# Aberforth Smaller Companies Trust plc

## Half Yearly Report

**30 June 2016**

# Investment Objective

The investment objective of Aberforth Smaller Companies Trust plc (ASCoT) is to achieve a net asset value total return (with dividends reinvested) greater than on the Numis Smaller Companies Index (excluding Investment Companies) over the long term.

# Contents



All data throughout this Half Yearly Report are to, or as at, 30 June 2016 as applicable, unless otherwise stated.

# Financial Highlights

## Six months to 30 June 2016

| Total Return Performance | % |
|---|---|
| **Net Asset Value[1]** | **-11.3** |
| **Numis Smaller Companies Index (XIC)[2]** | **-5.6** |
| **Ordinary Share Price[3]** | **-22.3** |

| | 30 June 2016 | 31 December 2015 | 30 June 2015 |
|---|---|---|---|
| Shareholders' Funds | **£1,034.8m** | £1,191.9m | £1,256.7m |
| Market Capitalisation | **£859.9m** | £1,133.6m | £1,133.4m |
| Actual Gearing employed | **2.8%** | 0.3% | 4.7% |
| Ordinary Share net asset value | **1,092.06p** | 1,254.30p | 1,320.66p |
| Ordinary Share price | **907.50p** | 1,193.00p | 1,191.00p |
| Ordinary Share price discount | **16.9%** | 4.9% | 9.8% |

| Cumulative Returns (%) Period to 30 June 2016 | NAV[1] | Index[2] | Share Price[3] |
|---|---|---|---|
| 1 year | -15.2 | -6.6 | -21.7 |
| 3 years | 26.7 | 24.0 | 20.4 |
| 5 years | 57.6 | 56.7 | 52.3 |
| 10 years | 101.2 | 122.6 | 97.2 |
| 15 years | 308.2 | 272.5 | 308.3 |
| Since inception on 10 December 1990 | 2,233.5 | 1,243.0 | 1,868.4 |

1 Represents Net Asset Value return (Fully Diluted Net Asset Value prior to 1 April 2003) with dividends reinvested.

2 Represents the return on the Numis Smaller Companies Index (excluding Investment Companies) (NSCI (XIC)) with dividends reinvested. This index comprises the bottom 10% of all UK quoted companies by market value, which at 1 January 2016 consisted of 349 companies, the largest market capitalisation of which was £1.3 billion and the aggregate market capitalisation of which was £150 billion.

3 Represents Ordinary Share price with dividends reinvested.

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.

# Chairman's Statement

## Review of performance

For the six months to 30 June 2016, the net asset value total return of Aberforth Smaller Companies Trust plc (ASCoT) was -11.3%, which compares with a total return of -5.6% from the Company's investment benchmark, the Numis Smaller Companies Index (excluding Investment Companies) (NSCI (XIC)). The FTSE All-Share Index, which is dominated by larger companies, generated a return of +4.3% over the same period. The discount on the Company's shares widened from 5% at the start of the period to 17% as at 30 June.

It is clear that this has been a disappointing six-month period in both absolute and relative terms. In financial markets, describing events as "exceptional" has been a somewhat overused cliché in recent years. In the aftermath of the Brexit referendum and with ten year gilt yields falling below 1%, such a description of the six months to 30 June 2016 seems entirely appropriate. The Managers' Report expands on both occurrences and reviews other factors that have influenced the Company's returns during the first six months of the year.

## Dividends

In recent reports to shareholders, I have highlighted the excellent dividend environment that has prevailed since the recovery in 2010. The first half of 2016 witnessed a continuation of that environment. Accordingly, the Board is pleased to announce an interim dividend of 8.60p per Ordinary Share for the year to 31 December 2016. The interim dividend will be paid on 25 August 2016 to Shareholders on the register as at close of business on 5 August 2016. The ex dividend date is 4 August 2016.

The Company operates a Dividend Reinvestment Plan. Details of the plan, including the Form of Election, are available from Capita Registrars or on its website, www.capitaassetservices.com.

The growth of 5.2% in the 2016 interim dividend when compared with 2015 maintains the roughly 5% rate of progress that shareholders have seen in both 2014 and 2015. Against a backdrop of extremely low inflation, the majority of that growth rate can be thought of as real, i.e. inflation adjusted. This current rate of real dividend growth compares very favourably with the average of around 2.5% that has been witnessed from the NSCI (XIC) since its start date in 1955. The period since 2010 has been unusually strong in terms of dividends for shareholders in small UK quoted companies.

In determining its progressive dividend policy, the Board has been acutely conscious that such high rates of real growth must inevitably decline. However, the pace and timescale of such a fading are much harder to forecast. This uncertainty has encouraged the Board to balance its ambition to expand ASCoT's dividends in a progressive fashion with a strengthening of revenue reserves. The Company had revenue reserves of 45.2p per share at 31 December 2015, which represent 1.7 times the total of the 2015 final and 2016 interim dividends. This compares with 1.3 times in the immediate aftermath of the Global Financial Crisis in 2010. This represents an encouraging position for the Board to deliver its progressive dividend policy.

## Gearing

Gearing has shown little change over the period and stood at 2.8% of Shareholders' Funds at 30 June 2016. The Board reviews the level of gearing regularly and is comfortable that the Company has access to sufficient liquidity for investment purposes and also to fund share buy-

# Chairman's Statement

backs, as and when appropriate. It remains the Company's current policy to use gearing in a tactical manner.

## Share buy-in

During the six months to 30 June 2016, 271,000 shares (0.3% of the issued share capital) were bought in for a total consideration of £2,751,000. The Board keeps under review the circumstances in which the authority is utilised.

## Conclusion

Following the result of the Brexit referendum, the investment climate has become more uncertain. Currently, the UK is very much centre-stage, as economists, politicians and journalists attempt to predict both the near-term pathway for the UK economy and the longer-term implications of the "out" vote. Stockmarkets do not wait for leadership elections or European diplomacy and almost instantaneously discounted tougher times for UK domestic-facing businesses over the coming months. Unsurprisingly, in the short term, this has had the most impact in the small and mid cap sectors of the UK stockmarket. Alongside the decline in sterling, we have seen some early policy shifts from both the Bank of England and George Osborne, which are aimed at providing additional support to the UK economy. In the short run, macro factors are likely to be at the front of investors' minds, despite the fact that numerous academic works highlight GDP growth and stockmarket returns as being uncorrelated. Other academic studies, and experience, suggest that valuations matter more and in that regard the de-rating of the NSCI (XIC) over the past two years both in absolute terms and relative terms, when compared to the larger companies, may suggest a reasonable proportion of an earnings decline is priced in.

Over the first half of 2016, the Company has had to contend with the adversities of a weakening UK economy, small and mid-cap underperformance, ten year gilt yields at less than 1% and a resurgent resources sector. And, in what could easily be described as a perfect storm, a large widening of the discount over the six month period has produced one of the most painful six monthly results for shareholders in ASCoT's history. Such setbacks have in the past been followed by sharp rebounds in performance. This time round, headwinds for small companies and the value style may blow for longer as much of the developed world becomes subsumed by negative real interest rates.

However, with valuations already almost a third below their peak of the last three years and with ASCoT's robust income characteristics, this situation will not last indefinitely. Moreover, the Managers are well placed to take advantage of the market volatility that has followed the referendum and that has given rise to some anomalous valuations for good businesses. ASCoT remains heavily differentiated from its benchmark and from its peer group, which is in part a result of the Managers' value investment philosophy. The Board remains firmly of the view that the Company will benefit from this philosophy consistently pursued by the well resourced and experienced team at Aberforth.

Paul Trickett
*Chairman*
27 July 2016
paul.trickett@aberforth.co.uk

# Managers' Report

## Introduction

What had already proved a challenging start to 2016 became distinctly more so with the outcome of the EU referendum at the end of June. The year had commenced with familiar concerns about US and Chinese economic growth affecting stockmarket sentiment. A powerful rally, led by the resources companies, then commenced in mid February. Its momentum diminished as the EU referendum campaign progressed and the chance of an "out" vote rose. Still, the eventual outcome was unexpected and initiated what could be a protracted period of intense uncertainty for the UK and for Europe more broadly.

The net effect of these developments was a total return of 4.3% for the FTSE All-Share over the six months to 30 June 2016. Large companies benefited from their substantial exposure to overseas earners and to resources companies, though they also had to contend with the drag from banks in the wake of the "out" vote. Small companies have less exposure than large to both banks and resources, but they have a greater reliance on the domestic economy, which seems likely to experience a slowdown as a result of the referendum. Hence the NSCI (XIC) experienced a total return of -5.6%. ASCoT's NAV total return was -11.3%. This was clearly a disappointing result in both absolute and relative terms. While the greatest impact on the absolute number was the referendum outcome, the more significant relative influence came earlier in the period and was related to the resources rebound. This is explained in more detail in the Investment Performance section of this report.

ASCoT's NAV performance was made more painful for shareholders by an expansion in the discount of the share price to the NAV from an unusually tight 5% at the start of the year to an unusually wide 17% at 30 June 2016. Thus, the share price total return over the six month period was -22.3%. ASCoT was not alone: discounts across the range of UK small and mid cap investment trusts expanded in the period. Brexit was a significant influence, since, with their greater exposure to the domestic economy, small companies are likely to be more disadvantaged by the greater uncertainty that accompanied the "out" vote.

It is probable that Brexit will undermine the UK's economic growth in the near term. Small companies have less overseas exposure and so, all else being equal, will suffer more than their larger peers from a UK recession. The referendum result also ushers in an indeterminate period of intense uncertainty for financial markets. Crucial issues – such as government, the timescales for the exit itself, terms of trade, the make-up of the UK – are up in the air. Accordingly, it is difficult to argue that UK equities do not now merit lower valuations, even if, over the longer term, the "Brexiteers" are proved right in their belief that the economy has been stifled by EU membership.

Of course, the implications of the Brexit vote are not confined to the UK. Political risk across Europe has risen as a result of the UK's decision: with the arguments of break-away parties in other countries now carrying more weight, the threat to the stability of the Eurozone, with its structural challenges, has undoubtedly risen. More broadly, Brexit may embolden populist anti-establishment movements around the world and confirms that politics is creating more volatility in equity valuations than at any time since the end of the Cold War.

# Managers' Report

## Investment performance

Over the six months to 30 June 2016, ASCoT's NAV total return was -11.3% against -5.6% for the NSCI (XIC). The following table analyses the difference between these numbers, while the subsequent paragraphs give additional detail about the influences on performance.

| For the six months ended 30 June 2016 | Basis points |
|---|---|
| Stock selection | (394) |
| Sector selection | (146) |
| **Attributable to the portfolio of investments, based on mid prices** | **(540)** |
| (after transaction costs of 8 basis points) | |
| Movement in mid to bid price spread | 29 |
| Cash/gearing | (20) |
| Purchase of ordinary shares | 3 |
| Management fee | (36) |
| Other expenses | (3) |
| **Total attribution based on bid prices** | **(567)** |

Note: 100 basis points = 1%. Total Attribution is the difference between the total return of the NAV and the Benchmark Index (i.e. NAV = -11.27%; Benchmark Index = -5.60%; difference is 5.67% being 567 basis points).

### *Size*

For reasons that are set out in the **Valuation** section of this report, ASCoT's portfolio remains biased to the "smaller small" companies within the NSCI (XIC). This positioning was modestly helpful in the first six months of 2016, as may be demonstrated by comparing the total returns of the FTSE SmallCap index and the FTSE 250 index. The former was down by 4.6%, whereas the latter experienced a decline of 6.2%, which suggests that "smaller small" companies performed less weakly.

### *Style & sectors*

The fortunes of Aberforth's value investment style were bound up with those of the resources sectors in the first half of 2016. As was the case in the large cap world, within the NSCI (XIC) value out-performed growth in headline terms. This was because nearly all the resources companies within the index are classified as value stocks at the present time and their share prices rebounded significantly. With the resources companies excluded, the value style under-performed growth in the six months.

In 2015, ASCoT benefited from its under-weight position in resources and the miners in particular. However, the Managers did not possess sufficient foresight to embrace the sector in advance of its bounce, which commenced in mid February. Through the first half of 2016, the continuing under-weight in resources was therefore a drag to relative returns and the resources sectors in aggregate cost the portfolio 189 basis points of relative performance.

Resources companies, especially the miners, represent a particular challenge for the Managers. Small cap miners are typically focused on one asset, which is often located in a part of the world that does not enjoy the established property rights of the UK. Cash flows are weak as a result of large investment programmes and dividends are unusual. Moreover, the ownership structures of small resources companies are frequently such that corporate governance standards are in doubt. To be clear, none of these are reasons to justify ignoring the resources sector: the Managers carry out the analysis that they would on any company and, indeed, the portfolio contained nine resources companies at 30 June 2016. However, the risks already highlighted are reflected in the requirement for a higher margin of safety to be embedded in the valuation and in a smaller than average holding size in individual companies. The recent flurry of interest in the resources sector has not altered this approach and has not given extra impetus to increase exposure to that area of the market.

The EU referendum is also relevant to sector performance. The higher chance of a domestic recession and the weakness of sterling since the "out" vote have seen significant differentiation in sector performance: those parts of the market close to the domestic economy – such as the housebuilders, retailers and property companies – have been weaker than those parts with an overseas orientation that are beneficiaries of a weaker currency. The portfolio's exposure to the domestic economy is similar to that of the NSCI (XIC): the companies in the portfolio derive 52% of their revenues from the UK against 54% for the index. In most cases, the stockmarket has been reasonably efficient and has already built in the heightened risk faced by domestic businesses into their valuations. However, there are anomalies and the Managers expect opportunities to arise among both the overseas and domestic earners.

### *Corporate activity*

M&A and IPOs abounded in 2015. This was not the case in the first half of 2016. Concerns about the EU referendum appear to be responsible: reluctance on the part of an overseas company to commit to acquiring sterling assets is understandable. In total, bids for nine constituents of the NSCI (XIC) have been announced over the past six months. Of those, ASCoT held three in its portfolio. The paucity of bid activity is a hindrance to the Managers' value investment style: history suggests that corporate acquirers are often more prepared to recognise value than other stockmarket participants. While the uncertainty of Brexit complicates a recovery in M&A, the fall in sterling has rendered UK assets more affordable for overseas buyers. It is notable that there have been deal announcements since the referendum. As regards IPOs, there were eight in the first half. None of these was taken by ASCoT: the Managers spent time to understand the underlying businesses but were dissuaded from investing by the valuations demanded by the vendors.

### *Income*

The dividend performance of small companies remained strong through the first six months of 2016. In contrast to that of the FTSE All-Share, the income generated from the NSCI (XIC) stands out for its good dividend cover – 2.9x against 1.5x – and for its low reliance on a handful of very large dividend payers. It is likely that dividend growth across the NSCI (XIC) in 2016 will for another year exceed the long term average of 2.5% in real terms and that companies will continue to supplement ordinary dividend payments with special dividends.

ASCoT has benefited from these trends in recent years and, indeed, in the first half of 2016. This bodes well for the year as a whole. It is worth noting that, had the Managers anticipated the rally in the share prices of the nil yielding resources companies, the income performance of the portfolio would, all else being equal, be less robust. It also bears repeating that, in this world of zero or negative interest rate policy, there is a clamouring for income. Company boards are alive to this and, in certain cases, their dividend decisions may have been influenced accordingly. The risk is that some of these decisions will prove to have been ill-judged when the next recession happens. Following the EU referendum, the test might now come sooner than previously expected.

*Turnover*

Portfolio turnover in the first six months of 2016 was unusually low, annualising at 16%. This compares with a long term average of around 35%. There is a connection between investment style and the rate of turnover: if the broader stockmarket is uninterested in the value stocks within the portfolio and is therefore not revaluing them, there is little motivation for the Managers to sell and reinvest. Hence for a value manager, a pick-up in turnover can be associated with improved relative performance.

*Active share*

This is a measure of how different a portfolio is from an index. The higher the active share ratio, the greater the difference. A higher ratio increases the probability that the portfolio will perform differently from the index, though it offers no guarantees as to direction. The Managers use active share as a tool to ensure that the portfolio does not become a closet index tracker and target a ratio of at least 70%. At 30 June 2016, the ratio was 78%.

## Valuations

| | **30 June 2016** | | 30 June 2015 | |
|---|---|---|---|---|
| **Portfolio characteristics** | **ASCoT** | **NSCI (XIC)** | ASCoT | NSCI (XIC) |
| Number of companies | **83** | **339** | 90 | 357 |
| Weighted average market capitalisation | **£514m** | **£823m** | £700m | £874m |
| Price earnings (PE) ratio (historic) | **10.5x** | **12.4x** | 14.1x | 15.7x |
| Dividend yield (historic) | **3.4%** | **2.8%** | 2.6% | 2.4% |
| Dividend cover | **2.8x** | **2.9x** | 2.7x | 2.6x |

The valuation metrics in the table above are consistent with the Managers' value investment style: the portfolio has a lower PE ratio and a higher dividend yield than the NSCI (XIC)'s. The historical PE ratio of the FTSE All-Share was 18.0x. Therefore, large companies presently command a substantial 45% PE premium to small, compared with a 9% premium on average over the past 25 years. The greater weighting of the resources sectors in the FTSE All-Share is influential: many resources companies are currently very highly rated as the stockmarket anticipates a recovery in profits.

# Managers' Report

| EV/EBITA | | 43 growth companies | 240 other companies | Tracked Universe | Portfolio |
|---|---|---|---|---|---|
| 2016 | | 15.6x | 11.3x | 12.0x | 9.9x |
| 2017 | pre Brexit | 13.8x | 9.8x | 10.4x | 8.5x |
| | assuming recession | 14.8x | 11.5x | 12.0x | 9.8x |

The table above examines the valuation of the portfolio and the tracked universe on the basis of the Managers' favoured metric, the ratio of enterprise value to earnings before interest, tax and amortisation (EV/EBITA). Given the uncertainties of Brexit and the likelihood of a UK downturn, it shows two scenarios for 2017. The principal assumptions behind the recession scenario are that the downturn starts on 1 January 2017 and that the profits of domestic businesses decline by 25% on average. It can be inferred that this would result in little profit growth for the portfolio and the tracked universe as a whole, but that the 43 growth companies still make progress. This resilience on the part of the growth companies is precisely why they are accorded high valuations. However, this scenario still leaves growth companies on a 51% premium to the portfolio. This might suggest that recession risk is already substantially discounted in present valuations. A narrowing of that premium should be consistent with superior performance from the portfolio.

| Market capitalisation range: | < £100m | £100-250m | £250-500m | £500-750m | > £750m |
|---|---|---|---|---|---|
| Portfolio weight | 6% | 27% | 23% | 18% | 25% |
| Tracked universe weight | 1% | 8% | 20% | 19% | 52% |
| Tracked universe 2016 EV/EBITA | 7.8x | 8.8x | 10.7x | 11.5x | 13.9x |

The final valuation table examines the interplay of valuation and size. ASCoT's portfolio is heavily under-exposed to the "larger small" companies within the NSCI (XIC). Higher weightings in the "smaller small" companies make up for this. The rationale for this positioning is clear from the final row: the "smaller small" companies are on substantially lower valuations, despite being anticipated to grow more quickly. From a long term perspective, this is an unusual state of affairs but has persisted for several years since the financial crisis. The explanation probably resides in a more pervasive and intense reluctance since the crisis to take on the risk of lower liquidity that comes with investment in "smaller small" companies. For the Managers this is anomalous and represents a compelling opportunity, which ASCoT – a closed-end fund able to adopt a long term investment horizon – is well placed to exploit.

# Managers' Report

## Outlook and conclusion

The modest valuations that characterise the portfolio, and indeed much of the UK small company universe, declined in the wake of the EU referendum. The coming months will determine whether investors in general deem these valuations to be sufficiently low to compensate for greater uncertainty. The "out" vote undeniably complicates the outlook for the UK economy and therefore for many small UK quoted companies. It comes at a time of a wide current account deficit and a still large public sector borrowing requirement. With interest rates already very low, the monetary policy response is limited, but a relaxation of the austerity strategy might allow fiscal policy to take the strain. Sterling has already offered some relief, but it would not surprise were the economy to enter recession as spending and investment decisions continue to be deferred.

This is a somewhat downbeat prospect for small companies. However, the passage of time will see today's uncertainties addressed, as has been seen already with the prompt appointment of a new prime minister. Moreover, it is worth recalling the nimbleness and resilience that small companies displayed in the last downturn eight years ago: they emerged from a global recession in a better state than they had entered it, to which their subsequent outstanding dividend performance attests. Beyond that, the structural advantages enjoyed by the UK, which have helped small companies generate such strong returns over the long term, remain largely intact: language, time-zone, property rights, corporate governance and, perhaps now debatably, political stability and openness.

Notwithstanding the ramifications of Brexit, the Managers believe that small companies can continue their long term record of strong returns. As a reminder, the NSCI (XIC) has seen £1,000 invested on 31 December 1990 grow to £13,545 on a total return basis, which compares with £8,351 for large companies. This superior performance has been achieved in a volatile fashion: were an investor to have missed the best five months for small companies in this period, the premium over large companies would be eliminated. This predicament for small cap investors is demonstrated by the suddenness of the rebound in small company share prices during the last slowdown in 2009.

History is a useful guide but, with no precedent for Brexit, can offer no guarantees. The Managers nevertheless retain confidence in ASCoT's diversified portfolio of companies and in its ability to recover from a period of weak performance, as it has in the past. With valuations at current levels, much of the downside seems already to have been discounted and the number of attractive investment opportunities has increased.

Aberforth Partners LLP
*Managers*

27 July 2016

# Investment Portfolio

## Fifty Largest Investments as at 30 June 2016

| No. | Company | Valuation £'000 | % of Total | Business Activity |
|---|---|---|---|---|
| 1 | FirstGroup | 32,601 | 3.2 | Bus & rail operator |
| 2 | e2v technologies | 28,542 | 2.8 | Electronic components & subsystems |
| 3 | International Personal Finance | 27,835 | 2.7 | Home credit provider |
| 4 | Vesuvius | 25,383 | 2.4 | Metal flow engineering |
| 5 | Centamin | 25,288 | 2.4 | Gold miner |
| 6 | Hogg Robinson Group | 23,594 | 2.3 | Travel & expense management |
| 7 | Brewin Dolphin Holdings | 23,369 | 2.2 | Private client fund manager |
| 8 | Hilton Food Group | 23,056 | 2.2 | Food manufacturer |
| 9 | Grainger | 23,037 | 2.2 | Property – residential rentals |
| 10 | Keller | 21,278 | 2.1 | Ground engineering services |
| | **Top Ten Investments** | **253,983** | **24.5** | |
| 11 | De La Rue | 20,959 | 2.0 | Bank note printer |
| 12 | Ladbrokes | 20,864 | 2.0 | Bookmaker & online gaming |
| 13 | Shanks Group | 20,278 | 2.0 | Waste services |
| 14 | Northgate | 20,254 | 2.0 | Van rental |
| 15 | Urban&Civic | 19,931 | 1.9 | Property – investment & development |
| 16 | Paragon Group | 19,835 | 1.9 | Specialist lender |
| 17 | Wincanton | 19,467 | 1.9 | Logistics |
| 18 | SDL | 18,564 | 1.8 | Software – translation & content management |
| 19 | Morgan Advanced Materials | 18,494 | 1.8 | Manufacture of carbon & ceramic materials |
| 20 | Hansteen Holdings | 18,442 | 1.8 | Property – industrial |
| | **Top Twenty Investments** | **451,071** | **43.6** | |
| 21 | Senior | 18,278 | 1.8 | Aerospace & automotive engineering |
| 22 | Mothercare | 18,085 | 1.7 | Retailing – maternity & children's products |
| 23 | Vectura Group | 17,916 | 1.7 | Inhaled pharmaceuticals – respiratory specialism |
| 24 | Bovis Homes Group | 17,834 | 1.7 | Housebuilding |
| 25 | Go-Ahead Group | 17,750 | 1.7 | Bus & rail operator |
| 26 | RPS Group | 17,564 | 1.7 | Energy & environmental consulting |
| 27 | Connect Group | 17,463 | 1.7 | Newspaper distribution |
| 28 | Vitec Group | 17,418 | 1.7 | Photographic & broadcast accessories |
| 29 | Bodycote | 17,060 | 1.7 | Engineering – heat treatment |
| 30 | TT Electronics | 16,685 | 1.6 | Sensors & other electronic components |
| | **Top Thirty Investments** | **627,124** | **60.6** | |

# Investment Portfolio

## Fifty Largest Investments as at 30 June 2016

| No. | Company | Valuation £'000 | % of Total | Business Activity |
|---|---|---|---|---|
| 31 | Computacenter | 15,888 | 1.5 | IT services |
| 32 | Nostrum Oil & Gas | 15,360 | 1.5 | Oil & gas exploration and production |
| 33 | Robert Walters | 15,104 | 1.5 | Recruitment |
| 34 | Trinity Mirror | 14,209 | 1.4 | UK newspaper publisher |
| 35 | Premier Farnell | 13,826 | 1.3 | Electronic components distribution |
| 36 | EnQuest | 13,727 | 1.3 | Oil & gas exploration and production |
| 37 | Huntsworth | 13,048 | 1.2 | Public relations |
| 38 | Novae Group | 12,848 | 1.2 | Lloyd's insurer |
| 39 | Speedy Hire | 12,009 | 1.2 | Plant hire |
| 40 | Spirent Communications | 11,950 | 1.2 | Telecoms test equipment |
| | **Top Forty Investments** | **765,093** | **73.9** | |
| 41 | John Laing Group | 11,903 | 1.2 | Infrastructure investment |
| 42 | McKay Securities | 11,774 | 1.1 | Property – London & South East offices |
| 43 | Castings | 11,618 | 1.1 | Engineering – automotive castings |
| 44 | Flybe Group | 11,304 | 1.1 | Airline |
| 45 | RM | 11,279 | 1.1 | IT services for schools |
| 46 | Pendragon | 11,277 | 1.1 | Automotive retailer |
| 47 | Coats Group | 10,981 | 1.1 | Manufacture of industrial textiles |
| 48 | KCOM Group | 10,158 | 1.0 | Telecoms & related services |
| 49 | Eurocell | 9,892 | 1.0 | Manufacture of UPVC building products |
| 50 | Games Workshop Group | 9,694 | 0.9 | Tabletop fantasy wargames |
| | **Top Fifty Investments** | **874,973** | **84.6** | |
| | Other Investments (33) | 188,676 | 18.2 | |
| | **Total Investments** | **1,063,649** | **102.8** | |
| | Net Liabilities | (28,889) | (2.8) | |
| | **Total Net Assets** | **1,034,760** | **100.0** | |

# Long-Term Investment Record

## Historic Total Returns

| Period | Discrete Annual Returns (%) NAV[1] | Index[2] | Share Price[3] |
|---|---|---|---|
| 1 year to 30 June 2016 | -15.2 | -6.6 | -21.7 |
| 1 year to 30 June 2015 | 13.4 | 10.4 | 16.6 |
| 1 year to 30 June 2014 | 31.8 | 20.3 | 31.9 |
| 1 year to 30 June 2013 | 36.3 | 31.8 | 44.6 |
| 1 year to 30 June 2012 | -8.7 | -4.1 | -12.6 |
| 1 year to 30 June 2011 | 36.3 | 34.2 | 36.3 |
| 1 year to 30 June 2010 | 18.9 | 28.0 | 15.2 |
| 1 year to 30 June 2009 | -16.6 | -12.4 | -8.5 |
| 1 year to 30 June 2008 | -25.6 | -24.8 | -26.5 |
| 1 year to 30 June 2007 | 26.9 | 25.4 | 22.6 |

| | Annualised Returns (%) | | | Cumulative Returns (%) | | |
|---|---|---|---|---|---|---|
| Periods to 30 June 2016 | NAV[1] | Index[2] | Share Price[3] | NAV[1] | Index[2] | Share Price[3] |
| 2 years | -1.9 | 1.5 | -4.4 | -3.9 | 3.1 | -8.7 |
| 3 years | 8.2 | 7.4 | 6.4 | 26.7 | 24.0 | 20.4 |
| 4 years | 14.6 | 13.1 | 14.9 | 72.7 | 63.4 | 74.1 |
| 5 years | 9.5 | 9.4 | 8.8 | 57.6 | 56.7 | 52.3 |
| 6 years | 13.6 | 13.2 | 12.9 | 114.9 | 110.4 | 107.6 |
| 7 years | 14.3 | 15.2 | 13.3 | 155.5 | 169.3 | 139.2 |
| 8 years | 9.9 | 11.3 | 10.3 | 113.0 | 136.0 | 118.9 |
| 9 years | 5.3 | 6.6 | 5.4 | 58.5 | 77.5 | 60.8 |
| 10 years | 7.2 | 8.3 | 7.0 | 101.2 | 122.6 | 97.2 |
| 15 years | 9.8 | 9.2 | 9.8 | 308.2 | 272.5 | 308.3 |
| 25.6 years from inception[4] | 13.1 | 10.7 | 12.4 | 2,233.5 | 1,243.0 | 1,868.4 |

1 Represents Net Asset Value (Fully Diluted Net Asset Value prior to 1 April 2003) with dividends reinvested.

2 Represents capital appreciation/(depreciation) on the Numis Smaller Companies Index (excluding Investment Companies) with dividends reinvested.

3 Represents Ordinary Share price with dividends reinvested.

4 Inception date of the Company was 10 December 1990.

# Interim Management Report

A review of the half year and the outlook for the Company can be found in the Chairman's Statement and the Managers' Report.

## Risks and Uncertainties

The Directors have established an on-going process for identifying, evaluating and managing the principal risks faced by the Company. The Board believes that the Company has a relatively low risk profile in the context of the investment trust industry. This belief arises from the fact that the Company has a simple capital structure; invests only in small UK quoted companies; has never been exposed to derivatives and does not presently intend any such exposure; and outsources all the main operational activities to recognised, well established firms.

The principal risks faced by the Company relate to investment policy/performance, share price discount, gearing, reputational risk and regulatory risk. An explanation of these risks and how they are managed can be found in the Strategic Report contained within the 2015 Annual Report. These principal risks and uncertainties have not changed from those disclosed in the 2015 Annual Report.

## Going Concern

The Directors are satisfied that the Company has sufficient resources to continue in operation for the foreseeable future, a period of not less than 12 months from the date of this report. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

# Directors' Responsibility Statement

The Directors confirm that, to the best of their knowledge:

(i) the condensed set of financial statements has been prepared in accordance with the Statement "Half-yearly financial reports" issued by the Financial Reporting Council; and

(ii) the Half Yearly Report includes a fair review of information required by:

   (a) DTR 4.2.7R of the Disclosure and Transparency Rules, being an indication of important events during the first six months of the year and their impact on the financial statements together with a description of the principal risks and uncertainties for the remaining six months of the year; and

   (b) DTR 4.2.8R of the Disclosure and Transparency Rules, being disclosure of related party transactions and changes therein.

(iii) the Half Yearly Report, taken as whole, is fair, balanced and understandable and provides information necessary for Shareholders to assess the Company's performance, objective and strategy.

On behalf of the Board
Paul Trickett
*Chairman*

27 July 2016

# Income Statement

*(unaudited)*

For the six months ended 30 June 2016

| | Six months ended 30 June 2016 Revenue £'000 | Capital £'000 | Total £'000 |
|---|---|---|---|
| Realised net (losses)/gains on sales | – | (5,633) | (5,633) |
| Movement in fair value | – | (147,059) | (147,059) |
| Net (losses)/gains on investments | – | (152,692) | (152,692) |
| Investment income | 23,577 | 251 | 23,828 |
| Other income | – | – | – |
| Investment management fee (Note 2) | (1,588) | (2,647) | (4,235) |
| Transaction costs | – | (1,003) | (1,003) |
| Other expenses | (319) | – | (319) |
| **Net return before finance costs and tax** | 21,670 | (156,091) | (134,421) |
| Finance costs | (125) | (208) | (333) |
| **Return on ordinary activities before tax** | 21,545 | (156,299) | (134,754) |
| Tax on ordinary activities | (39) | – | (39) |
| **Return attributable to equity shareholders** | 21,506 | (156,299) | (134,793) |
| Returns per Ordinary Share (Note 4) | 22.67p | (164.75)p | (142.08)p |

### Dividends

On 27 July 2016, the Board declared an interim dividend for the year ending 31 December 2016 of 8.60p per Ordinary Share (2015 – 8.15p) which will be paid on 25 August 2016.

# Income Statement

| Six months ended 30 June 2015 Revenue £'000 | Capital £'000 | Total £'000 | Year ended 31 December 2015 Revenue £'000 | Capital £'000 | Total £'000 |
|---|---|---|---|---|---|
| – | 62,880 | 62,880 | – | 186,289 | 186,289 |
| – | 88,010 | 88,010 | – | (99,157) | (99,157) |
| – | 150,890 | 150,890 | – | 87,132 | 87,132 |
| 22,218 | 1,462 | 23,680 | 37,652 | 1,462 | 39,114 |
| – | – | – | – | – | – |
| (1,606) | (2,677) | (4,283) | (3,283) | (5,472) | (8,755) |
| – | (1,884) | (1,884) | – | (3,890) | (3,890) |
| (341) | – | (341) | (778) | – | (778) |
| 20,271 | 147,791 | 168,062 | 33,591 | 79,232 | 112,823 |
| (119) | (199) | (318) | (242) | (403) | (645) |
| 20,152 | 147,592 | 167,744 | 33,349 | 78,829 | 112,178 |
| – | – | – | – | – | – |
| 20,152 | 147,592 | 167,744 | 33,349 | 78,829 | 112,178 |
| 21.15p | 154.89p | 176.04p | 35.03p | 82.80p | 117.83p |

# Reconciliation of Movements in Shareholders' Funds

*(unaudited)*

## For the six months ended 30 June 2016

| | Share capital £'000 | Capital redemption reserve £'000 | Special reserve £'000 | Capital reserve £'000 | Revenue reserve £'000 | Total £'000 |
|---|---|---|---|---|---|---|
| **Balance as at 31 December 2015** | **950** | **38** | **172,625** | **955,881** | **62,385** | **1,191,879** |
| Return on ordinary activities after tax | – | – | – | (156,299) | 21,506 | (134,793) |
| Equity dividends paid | – | – | – | – | (19,575) | (19,575) |
| Purchase of Ordinary Shares | (2) | 2 | (2,751) | – | – | (2,751) |
| **Balance as at 30 June 2016** | **948** | **40** | **169,874** | **799,582** | **64,316** | **1,034,760** |

## For the six months ended 30 June 2015

| | Share capital £'000 | Capital redemption reserve £'000 | Special reserve £'000 | Capital reserve £'000 | Revenue reserve £'000 | Total £'000 |
|---|---|---|---|---|---|---|
| Balance as at 31 December 2014 | 953 | 35 | 176,300 | 877,052 | 53,000 | 1,107,340 |
| Return on ordinary activities after tax | – | – | – | 147,592 | 20,152 | 167,744 |
| Equity dividends paid | – | – | – | – | (16,209) | (16,209) |
| Purchase of Ordinary Shares | (1) | 1 | (2,134) | – | – | (2,134) |
| Balance as at 30 June 2015 | 952 | 36 | 174,166 | 1,024,644 | 56,943 | 1,256,741 |

## For the year ended 31 December 2015

| | Share capital £'000 | Capital redemption reserve £'000 | Special reserve £'000 | Capital reserve £'000 | Revenue reserve £'000 | Total £'000 |
|---|---|---|---|---|---|---|
| Balance as at 31 December 2014 | 953 | 35 | 176,300 | 877,052 | 53,000 | 1,107,340 |
| Return on ordinary activities after tax | – | – | – | 78,829 | 33,349 | 112,178 |
| Equity dividends paid | – | – | – | – | (23,964) | (23,964) |
| Purchase of Ordinary Shares | (3) | 3 | (3,675) | – | – | (3,675) |
| Balance as at 31 December 2015 | 950 | 38 | 172,625 | 955,881 | 62,385 | 1,191,879 |

# Balance Sheet

*(unaudited)*

As at 30 June 2016

| | **30 June 2016 £'000** | 31 December 2015 £'000 | 30 June 2015 £'000 |
|---|---|---|---|
| **Fixed assets:** investments at fair value through profit or loss | **1,063,649** | 1,195,581 | 1,315,440 |
| **Current assets** | | | |
| Amounts due from brokers | **191** | – | 196 |
| Other debtors | **6,329** | 2,725 | 3,650 |
| Cash at bank | **59** | 1,025 | 17 |
| | **6,579** | 3,750 | 3,863 |
| **Creditors** (amounts falling due within one year) | | | |
| Amounts due to brokers | **(2,102)** | (293) | (8,974) |
| Bank debt facility | **(33,212)** | – | – |
| Other creditors | **(154)** | (217) | (166) |
| | **(35,468)** | (510) | (9,140) |
| **Net current (liabilities)/assets** | **(28,889)** | 3,240 | (5,277) |
| **Total assets less current liabilities** | **1,034,760** | 1,198,821 | 1,310,163 |
| **Creditors** (amounts falling due after more than one year) | | | |
| Bank debt facility | **–** | (6,942) | (53,422) |
| **TOTAL NET ASSETS** | **1,034,760** | 1,191,879 | 1,256,741 |
| **CAPITAL AND RESERVES: EQUITY INTERESTS** | | | |
| Share Capital: Ordinary Shares | **948** | 950 | 952 |
| **Reserves:** | | | |
| Capital redemption reserve | **40** | 38 | 36 |
| Special reserve | **169,874** | 172,625 | 174,166 |
| Capital reserve | **799,582** | 955,881 | 1,024,644 |
| Revenue reserve | **64,316** | 62,385 | 56,943 |
| **TOTAL SHAREHOLDERS' FUNDS** | **1,034,760** | 1,191,879 | 1,256,741 |
| **Net asset value per share (Note 6)** | **1,092.06p** | 1,254.30p | 1,320.66p |
| **Share price** | **907.50p** | 1,193.00p | 1,191.00p |

# Cash Flow Statement

*(unaudited)*

For the six months ended 30 June 2016

| | **Six months ended 30 June 2016 £'000** | Six months ended 30 June 2015 £'000 | Year ended 31 December 2015 £'000 |
|---|---|---|---|
| **Net cash inflow from operating activities** | **15,561** | 17,619 | 29,137 |
| **Investing activities** | | | |
| Purchases of investments | **(112,037)** | (225,154) | (452,925) |
| Sales of investments | **91,892** | 206,721 | 480,102 |
| **Cash (outflow)/inflow from investing activities** | **(20,145)** | (18,433) | 27,177 |
| **Financing activities** | | | |
| Purchase of Ordinary Shares | **(2,751)** | (2,134) | (3,675) |
| Equity dividends paid | **(19,575)** | (16,209) | (23,964) |
| Interest and fees paid | **(306)** | (314) | (638) |
| Net drawdown/(repayment) of bank debt facilities (before costs) | **26,250** | 19,250 | (27,250) |
| **Cash inflow/(outflow) from financing activities** | **3,618** | 593 | (55,527) |
| **Change in cash during the period** | **(966)** | (221) | 787 |
| Cash at the start of the period | **1,025** | 238 | 238 |
| Cash at the end of the period | **59** | 17 | 1,025 |

# Notes to the Financial Statements

### 1. Accounting Standards

The financial statements have been prepared on a going concern basis and in accordance with the Financial Reporting Standard 104 and the AIC's Statement of Recommended Practice "Financial Statements of Investment Trust Companies and Venture Capital Trusts" issued in 2014. The total column of the Income Statement is the profit and loss account of the Company. All revenue and capital items in the Income Statement are derived from continuing operations. No operations were acquired or discontinued in the period. The same accounting policies used for the year ended 31 December 2015 have been applied.

### 2. Investment Management Fee

The Managers, Aberforth Partners LLP, receive an annual management fee, payable quarterly in advance, equal to 0.75% of net assets up to £1 billion, and 0.65% thereafter.

The investment management fee has been allocated 62.5% to capital reserve and 37.5% to revenue reserve, in line with the Board's expected long term split of returns, in the form of capital gains and income respectively, from the investment portfolio of the Company.

### 3. Dividends

| | **Six months ended 30 June 2016 £'000** | Six months ended 30 June 2015 £'000 | Year ended 31 December 2015 £'000 |
|---|---|---|---|
| **Amounts recognised as distributions to equity holders in the period:** | | | |
| Final dividend of 17.00p for the year ended 31 December 2014 | **–** | 16,209 | 16,209 |
| Interim dividend of 8.15p for the year ended 31 December 2015 | **–** | – | 7,755 |
| Final dividend of 17.85p for the year ended 31 December 2015 | **16,962** | – | – |
| Special dividend of 2.75p for the year ended 31 December 2015 | **2,613** | – | – |
| | **19,575** | 16,209 | 23,964 |

The interim dividend for the year ending 31 December 2016 of 8.60p (2015 – 8.15p) will be paid on 25 August 2016 to shareholders on the register on 5 August 2016. The ex dividend date is 4 August 2016. The interim dividend has not been included as a liability in these financial statements.

# Notes to the Financial Statements

### 4. Returns per Ordinary Share

The returns per Ordinary Share are based on:

| | **30 June 2016** | 30 June 2015 | 31 December 2015 |
|---|---|---|---|
| Returns attributable to Ordinary Shareholders | **£(134,793,000)** | £167,744,000 | £112,178,000 |
| Weighted average number of shares in issue during the period | **94,869,880** | 95,288,936 | 95,200,792 |
| Return per Ordinary Share | **(142.08)p** | 176.04p | 117.83p |

### 5. Investments at fair value

In accordance with FRS 102 and FRS 104, fair value measurements have been classified using the fair value hierarchy:

Level 1 - using unadjusted quoted prices for identical instruments in an active market;
Level 2 - using inputs, other than quoted prices included within Level 1, that are directly or indirectly observable (based on market data); and

Level 3 - using inputs that are unobservable (for which market data is unavailable).

**Investments held as fair value through profit or loss**

| **As at 30 June 2016** | **Level 1 £'000** | **Level 2 £'000** | **Level 3 £'000** | **Total £'000** |
|---|---|---|---|---|
| **Listed equities** | **1,043,371** | **20,278** | **–** | **1,063,649** |
| **Unlisted equities** | **–** | **–** | **–** | **–** |
| **Total financial asset investments** | **1,043,371** | **20,278** | **–** | **1,063,649** |

| As at 31 December 2015 | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 | Total £'000 |
|---|---|---|---|---|
| Listed equities | 1,195,581 | – | – | 1,195,581 |
| Unlisted equities | – | – | – | – |
| Total financial asset investments | 1,195,581 | – | – | 1,195,581 |

| As at 30 June 2015 | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 | Total £'000 |
|---|---|---|---|---|
| Listed equities | 1,315,440 | – | – | 1,315,440 |
| Unlisted equities | – | – | – | – |
| Total financial asset investments | 1,315,440 | – | – | 1,315,440 |

## 6. Net Asset Value per Ordinary Share

The net assets and the net asset value per share attributable to the Ordinary Shares at each period end are calculated in accordance with their entitlements in the Articles of Association and were as follows:

| | **30 June 2016 £'000** | 31 December 2015 £'000 | 30 June 2015 £'000 |
|---|---|---|---|
| Net assets attributable | **1,034,760** | 1,191,879 | 1,256,741 |
| Ordinary Shares in issue at end of period | **94,752,792** | 95,023,792 | 95,159,792 |
| Net asset value per Ordinary Share | **1,092.06p** | 1,254.30p | 1,320.66p |

## 7. Share Capital

During the period, the Company bought in and cancelled 271,000 shares (2015: 185,000) at a total cost of £2,751,000 (2015: £2,134,000). 30,500 shares have been bought back for cancellation between 1 July 2016 and 27 July 2016 at a total cost of £277,000.

## 8. Related party transactions

There were no matters during the six months ended 30 June 2016 requiring disclosure under s412 of the Companies Act 2016.

## 9. Further Information

The foregoing do not constitute statutory accounts of the Company (as defined in section 434(3) of the Companies Act 2006). The financial information for the year ended 31 December 2015 has been extracted from the statutory accounts which have been filed with the Registrar of Companies. The Auditor issued an unqualified opinion on those accounts and did not make any statements under section 498(2) or (3) of the Companies Act 2006. All information shown for the six months to 30 June 2016 is unaudited.

Certain statements in this report are forward looking. By their nature, forward looking statements involve a number of risks, uncertainties or assumptions that could cause actual results or events to differ materially from those expressed or implied by those statements. Forward looking statements regarding past trends or activities should not be taken as representation that such trends or activities will continue in the future. Accordingly, undue reliance should not be placed on forward looking statements.

**J. Thomson** Colour Printers

# Corporate Information

## Directors
S Paul Trickett (Chairman)
Paula M Hay-Plumb
David J Jeffcoat
Julia Le Blan
Richard A Rae

## Investment Managers & Secretaries
Aberforth Partners LLP
14 Melville Street
Edinburgh EH3 7NS
Tel: 0131 220 0733
Email: enquiries@aberforth.co.uk
www.aberforth.co.uk

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

## Registrars
Capita Asset Services
Shareholder Solutions
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU

Shareholder enquiries:
Tel: 0871 664 0300
(Calls cost 10p per minute plus network extras)
Email: ssd.services@capitaregistrars.com
www.capitaassetservices.com
Share Portal:
www.capitashareportal.com/forms/Welcome.aspx

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

## Bankers
The Royal Bank of Scotland plc
36 St Andrew Square
Edinburgh EH2 2YB

## Independent Auditor
Deloitte LLP
Saltire Court
20 Castle Terrace
Edinburgh EH1 2DB

## Lawyers & Sponsors
Dickson Minto WS
16 Charlotte Square
Edinburgh EH2 4DF

## Registered Office
14 Melville Street
Edinburgh EH3 7NS

Registered in Scotland No:
SC 126524

## Security Codes
| | |
|---|---|
| SEDOL: | 0006655 |
| Bloomberg : | ASL LN |
| Reuters: | ASL.L |
| GIIN: | U6SSZS.99999.SL.826 |