# Aberforth UK Small Companies Fund

Annual Report and Financial Statements

31 December 2017

# Investment Objective & Policy

The objective of Aberforth UK Small Companies Fund (the "Fund") is to achieve a total return (with income reinvested) greater than that of the Numis Smaller Companies Index (excluding Investment Companies) over the long term by investing in a diversified portfolio of small UK quoted companies.

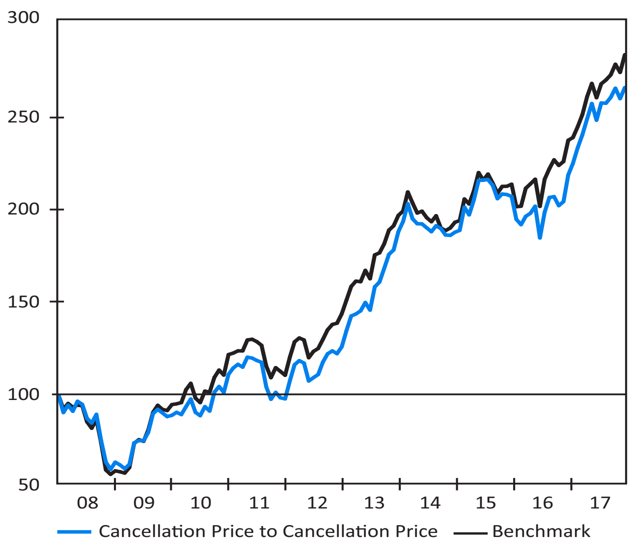
## Contents



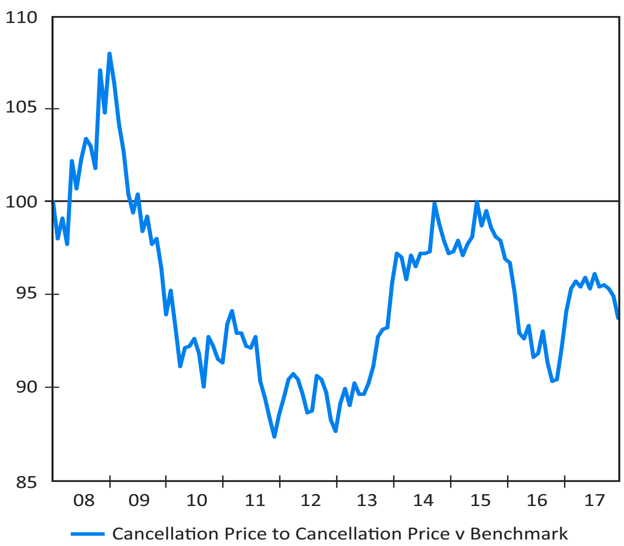
Data has been sourced from Aberforth Partners LLP unless otherwise stated.

## Ten Year Investment Record

**Absolute Performance**
(figures are total returns and have been rebased to 100 at 31 Dec 2007)




**Relative Performance**
(figures are total returns and have been rebased to 100 at 31 Dec 2007)



# Investment Record

| Performance for the year to 31 December 2017 | % |
|---|---|
| **The Fund**[1] | **21.6** |
| **Benchmark Index**[2] | **19.5** |

| Prices & Yield | | 2 January 2018[3] | 3 January 2017[3] |
|---|---|---|---|
| Accumulation Units | Issue Price | **£268.84** | £221.32 |
| | Cancellation Price | **£263.41** | £217.52 |
| Income Units (xd) | Issue Price | **£205.47** | £173.76 |
| | Cancellation Price | **£201.32** | £170.77 |
| | Yield[4] | **2.6%** | 2.8% |
| Dealing Spread | | **2.0%** | 1.7% |

| Size & Charges | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Total Net Assets | **£249.0m** | £201.8m |
| Ongoing Charges[5] | **0.79%** | 0.80% |
| Initial Charge | **Nil** | Nil |
| Exit Charge | **Nil** | Nil |

| Historic Returns | Discrete Annual Returns (%) The Fund[1,6] | Index[2] |
|---|---|---|
| 1 year to 31 December 2017 | 21.6 | 19.5 |
| 1 year to 31 December 2016 | 5.6 | 11.1 |
| 1 year to 31 December 2015 | 10.3 | 10.6 |
| 1 year to 31 December 2014 | -0.2 | -1.9 |
| 1 year to 31 December 2013 | 49.4 | 36.9 |

| Historic Returns | Annualised Returns (%) | | Cumulative Returns (%) | |
|---|---|---|---|---|
| Periods to 31 December 2017 | The Fund[1] | Index[2] | The Fund[1] | Index[2] |
| 2 years from 31 December 2015 | 13.3 | 15.2 | 28.4 | 32.7 |
| 3 years from 31 December 2014 | 12.3 | 13.7 | 41.6 | 46.8 |
| 4 years from 31 December 2013 | 9.0 | 9.6 | 41.4 | 44.1 |
| 5 years from 31 December 2012 | 16.1 | 14.6 | 111.1 | 97.3 |
| 10 years from 31 December 2007 | 10.3 | 11.0 | 166.9 | 184.7 |
| 15 years from 31 December 2002 | 13.7 | 14.2 | 585.9 | 637.0 |
| 26.8 years from inception on 20 March 1991 | 13.2 | 10.8 | 2,677.4 | 1,475.7 |

1 Represents cancellation price to cancellation price (accumulation units).

2 Represents capital appreciation on the Numis Smaller Companies Index (Excluding Investment Companies) with net dividends reinvested. This index comprises the bottom 10% of the main UK equity market by market value which at 1 January 2018 included some 350 companies, the largest market capitalisation of which was £1.5 billion and the aggregate market capitalisation of which was £169 billion.

3 Prices stated are for the first valuation point after the period end, being the distribution xd date.

4 The Yield reflects distributions declared over the past twelve months as a percentage of the mid-market unit price as at the date shown. It does not include any initial charge and investors may be subject to tax on their distributions.

5 This is based on actual expenses for the year ended 31 December 2017. It covers all aspects of operating the Fund during the year including fees paid for investment management, administration, safeguarding the Fund's assets, audit and to the regulator. It does not include payments to your financial advisor or any other firm through which you may invest. You may pay for their services, if any, directly.

6 This table is in accordance with the Financial Conduct Authority's regulations.

Past performance is not a guide to future performance. Stockmarket movements may cause the capital value of an investment and the income derived from it to go down as well as up and investors may get back less than they originally invested.

# Manager’s Report

This report has been prepared in accordance with the requirements of the Collective Investment Schemes Sourcebook as issued and amended by the Financial Conduct Authority.

## Status

Aberforth UK Small Companies Fund (the “Fund”) was constituted by a Trust Deed dated 17 December 1990 and is an authorised unit trust scheme under the Financial Services & Markets Act 2000 (the “Act”). The Fund is a UCITS scheme as defined by the Collective Investment Schemes Sourcebook.

## Information on Aberforth Unit Trust Managers Limited

The Manager is wholly owned by Aberforth Partners LLP (the “firm”). The business was established in 1990 to provide institutional and wholesale investors with a high level of resources focused exclusively on small UK quoted companies. Since then funds under management have grown to £2.5 billion (as at 31 December 2017). The firm is wholly owned by seven partners – six investment managers and Alan Waite, who is responsible for the firm’s administration. The six investment managers work as a team managing the Fund’s portfolio on a collegiate basis.

Further information on Aberforth Partners LLP and its clients is available on its website – www.aberforth.co.uk.

## Changes to Prospectus

During the year, the Prospectus was updated to note:-

1. the appointment of two new directors of the Manager; and
2. the change of name and registered office address following the sale of Capita Financial Administrators Limited to Link Fund Administrators Limited.

## Remuneration Policy

The Manager has delegated all investment management activities for the Fund to Aberforth Partners LLP. Directors and staff working on the Fund are not remunerated by the Manager. Aberforth Partners LLP is subject to regulatory requirements on remuneration that are equally effective under BIPRU and AIFMD. Details of its remuneration policy are available on request.

## Introduction

The Fund rode the wave of rising equity valuations around the world in 2017 and delivered a strong performance in both absolute and relative terms. Its total return was 21.6%, which may be compared with 19.5% for its benchmark, the NSCI (XIC), and with 13.1% for the FTSE All-Share index, which is a gauge of the performance of larger companies.

All the Fund’s relative gains were secured in the first half of the year: as the year progressed, conditions became more hostile to the value investor, details of which are provided in the **Investment performance** section of this report. That the value style should have encountered such headwinds is at one level surprising. One of the most notable developments of 2017 was the synchronisation of economic recovery around the globe, with all major economies enjoying GDP growth for the first time since the financial crisis. While the rate of progress of the US economy eased, tax reform offers the prospect of renewed impetus. Meanwhile, Chinese activity benefited from a bout of stimulus and, perhaps more significantly, the Eurozone returned to growth as the impact of quantitative easing was finally felt. The broad trend of improvement was seized upon promptly by the equity markets and has been termed the “reflation trade”.

Its sustainability was, however, brought into question by the words and actions of the world’s central banks, apparently keen to display their inflation-fighting credentials. Three interest rate rises in the US have been accompanied by commentary on how and when the Federal Reserve’s balance sheet, bloated by quantitative easing, might be run down. To date, the Eurozone has seen no action but plenty of rhetoric, while the UK has witnessed its first interest rate rise for ten years. It is to be hoped that the central banks are not too focused on fighting yesterday’s war and that they have judged the risks of runaway economic activity and inflation accurately. In this regard, a bit more nervousness on the part of government bond markets might have been encouraging: yields in 2017 were essentially unchanged and thus remain at extremely low levels in a historical context. The behaviour of bond investors suggests that the “reflation trade” is merely another of those false dawns to have punctuated the period since the financial crisis and that underlying economic issues of debt and demographics are so intractable as to condemn the world to very low rates of economic growth for years to come.

Such prospects are some of the factors contributing to the emergence of reactionary populism around the globe, though, again, bond investors appear little concerned by the inflationary effects of populist policies. To be fair, a useful test-case of populism, the UK’s EU referendum, has hardly been a cause of concern for bond markets. There was no implosion in the immediate aftermath of the vote, but the second order effects of sterling’s devaluation are now permeating the economy: inflation is picking up, real wages are coming back under pressure and to this extent the outlook for real growth is deteriorating. Though GDP growth forecasts should be taken with a pinch of salt, the trajectory that has taken the UK from the fastest growing G7 nation in 2014 to the slowest in 2017 is hardly encouraging. Meanwhile, the government is in a difficult position, undermined by the outcome of the general election, riven ideologically by differing views on the EU and inevitably focused on divorce negotiations.

# Manager's Report

Against this complicated background, investment in small UK quoted companies in 2017 was remarkably straightforward. Leaving aside for now a small number of highly valued growth stocks, the most important issue was the split of exposure to those companies earning their profits overseas and those that rely on the domestic economy. To have had a lot of the former, which benefited from the weak pound and saw their profits expand to historically high levels, was a significant boost to investment returns. The Fund was a beneficiary and its experience is described in the **Investment performance** section of this report.

## Investment performance

The Fund's total return in 2017 was 21.6%; the NSCI (XIC)'s was 19.5%. The table below analyses the difference between these two figures, while the subsequent paragraphs provide more detail on how the Fund's performance was achieved.

| For the 12 months ended 31 December 2017 | Basis points |
|---|---|
| Stock selection | 421 |
| Sector selection | (67) |
| **Attributable to the portfolio of investments, based on mid prices** | **354** |
| Movement in mid to bid price spread | (48) |
| Cash/overdraft | (19) |
| Management fee | (75) |
| Other expenses | (4) |
| **Total attribution based on bid prices** | **208** |

Note: 100 basis points = 1%. Total Attribution is the difference between the total return of the Fund and the Benchmark Index (i.e. the Fund = 21.58%; Benchmark Index = 19.50%; difference is 2.08% being 208 basis points).

### *Style*

The dynamics behind the "reflation trade" of 2017 should have been conducive to a strong relative performance from the value style. While this was indeed the case in the early months of the year, the growth style fought back as government bond yields failed to respond. For the year as a whole, analysis of data from both the London Business School (LBS) and Style Research points to significant headwinds for the value style; indeed, the LBS model suggests it was the ninth worst year since 1955. In this context, the Fund's positive relative performance might be considered so surprising as to call into question the Manager's dedication to value investment. However, two other factors – size and sectors described below – offered mitigation and some strong individual stock selection numbers, as illustrated in the table above, helped the portfolio's performance exceed that of the benchmark. The experience of 2017 also usefully illustrates the difference of approach between the third-party models and Aberforth in determining value: the former use only price to book, while the Manager's methodology encompasses other valuation metrics, notably the ratio of enterprise value to earnings before interest, tax and amortisation. Nevertheless, the chance of the Fund overcoming a repeat of such adverse conditions for the value style is not high.

### *Size*

The size factor within the NSCI (XIC) was a slight boost to the Fund's returns in 2017. The NSCI (XIC) represents the bottom tenth of the UK stockmarket by value and includes companies with market capitalisations up to around £1.5 billion. It thus overlaps with the FTSE 250 index. At the start of 2017 this overlap represented 62% of the value of the NSCI (XIC). In 2017, the performance of the FTSE 250 stocks within the NSCI (XIC), its larger constituents, was very slightly behind that of its smaller constituents. This was to the Fund's advantage, albeit to a modest degree, since 60% of its portfolio was invested in "smaller small" companies at the start of the 2017. The reason for this disposition is the valuation premium accorded to larger companies and set out in the **Valuation** section of this report. While the superior returns from "smaller smalls" reduced their valuation advantage in 2017, it remains wide and with the bottom-up prospects for these businesses still positive, the portfolio enters 2018 in a familiar shape with regard to size.

### *Sectors*

The crucial sector issue in 2017 was the divergent performance of overseas and domestic companies. As noted above, relative performance was improved by a comparatively high exposure to those companies earning their money outside the UK. At the start of the year, 47% of the aggregate sales of the Fund's portfolio holdings was generated overseas, more than the 41% for the NSCI (XIC). As a gauge of the benefit afforded by this positioning, the NSCI (XIC) may be divided into groups of sectors determined by where these sectors earn their money and the performance of these groups may be compared. The overseas group enjoyed a total return of 32% in 2017, whereas the domestic group's return was 19%. Sterling's weakness after the EU referendum explains the gap: the overseas group benefited from the translation of profits at more favourable exchange rates and almost two thirds of the companies therein have seen profit expectations for 2017 raised since the referendum; in contrast, the domestic group has had to contend with the impact of sterling on inflation and real wages, so that only one third of its companies has enjoyed higher estimates.

# Manager's Report

The net effect has been a widening valuation premium of overseas exposed companies to domestics, even though sterling itself was unchanged on a trade weighted basis in 2017. At the margin, this has motivated the Manager to bias purchases through the latter part of the year to the domestics, always taking into account the likelihood of more challenging trading conditions in the UK economy. However, experience suggests that the stockmarket is prone to overreact and when strong businesses with a domestic bias but attractive financial characteristics and defendable market positions are significantly de-rated the Manager is willing to commit capital. So far, this re-orientation of the portfolio, which is consistent with the application of a value investment philosophy, has been modest, with the portfolio at the start 2018 still generating 46% of its aggregate sales from overseas.

*Stocks*

In 2017's challenging environment for the value style, the portfolio's exposure to "smaller small" companies and to overseas earners offered some mitigation. However, stock selection also played an important role, as the table at the top of this section makes clear. In last year's Manager's Report, it was argued that "for the Fund to generate superior returns for its shareholders, getting more investment decisions right than wrong … probably does the job". While over time the Manager's investment approach and experience can hopefully ensure that this deceptively unambitious target is met, it is fair to state that good fortune played a part in the high stock contribution in 2017. Despite an uptick in profit warnings across the stockmarket as the year progressed, the Fund encountered few serious declines in share prices and, on the other hand, saw its patience rewarded with unusually large rises in the valuations of some of the long-standing holdings into which capital had been fed steadily over time.

Additionally, the stockmarket offered several opportunities to take advantage of the de-ratings of previously inherently strong but highly valued businesses whose trading difficulties had precipitated substantial share price falls. While holdings in these businesses were taken with a five year investment horizon, in some cases the actual holding period proved much shorter as trading improved and the stockmarket chose once again to re-rate the prospects of the company in question. When the stockmarket will yield such opportunities in the future is uncertain. What is certain is that there will be years in which, despite the consistent application of the value investment philosophy through a seasoned investment process, stock selection will prove as unrewarding as it was rewarding in 2017.

*Corporate activity*

With 17 bids for NSCI (XIC) constituents completed or outstanding at the end of the year, M&A activity in 2017 was at a similar level to that of 2016. Both these years undershot the 27 deals that took place in 2015 and it is tempting to attribute some of the slowdown since then to the uncertainties stemming from the EU referendum, even though the weakness of sterling ought to add to the appeal of UK assets to overseas buyers. Of the 17 bid situations, the Fund held six, though in three cases the announcement of the approach and thus the boost to the share prices came at the end of 2016. Overall, M&A was a very small boost to returns in 2017.

The number of initial public offerings in 2017 was 21, which represents a modest rise on the previous year. The Fund does not often participate in IPOs but did take part in two of the 2017 deals. In both cases, the Manager judged that the valuation offered sufficient compensation for the informational advantage usually enjoyed by the private equity sellers of the businesses.

*Balance sheets*

For much of the last ten years, the small UK quoted company universe has been characterised by strong and strengthening balance sheets, which inevitably reflected the impact of the financial crisis on the thinking of company directors. In the last three years, however, there have been indications of less caution. In the case of the Fund's portfolio, this is manifest in the proportion of the portfolio that is invested in companies with net cash on their balance sheets, which has declined from 35% in 2014 to 21% at the end of 2017. For the Manager, this development is on balance positive, since it is driven by more investment, returns of surplus cash and, though not to be welcomed in every case, acquisitions. Clearly, however, higher leverage brings risks, particularly if it coincides with an economic downturn. Comfort may be derived from the portfolio's bias to businesses with less than two times leverage (net debt divided by earnings before interest, tax, depreciation and amortisation), which was almost 75% at the end of 2017. Those with higher leverage ratios tend to be property companies, though the portfolio always has some exposure to more highly indebted businesses where the potential upside justifies additional risk.

*Income*

The table below splits the portfolio's holdings into categories that are determined by each company's most recent dividend announcement. The profile is familiar from similar analyses in recent years: a small minority of dividend cutters, the persistence of several nil payers and a bias to companies that most recently increased their dividends. The "Other" category includes companies that have returned to the dividend register or that have paid dividends for the first time and that therefore do not have a meaningful comparative payment in the previous year.

| Down | Nil payers | No change | Increase | Other |
|---|---|---|---|---|
| 7 | 13 | 22 | 41 | 3 |

# Manager's Report

The portfolio's dividend experience reflects what remains a buoyant backdrop for dividends across the universe of small UK quoted companies. Robust balance sheets and dividend cover of 2.8x for the portfolio, are supportive of further increases, though it would seem likely that the rate of dividend growth across the NSCI (XIC) is moderating from the low double digits of recent years to mid to high single digits. However, in comparison with inflation, this degree of progress remains well above the 61 year average real dividend growth from smaller companies of 2.5%.

*Turnover*

Portfolio turnover in 2017 was 32%, which was up from 23% in 2016. In any period, the level of activity is influenced by unitholder inflows and outflows, as well as by the Manager's underlying investment decisions. It should be noted that in some cases, such as when stocks have become too large for the NSCI (XIC) or when investee companies are subject to M&A, the Manager becomes in effect a forced seller. The increase in turnover compared with 2016 was correlated with the improvement in investment performance. Consistent with the value investment philosophy, the Manager strives to rotate capital from holdings that have performed well and are close to their target valuations into companies with depressed valuations and greater upside. This basic dynamic ought to benefit returns, but it can only be put into action if the broad stockmarket is inclined to re-rate holdings, as was the case in 2017.

*Active share*

Active share is a measure of how different a portfolio is from an index. It is calculated as half of the sum of the absolute differences between each stock's weighting in an index and its weighting in the portfolio. A higher active share would indicate that a portfolio has a better chance of performing differently from the index, for better or worse. The Manager targets a ratio of at least 70% for the Fund in relation to the NSCI (XIC) and at the end of December the ratio was 77%.

## Valuations

The strength of equity markets in 2017 has seen valuations rise and, as the table below sets out, the universe of small UK quoted companies has participated in this trend. The 14.3x PE of the NSCI (XIC) at the end of December was 6% above its average since 1990 of 13.5x, while the 12.4x PE of the Fund's portfolio was 4% above its 12.0x long term average. While neither the asset class nor the portfolio is significantly above normal, the same cannot be claimed of large companies. The historical PE of the FTSE All-Share at the end of 2017 was 21.7x, which is 42% above its average since 1990. This PE reflects the implicit expectation of strong profit growth from large companies in coming months, helped by the translation of overseas profits at lower sterling exchange rates, by the restructuring undertaken in recent times by resources companies and by the effect of rising commodity prices on these companies' profits.

| | **31 December 2017** | | 31 December 2016 | |
|---|---|---|---|---|
| Characteristics | **The Fund** | **NSCI (XIC)** | The Fund | NSCI (XIC) |
| Number of companies | **86** | **350** | 87 | 349 |
| Weighted average market capitalisation | **£710m** | **£878m** | £618m | £800m |
| Price earnings ratio or PE (historic) | **12.4x** | **14.3x** | 11.3x | 12.5x |
| Dividend yield (historic) | **2.9%** | **2.8%** | 3.0% | 2.8% |
| Dividend cover | **2.8x** | **2.5x** | 3.0x | 2.9x |

The following table sets out the forward valuations of the Fund's portfolio and the tracked universe, which is the set of stocks covered closely by the Manager and represents 97% by value of the NSCI (XIC). The valuation metric – the ratio of enterprise value to earnings before interest, tax and amortisation (EV/EBITA) – is the one favoured by the Manager. As should be expected of a portfolio put together in accordance with a value investment philosophy, the Fund's holdings are cheaper than the tracked universe as a whole and much cheaper than a subset of 44 growth stocks: at the end of December, the premium of the growth stocks to the portfolio was 74% on the basis of 2018 estimates.

| **EV/EBITA** | **2017** | **2018** | **2019** |
|---|---|---|---|
| The Fund | 12.1x | 10.4x | 9.0x |
| Tracked universe (285 stocks) | 14.2x | 12.8x | 11.3x |
| – 44 growth stocks | 21.8x | 18.1x | 16.0x |
| – 241 other stocks | 13.2x | 12.0x | 10.6x |

# Manager’s Report

The final valuation table highlights a valuation anomaly that has persisted for several years. Despite the superior returns from “smaller small” companies in 2017, the lowest valuations in the UK stockmarket are still accorded to the smallest companies and, as a consequence, the Fund’s exposure to those companies is higher than that of the NSCI (XIC) as a whole. In the Manager’s experience, the present relationship is unusual: in the years before the financial crisis, the superior growth of “smaller small” companies tended to be rewarded by higher valuations. However, many investors are today nervous about illiquidity and are reluctant to commit to the stockmarket’s smaller denizens.

| Market capitalisation range: | < £100m | £100-250m | £250-500m | £500-750m | > £750m |
|---|---|---|---|---|---|
| Portfolio weight | 3% | 15% | 25% | 22% | 35% |
| Tracked universe weight | 1% | 5% | 18% | 15% | 61% |
| Tracked universe 2018 EV/EBITA | 7.4x | 10.3x | 11.4x | 12.2x | 13.9x |

## Conclusion & outlook

In broad terms, today’s universe of small UK quoted companies can be split into three groups, a framework that has been useful for the majority of time since the financial crisis.

- The first comprises secular growth companies, whose valuations benefit from the low discount rates that encourage investors to extend their investment horizons well beyond historical norms. Decent memories are now required of the last time that capital became effectively costless for growth companies during the TMT boom. This is not to deny the existence of some truly outstanding business franchises among the technology behemoths of the US and China or even, indeed, within the NSCI (XIC). However, experience suggests that capital does not remain costless indefinitely, that many growth businesses are being valued as if they are the next Amazon and that few businesses succeed in retaining high stockmarket valuations for extended periods.
- The second group comprises companies whose growth is low but dependable and that tend to pay out a large proportion of their profits as dividends. Before the financial crisis these would have been described pejoratively as “dull” or “ersatz bonds” and, condemned to low valuations, might have fitted into a value portfolio. However, since the advent of quantitative easing with its suppressive effect on bond yields, the increasingly desperate search for income has seen them re-rated to high valuations.
- The final group is everything else – the rump of companies that are lowly valued, typically cyclical, often reliant on the domestic economy, sometimes illiquid and thus uncomfortable for many investors to own. None of these characteristics means that these are all poor businesses that face an existential threat. Some will undoubtedly fall victim to the forces of disruption and these are to be avoided, unless prevailing valuations exaggerate the rate of decline and offer an opportunity for investment. However, many members of this group boast defendable market positions, volatile but good returns on capital through the cycle and the opportunity to grow though not necessarily year-in-year-out. For better or worse, these are the typical holdings of a small cap value fund just now.

An implication of this characterisation is that the big-picture issues of macroeconomics, government bond yields and politics are at present disproportionately influential on the valuations of the three groups that make up the universe of small UK quoted companies. The uncertainties stemming from the EU referendum play a part, but the more significant influence remains the extraordinary monetary policies that anchor bond yields in many parts of the world at very low levels. As long as this continues to be the case, issues specific to individual businesses are likely to play a secondary role in determining the Fund’s returns, though the experience of 2017 suggests that stock selection can make a difference with the help of some good fortune.

So what might move the world’s major bond markets? A year ago, a reasonable response, though one that appeared unlikely to come to pass, might have mentioned a bout of synchronised global growth accompanied by higher inflation, tax cuts for the world’s largest economy and monetary tightening. And yet government bond markets are unyielding. Perhaps in the face of a decades-long bull market in bonds, which has only intensified since the financial crisis, more convincing evidence is required and perhaps 2017’s “reflation trade” will be condemned to the same fate as 2013’s “great rotation”. Financial markets certainly remain set up for more of the same: corporate bond spreads are extremely narrow, equity markets are led by a small number of beneficiaries of low rates and, to judge by the world of small UK quoted companies, funds tend to be heavily biased to those favourite stocks. With its commitment to value investment, the Fund continues to stand apart and in doing so is arguably as relevant as at any point in its almost 27 year history.

K F Muir, Director
R M J Newbery, Director
Aberforth Unit Trust Managers Limited
26 January 2018

# Summary of Material Portfolio Changes

## For the year ended 31 December 2017

| Purchases | Cost £'000 |
|---|---|
| Stagecoach Group | 2,923 |
| Non-Standard Finance | 2,896 |
| Mitchells & Butlers | 2,770 |
| Bovis Homes Group | 2,726 |
| Forterra | 2,698 |
| Essentra | 2,425 |
| Restaurant Group | 2,219 |
| Dunelm Group | 1,904 |
| Nostrum Oil & Gas | 1,867 |
| ei group | 1,802 |
| Just Group | 1,801 |
| Spirent Communications | 1,790 |
| Keller | 1,742 |
| SIG | 1,666 |
| Servelec Group | 1,617 |
| Topps Tiles | 1,598 |
| U and I Group | 1,586 |
| FirstGroup | 1,565 |
| KCOM Group | 1,552 |
| Vesuvius | 1,545 |
| Other purchases | 47,252 |
| **Total Cost of Purchases** | **87,944** |

| Sales | Proceeds £'000 |
|---|---|
| Paragon Banking Group | 5,935 |
| e2v technologies | 5,933 |
| Games Workshop Group | 4,558 |
| Ladbrokes Coral | 3,552 |
| John Laing Group | 3,524 |
| Renewi | 3,342 |
| Hansteen Holdings | 2,864 |
| Microgen | 2,814 |
| Novae Group | 2,794 |
| Hilton Food Group | 2,736 |
| NCC Group | 2,540 |
| Punch Taverns | 2,050 |
| Centamin | 2,043 |
| Mothercare | 2,036 |
| Imagination Technologies Group | 1,952 |
| SDL | 1,456 |
| Findel | 1,321 |
| Computacenter | 1,190 |
| Robert Walters | 1,162 |
| Vitec Group | 1,149 |
| Other sales | 24,700 |
| **Total Proceeds of Sales** | **79,651** |

# Portfolio Statement

As at 31 December 2017

| Holding | Security | 31 December 2017 Value £'000 | 31 December 2017 % of Total Net Assets | 31 December 2017 % of Index[3] | 31 December 2016 % of Total Net Assets | 31 December 2016 % of Index |
|---|---|---|---|---|---|---|
| **Oil & Gas Producers** | | **9,757** | **3.9** | **2.6** | 5.7 | 3.3 |
| 13,013,266 | EnQuest | 3,709 | 1.5 | | | |
| 1,387,587 | Hardy Oil & Gas | 201 | 0.1 | | | |
| 1,394,828 | Nostrum Oil & Gas | 4,537 | 1.8 | | | |
| 1,188,540 | Soco International | 1,310 | 0.5 | | | |
| **Oil Equipment, Services & Distribution** | | **1,761** | **0.7** | **1.1** | 0.6 | 1.1 |
| 3,936,103 | Gulf Marine Services | 1,761 | 0.7 | | | |
| **Alternative Energy** | | **–** | **–** | **–** | – | – |
| **Chemicals** | | **1,205** | **0.5** | **1.7** | 0.6 | 1.9 |
| 995,635 | Carclo | 1,205 | 0.5 | | | |
| **Industrial Metals & Mining** | | **–** | **–** | **–** | – | 0.5 |
| 9,832,752 | International Ferro Metals[1] | – | – | | | |
| **Mining** | | **4,133** | **1.7** | **2.5** | 2.7 | 2.1 |
| 2,135,965 | Anglo Pacific Group | 3,225 | 1.3 | | | |
| 1,279,037 | Gem Diamonds | 908 | 0.4 | | | |
| 2,717 | Kenmare Resources Warrants 2019[2] | – | – | | | |
| **Construction & Materials** | | **12,509** | **5.0** | **4.9** | 3.4 | 4.3 |
| 1,319,476 | Eurocell | 2,771 | 1.1 | | | |
| 1,393,706 | Forterra | 4,146 | 1.7 | | | |
| 575,913 | Keller | 5,592 | 2.2 | | | |
| **Aerospace & Defence** | | **5,699** | **2.3** | **2.6** | 1.6 | 1.9 |
| 1,744,263 | Senior | 4,546 | 1.8 | | | |
| 85,600 | Ultra Electronics Holdings | 1,153 | 0.5 | | | |
| **General Industrials** | | **17,121** | **6.9** | **0.9** | 4.6 | 1.2 |
| 7,524,554 | Coats Group | 6,678 | 2.7 | | | |
| 2,723,945 | Low & Bonar | 1,451 | 0.6 | | | |
| 1,539,791 | Vesuvius | 8,992 | 3.6 | | | |
| **Electronic & Electrical Equipment** | | **8,751** | **3.5** | **2.1** | 6.0 | 2.1 |
| 995,487 | Morgan Advanced Materials | 3,341 | 1.3 | | | |
| 2,442,370 | TT Electronics | 5,410 | 2.2 | | | |
| **Industrial Engineering** | | **12,296** | **4.9** | **2.1** | 4.3 | 2.5 |
| 467,154 | Bodycote | 4,256 | 1.7 | | | |
| 472,716 | Castings | 2,084 | 0.8 | | | |
| 527,116 | Vitec Group | 5,956 | 2.4 | | | |
| **Industrial Transportation** | | **4,273** | **1.7** | **2.3** | 2.1 | 2.1 |
| 1,833,853 | Wincanton | 4,273 | 1.7 | | | |
| **Support Services** | | **36,990** | **14.8** | **11.3** | 15.4 | 11.5 |
| 1,166,393 | Capital Drilling | 420 | 0.2 | | | |
| 2,163,471 | Connect Group | 2,358 | 0.9 | | | |
| 532,690 | De La Rue | 3,415 | 1.4 | | | |
| 731,407 | Essentra | 3,862 | 1.6 | | | |
| 4,787,593 | Hogg Robinson Group | 3,842 | 1.5 | | | |
| 8,582,977 | Management Consulting Group | 537 | 0.2 | | | |
| 209,600 | Menzies (John) | 1,412 | 0.6 | | | |
| 1,137,126 | Northgate | 4,335 | 1.7 | | | |
| 895,498 | Robert Walters | 5,176 | 2.1 | | | |
| 1,784,134 | RPS Group | 4,835 | 1.9 | | | |
| 1,690,276 | SIG | 2,978 | 1.2 | | | |
| 6,262,913 | Speedy Hire | 3,820 | 1.5 | | | |

# Portfolio Statement

As at 31 December 2017

| Holding | Security | 31 December 2017 Value £'000 | 31 December 2017 % of Total Net Assets | 31 December 2017 % of Index[3] | 31 December 2016 % of Total Net Assets | 31 December 2016 % of Index |
|---|---|---|---|---|---|---|
| **Automobiles & Parts** | | **–** | **–** | **0.8** | – | – |
| **Beverages** | | **–** | **–** | **0.7** | – | 0.6 |
| **Food Producers** | | **3,593** | **1.4** | **2.8** | 1.6 | 2.6 |
| 810,100 | Bakkavor Group | 1,556 | 0.6 | | | |
| 44,200 | Devro | 100 | – | | | |
| 301,800 | Greencore Group | 693 | 0.3 | | | |
| 407,921 | R.E.A. Holdings | 1,244 | 0.5 | | | |
| **Household Goods & Home Construction** | | **7,637** | **3.1** | **3.5** | 1.6 | 4.5 |
| 652,187 | Bovis Homes Group | 7,637 | 3.1 | | | |
| **Leisure Goods** | | **1,352** | **0.5** | **0.9** | 1.3 | 0.6 |
| 51,357 | Games Workshop Group | 1,352 | 0.5 | | | |
| **Personal Goods** | | **–** | **–** | **1.6** | – | 2.0 |
| **Health Care Equipment & Services** | | **–** | **–** | **1.9** | – | 1.9 |
| **Pharmaceuticals & Biotechnology** | | **3,104** | **1.2** | **2.0** | 1.4 | 2.6 |
| 2,641,592 | Vectura Group | 3,104 | 1.2 | | | |
| **Food & Drug Retailers** | | **3,375** | **1.4** | **1.0** | 1.1 | 0.8 |
| 1,303,143 | McColl's Retail Group | 3,375 | 1.4 | | | |
| **General Retailers** | | **13,600** | **5.6** | **6.1** | 5.1 | 5.5 |
| 855,995 | Carpetright | 1,455 | 0.6 | | | |
| 992,700 | DFS Furniture | 1,931 | 0.8 | | | |
| 286,700 | Dunelm Group | 1,985 | 0.8 | | | |
| 624,400 | Halfords Group | 2,184 | 0.9 | | | |
| 828,029 | N Brown Group | 2,235 | 0.9 | | | |
| 7,807,967 | Pendragon | 2,128 | 0.9 | | | |
| 2,122,548 | Topps Tiles | 1,682 | 0.7 | | | |
| **Media** | | **13,775** | **5.5** | **4.3** | 3.7 | 3.9 |
| 2,481,614 | Centaur Media | 1,117 | 0.4 | | | |
| 1,089,112 | Future | 4,607 | 1.9 | | | |
| 6,629,481 | Huntsworth | 5,337 | 2.1 | | | |
| 3,145,097 | Trinity Mirror | 2,437 | 1.0 | | | |
| 117,800 | Wilmington Group | 277 | 0.1 | | | |
| **Travel & Leisure** | | **24,138** | **9.6** | **7.8** | 9.9 | 8.8 |
| 550,425 | Air Partner | 743 | 0.3 | | | |
| 1,297,700 | ei group | 1,830 | 0.7 | | | |
| 6,153,041 | FirstGroup | 6,774 | 2.7 | | | |
| 4,844,079 | Flybe Group | 1,526 | 0.6 | | | |
| 225,409 | Go-Ahead Group | 3,354 | 1.3 | | | |
| 1,097,635 | Mitchells & Butlers | 3,104 | 1.2 | | | |
| 1,552,000 | Restaurant Group | 4,672 | 1.9 | | | |
| 1,296,300 | Stagecoach Group | 2,135 | 0.9 | | | |
| **Fixed Line Telecommunications** | | **1,553** | **0.6** | **1.8** | 0.1 | 1.1 |
| 1,711,089 | KCOM Group | 1,553 | 0.6 | | | |

# Portfolio Statement

As at 31 December 2017

| Holding | Security | Value £'000 (31 December 2017) | % of Total Net Assets (31 December 2017) | % of Index[3] (31 December 2017) | % of Total Net Assets (31 December 2016) | % of Index (31 December 2016) |
|---|---|---|---|---|---|---|
| **Electricity** | | **–** | **–** | **0.7** | – | 0.1 |
| **Gas, Water & Multiutilities** | | **–** | **–** | **–** | – | 0.1 |
| **Banks** | | **–** | **–** | **3.5** | – | 3.3 |
| **Nonlife Insurance** | | **1,141** | **0.5** | **1.8** | 1.0 | 1.7 |
| 422,300 | Sabre Insurance Group | 1,141 | 0.5 | | | |
| **Life Insurance** | | **5,745** | **2.3** | **0.4** | 1.8 | 1.3 |
| 1,378,918 | Hansard Global | 1,186 | 0.5 | | | |
| 2,675,501 | Just Group | 4,559 | 1.8 | | | |
| **Real Estate Investment & Services** | | **14,441** | **5.9** | **5.7** | 5.1 | 6.0 |
| 1,894,191 | Grainger | 5,472 | 2.2 | | | |
| 1,751,756 | U and I Group | 3,363 | 1.4 | | | |
| 2,002,000 | Urban&Civic | 5,606 | 2.3 | | | |
| **Real Estate Investment Trusts** | | **6,094** | **2.4** | **5.4** | 2.7 | 5.6 |
| 611,500 | Capital & Regional | 355 | 0.1 | | | |
| 1,703,657 | Hansteen Holdings | 2,436 | 1.0 | | | |
| 1,436,252 | McKay Securities | 3,303 | 1.3 | | | |
| **Financial Services** | | **16,418** | **6.6** | **8.3** | 9.3 | 6.7 |
| 1,760,225 | Brewin Dolphin Holdings | 6,854 | 2.8 | | | |
| 625,151 | Charles Stanley Group | 2,315 | 0.9 | | | |
| 766,600 | CMC Markets | 1,148 | 0.5 | | | |
| 1,806,027 | International Personal Finance | 3,567 | 1.4 | | | |
| 3,726,300 | Non-Standard Finance | 2,534 | 1.0 | | | |
| **Software & Computer Services** | | **13,159** | **5.3** | **4.0** | 5.3 | 4.5 |
| 446,263 | Computacenter | 5,141 | 2.1 | | | |
| 100,652 | Microgen | 463 | 0.2 | | | |
| 1,693,143 | RM | 3,306 | 1.3 | | | |
| 748,277 | SDL | 3,180 | 1.3 | | | |
| 341,500 | Servelec Group | 1,069 | 0.4 | | | |
| **Technology Hardware & Equipment** | | **6,257** | **2.5** | **0.9** | 2.0 | 1.3 |
| 1,580,800 | Laird | 2,174 | 0.9 | | | |
| 4,023,000 | Spirent Communications | 4,083 | 1.6 | | | |
| **Investments as shown in the Balance Sheet** | | **249,877** | **100.3** | **100.0** | 100.0 | 100.0 |
| **Net Current Liabilities** | | **(861)** | **(0.3)** | – | – | – |
| **Total Net Assets** | | **249,016** | **100.0** | **100.0** | 100.0 | 100.0 |

All investments are listed on the London Stock Exchange unless otherwise stated.

[1] Listing suspended

[2] Unquoted security

[3] Reflects the rebalanced index as at 1 January 2018

# Comparative Tables

| Income Unit | 31 December 2017 £/unit | 31 December 2016 £/unit | December 2015 £/unit |
|---|---|---|---|
| **Change in net assets per unit** | | | |
| Opening net asset value per unit | **170.14** | 166.09 | 154.50 |
| Return before operating charges* | **38.12** | 10.14 | 17.54 |
| Operating charges | **(1.52)** | (1.28) | (1.42) |
| Return after operating charges | **36.60** | 8.86 | 16.12 |
| Distributions on income units | **(5.36)** | (4.81) | (4.53) |
| Closing net asset value per unit | **201.38** | 170.14 | 166.09 |
| *after direct portfolio transaction costs of: | **(0.55)** | (0.48) | (0.55) |
| **Income Unit** | | | |
| **Performance** | | | |
| Total return after charges[1] | **21.5%** | 5.3% | 10.4% |
| **Other information** | | | |
| Closing net asset value (£'000) | **48,686** | 62,887 | 62,511 |
| Closing number of units | **241,758.267** | 369,607.953 | 376,364.352 |
| Operating charges | **0.79%** | 0.80% | 0.83% |
| Direct portfolio transaction costs | **0.28%** | 0.30% | 0.32% |
| **Prices** | | | |
| Highest issue price (£) | **207.98** | 175.14 | 183.70 |
| Lowest cancellation price (£) | **170.73** | 140.11 | 153.12 |

| Accumulation Unit | 31 December 2017 £/unit | 31 December 2016 £/unit | December 2015 £/unit |
|---|---|---|---|
| **Change in net assets per unit** | | | |
| Opening net asset value per unit | **216.72** | 205.20 | 186.02 |
| Return before operating charges* | **48.73** | 13.12 | 20.90 |
| Operating charges | **(1.96)** | (1.60) | (1.72) |
| Return after operating charges | **46.77** | 11.52 | 19.18 |
| Distributions | **(6.87)** | (5.99) | (5.49) |
| Retained distributions on accumulation units | **6.87** | 5.99 | 5.49 |
| Closing net asset value per unit | **263.49** | 216.72 | 205.20 |
| * after direct portfolio transaction costs of: | **(0.71)** | (0.60) | (0.66) |
| **Accumulation Unit** | | | |
| **Performance** | | | |
| Total return after charges | **21.6%** | 5.6% | 10.3% |
| **Other information** | | | |
| Closing net asset value (£'000) | **200,330** | 138,930 | 105,970 |
| Closing number of units | **760,295.152** | 641,058.237 | 516,414.412 |
| Operating charges | **0.79%** | 0.80% | 0.83% |
| Direct portfolio transaction costs | **0.28%** | 0.30% | 0.32% |
| **Prices** | | | |
| Highest issue price (£) | **269.08** | 220.73 | 221.18 |
| Lowest cancellation price (£) | **217.47** | 173.37 | 184.36 |

[1] Does not assume reinvestment of the interim distribution.

# Responsibility Statements

### STATEMENT OF THE MANAGER'S RESPONSIBILITIES IN RELATION TO THE REPORT AND ACCOUNTS OF THE SCHEME

The Financial Conduct Authority's Collective Investment Schemes Sourcebook, as amended, ("the Regulations") requires the Manager to prepare accounts for each annual accounting period which give a true and fair view of the financial position of the scheme and of its net revenue and capital gains for the period. In preparing the accounts the Manager is required to:

- select suitable accounting policies and then apply them consistently;
- comply with the disclosure requirements of the Statement of Recommended Practice relating to Authorised Funds;
- follow United Kingdom accounting standards;
- keep proper accounting records which enable it to demonstrate that the accounts as prepared comply with the above requirements;
- take reasonable steps for the prevention and detection of fraud and non-compliance with laws and regulations; and
- prepare the financial statements on a going concern basis unless it is considered inappropriate.

The Manager is responsible for the management of the scheme in accordance with its trust deed, prospectus and the Regulations.

This report has been prepared in accordance with the requirements of the Collective Investment Schemes Sourcebook as issued and amended by the Financial Conduct Authority.

K F Muir, *Director*
R M J Newbery, *Director*
Aberforth Unit Trust Managers Limited

26 January 2018

# Responsibility Statements

## STATEMENT OF THE TRUSTEE'S RESPONSIBILITIES AND REPORT OF THE TRUSTEE TO THE UNITHOLDERS OF ABERFORTH UK SMALL COMPANIES FUND FOR THE YEAR ENDED 31 DECEMBER 2017

The Trustee must ensure that the Scheme is managed in accordance with the Financial Conduct Authority's Collective Investment Schemes Sourcebook, the Financial Services and Markets Act 2000, as amended, (together "the Regulations"), the Trust Deed and Prospectus (together "the Scheme documents") as detailed below.

The Trustee must in the context of its role act honestly, fairly, professionally, independently and in the interests of the Scheme and its investors.

The Trustee is responsible for the safekeeping of all custodial assets and maintaining a record of all other assets of the Scheme in accordance with the Regulations.

The Trustee must ensure that:

- The Scheme's cash flows are properly monitored and that cash of the Scheme is booked into the cash accounts in accordance with the Regulations;
- the sale, issue, redemption and cancellation of units are carried out in accordance with the Regulations;
- the value of units of the Scheme is calculated in accordance with the Regulations;
- any consideration relating to transactions in the Scheme's assets is remitted to the Scheme within the usual time limits;
- the Scheme's income is applied in accordance with the Regulations; and
- the instructions of the Authorised Fund Manager ("the AFM") are carried out (unless they conflict with the Regulations).

The Trustee also has a duty to take reasonable care to ensure that the Scheme is managed in accordance with the Regulations and the Scheme documents in relation to the investment and borrowing powers applicable to the Scheme.

Having carried out such procedures as we consider necessary to discharge our responsibilities as Trustee of the Scheme, it is our opinion, based on the information available to us and the explanations provided, that in all material respects the Scheme, acting through the AFM:

(i) has carried out the issue, sale, redemption and cancellation, and calculation of the price of the Scheme's units and the application of the Schemes income in accordance with the Regulations and the Scheme documents, and

(ii) has observed the investment and borrowing powers and restrictions applicable to the Scheme.

National Westminster Bank plc
Corporate Banking
3 Redheughs Avenue
Edinburgh EH12 9RH

26 January 2018

# Independent Auditors’ Report to the Unitholders of Aberforth UK Small Companies Fund

## Report on the audit of the financial statements

### Opinion

In our opinion, Aberforth UK Small Companies Fund financial statements:

- give a true and fair view of the financial position of the Fund as at 31 December 2017 and of the net revenue and the net capital gains on its scheme property for the year then ended; and
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 102 “The Financial Reporting Standard applicable in the UK and Republic of Ireland”), and applicable law, the Statement of Recommended Practice for UK Authorised Funds, the Collective Investment Schemes sourcebook and the Trust Deed.

We have audited the financial statements, included within the Annual Report and Financial Statements of Aberforth UK Small Companies Fund which comprise: the Balance Sheet as at 31 December 2017; the Statement of Total Return, Statement of Change in net assets attributable to unitholders and the Cash Flow Statement for the year then ended; the Distribution Tables; and the Notes to the Financial Statements, which include a description of the significant accounting policies.

### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (“ISAs (UK)”) and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors’ responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

*Independence*

We remained independent of the Fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC’s Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

## Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which ISAs (UK) require us to report to you when:

- the Authorised Fund Manager’s use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Authorised Fund Manager has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Fund’s ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Fund’s ability to continue as a going concern.

## Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors’ report thereon. The Authorised Fund Manager is responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

*Manager’s Report*

In our opinion, the information given in the Authorised Fund Manager’s Report for the financial period for which the financial statements are prepared is consistent with the financial statements.

# Independent Auditors' Report to the Unitholders of Aberforth UK Small Companies Fund

## Responsibilities for the financial statements and the audit

*Responsibilities of the Authorised Fund Manager for the financial statements*

As explained more fully in the Manager's Responsibilities Statement set out on page 12, the Authorised Fund Manager is responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The Authorised Fund Manager is also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Authorised Fund Manager is responsible for assessing the Fund's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the Authorised Fund Manager either intend to wind up or terminate the Fund, or have no realistic alternative but to do so.

*Auditors' responsibilities for the audit of the financial statements*

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

*Use of this report*

This report, including the opinions, has been prepared for and only for the Fund's unitholders as a body in accordance with paragraph 4.5.12 of the Collective Investment Schemes sourcebook and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

## Other required reporting

### Opinion on matter required by the Collective Investment Schemes sourcebook

In our opinion, we have obtained all the information and explanations we consider necessary for the purposes of the audit.

### Collective Investment Schemes sourcebook exception reporting

Under the Collective Investment Schemes sourcebook we are also required to report to you if, in our opinion:

- proper accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
144 Morrison Street
Edinburgh
EH3 8EB
United Kingdom

26 January 2018

# Financial Statements

## For the year ended 31 December 2017

## Statement of Total Return

| | Notes | **2017** £'000 | **2017** £'000 | 2016 £'000 | 2016 £'000 |
|---|---|---|---|---|---|
| Income: | | | | | |
| Net capital gains | 4 | | **39,694** | | 6,382 |
| Revenue | 5 | **7,896** | | 5,996 | |
| Expenses | 6 | **(1,996)** | | (1,445) | |
| Interest payable and similar charges | | **(1)** | | (8) | |
| Net revenue before taxation | | **5,899** | | 4,543 | |
| Taxation | 7 | **–** | | (5) | |
| Net revenue after taxation | | | **5,899** | | 4,538 |
| **Total return before distributions** | | | **45,593** | | 10,920 |
| Distributions | 8 | | **(7,089)** | | (5,383) |
| **Change in net assets attributable to Unitholders from investment activities** | | | **38,504** | | 5,537 |

## Statement of Change in net assets attributable to unitholders

| | **2017** £'000 | **2017** £'000 | 2016 £'000 | 2016 £'000 |
|---|---|---|---|---|
| **Opening net assets** | | **201,817** | | 168,481 |
| Amounts receivable on issue of units | **61,654** | | 56,124 | |
| Amounts payable on cancellation of units | **(58,148)** | | (32,318) | |
| | | **3,506** | | 23,806 |
| Change in net assets attributable to unitholders from investment activities | | **38,504** | | 5,537 |
| Retained distribution on accumulation units | | **5,189** | | 3,993 |
| **Closing net assets attributable to unitholders** | | **249,016** | | 201,817 |

# Financial Statements

As at 31 December 2017

## Balance Sheet

| | Notes | 2017 £'000 | 2017 £'000 | 2016 £'000 | 2016 £'000 |
|---|---|---|---|---|---|
| ASSETS | | | | | |
| Fixed assets: | | | | | |
| Investments assets | 16 | | **249,877** | | 201,889 |
| Current assets: | | | | | |
| Debtors | 9 | **660** | | 458 | |
| Cash and bank balances | | **–** | | 438 | |
| Total other assets | | | **660** | | 896 |
| Total assets | | | **250,537** | | 202,785 |
| LIABILITIES | | | | | |
| Creditors: | | | | | |
| Bank overdraft | | **(770)** | | – | |
| Other creditors | 10 | **(190)** | | (286) | |
| Distribution payable on income units | | **(561)** | | (682) | |
| Total liabilities | | | **(1,521)** | | (968) |
| **Net assets attributable to unitholders** | | | **249,016** | | 201,817 |

## Cash Flow Statement

For the year ended 31 December 2017

| | Notes | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| **Net cash inflow from operating activities** | 11 | **5,772** | 5,237 |
| **Investing activities** | | | |
| Purchases of investments | | **(87,982)** | (68,879) |
| Sales of investments | | **79,650** | 40,611 |
| Cash outflow from investing activities | | **(8,332)** | (28,268) |
| **Financing activities** | | | |
| Amounts received from issue of units | | **61,925** | 57,675 |
| Amounts paid on cancellation of units | | **(58,762)** | (32,414) |
| Distributions paid | | **(1,810)** | (1,834) |
| Interest paid | | **(1)** | (8) |
| Cash inflow from financing activities | | **1,352** | 23,419 |
| **(Decrease)/increase in cash and cash equivalents** | | **(1,208)** | 388 |
| Cash and cash equivalents at the start of the year | | **438** | 50 |
| Cash and cash equivalents at the end of the year | | **(770)** | 438 |

# Notes to the Financial Statements

## 1 Accounting Policies

(a) The financial statements have been prepared under the historical cost basis, as modified by the revaluation of investments, and in accordance with the Statement of Recommended Practice 'Financial Statements of UK Authorised Funds' issued by the Investment Management Association ('IMA') in May 2014 (the SORP), the Financial Reporting Standard 102 (FRS102), the Financial Conduct Authority's Collective Investment Schemes Sourcebook (COLL) and the Trust Deed. The financial statements have been prepared on a going concern basis.

(b) In accordance with the SORP the investments of the Fund have been valued at a fair value, which is represented by the bid price as at close of business on 31 December 2017. Suspended securities are initially valued at the suspension price but are subject to constant review.

(c) Dividends on equities are recognised when the security is quoted ex-dividend. Overseas dividends are grossed up at the appropriate rate of withholding tax and the tax consequences are shown within the tax charge. Interest receivable is accounted for on an accruals basis and treated as revenue.

(d) The ordinary element of scrip dividends is treated as revenue and forms part of the distribution. Special dividends are treated as income or capital depending on the facts of each particular case.

(e) All expenses are recognised on an accruals basis and are charged to revenue with the exception of the Manager's periodic charge, of which 5/8 of the Manager's periodic charge is allocated to capital and the remaining 3/8 charged to revenue, and a proportion of the safe custody fees taken to capital which relate to purchases and sales transactions.

(f) The charge for tax is based on the results for the year. In general, the tax accounting treatment follows that of the principal amount. The rate of corporate tax for the Fund is 20%, although certain revenue is exempt from tax. Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay less or receive more tax. Deferred tax assets are recognised only to the extent that the manager considers that it is more likely than not that there will be taxable profits from which the underlying timing differences can be deducted.

(g) The quoted investments of the Fund have been valued at bid market value at 12.30pm on the last working day of the accounting period.

## 2 Distribution Policies

The policy is to distribute all available revenue, after deduction of those expenses which are chargeable in calculating the distribution. 3/8 of the Manager's periodic charge is deducted from revenue for purposes of calculating the distribution, the balance being borne by capital. The Fund is not more than 60% invested in qualifying investments (as defined in Section 468L, Income and Corporation Taxes Act 1988) and will pay a dividend distribution.

## 3 Risk Management Policies

In pursuing its investment objective, certain risks arise for the Fund in relation to the investment portfolio and cash balances held. All assets and liabilities are denominated in sterling. Therefore no direct currency risk arises.

The main risks arising are market, liquidity and credit risks. The Manager has policies for managing each of these risks. These policies have remained unchanged since the beginning of the year to which these financial statements relate. The current synthetic risk and reward indicator is 5 and was unchanged during the year. Further information can be found in the Key Investor Information Document available on the Manager's website.

### Market Risk

Market risk arises mainly from uncertainty about future prices of financial instruments held. It represents the potential loss the Fund might suffer through holding market positions in the face of price movements. The Manager does not seek to hedge this exposure as it does not consider this to be beneficial to the Fund in the long term.

### Liquidity Risk

The Fund's assets comprise mainly securities that are considered to be readily realisable in accordance with the market practices of the London Stock Exchange. Liquidity may, however, be affected by market events.

The risk of low market liquidity through reduced trading volumes may affect the Fund's ability to trade investments at values previously indicated by brokers.

The main liability of the Fund is the redemption of units that investors wish to sell. In general the cash levels of the Fund are managed to ensure liabilities can be met. Where investments cannot be realised to meet any potential liability, the Fund may borrow up to 10% of its value to ensure settlement. In addition, in accordance with the Prospectus terms, redemptions may be settled by an in specie transfer of assets.

# Notes to the Financial Statements

### Credit Risk

Certain transactions in securities that the Fund enters into expose it to the risk that the counter-party will not deliver the investment (purchase) or cash (sale) after the Fund has fulfilled its responsibilities.

The investment transactions of the Fund are generally undertaken on a delivery versus payment basis. In addition, the Manager only buys and sells investments through brokers who are authorised and regulated by the Financial Conduct Authority, who have formally agreed terms of business with the Manager, and who are considered to have execution arrangements that enable the Manager to comply with its obligation to obtain the best possible result for the Fund. The Manager closely monitors market developments that may impact a broker's creditworthiness, market reputation and expectations of future financial performance. A range of brokers is utilised by the Manager.

Cash balances are placed with a selection of banking institutions. The Manager reviews the banking partners and the deposit levels on a periodic basis. The Manager aims to have the Fund fully invested.

### Interest Rate Risk

The majority of the Fund's financial assets are equity shares, which do not pay interest or have a maturity date. The Fund's exposure to interest rate risk is therefore insignificant.

## 4 Net Capital Gains

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| The gains on investments during the year comprise: | | |
| Equity investments | **39,694** | 6,382 |

## 5 Revenue

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| UK dividends | **7,444** | 5,660 |
| Property income distributions | **152** | 87 |
| Overseas dividends | **300** | 238 |
| Bank Interest | **–** | 4 |
| Placing commission | **–** | 7 |
| Total income | **7,896** | 5,996 |

## 6 Expenses

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Payable to the Manager or associate of the Manager: | | |
| Manager's periodic fee | **1,895** | 1,344 |
| Payable to the Trustee or associate of the Trustee: | | |
| Trustee's fees | **51** | 46 |
| Other expenses: | | |
| Audit fee | **12** | 13 |
| Safe custody fees | **19** | 15 |
| Registration fees | **10** | 4 |
| Legal fees | **–** | 14 |
| Printing fees | **7** | 7 |
| Taxation services | **2** | 2 |
| | **50** | 55 |
| Total expenses | **1,996** | 1,445 |

The Manager's periodic fee is 0.75% per annum of the valuation of the Fund's property which accrues and is paid monthly in arrears. Included within this fee is £1,184,000 borne by the capital of the Fund (2016: £840,000). Further details of the management fees, Trustee's fees and other expenses of the Fund are available in the Fund's Prospectus.

# Notes to the Financial Statements

## 7 Taxation

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| (a) Analysis of charge in the year: | | |
| Irrecoverable overseas tax | – | 5 |
| Total current tax charge for the year (note 7(b)) | – | 5 |
| (b) Factors affecting current tax charge for the year: | | |
| Net revenue before taxation | 5,899 | 4,544 |
| Corporation tax at 20% | 1,180 | 909 |
| Effects of: | | |
| Non-taxable dividends | (1,489) | (1,132) |
| Non-taxable overseas dividends | (60) | (48) |
| Unutilised management expenses | 369 | 271 |
| Irrecoverable overseas tax | – | 5 |
| | (1,180) | (904) |
| Current tax charge (Note 7(a)) | – | 5 |

At the balance sheet date, the Fund had excess management expenses of £44,742,000 (2016: £42,931,000). It is unlikely that the Fund will generate sufficient taxable profits in the future to utilise these expenses and therefore, no deferred tax asset has been recognised. The deferred tax amount, being 20% of the excess management expenses, equates to £8,948,000 (2016: £8,586,000).

## 8 Distributions

| | 2017 £'000 | 2016 £'000 |
|---|---|---|

The distributions take account of income received on the creation of units and income deducted on the cancellation of units, and comprise:

| | | |
|---|---|---|
| Interim | 4,034 | 3,667 |
| Final | 2,845 | 2,174 |
| | 6,879 | 5,841 |
| Add: Income deducted on cancellation of units | 517 | 183 |
| Less: Income received on creation of units | (307) | (641) |
| Total distributions | 7,089 | 5,383 |

| | 2017 £'000 | 2016 £'000 |
|---|---|---|

The difference between the net revenue after taxation and the distributions for the year are as follows:

| | | |
|---|---|---|
| Net revenue after taxation | 5,899 | 4,538 |
| Add: Manager's periodic fee taken to capital | 1,184 | 841 |
| Add: Safe custody fee taken to capital | 6 | 4 |
| Distributions | 7,089 | 5,383 |

Details of the distribution per unit are shown on page 24.

# Notes to the Financial Statements

## 9 Debtors

| | 2017<br>£'000 | 2016<br>£'000 |
|---|---|---|
| Amounts receivable for creation of units | **36** | – |
| Accrued income | **624** | 458 |
| Total debtors | **660** | 458 |

## 10 Other Creditors

| | 2017<br>£'000 | 2016<br>£'000 |
|---|---|---|
| Amounts payable for cancellation of units | **6** | 103 |
| Purchases awaiting settlement | **–** | 37 |
| Accrued management fee | **157** | 121 |
| Other accrued expenses | **27** | 25 |
| Total creditors | **190** | 286 |

## 11 Reconciliation of net revenue before taxation to net cash flow from operating activities

| | 2017<br>£'000 | 2016<br>£'000 |
|---|---|---|
| Net revenue before taxation | **5,899** | 4,543 |
| Adjusted for: | | |
| Interest payable and similar charges | **1** | 8 |
| Debtors: | | |
| Increase in accrued income | **(166)** | (84) |
| Decrease in other debtors | **–** | 8 |
| Creditors: | | |
| Increase in accrued management fee | **36** | 13 |
| Increase/(decrease) in accrued other expenses | **2** | (2) |
| Taxation | **–** | (5) |
| Special dividends taken to capital | **–** | 756 |
| Net cash flow from operating activities | **5,772** | 5,237 |

# Notes to the Financial Statements

## 12 Portfolio Transaction Costs

| | £'000 | 2017 % of purchases | % Average Net Asset Value | £'000 | 2016 % of purchases | % Average Net Asset Value |
|---|---|---|---|---|---|---|
| Equity purchases in period before transaction costs | **86,770** | | | 66,146 | | |
| Commissions | **173** | **0.20** | **0.07** | 138 | 0.20 | 0.08 |
| Taxes | **422** | **0.48** | **0.17** | 328 | 0.48 | 0.18 |
| Total equity purchases costs | **595** | **0.68** | **0.24** | 466 | 0.68 | 0.26 |
| Corporate actions during the period | **579** | | | 2,260 | | |
| Total purchase consideration after direct transaction costs | **87,944** | | | 68,872 | | |

| | £'000 | 2017 % of sales | % Average Net Asset Value | £'000 | 2016 % of sales | % Average Net Asset Value |
|---|---|---|---|---|---|---|
| Gross equity sales in period before transaction costs | **69,267** | | | 39,004 | | |
| Commissions | **(125)** | **(0.16)** | **(0.05)** | (73) | (0.18) | (0.04) |
| Total equity sales costs | **(125)** | **(0.16)** | **(0.05)** | (73) | (0.18) | (0.04) |
| Corporate actions during the period | **10,509** | | | 1,680 | | |
| Total sales after transaction costs | **79,651** | | | 40,611 | | |

The Fund incurs commissions and taxes on buying and selling investment securities in pursuance of the investment objective. Over the last three financial years, commissions have averaged 0.13% per annum (2016: 0.15% per annum) of the Fund's average net asset value and taxes have averaged 0.17% per annum (2016: 0.18% per annum) over the same period.

Share dealing generally incurs broker commissions and stamp duty and these are paid by the Fund on each transaction where appropriate. In addition there is a dealing spread between the buying and selling prices of the underlying investments. As at 31 December 2017, the average dealing spread for the underlying Fund investments is 1.20% (2016: 1.08%).

Comparing portfolio transaction costs for a range of funds may give a misleading impression of the relative costs of investing in those funds for the following reasons:

- Historic transaction costs are not an effective indicator of the future impact on performance.
- Transactions costs for buying and selling investments due to other investors joining or leaving the fund are recovered from those investors.
- Transaction costs vary depending on the types of investment in which a fund invests.

# Notes to the Financial Statements

### 13 Unitholders' Funds

The Fund has income and accumulation units. The net asset value per unit; the number of units and the accumulation/distribution per unit are shown on page 11. All units, adjusted for the current accumulation factor, have the same rights on winding-up.

| Number of units | Opening 1 Jan 2017 | Issued | Redeemed | Converted | Closing 31 Dec 2017 |
|---|---|---|---|---|---|
| Accumulation | 641,058.237 | 163,796.797 | (44,566.219) | 6.337 | 760,295.152 |
| Income | 369,607.953 | 124,134.166 | (251,975.654) | (8.198) | 241,758.267 |

### 14 Related Party Transactions

Management fees paid to Aberforth Unit Trust Managers Limited are shown in note 6 and details of units created and cancelled are shown in the Statement of Change in Unitholders' Net Assets. The balance due from Aberforth Unit Trust Managers Limited at the year end in respect of these transactions was £127,000 (31 December 2016: £224,000). Trustee fees paid are shown in note 6. The balance due to National Westminster Bank plc at the year end in respect of these fees was £4,400 (31 December 2016: £4,000).

### 15 Contingencies and financial commitments

The Fund had no financial commitments, contingent assets or liabilities as at 31 December 2017 (2016: nil).

### 16 Fair value disclosure

Fair value hierarchy is intended to prioritise the inputs used to measure the fair value of assets and liabilities as prescribed by FRS102. The hierarchy is split into the following 3 levels:

Level 1 - Using unadjusted quoted prices for identical instruments in an active market.

Level 2 - Using inputs, other than quoted prices included in level 1 that are directly or indirectly observable based on market data.

Level 3 - Using unobservable inputs due to market data being unavailable.

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Assets £'000** | **Liabilities £'000** | Assets £'000 | Liabilities £'000 |
| Level 1 | **249,877** | – | 201,889 | – |
| **Total** | **249,877** | – | 201,889 | – |

### Market price risk

The Company's investment portfolio is exposed to market price fluctuations, which are monitored by the Manager in pursuance of the investment objective. It is not the Fund's policy to use derivatives or hedging instruments to manage market price risk.

At the year end date, 100% (2016: 100%) of the net assets of the Fund were invested in ordinary shares or stock units admitted to an official stock exchange. If the investment portfolio valuation fell by 10% at 31 December 2017, the impact on Unitholders' funds would have been negative £24.9m (2016: negative £20.2m). If the investment portfolio valuation rose by 10% at 31 December 2017, the impact on Unitholders' funds would have been positive £24.9m (2016: positive £20.2m). The calculations are based on the portfolio valuation as at the respective balance sheet dates and are not representative of the year as a whole. All other variables are assumed to remain constant.

As at 31 December 2017, all of the Fund's financial instruments were included in the balance sheet at fair value. The investment portfolio consisted of investments valued at bid prices which represent fair value. The only exceptions to this were Kenmare Resources Warrants and International Ferro Metals which have been fair valued at £nil.

# Distributions

## Distribution Table

### For the six months to 31 December 2017

| | Net Income Dec 2017 | Equalisation† Dec 2017 | Distribution/ Accumulation Dec 2017 | Distribution/ Accumulation Dec 2016 |
|---|---|---|---|---|
| Income units (payable 28 February 2018) | | | | |
| Group 1: Units purchased prior to 1 July 2017 | **232.1606p** | – | **232.1606p** | 184.6361p |
| Group 2: Units purchased on or after 1 July 2017 | **134.0104p** | **98.1502p** | **232.1606p** | 184.6361p |
| Accumulation units | | | | |
| Group 1: Units purchased prior to 1 July 2017 | **300.3617p** | – | **300.3617p** | 232.6989p |
| Group 2: Units purchased on or after 1 July 2017 | **173.3782p** | **126.9835p** | **300.3617p** | 232.6989p |

### For the six months to 30 June 2017

| | Net Income Jun 2017 | Equalisation† Jun 2017 | Distribution/ Accumulation Jun 2017 | Distribution/ Accumulation Jun 2016 |
|---|---|---|---|---|
| Income units (payable 31 August 2017) | | | | |
| Group 1: Units purchased prior to 1 January 2017 | **303.3928p** | – | **303.3928p** | 296.6426p |
| Group 2: Units purchased on or after 1 January 2017 | **201.9968p** | **101.3960p** | **303.3928p** | 296.6426p |
| Accumulation units | | | | |
| Group 1: Units purchased prior to 1 January 2017 | **386.4433p** | – | **386.4433p** | 366.4933p |
| Group 2: Units purchased on or after 1 January 2017 | **257.2912p** | **129.1521p** | **386.4433p** | 366.4933p |

† When buyers purchase units, the purchase price includes the value of securities and revenue up to the date of purchase. All unitholders receive the same distribution, in pence per unit, however equalisation applies only to units purchased during the distribution period (Group 2 units). Equalisation is the average amount of income included in the purchase of all Group 2 units and is refunded to holders of these units as a return of capital. Being capital, it is not liable to income tax but must be deducted from the cost of units for capital gains tax purposes.

## Distribution Record

| Year to | Accumulation Units Net income per Unit (p) | Income Units Net income per Unit (p) |
|---|---|---|
| 31 December 2013 | 399.7750 | 345.5453 |
| 31 December 2014 | 416.0784 | 351.3320 |
| 31 December 2015 | 548.9197 | 453.1564 |
| 31 December 2016 | 599.1922 | 481.2787 |
| **31 December 2017** | **686.8050** | **535.5534** |

# Management and Administration

## Manager
Aberforth Unit Trust Managers Limited*
14 Melville Street
Edinburgh EH3 7NS
Telephone – Dealing: 0345 608 0940
– Enquiries: 0131 220 0733
Dealing: ordergroup@linkgroup.co.uk
Email: enquiries@aberforth.co.uk
Website: www.aberforth.co.uk

## Trustee & Depositary
National Westminster Bank plc*
Trustee & Depositary Services
The Younger Building
1st Floor
3 Redheughs Avenue
Edinburgh EH12 9RH

## Investment Adviser
Aberforth Partners LLP*
14 Melville Street
Edinburgh EH3 7NS

## Registrar
Link Fund Administrators Limited*
PO Box 388
Unit 1, Roundhouse Road,
Darlington
DL1 9UE
Telephone: 0345 608 0940

## Custodian
The Northern Trust Company*
50 Bank Street
Canary Wharf
London E14 5NT

## Auditors
PricewaterhouseCoopers LLP
Atria One
144 Morrison Street
Edinburgh EH3 8EX

**Authorised and regulated by the Financial Conduct Authority*

## Buying and Selling
The terms on which units can be bought and sold are set out in the Prospectus, Key Investor Information Document, Supplementary Information Document and Application Pack that are all available on the Manager's website www.aberforth.co.uk. These documents provide up to date terms on which Units are issued and redeemed, how and when money is held in a client money account and the risks relating to that.

Units may be bought and sold by contacting the Manager by telephone using the dealing number shown above. Alternatively, please contact Link, the Registrar, using the address above or by email (ordergroup@linkgroup.co.uk). In addition, orders can be placed electronically via various transaction networks including EMX and Calastone. Valuation of the Fund normally takes place each business day at 4.30 pm (or such other time as the market closes) on a forward pricing basis.

## Tax Compliance Requirements
Due to regulatory requirements to gather more information about investments being made by overseas investors, the Manager is required to submit a report to HMRC on an annual basis to provide details of all investments held and distributions received by overseas investors. Further information is available on the Manager's website.

## Beware of Investor Fraud
Unitholders may receive unsolicited phone calls or correspondence concerning investment matters which imply a connection to the Fund. These are typically from overseas based 'brokers' who target UK investors offering to sell them what often turn out to be worthless or high risk investments. Unitholders may also be advised that there is an imminent offer for the Fund, and the caller may offer to buy units at significantly above the market price if an administration fee is paid. This is known as 'boiler room fraud'. All such calls or correspondence should be ignored.

You can find more information about investment scams at the Financial Conduct Authority (FCA) website www.fca.org.uk/scams. You can also call the FCA Consumer Helpline on 0800 111 6768.

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