Ennismore European Smaller Companies Fund

Investor Newsletter for the month of December 2010

Issued on 11 January 2011

Important Notice

For the first time since launching the Fund more than a decade ago we went on a roadshow to meet potential new investors in November. Our target is to raise EUR 70m of new money across the two funds managed by Ennismore Fund Management, after which we will again hard close the Fund by capping the number of shares in issue. The purpose of this fundraising is to diversify further our client base and we remain absolutely committed to limiting assets under management. We are looking for like-minded investors who are both willing and able to invest for the long term. Further details can be found in our roadshow presentation which is available on our website www.ennismorefunds.com. If you would like to subscribe please call Eleanor Scott on +44 (0) 20 7368 4219 or email subs@ennismorefunds.com. Redemptions can be made through the Administrator in the usual way. Please also note that on 4th January 2011 Northern Trust International Fund Administration Services (Ireland) Limited was appointed as Administrator.

Fund Details

Daily dealing UCITS and Irish Financial Services Regulatory Authority regulated open-ended investment company with Financial Services Authority approval, registered in Ireland and listed on the Irish Stock Exchange. The Fund has an A S&P Fund Research Fund Rating. The Fund size was GBP 99m as at 31st December. Total assets under management by Ennismore Fund Management were GBP 153m. Further background information, including all past newsletters, can be found on our website.

The Fund is managed as an absolute return fund with the objective of generating positive returns irrespective of market conditions rather than performing relative to any benchmark index. Index data is provided in the following table as a guide to general equity market conditions.

Performance as at 31 December 2010

	GBP			EUR			
Period	Fund NAV[1] Per Share	Fund NAV[2] Per Share % Change	HSBC Index[3] % Change	Fund NAV[1] Per Share	Fund NAV[2] Per Share % Change	HSBC Index[3] % Change	MSCI Index[4] % Change
December 10	**57.90**	**6.0**	**12.7**	**67.57**	**3.4**	**10.0**	**5.5**
November 10	54.64	-0.4	-4.7	65.37	3.6	-1.1	-3.3
October 10	54.87	2.3	3.6	63.12	2.0	3.2	3.0
September 10	53.63	3.4	10.4	61.90	-1.3	5.5	5.3
August 10	51.85	-1.5	-2.0	62.70	-0.9	-1.5	-2.2
July 10	52.63	2.4	6.7	63.27	0.8	5.1	5.9
June 10	51.39	-0.3	-3.6	62.77	3.9	-0.3	-2.5
May 10	51.52	-1.6	-9.4	60.41	0.2	-6.9	-5.8
April 10	52.36	1.0	-0.4	60.28	3.7	1.8	-1.8
March 10	51.84	2.0	7.9	58.12	2.5	8.4	6.9
February 10	50.82	3.0	1.2	56.69	-0.3	-1.9	0.7
January 10	49.32	0.9	-0.1	56.86	3.3	2.1	-3.8
2010 to date	**57.90**	**18.4**	**21.9**	**67.57**	**22.8**	**25.9**	**6.8**
Annualised return[5]		**16.0**	**9.8**		**14.1**	**7.8**	**2.4**
Since launch (27/01/99)		**489.9**	**203.9**		**379.8**	**146.2**	**32.6**

[1] Source: Administrator, Net Asset Value. [2] Source: Administrator, Net Asset Value, net income reinvested. [3] Source: Bloomberg, HSBC Smaller European Total Return Index.
[4] Source: Bloomberg, MSCI Europe Index, local currencies, total return. [5] Since inception, to date. Note: All performance figures net of fees.

Comments below on performance refer to GBP NAV per share unless otherwise stated, exclude cash returns and are prior to expenses. No value has been attributed to the Fund's claim for USD 7.8m in the administration of Lehman Brothers International (Europe) due to the uncertainty of both the timing and amount of any eventual recovery. The Fund's holding in Trader Media East continues to be valued based on the latest net asset value reported by that company, as explained in our October 2009 newsletter.

The Fund's NAV increased by 6.0% in December. Our long book added 7.7% while the Fund's short exposure cost 0.4%. The strongest contribution came from cement maker Buzzi Unicem, which added 0.9%. Consumption in its most important end market, the USA, has shown signs of improving with October shipments (the most recent data available) up 14% year on year. Given currently depressed levels of industry utilisation, if this pickup in demand can be sustained it will have a dramatic effect on Buzzi's overall profitability. Sto also continued to contribute positively, adding 0.9%, having upgraded guidance in November. Shares in UK fashion retailer French Connection were up over 60% in December, contributing 0.6%, and Xing added 0.6%. LSL Property Services, which is covered in detail in the stock comment below, also contributed 0.6%.

Portfolio Activity

Figures in brackets refer to previous month end; * = positions > 0.5% of NAV.

As at 31st December the Fund was invested in 73 (78)* stocks.

LSL Property Services – UK residential surveyor and estate agency (2.9% of NAV)

LSL is the largest surveyor of residential property in the UK and the second largest estate agency chain. LSL's main business is valuing residential properties for lenders to use as a basis for mortgages, with an average fee of about GBP 150 per survey. The company has grown its market share from less than 10% in 2003 to close to 45% in the first half of this year. They have mostly benefitted from a strong trend towards outsourcing by lenders and also from their main competitors' focus on estate agency rather than surveying. Despite a massive decline in property market activity in the UK – there were around 1.3m mortgage approvals in 2009 compared to an annual average of 2.9m over the 1998-2008 period – LSL has increased surveying profits. As well as increased volume coming from higher market share, profitability is also helped by a business model that provides economies of scale and is cyclically defensive. The key is that many of the jobs managed by LSL for lenders are then outsourced to independent surveyors at very low margin. LSL keeps the jobs that maximise utilisation of its own surveyors, allowing them to perform a higher number of jobs per day than their competitors (economies of scale), and cuts the number of jobs that are outsourced when market volume declines (meaning LSL's profitable in-house surveying is much less cyclical). The result of this is that the operating profit from the division has been stable around GBP 25m for the past five years. We believe this alone justifies the company's enterprise value of GBP 280m.

Estate agency is by nature more cyclical as the cost structure is less variable. Profits from this division peaked at GBP 13m in 2007 and it will be profitable again this year. However the historic numbers do not reflect the transformational deal done in 2009 which made LSL the second largest player in the UK. LSL was effectively paid GBP 26m in cash to take the heavily loss-making Halifax chain from Lloyds Banking Group, which had acquired it as part of the shotgun marriage with HBOS brokered by the UK government at the height of the financial crisis. Having spent less than GBP 20m in cash restructuring the chain, and after only one year, the acquired business is already able to show a profit for the second half of 2010. As a whole LSL's estate agency division now has double the market share of five years ago and, over the cycle, we expect it to produce average annual earnings of at least GBP 15m.

The resilience of the surveying business model and the opportunistic expansion of the agency business at close to the trough in real estate activity in the UK reflect the excellent management team in place at LSL. Importantly they own 30% of the company, having led an MBO from insurer Aviva in 2004. The current market valuation of LSL on twelve times 2010 earnings is at least a third too low in our view. While overall volumes in the UK residential property market are likely to decline slightly again in 2011 LSL's proven business model in surveying should remain resilient. Estate agency profitability will rebound strongly as and when the market recovers and this is currently not priced into the shares at all.

Top Five Holdings as at 31 December 2010

	Company	Country	Sector	% of NAV
1	Sto	Germany	Construction	9.3
2	Xing	Germany	Technology	5.7
3	Buzzi Unicem	Italy	Construction	3.7
4	Kentz Corp	United Kingdom	Industrials	3.1
5	LSL Property Services	United Kingdom	Property	2.9
				24.7

Exposures as at 31 December 2010

Longs %	Shorts %	Gross Exposure %	Net Exposure %
87.0 (91.2)	31.1 (35.2)	118.1 (126.4)	55.9 (56.0)

Figures in brackets refer to previous month end.

Exposures by Country, Market Cap and Sector as % NAV as at 31 December 2010

Country	Gross%	Net%
Bermuda	1.7	-0.7
Denmark	2.1	2.1
France	3.6	-1.3
Germany	33.4	21.9
Ireland	4.1	4.1
Isle Of Man	1.0	1.0
Italy	8.4	7.0
Jersey	4.7	2.9
Netherlands	3.0	3.0
Spain	2.0	-2.0
Sweden	1.5	-0.1
Switzerland	4.4	0.2
UK	39.6	18.0
US	6.8	-2.0
Other	1.8	1.8

Market Cap	Gross%	Net%
>£2bn	8.5	-1.9
£700m - £2bn	10.5	-3.1
£200m - £700m	47.9	19.7
<£200m	51.2	41.2

Sector	Gross%	Net%
Construction	16.8	16.7
Consumer	12.2	3.1
Energy	4.0	-1.3
Financial	3.6	0.9
Food	2.0	-0.3
Industrials	14.2	6.2
Leisure	4.2	-2.6
Materials	1.7	0.1
Media	17.4	13.3
Property	6.8	6.8
Services	8.4	4.1
Technology	20.0	9.2
Telecoms	4.5	-2.6
Transport	1.9	1.9
Other	0.4	0.4

The geographic analysis relates to country of incorporation or listing. This may not represent the underlying economic exposure of the operating business.

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