

## Montanaro European Smaller Companies Trust

### Quality businesses at sensible prices

Montanaro European Smaller Companies Trust (MTE) is an investment trust that has a focused portfolio of growing companies selected for the quality of their business franchise, management, earnings and corporate structure. Over time, this emphasis on quality has stood it in good stead, especially in periods where investors become increasingly nervous, as has been the case recently. The result is that MTE is the best-performing European smaller companies trust by some margin (see page 13).

European smaller companies lagged larger ones in the second half of 2018, bucking a long-term trend. There may be good reasons for investors' unease with the European economy, but the structural growth themes that MTE's portfolio is exposed to should persist regardless.

### Continental European smaller companies

MTE aims to achieve capital growth by investing principally in Continental European quoted smaller companies. The benchmark index is the MSCI Europe ex UK Small Cap Index (in sterling terms).

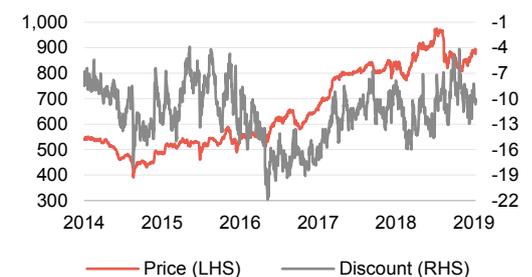
Year ended	Share price total return (%)	NAV total return (%)	MSCI Europe ex UK Small Cap TR (%)	MSCI Europe ex UK TR (%)	MSCI World total return (%)
28/02/15	(9.1)	(5.3)	0.7	4.5	17.0
28/02/16	12.9	13.9	6.8	(6.0)	(1.3)
28/02/17	23.2	28.5	30.4	26.2	35.8
28/02/18	28.0	16.9	20.2	11.2	6.0
28/02/19	7.0	6.3	(10.0)	(3.6)	4.0

Source: Morningstar, Marten & Co

<b>Sector</b>	European smaller companies
<b>Ticker</b>	MTE LN
<b>Base currency</b>	GBP
<b>Price</b>	875.0p
<b>NAV</b>	979.7p
<b>Premium/(discount)</b>	(10.7%)
<b>Yield</b>	1.0%

### Share price and discount

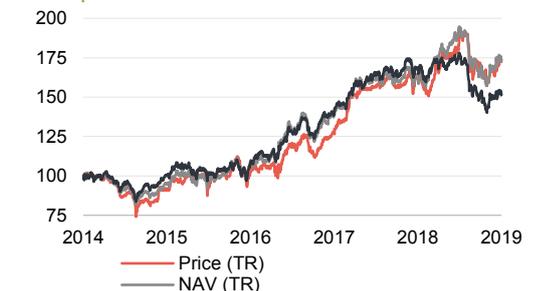
Time period 28/02/2014 to 07/03/2019



Source: Morningstar, Marten & Co

### Performance over five years

Time period 28/02/2014 to 28/02/2019



Source: Morningstar, Marten & Co

<b>Domicile</b>	Scotland
<b>Strategy inception date</b>	4 Sep. 2006
<b>Manager</b>	George Cooke
<b>Market cap</b>	146.4m
<b>Shares outstanding</b>	16.733m
<b>Daily vol. (1-yr. avg.)</b>	33,562 shares
<b>Net gearing</b>	0.6%

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## Fund profile

More information is available from the manager's website [www.montanaro.co.uk](http://www.montanaro.co.uk)

Montanaro European Smaller Companies Trust (MTE) aims to achieve capital growth by investing principally in smaller, quoted, Continental European companies (those within the European Union, Norway and Switzerland) but is not restricted from investing in smaller companies quoted on other European stock exchanges. The benchmark index is the MSCI Europe ex UK Small Cap Index (in sterling terms).

The original company dates back to 1981, but Montanaro Asset Management Limited (MAML) took on the management of the trust in September 2006 and the European small cap investment approach dates from then. MAML had £2bn of assets under management at the end of December 2018. The key members of the team are listed on page 16.

## Market backdrop

Europe is growing but more slowly

The EU economy, as measured by GDP growth, is thought to be slowing as we enter 2019. European Commission (EC) forecasts are slightly more optimistic than those of the International Monetary Fund (IMF); the European Commission expects growth to slow to 1.5% in 2019 from 1.8% in 2018, but they are looking to a reacceleration of growth in the second half of 2019, and a better 2020. One of the brakes acting on EU growth is a sharp fall in German exports to China, which is reflective of weak Chinese demand.

Monetary policy is accommodative

European Central Bank (ECB) policy remains accommodative, with the [repo rate](#) set at zero and no move yet to reverse quantitative easing (QE). Unemployment has been on a declining trend and this is supportive of retail sales growth. Official figures suggest that sales grew by 1.4% year-on-year in 2018 within the euro area, and by 2.0% across the EU as a whole.

It is worth noting that the EU figures include the UK, which has been one of the worst-performing European economies as we approach Brexit. The EU acknowledges that Brexit creates some uncertainty around forecasts for 2019.

After a long run of outperformance, European small cap stocks underperformed large caps in 2018, but, as discussed later, MTE strongly outperformed its benchmark.

Figure 1: MSCI Europe ex UK small cap relative to MSCI Europe ex UK large cap



Source: Morningstar, Marten & Co

Investors focus more on quality when they are nervous

The manager acknowledges that high-quality companies and growth companies go in and out of fashion with investors. As growth concerns have become heightened, investors have become more nervous. The manager notes that nervous markets punish stocks that disappoint by missing earnings or sales growth targets. In such an environment, high-quality companies are favoured. This suits MAML's investment style.

A number of structural growth themes are factored into stock selection

MAML's investment approach is driven by stock selection and, while macroeconomics is factored into decision making, it does not drive asset allocation. MAML likes companies exposed to structural growth themes. Currently, these include:

- Demographics – ageing populations;
- Healthcare – older, richer people demand more healthcare and novel therapies create new markets;
- Nutrition – feeding a growing, more affluent and more discerning world;
- Outsourcing – drive to cut costs;
- Leisure – as MAML says “we all want to have fun”;
- Innovation – software, robotics, efficient manufacturing;
- Connectivity – the world at our fingertips; and
- Environment – addressing climate change, pollution and finite resources.

## Investment process

### The underlying philosophy

Simple, niche, market leaders with high and sustainable returns, profitable and with good management

MAML wants to invest in:

- simple businesses that it can understand;
- niche businesses in growth markets (companies whose fortunes don't wax and wane with economic cycles, growing organically);
- market leaders (strong, defensible market positions and pricing power);

- companies with high operating margins and high returns on capital (barriers to entry/a sustainable competitive advantage);
- profitable companies trading at sensible valuations; and
- good management that it trusts (aligned to shareholders and demonstrating sound environmental, social and governance (ESG) practices).

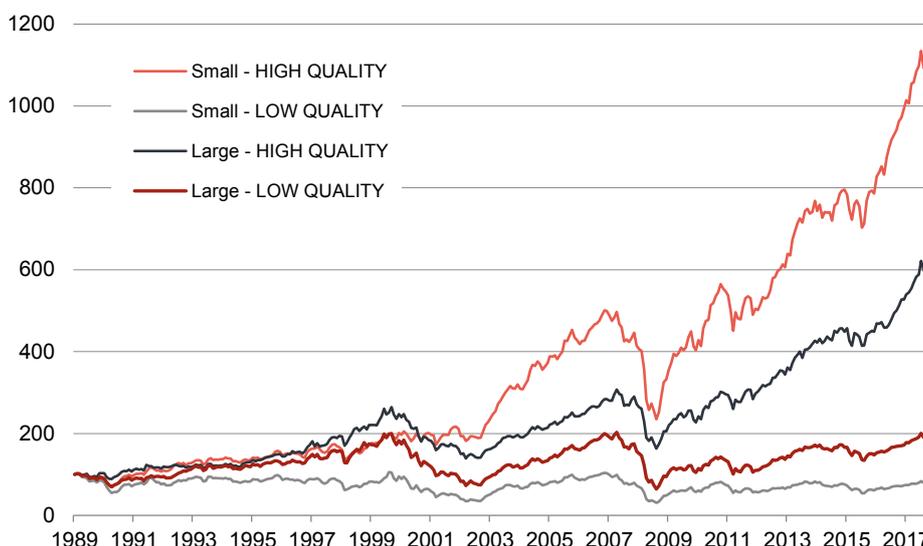
This could be summed up as investing in high quality businesses at sensible prices. Furthermore, MAML believes it is important to:

- do the work yourself (rather than relying on brokers);
- be passionate; and
- learn from mistakes (humility goes a long way).

MAML believes that it is easier for small cap managers to beat indices than large cap managers

In addition, MAML believes that it is easier to add value through stock selection for a small and mid-cap portfolio, especially given the relative lack of research available on these companies.

**Figure 2: Small cap “quality growth” has performed best – global excess returns by size and quality 1989-2018, excess returns versus T-Bills**



Source: AQR Capital Management, MAML

Over the past 20 years, European small cap has beaten large cap by 5.4% per annum

Figure 2 might suggest that this approach works. Figure 1 showed the outperformance of European smaller companies relative to the wider MSCI Europe index over five years. Taking a longer-term view, over the 20 years ending 31 January 2019, European smaller companies (as represented by the MSCI Europe ex UK Small Cap index) have outperformed larger companies (as represented by the MSCI Europe ex UK large Cap index) by 5.4% per annum (source: Morningstar).

### Sifting through the universe

MAML’s approach is designed to select around 200 quality companies from a universe of about 4,000

The constituents for MTE’s portfolio are drawn from a universe of about 4,000 companies listed in Europe. The focus is on those with a market cap between €100m and €5bn (about 2,300) and, as described below, unprofitable companies are excluded which reduces the pool to about 1,700 stocks. The benchmark index currently includes stocks with market caps of up to €7bn.

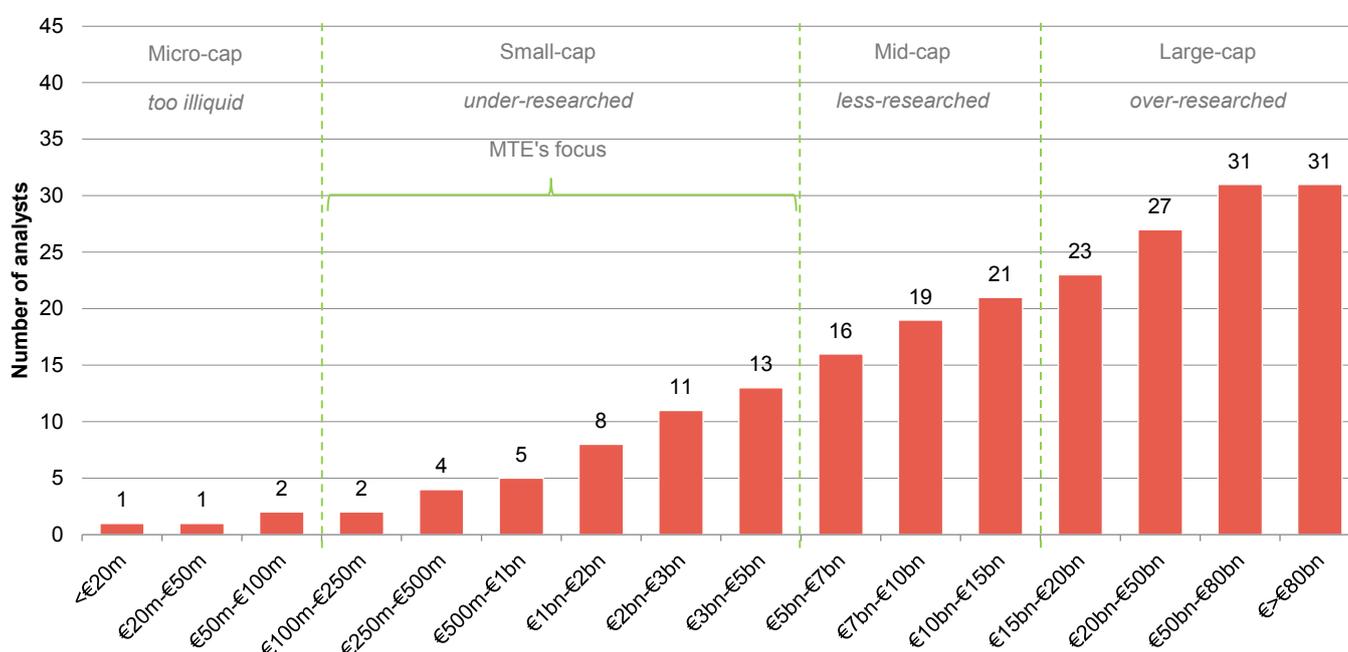
MTE is a true stock-picking portfolio; index-weightings play no part in forming its portfolio construction. MAML has always generated its own investment ideas rather than relying on external analysts. There are many good reasons for this but it is also

fortunate as the availability and quality of external analysis, which MAML believes has been on a declining trend for some time, has been exacerbated by MiFID II (regulations brought in last year that, amongst other things, make brokers charge people to read their research). The upshot is that there are many stocks within MTE's universe that have no research coverage at all. This should give MAML a competitive edge, that is sharpened by the strength and depth of its research team (see page 16).

The depth and experience of MAML's team gives the firm a competitive edge

The size of the team allows for some theoretical research and lateral creative thought is encouraged. MAML is an entrepreneurial boutique with a flat structure that allows for quick decision-making and avoids the politics that bog down more bureaucratic large asset managers. MAML does not encourage the development of 'star' fund managers but is focused on staff retention, including the granting of staff options over MAML equity. MAML's 'back office' functions are carried out in-house rather than being outsourced (as they are in many smaller investment management boutiques).

Figure 3: Average number of sell-side analysts by market cap (pan-Europe)



Source: MAML, Factset as at 30 June 2018

Research responsibilities are distributed amongst the team on a sector, pan-European basis (although analysts may also compare and contrast European companies to global peers). Emphasis is placed on being well-prepared for meetings, which is possible as the research team is well-resourced. MAML's analysts can then set the agenda, challenge management and get the information that they need. Site visits are encouraged (another perk of having a large team is that it is not desk-bound).

On average, each analyst will seek to identify 20 stocks within their sector coverage worthy of closer scrutiny. These will form the pool from which portfolio constituents are drawn. The first part of the process is to eliminate poor-quality companies. These stocks are identified by applying a quantitative (numbers-based) screen to the wider universe. Loss-making companies, those with poor cash flow and highly indebted businesses are all rejected. Stocks that fit structural growth themes that the team has identified may be prioritised. Each company within the universe is assigned a quality rating (D to AAA).

All stock ideas are reviewed and approved by an investment committee

Then the detailed work starts. The analysts build a financial model and conduct a 'SWOT' (strengths, weaknesses, opportunities and threats) analysis on each stock. They also check whether a stock meets MAML's ESG criteria (see below). Then the

Value is assessed on a range of measures but only after the quality evaluation is complete

idea is put before MAML's investment committee, who challenge assumptions and ask for more information if they feel this is warranted. Stocks that pass these quality thresholds may then go on to an approved list of approximately 200 companies. No fund manager can buy a company that is not on the approved list.

Now, attention turns to valuation. Various valuation tools are considered. There is a strong emphasis on discounted cash flows but price/earnings ratios, free cash flow yield, dividend yield (both in absolute terms and relative to peers) are also included. The team operates with a time horizon of five to 10 years. The ideal investment should provide a margin of safety in excess of 25% over its intrinsic value. Analysts will also look at risk factors before assigning a recommendation to each stock. These will be presented to the whole team at weekly meetings and the fund managers will then decide which stocks make it into portfolios. Once a stock makes it into a portfolio, it will usually remain there for many years.

## Portfolio construction

MTE's investment policy is more fully described in its Annual Report. It only invests in listed securities and MAML says that unquoted companies are not eligible for consideration.

Some other rules apply:

- MTE does not hedge its currency exposure;
- there are no formal restrictions on country or sector weightings but, in practice, the manager tries to ensure that MTE's portfolio is not more than 10% (in absolute terms) above/below the benchmark in any sector or country;
- MAML will hold no more than 10% of the voting rights in any company (across all funds managed by MAML); and
- no more than 10%, in aggregate, of the value of its total assets at the time of investment, will be invested in other investment trusts or investment companies admitted to the Official List of the UK Listing Authority. Currently, MTE has no holdings in other investment trusts nor does it expect to ever do so.

Position sizes determined by conviction

Typically, the target weighting for a new position will be between 1% and 3.5%, depending on both the strength of conviction that the manager has in the stock, and its liquidity. The total number of holdings is typically around 50. There is no obligation to sell a company if its market cap exceeds €5bn but these will be gradually reduced with the proceeds recycled into lower market cap companies. The manager will ensure that a single position does not exceed 7.5% of the portfolio.

## ESG analysis

ESG principles are at the heart of MAML's stock selection decisions and a number of sectors will not be represented within the portfolio

MAML's focus on quality is supported by its commitment to ESG principles. It has an internal ESG committee that meets quarterly and oversees MAML's efforts in this area. MAML also has its own handbook, policies and checklists. It votes the shares it controls, and engages with companies. MAML expects the companies that it invests in to improve their ESG awareness and it monitors their progress.

Some sectors are excluded from portfolios on ESG grounds. MAML portfolios will not contain tobacco companies; companies manufacturing weapons, facilitating gambling or manufacturing alcohol; companies engaged in oil and coal-related exploration and production; companies involved with pornography; and those making high interest-rate loans. Corporate governance checks include an assessment of a company's remuneration policy.

### Sell discipline

Stocks exit the portfolio for a variety of reasons. For example, when they become significantly overvalued, if they become too big, or are subject to takeovers.

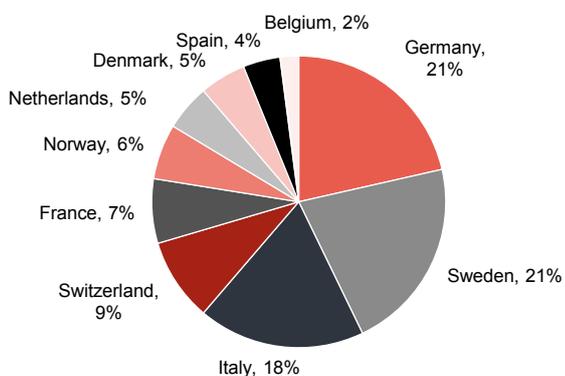
Furthermore, stocks may leave the portfolio if the analysts identify unfavourable changes in the fundamentals of the business or an unfavourable management change.

Stocks will also be sold if they no longer pass MAML's quality threshold, or if a new opportunity comes along that offers better prospects.

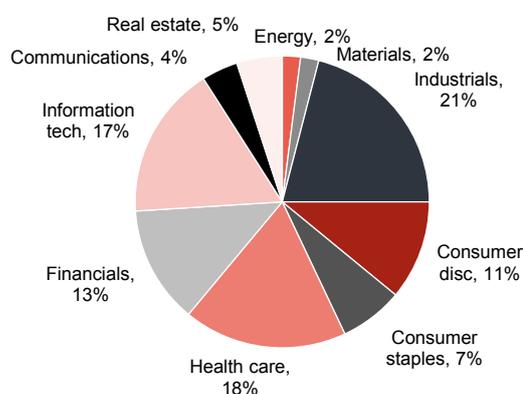
### Asset allocation

There were 54 holdings in the portfolio at the end of January 2019.

**Figure 4: Geographic asset allocation at 31 January 2019** **Figure 5: Sector asset allocation at 31 January 2019**



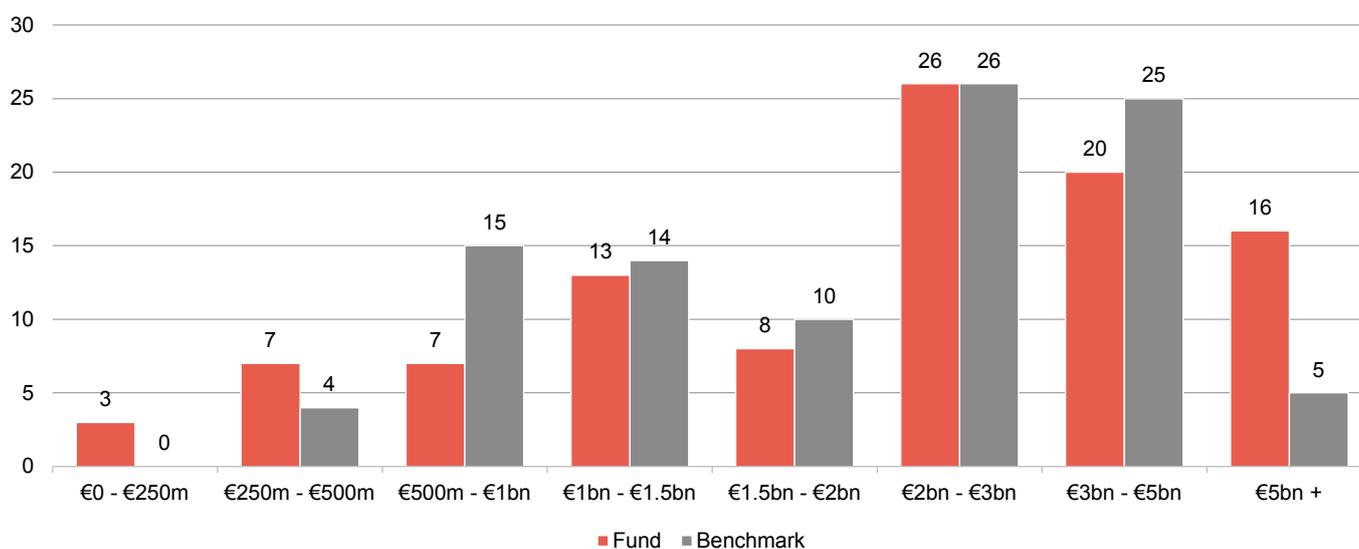
Source: MAML, Marten & Co



Source: MAML, Marten & Co

Geographic and sector allocations are a function of stock selection, but MTE has had a long-term overweight exposure to healthcare and technology companies relative to its benchmark.

**Figure 6: Percentage portfolio distribution by market cap at 31 December 2018**



Source: MAML

The 16% of the portfolio invested in stocks with a market cap greater than €5bn will be rotated gradually into new investment opportunities. Furthermore, the trust's relatively low level of gearing (see page 15) means that the manager has additional firepower to take advantage of opportunities as they arise.

10 largest holdings

Figure 7: MTE 10 largest holdings at 31 January 2019

Heading	Holding 31/01/19 (%)	Holding 30/09/18 (%)	Change (%)	Country	Sector
MTU Aero Engines	3.6	3.4	0.2	Germany	Aircraft engines and components
IMCD	3.5	3.4	0.1	Netherlands	Speciality chemicals distributor
CTS Eventim	3.1	3.0	0.1	Germany	Online ticketing platform
Recordati	3.1	2.6	0.5	Italy	Global pharmaceuticals
Merlin Properties	2.6	2.3	0.3	Spain	Spanish commercial property
Elekta	2.6	2.3	0.3	Sweden	Radiation therapy equipment and software
VZ Holding	2.5	2.6	(0.1)	Switzerland	Wealth manager
Cerved Group	2.5	2.8	(0.3)	Italy	Credit analysis/credit management
Simcorp	2.5	2.4	0.1	Denmark	Inv. management software
Nemetschek	2.5	1.9	0.6	Germany	Construction software
<b>Total</b>	<b>28.5</b>				

Source: MAML, Marten & Co

Looking at some of these in more detail:

MTU Aero Engines

Figure 8: MTU Aero Engines share price



Source: Bloomberg, Marten & Co

MTU Aero Engines ([www.mtu.de](http://www.mtu.de)) is a leading manufacturer of aircraft engines in Germany. In addition, it supplies components and undertakes maintenance, repair and overhaul work in support of a wide range of commercial and military aircraft and stationary gas turbines. It works with all the major OEMs (original equipment manufacturers). MAML notes that the company has collaborated on a geared turbo fan engine with Pratt & Whitney (the PW1100G-JM) that reduces fuel consumption and noise, and has been incorporated into the A320 neo, a new family of narrow-body planes being produced by Airbus. MTU Aero Engines recently reported a 17% increase in revenue and operating profit for 2018.

IMCD

Figure 9: IMCD share price



Source: Bloomberg, Marten & Co

IMCD ([www.imcdgroup.com](http://www.imcdgroup.com)) is a global distributor of speciality chemicals and food ingredients to a wide range of end users. These often form a small part of the cost of the final product, but are key to its production. The manufacturers outsource distribution to IMCD rather than deal with a large number of small customers. IMCD has few significant competitors, some manufacturers still sell directly but many other distributors are much smaller players. IMCD has been growing organically but has also made some bolt-on acquisitions. Its 2018 Q3 earnings report showed a year-on-year EBITDA (earnings before interest, tax, depreciation and amortisation) increase of 26% and a 23% increase in its cash earnings per share.

**Figure 10: CTS Eventim share price**



Source: Bloomberg, Marten & Co

**Figure 11: Recordati share price**



Source: Bloomberg, Marten & Co

## CTS Eventim

CTS Eventim ([www.eventim.de](http://www.eventim.de)) is a global ticketing business. It also operates several venues across Europe, including the EVENTIM Apollo in London. The manager considers that this is a growing market. CTS Eventim is dominant within its sector in Europe and has a platform on which to expand. It is possible that this company could be a bid target but it is not MAML's strategy to buy companies on this basis. CTS Eventim reported a 24% increase in revenue and a 17.5% rise in normalised EBITDA for the first nine months of 2018. Online ticketing grew organically by 8.7% over this period.

## Recordati

Recordati ([www.recordati.com/en](http://www.recordati.com/en)) is an Italian pharmaceutical company focused on developing therapies for rare diseases. It also has a portfolio of drugs targeted at the cardiovascular, gastrointestinal, urogenital, musculoskeletal, respiratory and other sectors. The manager added to the MTE holding on weakness and it has since recovered. The dip in the share price was triggered when the controlling family sold its stake at a discount to the market price to a private equity investor, CVC. 2018's results showed a 5% rise in revenue and 9.8% uplift in EBITDA.

## Portfolio characteristics

**Figure 12: Portfolio characteristics – comparison with MSCI Europe ex UK Small Cap, based on 2019 forecasts**

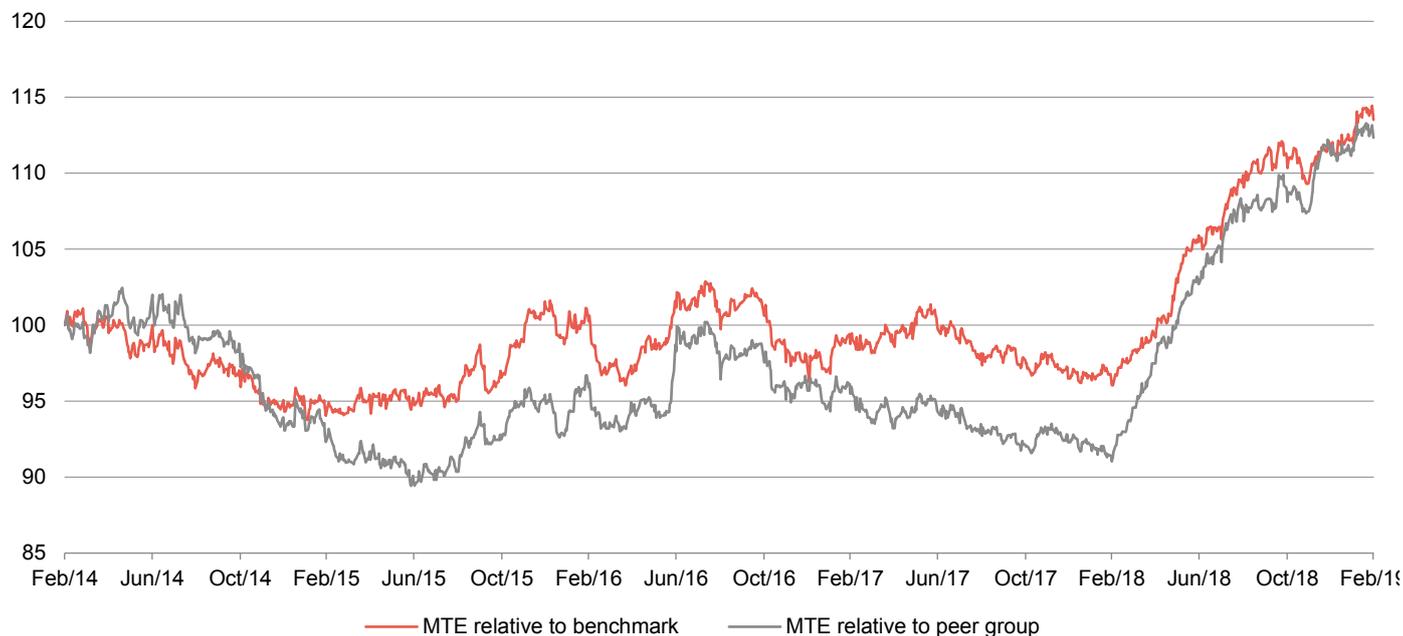
	MTE	Benchmark
Number of stocks	54	731
Weighted market cap (GBP)	2.6bn	2.2bn
EBIT margin	25%	18%
Return on Equity	17.0%	10.7%
Tracking error	5.6%	n/a
Net debt/equity	9%	33%
% of companies with net cash	43%	26%
Sales growth	7.2%	4.2%
EBIT growth	11.7%	8.6%
Earnings per share growth	14.7%	10.5%
Dividend per share growth	11.1%	9.4%
Price/earnings ratio	18.9	12.8

Source: MAML

The companies in MTE's portfolio typically deliver higher sales and earnings growth than the average European small cap company. Their higher quality is reflected in higher margins and returns on equity, as well as lower levels of debt.

## Performance

Figure 13: MTE NAV total return performance relative to MSCI Europe ex UK Small Cap and peer group average



Source: Morningstar, Marten & Co

Over the long term, MTE’s relative performance is determined by the cumulative effect of the manager’s stock selection decisions. However, short-term swings in market sentiment can also have an impact. While not shown in Figure 13, 2013 was a difficult year for the trust, as ECB chairman, Mario Draghi’s promise to do whatever it takes to save the Euro and the subsequent introduction of quantitative easing benefitted lower-quality stocks that might otherwise have struggled to survive. Likewise, periods of excessive exuberance, whilst positive for the NAV, are generally unhelpful for relative performance, as ‘blue sky’ stocks with dubious earnings potential are lauded by investors. There was an element of this in 2017 and the beginning of 2018.

Faced with stalling growth and discussion of an end to QE in Europe, investors began to look for quality of earnings in the second half of 2018, to the benefit of MTE. The manager also cut the trust’s borrowings ahead of 2018’s market turmoil and this proved beneficial.

Figure 14: MTE cumulative total return performance over periods ending 28 February 2019

	3 months (%)	6 Months (%)	1 year (%)	3 years (%)	5 years (%)
NAV	3.9	(9.5)	6.3	59.7	72.3
Share price	2.5	(8.1)	7.0	68.8	73.3
Benchmark	0.2	(13.1)	(10.0)	41.1	51.8
Peer group average (NAV)	(0.6)	(14.0)	(13.8)	36.4	53.4
Peer group average (Price)	(0.6)	(13.1)	(27.2)	47.7	57.7

Source: Morningstar, Marten & Co

As Figure 14 shows, MTE has outperformed its benchmark and the average of its peer group (defined on page 13) over most time periods.

### Performance attribution

Figure 15 sets out the largest positive and negative contributions to MTE's performance during 2018.

Figure 15: MTE performance attribution relative to benchmark over 2018 calendar year

Positive contributions			Negative contributions		
		(%)			(%)
Sartorius Stedim	Fra	+1.7	Cerved Group	Ita	(0.5)
SimCorp	Den	+1.2	Krones	Ger	(0.5)
MIPS	Swe	+1.0	Melexis	Bel	(0.4)
Elekta	Swe	+0.9	RaySearch Laboratories	Swe	(0.4)
Fortnox	Swe	+0.9	Dr. Hoenle	Ger	(0.3)

Source: MAML

Looking at some of these in more detail:

### Sartorius Stedim

The manager has been taking profits on Sartorius ([www.sartorius.com/en](http://www.sartorius.com/en)), which for some time was the largest position in the portfolio and has performed very well over the years. MAML added to the position about a year ago after it was hit by hurricane damage to its Puerto Rican manufacturing facility. The company makes equipment needed to produce biologics and biosimilars, such as vaccines and monoclonal antibodies. Their focus on single use equipment enables their customers to manufacture biologics in a cheaper and more flexible way than the traditional stainless-steel alternatives. MAML's sales of Sartorius were driven by the size of the position and the valuation (now a €10bn market cap company).

Figure 16: Sartorius Stedim share price



Source: Bloomberg, Marten & Co

### MIPS

MIPS ([www.mipsprotection.com](http://www.mipsprotection.com)) was an IPO a couple of years ago. It makes inserts for helmets that help absorb some of the impact of accidents on the brain (helping to reduce the transmission of rotational motion to the brain). MIPS's product is suitable for almost any helmet. The product is protected by patents, but these were challenged by the major helmet manufacturers. MIPS won the court case and the manager, having monitored and analysed the stock for some time before this, bought a position.

Figure 17: MIPS share price



Source: Bloomberg, Marten & Co

### Cerved Group

Cerved Group ([www.cerved.com/en](http://www.cerved.com/en)) is a credit-scoring company in Italy used by businesses. It has high recurring revenue, high margins and some growth. Cerved also has a business that buys non-performing loans (those where the borrower has failed to make an interest payment or capital repayment on-time) for a fraction of face value and then works on recovering the debt. The shares have been weak on concerns about Italy's financial situation (including the budget dispute with the EU). There has also been some management change. MAML is retaining the holding.

Figure 18: Cerved Group share price



Source: Bloomberg, Marten & Co

### Peer group

MTE has been the best performing fund in the peer group. Up-to-date information is available from the [QuotedData website](#)

We have compared MTE with the other trusts in the AIC's European smaller companies sector. Whilst a respectable size, MTE is the smallest of these. It also has the lowest yield, reflecting the focus on growth companies (NB: European Asset's yield is artificially inflated by payments from capital). MTE's ongoing charges ratio is in line with funds of an equivalent size. MTE's discount is towards the lower end of the group (European Assets' discount may be depressed as investors have been attracted by its high yield).

Figure 19: Peer group comparison at 7 March 2019

Heading	Market cap (GBPm)	Premium/ (discount) (%)	Yield (%)	Ongoing charges (%)
Montanaro European Smaller Companies	146	(10.7)	1.0	1.20
European Assets	356	(9.3)	6.1	1.31
JPMorgan European Smaller Companies	549	(12.7)	1.9	1.03
TR European	433	(10.8)	2.5	0.70
Peer group average	371	(10.9)	2.9	1.06

Source: Morningstar, Marten & Co

MTE has been the best performing fund in the peer group over all time periods in Figure 20.

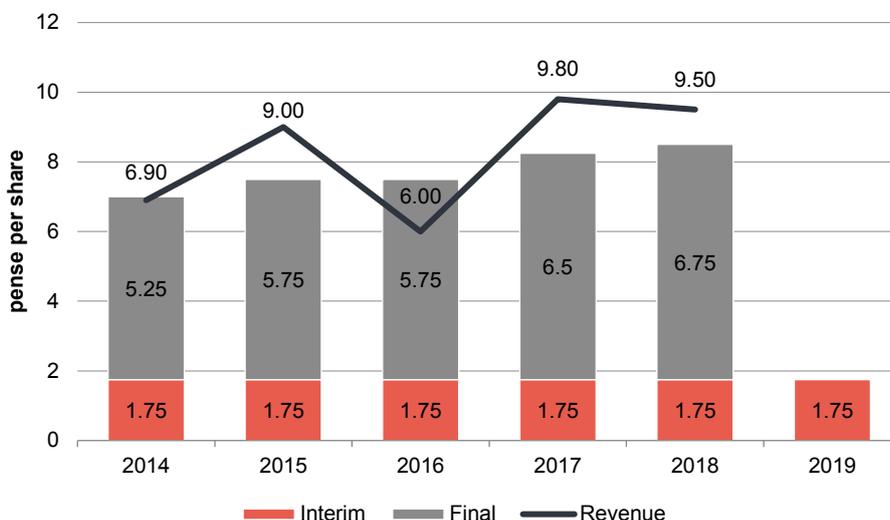
Figure 20: Peer group cumulative NAV total return performance over periods ending 28 February 2019

	3 months (%)	6 Months (%)	1 year (%)	3 years (%)	5 years (%)
Montanaro European Smaller Companies	3.9	(9.5)	6.3	59.7	72.3
European Assets	1.7	(11.0)	(9.3)	26.1	47.6
JPMorgan European Smaller Companies	(2.7)	(15.1)	(12.3)	39.0	54.7
TR European	(0.5)	(15.5)	(19.0)	44.6	57.8
Peer group average	(0.6)	(14.0)	(13.8)	36.4	53.4

Source: Morningstar, Marten & Co

### Dividend

Figure 21: MTE dividend history, accounting years ending 31 March

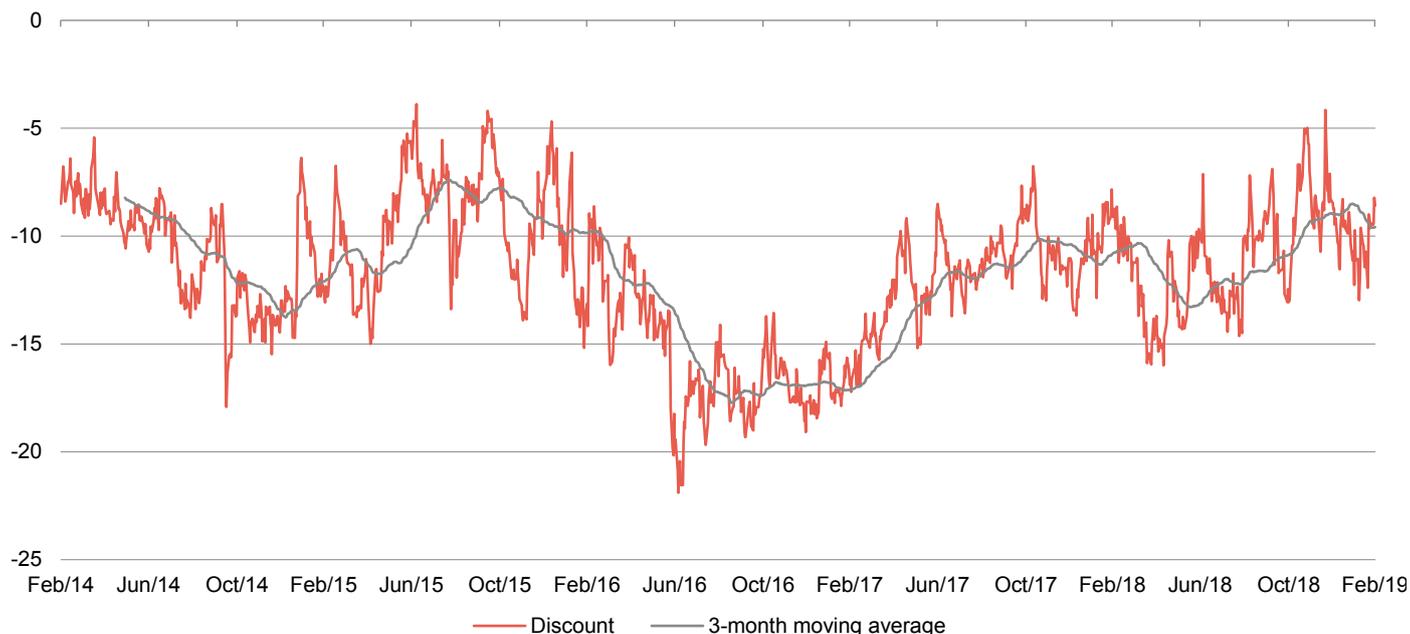


Source: MAML, Marten & Co

MTE's primary aim is to deliver capital growth to its shareholders. However, its substantial revenue reserve, combined with the long-term growth in dividends of the companies in which it invests, has allowed it to maintain a consistent dividend pay-out.

## Discount

Figure 22: MTE discount over five years ending 28 February 2019



Source: Morningstar, Marten & Co

MTE's discount has been on a narrowing trend for some time

MTE's discount has been on a narrowing trend for some time (effectively since the EU referendum, although this may just be coincidence and is more likely to reflect MTE's positive performance track record). Over the year to the end of February 2019, MTE's discount moved within a range of 4.2% to 16.0% and at 7 March 2019 it was 10.7%.

MTE has powers to issue and buyback shares, which it renews regularly at its annual general meeting. In practice, no shares have been issued or repurchased for some time. Shares repurchased can be held in treasury and may be reissued. The board has said that these would only be reissued at a premium to NAV at the time of reissue or at a discount, provided this discount was lower than the weighted average discount at the time the shares were repurchased. The net effect of this should be that purchasing the shares and reissuing them again is profitable for ongoing shareholders.

The board has stated that it will consider a buyback of shares where the discount of the share price to the NAV per share is greater than 10% for a sustained period of time and is significantly wider than the average for similar trusts. The board will take into consideration the effect of the buyback on the liquidity of the company's shares.

In addition, the board encourages the manager to market the company to new investors.

MAML's annual management charge is based on market cap which gives it an incentive to narrow the discount

## Fees and costs

MAML is MTE's investment manager and AIFM. It is entitled to receive a management fee of 0.9% of MTE's market capitalisation, payable monthly in arrears. Such a fee structure incentivises the manager to keep the company's discount narrow. MAML is also entitled to a fee of £50,000 a year for acting as the AIFM. There is no performance fee. The management contract can be terminated by either side on six months' notice. MTE charges 35% of the management fee against revenue and the balance against capital. The same methodology is applied to the accounting treatment for interest on MTE's borrowings.

BMO Investment Business Limited provides company secretarial and general administrative services currently (its fee was £129,000 for the year ended 31 March 2018). Equiniti Limited acts as Registrar and The Bank of New York Mellon (International) Limited as the company's Depositary. The company's auditor is Ernst & Young. The company's ongoing charges ratio for the year ended 31 March 2018 was 1.2%, unchanged from the previous year.

## Capital structure and life

MTE has 16,733,260 ordinary shares in issue and no other classes of share capital. In addition, 715,000 shares are held in treasury.

The company's accounting year end is 31 March. Annual accounts are published around the end of June/beginning of July and the AGM is usually held in July or August.

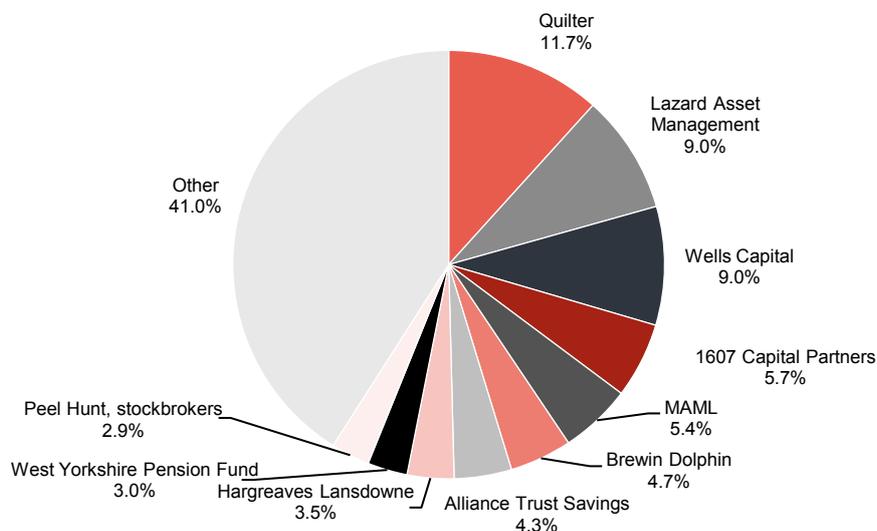
## Gearing

The board has set a maximum limit on borrowing, net of cash, of 30% of shareholders' funds at the time of borrowing. The board, in discussion with the manager, regularly reviews the company's gearing strategy and approves the arrangement of any gearing facility. The board believes that the ability to use gearing offers a strong competitive advantage over alternative open-ended investment funds. Therefore, it strongly encourages the active use of gearing by the manager. At the end of January 2019, MTE's gearing was 0.6%.

MTE has a €10m secured loan maturing on 13 September 2023 that carries a fixed rate of interest of 1.33%, and a €15m revolving credit facility until 13 September 2023, both provided by ING Bank NV.

Major shareholders

Figure 23: MTE's largest shareholders



Source: MTE, Marten & Co

Management team

The largest and most experienced small cap team in Europe

MAML was established in 1991 and is chaired and owned (100%) by Charles Montanaro. However, the wider team has options over 43% of the equity. The CEO is Cédric Durant des Aulnois. Mark Rogers is head of research and the lead manager on MTE is George Cooke. These four are all members of the investment committee, which also includes two other fund manager/analysts, Stefan Fischerfeier and Alex Magni.

They are supported by what MAML believes is the largest and most experienced team in Europe, specialising in researching and investing in quoted small and mid-cap companies. The team is 29-strong altogether, including an investment team of 11. The team is multi-lingual and multi-national (nine countries in all). All but one of the fund managers also have research responsibilities.

In addition to MTE, the team manages a range of funds focused on UK and European equities and, most recently, the Montanaro Better World Fund, an open-ended fund investing in small and mid-cap companies supporting the [UN Sustainable Development Goals](#). MAML's total assets under management at 31 December 2018 was £2bn.

**Charles Montanaro's** investment career began in 1980 with a spell as a private client broker at Merrill Lynch. He joined Dean Witter Reynolds in 1984 and Drexel Burnham Lambert in 1987. At both firms he was their top institutional broker in the UK. He joined Drexel's high yield bond team in 1989 and moved to MMG Patricof (now Apax Partners) in 1990 before founding MAML in August 1991.

**Cédric Durant des Aulnois** joined MAML in 2007 as an analyst and became responsible for business development in 2011. He was appointed CEO on 1 January 2016. His earlier career got under way in 2000 when, having graduated from the LSE, he joined IDEA Global as a UK equity analyst. He later joined Fox-Pitt Kelton as a French banking analyst and then moved to Lehman Brothers, where he spent three years analysing the French and Benelux banking markets.

**Mark Rogers** joined MAML in 2014 and is both head of research and the co-manager of the Better World Fund. His previous experience includes four years at Bankers Trust Asset Management (as a UK portfolio manager), 17 years at Nomura Asset Management (as a European equities investment manager and later as head of research), and seven years as director of European equity research for Fidelity Worldwide Investments in London.

**George Cooke** joined MAML in July 2010. After leaving university, he joined the graduate scheme at Aon Benfield (formerly Aon Re) and later became an analyst with its ReSolutions department, specialising on assisting with the capital and runoff issues of insurance and reinsurance companies.

## Board

The board consists of three directors, all of whom are independent of the manager and who do not sit together on other boards. Each director offers him- or herself up for re-election at each annual general meeting. The current fees were last increased with effect from 1 April 2017, and it is anticipated that these fees will remain unchanged at least until 31 March 2020.

**Figure 24: Board member - length of service and shareholdings**

Director	Position	Appointed	Length of service (years)	Annual director's fee (GBP)	Shareholding
<b>Richard Curling</b>	Chairman	2 November 2015	3.3	32,000	5,000
<b>Caroline Roxburgh</b>	Chair of the audit committee	8 November 2017	1.3	27,000	3,314
<b>Merryn Somerset Webb</b>	Senior independent director	17 May 2011	7.8	23,000	3,802

Source: Marten & Co

Richard Curling was appointed in 2015. He has over 30 years' experience as a fund manager and is currently an investment director at Jupiter Fund Management Plc. He also has extensive experience of investment trusts. Richard is chairman of the nominations committee.

Caroline Roxburgh is a Chartered Accountant with over 30 years' experience in finance and audit and was formerly a partner at PricewaterhouseCoopers LLP until her retirement in 2016. Caroline chairs the audit committee.

Merryn Somerset Webb was appointed in 2011. She is the editor-in-chief of UK personal finance magazine MoneyWeek, writes for the Financial Times and is a radio and television commentator on financial matters. She is also a director of Baillie Gifford Shin Nippon Plc. She is chairman of the remuneration committee.

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