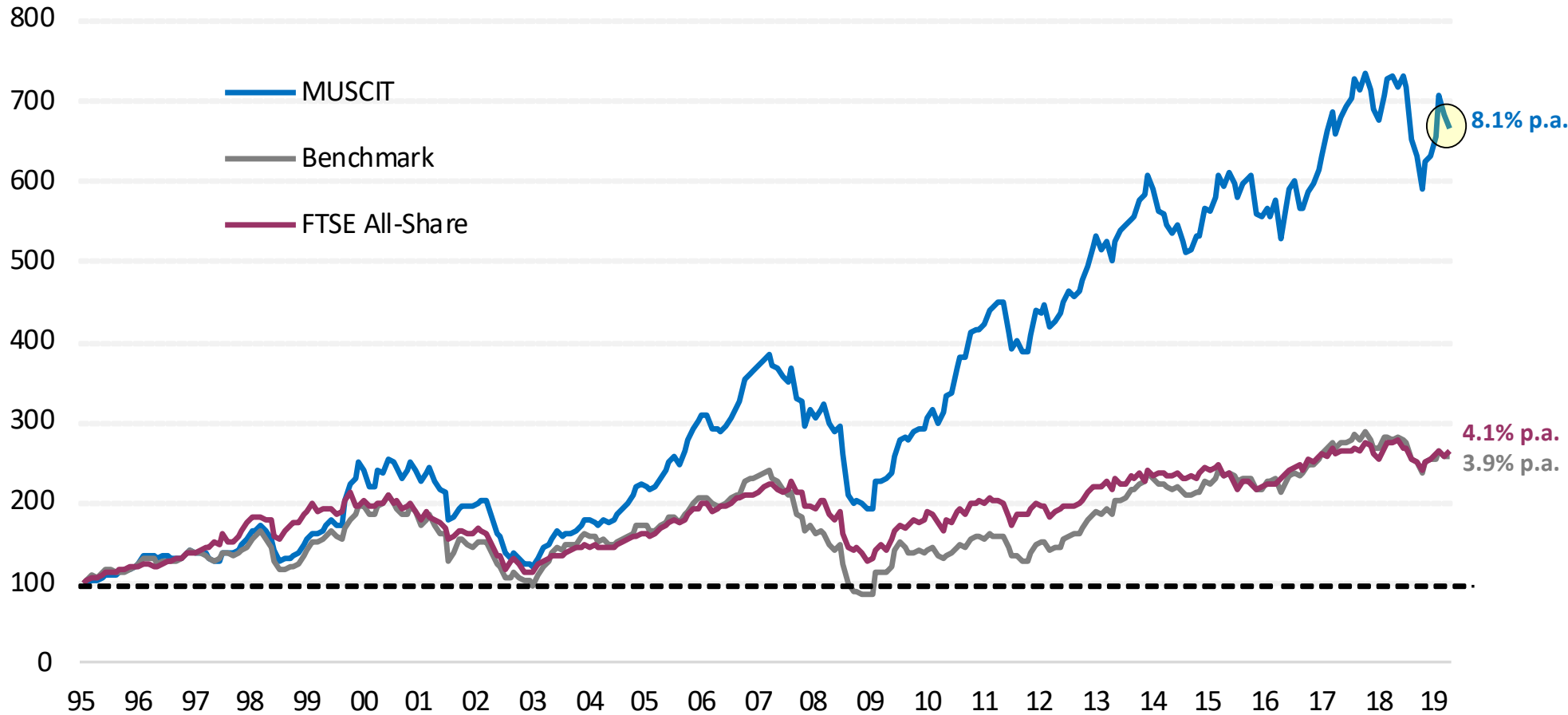
Discount



Source: Montanaro, Bloomberg.

MUSCIT has performed well since launch

Cumulative Returns since MUSCIT launch (31 Mar 1995 - 30 June 2019)



Source: Montanaro, Bloomberg.

Benchmark: Composite of the FTSE Small Cap (ex-ICs) until 1 April 2013 and the Numis Smaller Companies (ex-ICs) since then.

Note: Returns are NAV / Capital Returns.

Summary

1. Back in the saddle:
 - outperformed by c.4% in FY18
 - outperformed by c.2% in FY19
2. UK SmallCap could rebound as Brexit chaos nears resolution:
 - valuations are attractive
 - under-owned
 - medium-term upside
3. MUSCIT offers the most attractive yield in the sector (4.6%):
 - quarterly distributions (1% of NAV)
4. Despite a weakening economy, we expect a positive end to the year

Disclaimer

Important Notice

This document is issued by Montanaro Asset Management Limited (“MAM”) for distribution only to persons of the kind described in Article 11(3) of the Financial Services Act 1986 (Investment Advertisements) (Exemptions) Order 1995, or of a kind to whom this document may otherwise lawfully be issued or passed on. **It may not be copied or distributed or otherwise made available to any recipient without the express written consent of MAM.** The document is neither a prospectus, nor listing particulars, nor an offer or invitation to subscribe for, underwrite or purchase securities.

The information contained in this memorandum is intended for the use of professional and institutional investors only. It is for background purposes, is not to be relied upon by any recipient, and is subject to material updating, revision and amendment. No representation or warranty, expressed or implied, is made, and no liability whatsoever is accepted in relation thereto. This memorandum does not constitute investment advice. References to the outlook for markets are intended simply to help investors with their thinking about markets and the multiple possible outcomes. Investors should always consult their advisers before investing.

All data contained herein have MAM as its source unless otherwise stated. All data contained herein is at the date specified at the top of the page unless stated otherwise. All performance data have been calculated by MAM. Performance Attribution data in particular should be treated as indicative rather than definitive. Past performance is not necessarily a guide to future performance. The value of securities may go down as well as up. Foreign exchange exposure may increase the volatility of returns.

The value of securities may go down as well as up. As the discount or premium to which the investment trust shares trade relative to the NAV per share may vary significantly, the shorter term share price movements of the listed investment trust shares may not reflect the shorter term underlying investment performance in terms of NAV per share. The Board of Directors of the investment trust has authorised the Investment Manager to use bank borrowings, allowing increased portfolio investment, and therefore potentially to leverage the overall portfolio. This gearing as well as foreign exchange exposure may increase the volatility of returns.

MAM is authorised and regulated by the Financial Conduct Authority (“FCA”).