

# Strategic Equity Capital

## Interim Management Statement 30 September 2008

This interim management statement, issued in accordance with the UK Listing Authority's Disclosure and Transparency Rules, relates to the period from 1 July to 30 September 2008.

### Investment Highlights

- NAV negatively impacted by market turmoil.
- Majority of portfolio companies operating satisfactorily; strategic and operational plans broadly on track.
- Fund exhibiting attractive valuation characteristics.

### Financial Highlights

- Net assets of £43.9 million, or 63.1p per share; a decrease of 22.4% during the period (FTSE All Share down 12.2% and FTSE small cap (excluding investment trusts) index down 14.9%).
- Share price of 42.75p, a decrease of 35.5%.
- Company fully invested at the end of the period; net cash represented 0.9% of NAV.
- A further 1,463,000 shares bought into treasury at an average price of 57.02 pence.

### Investment Manager's Review

The third quarter was an extraordinary time for the UK equity markets, continuing an extremely uncertain period in equity market history. At 30 September 2008, from peak to trough, the FTSE All-Share Index had fallen by 29.7% and the FTSE Smaller Companies (ex Investment Trusts) Index by 48.7% as equity risk premia rose dramatically. Companies with debt have been particularly badly hit. Investors' concern about the general outlook for earnings and the potential impact of significant downgrades on banking covenants coupled with a severe reduction of credit availability has focused attention on balance sheets. Whilst the majority of portfolio companies have demonstrated comparatively resilient operational performance, the Company's net asset value has been materially affected by these conditions.

### Portfolio Activity

Overall, the portfolio saw limited activity during the quarter. We are seeing an increasing number of potential opportunities for new investments as conventional sources of finance have become increasingly scarce and we continue to evaluate these. However, liquidity in the small cap market remains extremely low and, although we benefitted from corporate activity in H1, we do not expect takeover activity to return in any meaningful way before the end of the year. Consequently, our focus

has been on working with the management teams of existing investments to ensure that all necessary operational action is taken in view of the economic climate.

The Company made two new small investments in the period. We made a modest investment in convertible preference shares issued by **Inspired Gaming**. Each preference share carries a payment in kind coupon of 7%, has a redemption price of £1.00, equivalent to 200% of the issue price, and is convertible at any time into one ordinary share. Certain mandatory redemption rights arise in the event of a takeover. Management are working with advisers to sell the business. The investment represented 0.9% of net assets at 30 September 2008.

**Avingtrans** is a small niche engineering conglomerate focused on value added products for critical applications predominantly in medical, nuclear and alternative energy, and aerospace sectors. The company has recently experienced wholesale management change led by the new chairman and now a significant shareholder, Roger McDowell. We supported an equity issue to support the expansion of the company's facilities in China on the back of contracted orders. We expect the business to focus on improving its return on capital as well as growing both organically and by acquisition. This should provide the opportunity to work with management and to put more capital to work in future. The investment represented 1.1% of net assets at 30 September 2008.

The Company had committed to three equity issues at 30 June 2008. The equity issue in **Renold** completed on 7 August 2008 and the company continues to trade well with the forward order book at 30 September 36% ahead of the comparable prior year period.

**Melrose** completed its equity issue supporting the acquisition of FKI Group and plans for FKI remain on track. These commenced with a buy-back offer for the existing FKI high yield bonds. The results for the business, excluding FKI, to 30 June showed a good performance in the Group's main businesses. The **Journey Group** equity issue and bond conversion completed successfully on 29 August. Results to 30 June showed a sharp turnaround from 2007, with the company producing an EBITDA profit of £0.7m for the six months against a loss of £2.1 million in the comparative prior year period. Whilst the outlook for the business remains challenging in light of the deterioration in the macroeconomic outlook, management has demonstrated the organic growth prospects and has

positioned the group for a number of strategic alternatives.

### Corporate Events

At the time of the Company's results, the Board announced that it was reviewing all options to reduce the level of discount over the medium term for the benefit of all shareholders. The Board subsequently announced that, having obtained the views of shareholders representing over 90% of the issued share capital, it was resolved to continue to support the existing investment policy whilst selectively continuing to use its existing buy-back authority. In addition, the Board undertook to present an ordinary resolution at the 2010 AGM to allow shareholders to vote on the continuation of the Company.

### Outlook

Given the high concentration of the Company's portfolio, we anticipate

continued volatility in the underlying net asset value until we see some stability returning to the equity markets. Despite this, we believe that this is a clear investment opportunity. The UK market is now looking good value, both relative to gilts and on a long term valuation basis. In our view, Strategic Equity Capital is attractively valued, exhibiting strong value and cashflow metrics. We believe that by avoiding companies that have deep structural issues and focusing on companies with value characteristics, smaller, cash generative companies, and incentivised management teams we should deliver strong returns for investors in Strategic Equity Capital.

As at 7 November 2008, the unaudited net asset value per Ordinary Share, including current period revenue, was 45.90 pence.

### Summary

(as at 30 September 2008)

Net assets	£43.9 million
Net Asset Value (NAV) per Ordinary share	63.06p
Net cash as % of funds invested	0.9%

### Top 10 Investments

Company name (as at 30 September 2008)	% invested in portfolio
Redstone	12.4
Pinewood Shepperton	8.1
Intec Telecom	7.4
Spirent Communications	7.1
Thorntons	7.1
4Imprint	6.2
Vintage I	5.2
RPC Group	5.1
Ora Capital	5.1
Renold	4.9

### Sector analysis

	% of portfolio
Technology	22.4
Industrials	14.8
Media	13.9
Telecom	13.0
Support services	12.7
Investment companies	7.8
Retail	7.0
Financial	5.1
Construction	1.6
Leisure	0.8
Net cash	0.9

### Size analysis (market cap)

	% of portfolio
Less than £100m	59.4
£100 – £300 million	24.4
£300 – £500 million	7.1
Greater than £500 million	9.1

### Contact details

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# Strategic Equity Capital

Strategic Equity Capital plc

## Investment Manager – SVG's Public Equity Team

SVG's Public Equity Team was established in 2002. Headed up by Tony Dalwood and Adam Steiner, the team now consists of seven investment professionals who combine a complimentary skill set of corporate finance, fund management, research and private equity experience.

## Investment process

The Manager seeks to identify investment opportunities by applying private equity appraisal techniques primarily in public markets.

After a potential investee company has been identified, initial due diligence is undertaken.

Before finalising an investment decision, the Manager will seek to engage directors, management and shareholders of potential investee companies in constructive dialogue directed towards the implementation of value creation strategies. Such strategies may include:

- capital raisings;
- financial restructurings;
- operational restructurings;
- trade sales; and
- public to private transactions.

The Company does not seek to involve itself in the day-to-day management of the companies in which it invests. The manager seeks to maintain regular contact with the managers and directors of investee companies.

## Fund facts

- A London Stock Exchange listed, UK domiciled investment trust
- Independent board chaired by John Hodson
- The objective is to achieve absolute returns over a medium term period, principally through capital gains
- The majority of the portfolio to be invested in 10-15 companies
- An investment horizon of typically two to five years for each investment
- A flexible gearing policy of up to 25% of net assets

## Principal terms

- Management fee of 1% of NAV per annum
- Performance fee of 15% of NAV gains (total return) in excess of 7% per annum compounding trigger, with high watermark

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## Risk considerations

You should remember that the value of investments, and the income from them, may go down as well as up, and is not guaranteed, and investors may not get back the amount of money invested. Past performance cannot be relied on as a guide to future performance. Exchange rate changes may cause the value of overseas investments or investments denominated in different currencies to rise or fall. In addition, there is no guarantee that the market price of shares will fully reflect their underlying net asset value and it is not uncommon for the market price of such shares to trade at a substantial discount to their net asset value.

These are not all the risks of an investment in Strategic Equity Capital shares. Investors should take advice from their own independent, professional financial advisers before making an investment decision and are responsible for ascertaining any income tax or other tax consequences which may affect their acquisition of any investment.

## The Strategic Advisory Board

The Investment Manager utilises a Strategic Advisory Board to assist in the analysis of company management and directors, business dynamics and investment opportunities. The Strategic Advisory Board also provides introductions to other industrialists for due diligence. Members of the Strategic Advisory Board include:

### Stewart Binnie

- Was at WH Smith plc from 1976 to 1984, latterly as merchandise controllers, and was Managing Director of Hatchards Bookshops Limited from 1984 to 1989
- He was a Partner of, and consultant to, Schroder Ventures (now known as Permira) until 1996. He has also been the Chairman of Helicon Publishing Group plc and TFPL Limited
- Currently Chairman of Mosaic Fashions hf



### Alan Mackay

- Managing Director and member of the leadership team in 3i's European buyouts business with 18 years of private equity experience
- Alan's board appointments include chairman of the supervisory board of a central European private fund TCEE NV. He is also a member of the board at Nordic industrial holding company Atle Industri AB, private equity manager 3TS Oy, and the British-Swedish Chamber of Commerce



### Ken Minton

- Has led successful turnarounds within a number of UK publicly listed companies. These include Laporte plc (where he was Chief Executive), Mowlem plc (as executive Chairman) and Arjo Wiggins Appleton plc (as Executive Chairman)
- He is currently Executive Chairman of 4imprint Group plc and non-executive Director at Tomkins plc and Solvay SA



### William Nabarro

- Was Vice Chairman of KPMG Corporate Finance
- Is currently non-executive Director of ICAP plc, Executive Director of Jardine Lloyd Thompson UK Ltd and Treasurer of the University of Leeds



### Sir Clive Thompson

- Chairman of Rentokil Initial plc until 2004, having been Chief Executive for twenty years until the end of 2002. Over this period the company averaged 20% growth in earnings per share per annum and a similar rate of growth in dividends per share
- Was President of the CBI (1998-2000), member of the Hampel Committee on Corporate Governance and Deputy Chairman of the Financial Reporting Council
- Has been a Director of Sainsbury plc, Wellcome PLC, Seaboard plc, Caradon PLC and BAT Industries PLC

