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ASSET MANAGEMENT

MESCT

Montanaro European Smaller Companies Trust

Quarterly review – Q1 2026

Key points:

- Escalating geopolitical tensions in the Middle East, particularly the Iran conflict, drove sharp market volatility and a rotation away from growth assets.
- Markets reacted in a disorderly fashion, with traditional diversification breaking down as commodities surged and both gold and crypto failed to provide protection
- Rapid advances in AI triggered a severe repricing across technology, particularly in software, as investors questioned business models, capital intensity and the risk of disruption
- This led to a broad derating of high-quality growth equities and a rotation towards more inflation- and energy-linked sectors.
- Against this backdrop, the portfolio remained focused on fundamentals and long-term opportunities, using the dislocation to selectively redeploy capital into high-quality businesses where valuations have become more attractive.

Paraphrasing Vladimir Lenin, there are decades when nothing happens; and quarters when decades happen. The first quarter of 2026 appears to be such a moment.

Geopolitics provided a volatile backdrop, but for much of the period market behaviour was driven less by individual events and more by the continuation of established trends from 2025. January and February saw a clear extension of three dominant trades: bifurcation within AI (with hardware outperforming software), the debasement trade, and strong demand for minerals over oil. Within this environment, the Trust's Quality Growth bias and limited exposure to capital-intensive and commodity-linked businesses proved a relative headwind.

The inflection point came in late February with the escalation of tensions between the US, Israel and Iran. The disruption to energy flows through the Strait of Hormuz triggered a sharp and disorderly repricing across asset classes, with oil prices, inflation expectations and bond yields all moving higher. European Small & MidCaps, already under pressure following several years of underperformance, sold off further as risk premia widened.

Importantly, the Iran shock also reversed several of the prevailing market dynamics. Energy and more cyclical areas of the market outperformed, while industrials and select growth segments lagged. Within technology, the earlier dominance of AI hardware faded, with more asset-light software businesses showing greater resilience. Despite this shift, the Trust's focus on high-quality, structurally growing companies remained out of favour in the quarter, contributing to the relative underperformance versus the benchmark.

Against this backdrop, we took the opportunity to further refine the portfolio, initiating positions in companies such as **Asta Energy**, where we see strong long-term structural growth supported by electrification and resilient end markets. These changes have enhanced diversification and further strengthened the Trust's alignment to company-specific drivers of return.

More broadly, the period has been characterised by a marked increase in geopolitical uncertainty — from US tariff policies to the recent escalation in the Middle East — alongside market-specific pressures such as the indiscriminate sell-off in software. While these factors have weighed on sentiment and delayed the recovery in European SmallCaps, underlying fundamentals remain robust.

This is clearly reflected within the portfolio. Recent results from holdings such as **Kitron**, **Bachem** and **Sectra** have demonstrated strong operational performance, with several companies delivering earnings ahead of expectations and, in some cases, upgrading guidance. Consensus expectations remain supportive, with earnings growth for the portfolio expected to exceed 15% in both 2026 and 2027.

Performance & Portfolio

During the quarter, the NAV total return of MESCT was -9.5% in GBP, an underperformance of 7.9% relative to the MSCI Europe SmallCap (ex UK) Index.

The **strongest contributors** during the quarter were:

- **Kitron** – the Norwegian electronics manufacturing services provider continued to deliver strong results and upgrades, supported by a strong defence order backlog and several major new contract wins.

- **Technoprobe** – the Italian developer of semiconductor testing equipment rose as rapid developments in AI drove higher demand for its probe cards.

- **NCAB Group** – the Swedish supplier of printed circuit boards saw improving results and strong momentum, with increasing conviction in a cyclical recovery.

The **weakest contributors** during the quarter were:

- **ChemoMetec** – the Danish provider of cell counting and analysis equipment for biopharma and research laboratories declined sharply after lowering guidance due to delayed customer purchasing decisions, amid continued cautious spending across the life sciences sector.

- **ATOSS Software** – the German provider of workforce management software weakened as part of the broader sell-off in SaaS names, driven by concerns that AI could disrupt traditional software models and compress long-term pricing power, despite continued strong execution, high recurring revenues and robust margins.

- **CTS Eventim** – the German operator of ticketing platforms and live entertainment services declined despite record ticket volumes and strong operational growth, as the 2026 outlook was softer than expected due to a one-off structural income change from a long-term contract expiration.

Engagement & ESG

ChemoMetec – Danish provider of cell analysis instrumentation

We engaged with ChemoMetec to facilitate collaboration with Tecan, a complementary company within the life sciences tools ecosystem that we previously held. The objective was to explore integration between ChemoMetec's cell analysis instruments and Tecan's laboratory automation platforms to improve the efficiency and scalability of laboratory workflows.

Following our introduction, the companies identified a strong strategic fit, resulting in the integration of ChemoMetec's NucleoCounter® NC-XM30 cell analyser into Tecan's Fluent® automation platform. This enables automated cell counting and viability analysis within robotic systems, enhancing precision and operational efficiency. The engagement demonstrates the role of active ownership in facilitating partnerships that strengthen portfolio company capabilities and support advances in biotechnology and pharmaceutical research. The engagement is now closed following successful delivery of the intended outcome.

VZ Holding – Swiss wealth management and financial advisory group

We engaged with VZ Holding to understand the drivers behind its MSCI ESG rating change and to improve alignment between external data and our internal ESG assessment. The company was upgraded from BB to BBB, primarily reflecting methodology changes in responsible investment indicators alongside incremental governance improvements. Through discussions with Investor Relations, we also sought to address data gaps and improve disclosure, with the company noting challenges in correcting historical inaccuracies in MSCI's assessment. VZ has since enhanced its disclosure through its 2025 Sustainability Report and intends to re-engage with MSCI under the updated methodology. The engagement provided useful insight into both the company's underlying ESG practices and the limitations of third-party data, and we will continue to monitor alignment as updated data becomes available.

Brunello Cucinelli – Italian luxury apparel company

We engaged with Brunello Cucinelli following an MSCI ESG rating downgrade from BBB to BB, primarily driven by weaker corporate behaviour scores and perceived risks around raw material sourcing. MSCI also flagged limited transparency on business ethics frameworks and a controversy linked to alleged anti-competitive practices, resulting in a notable divergence from our internal ESG assessment, which remains more favourable. The company attributes the downgrade largely to changes in MSCI's methodology and is formally challenging perceived inaccuracies. Engagement remains ongoing and we will continue to monitor developments and reassess alignment as further information becomes available.

Outlook

While the near-term backdrop remains uncertain, we believe it is important to distinguish between short-term macro volatility and the underlying strength of the asset class. European

Smaller Companies continue to benefit from structural growth drivers, strong balance sheets and leading positions in niche markets. Valuations remain attractive both in absolute terms and relative to LargeCaps, reinforcing our view that the current environment is more likely to delay rather than derail the recovery.

Recent history supports this perspective. Periods of heightened geopolitical stress have typically resulted in short-lived market dislocations, with European SmallCap often recovering strongly once uncertainty begins to recede. We believe the current environment is likely to follow a similar pattern.

From a portfolio perspective, we have avoided reacting to short-term noise and remained focused on high-quality growth businesses with pricing power, recurring revenues and low capital intensity. We have also taken the opportunity to selectively add to positions where share prices have been impacted by macro concerns rather than any deterioration in fundamentals.

Both the Board and the Manager viewed the recent sell-off as a compelling opportunity. As disclosed in the RNS dated 31 March, multiple parties purchased £456k of MTE shares, underlining their conviction in the Company's underlying value. In our view, this coordinated buying provides a clear signal of confidence in both the portfolio and the long-term outlook for European SmallCaps.

Looking ahead, we remain confident that the combination of strong underlying company fundamentals, accelerating earnings growth and attractive valuations positions the Trust well to benefit from any normalisation in market conditions. With an increasingly diversified portfolio and a clear focus on high-quality, structurally growing businesses, we believe MESCT is well placed to deliver attractive long-term returns for shareholders.

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