



STRATEGIC EQUITY CAPITAL PLC

Q3 Update 2016



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FE Crown Rating : 4 crown rating issued July 2016

Morningstar Rating™ for 3 and 5 Years: 5 star rating first issued October 2013

Money Observer: Rated Fund as at 31st March 2016

Runner Up 2016, Winner 2015, Highly Commended 2014: Money Observer Trust Awards. Category: Best UK Equity Trust

Highly Commended 2016, Winner 2015, Highly Commended 2014: Moneywise Investment Trust Awards . Category: UK Smaller Companies

Winner 2015 and 2014: What Investment Trust Awards . Category: Best UK Investment Trust

Winner 2015: Investment Adviser 100 Club Awards . Category: UK Smaller Companies

Winner 2015: Grant Thornton Quoted Company Awards . Category: Fund Manager of the Year

Winner 2014: PLC Awards . Category: Fund Manager of the Year

Winner 2014: Investment Week, Investment Company of the Year Awards . Category: UK Smaller Companies

Highly Commended 2012: Money Observer Trust Awards . Category: Best UK Smaller Companies Trust

Winner 2011: Investment Trust Magazine . Category: Best Small Companies Trust

Q3 update 2016

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Q3 UPDATE 2016

Q3 2016 Executive summary

- Net assets per share increased by 12.7%¹ over the period, with net cash averaging 12.8% over Q3
- FTSE Smaller Companies ex Investment Trusts Index increased by 12.8% in Q3 2016. We estimate that the IA UK Smaller Companies sector increased by 14.7%
- Net cash balance increased progressively from 9.5% to end the period at 17.0%
- Forecast portfolio earnings growth continues to exceed the FTSE Smaller Companies Index significantly, despite much lower financial gearing of the portfolio. Portfolio also less geared than equivalent AIM companies¹
- Portfolio rating has recovered – now trades at a similar multiple to December 2015
- Conscious profit taking from more highly rated holdings. During July, proceeds largely re-invested. Through the rest of the summer, we were cautious on new investments as markets continued to re-rate on low volumes and mixed news flow
- Clear evidence of operational progress at Goals and Tribal with their interim results. We believe that “Self-help” will continue to drive future returns

Share price & discount

- Average discount of c.7.5%¹ over the quarter, ending the period at c.8.8%

Q3 2016 Highlights

Investment highlights¹:

- Net assets per share increased by 12.7%, compared with the 12.8% rise in the FTSE Smaller Companies (ex investment trusts) index
- 17.0% net cash at the end of September reflects profit taking and lower re-investment rate due to caution on overall valuations. C.4% points of cash raised during September
- Portfolio forward earnings growth marginally decreased from 14.7% to 12.7% over the quarter. Portfolio rating has recovered
- Portfolio companies have traded resiliently since the result of the EU Referendum. A number will benefit from their exposure to US\$ earnings. Only obvious negative impact has been on IFG Group, which will see future profits fall due to the cut in base rates reducing net interest income
- Opportunistic new investment made in a specialist property company. Share price was heavily distressed during July following the referendum vote. Mini-block purchase from a forced seller at a very attractive price

Unaudited financial highlights¹:

- Net assets of 223.2p per share²
- Average discount in Q3 2016 was 7.5% compared to a discount of 4.2% in Q2 2016³

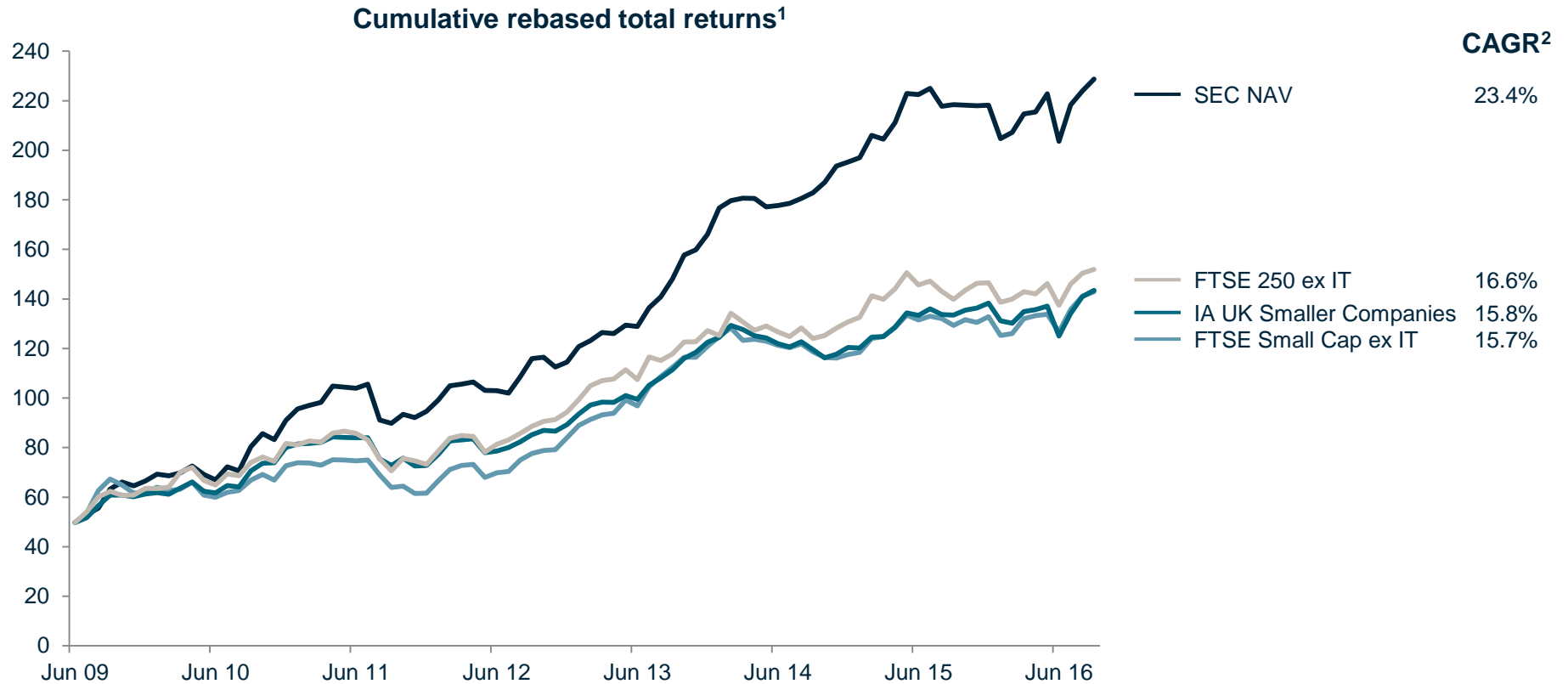
Strong portfolio performance. Net cash balance increased. Caution on deployment of capital

As at 30th September 2016

Source: 1. Bloomberg, Capita, GVMQIM. 2. NAV unaudited. 3. Bloomberg

Past performance is no guarantee of future performance and the value of investments can go down as well as up

Long term track record



Strong cumulative performance since process improvements in June 2009. No use of gearing or derivatives

As at 30th September 2016

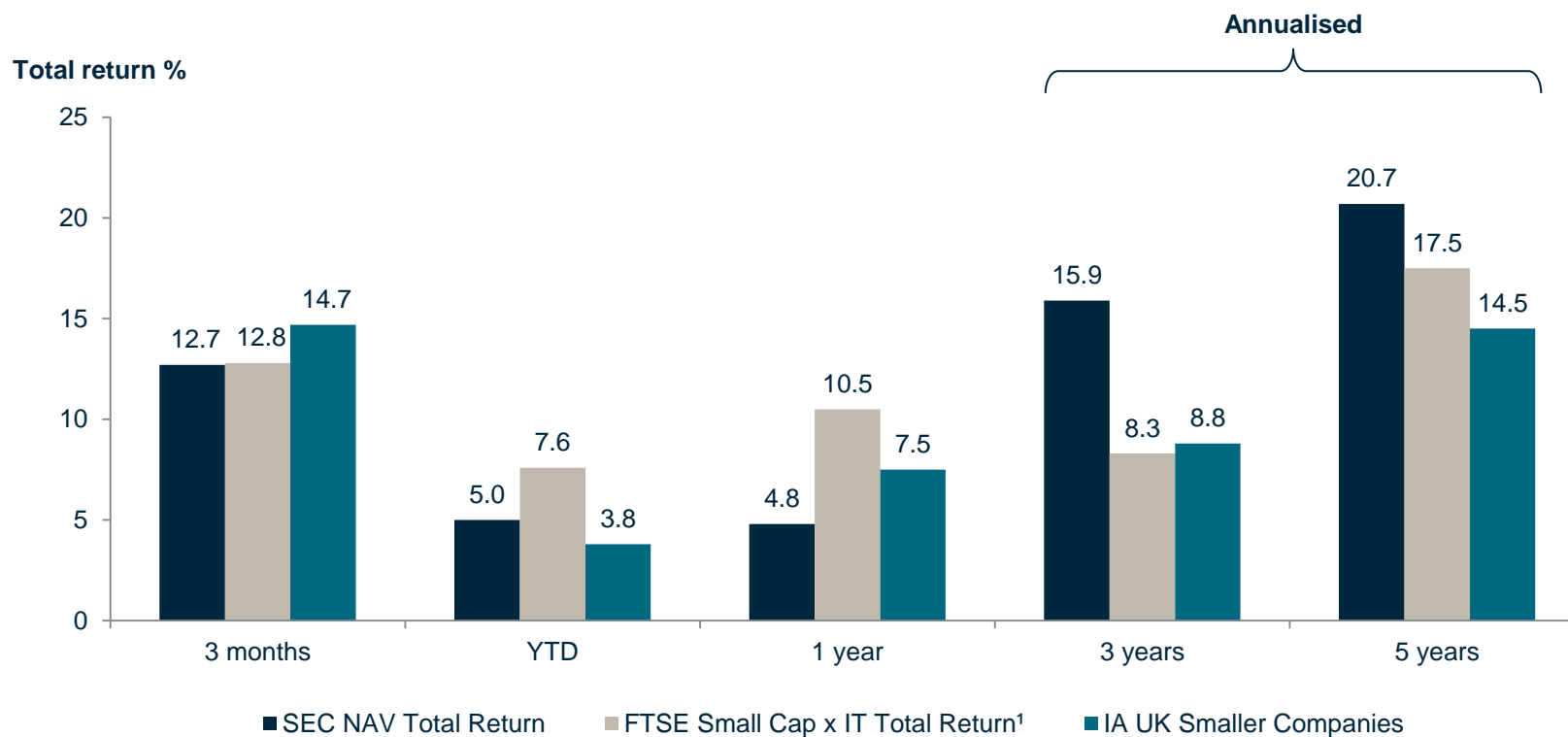
Source: IA; Bloomberg; Capita; iiii data

Note: 1. FTSE Small Cap, FTSE 250 and IA data rebased to SEC start NAV June 2009. 2. CAGR: compound annual growth rate

Past performance is no guarantee of future performance and the value of investments can go down as well as up

Medium and long term outperformance

SEC NAV performance against comparator index¹ & IA Sector²



Average Net Cash	12.8%	12.2%	11.9%	10.8%	9.2%
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Strong medium and long term annualised absolute and relative performance

As at 30th September 2016

Source: Unaudited Bloomberg; Capita; IA; GVQIM

Note: 1. Comparator index FTSE Small Cap ex Investment Trusts Total Return. 2. IA data aggregates performance of some 53 smaller company open ended funds
Past performance is no guarantee of future performance and the value of investments can go down as well as up

Q3 performance attribution

Company	Total return three months to 30 th September 2016 (%)	Contribution to return (bps)	GVQIM Comment
Top 5 contributors			
Servelec Group	28.9%	241	Recovers from oversold position. Interim results in line. Contract wins
4imprint	35.9%	209	Continued organic growth & US\$ exposure leads to re-rating
e2v technologies	20.1%	190	Recovers from oversold position. Significant US\$ earnings
Equiniti Group	29.0%	180	In line interim results. Increased investor interest and free float
Clinigen Group	18.5%	153	In line final results.
Bottom 5 contributors			
IFG	-12.7%	-35	Cut in base rates reduces interest income. CEO changes
Northbridge Industrial Services	0%	-3	Share price remains depressed given challenged end markets
Volution Group	0.7%*	1	Disposed of in July
Cash	0.1%	1	
VINTAGE	1.6%	2	Underlying NAV and currency
Total	12.7%		Average net cash position 12.8%
FTSE Small Cap Ex IT	12.8%		

Servelec recovers. 4imprint Clinigen & E2V significant US\$ earners. IFG impacted by base rates

As at 30th September 2016

Source: Attribution estimates based on FactSet Portfolio Analysis and GVQIM * to point of sale

Past performance is no guarantee of future performance and the value of investments can go down as well as up

Q3 saw realisations exceed investments

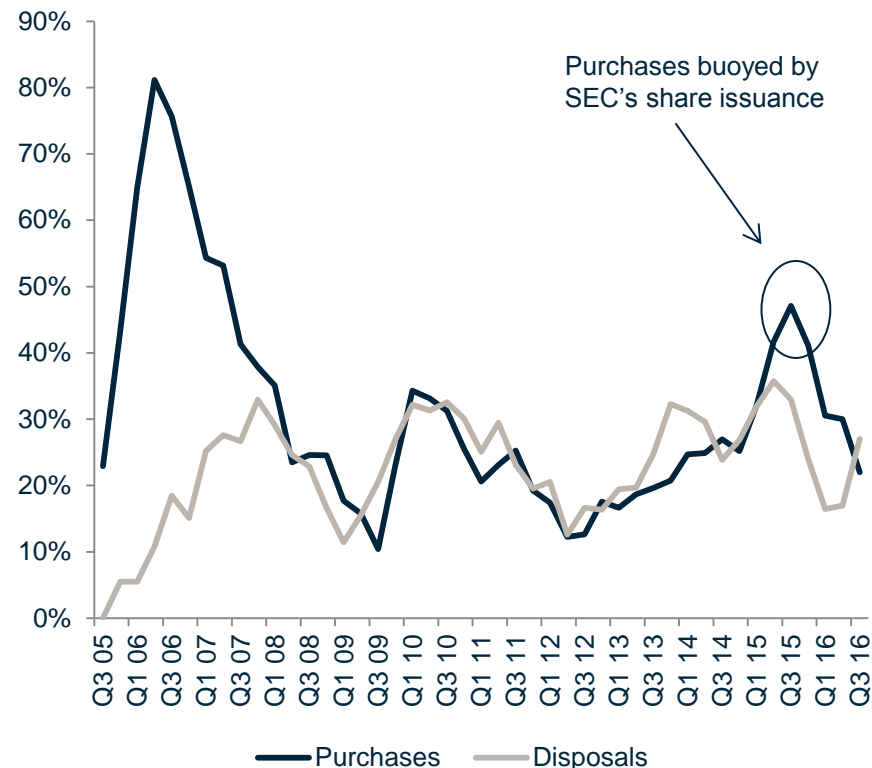
Investment highlights

- £2.8m new investment made in Harworth Group in July in a single market transaction. One of the UK's largest land owners. Distressed vendor led to attractive pricing - c.34% discount to NAV. Historically has traded at a premium to NAV. Low gearing (mid teens LTV)
- £1.2m shares in Servelec repurchased at depressed levels in July
- Opportunistic top-ups at attractive prices where volume allowed in Equiniti (£1.1m), Goals (£0.9m), Tribal (£0.5m)

Realisation highlights

- Exit of Volution raising £1.7m. Good business but concerns over FX drag on gross margins & organic growth
- Profit taking in Gooch & Housego (£3.5m), EMIS (£2.7m), E2V (£3.1m), 4imprint (£3.0m), Clinigen (£1.8m), Brooks MacDonald (£1.2m)

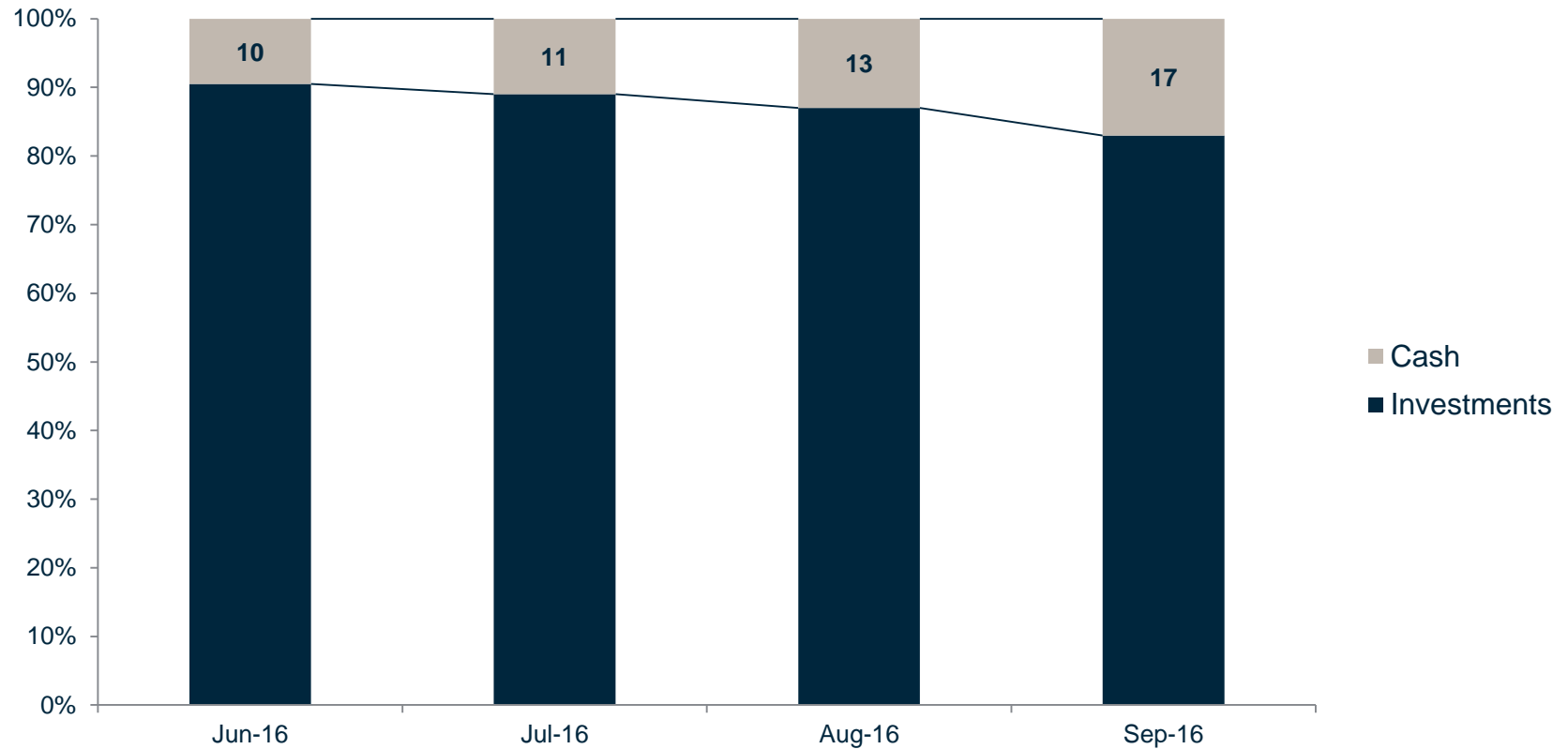
Moving annual total purchases and sales as % of NAV



Largely overseas earners & highly rated growth sold. Investments into value domestics/self-help

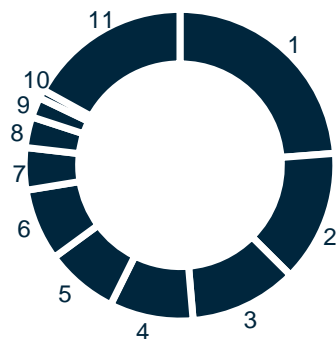
Net realisations accelerated in September

Portfolio breakdown

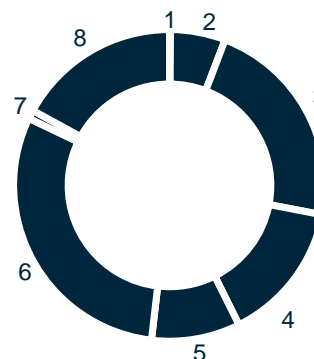


Buoyant share prices in some holdings led to profit taking in September

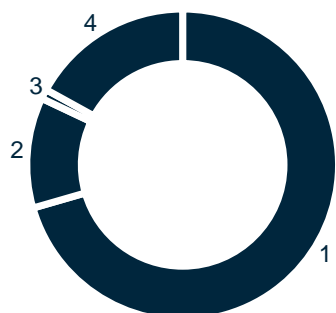
Highly concentrated and unconstrained portfolio



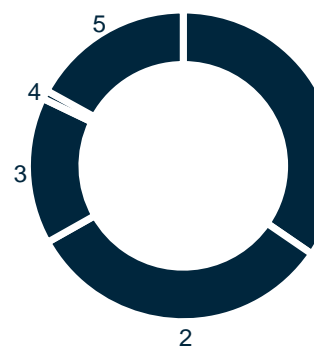
Sector exposure by value		
1	Technology – software & services	23.8%
2	Support Services	13.7%
3	Electronics	11.2%
4	Healthcare	8.7%
5	Media	7.6%
6	Financials	7.5%
7	Consumer Services	4.4%
8	Industrials	3.2%
9	Property	2.1%
10	Unlisted	0.9%
11	Net cash	17.0%



Value by market cap band		
1	<£50m	0.1%
2	£50m - £100m	5.7%
3	£100m - £200m	22.2%
4	£200m - £300m	14.6%
5	£300m - £500m	9.2%
6	> £500m	30.2%
7	Unlisted	0.9%
8	Net cash	17.0%



Concentration		
1	Top 10	70.6%
2	Rank 11 - 15	11.5%
3	Smaller holdings	1.0%
4	Net cash	17.0%



Value by index membership			No. Holdings
1	Small Cap	34.6%	5
2	Aim	32.3%	8
3	Other*	15.3%	3
4	Unlisted	0.9%	1
5	Net cash	17.0%	

Genuine small cap portfolio – no members of FTSE 250. Top 10 concentration reduced

As at 30th September 2016

Source: GVQIM. Tribal has been reclassified as Technology from Support Services, following its switch from full list (where it was in the Support Services sector) to AIM

Note: **Other*: UK listed companies which are not eligible for inclusion in indices either due to liquidity or dual listed with only standard list on the LSE, with market cap. of £150-£250m

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Portfolio valuation

	Portfolio weighted average	Portfolio weighted median	FTSE UK Small Cap ex investment trusts	FTSE UK Small Cap ex investment trusts ex resources	FTSE AIM ex resources
Number of securities	17	17	144	131	607
Market capitalisation (£m)	385	250	313	308	102
Consensus EV/EBITDA FY1	10.8x	8.3x	6.5x	7.4x	11.0x
Consensus price earnings FY1	17.2x	15.5x	12.2x*	12.2x*	16.6x
Consensus FY1 earnings growth	12.7%	8.3%	4.5%*	6.6%*	13.7%
Consensus dividend yield FY1	2.0%	2.5%	3.8%*	3.9%*	2.5%
Price/book FY1	3.1x	3.1x	1.1x	n/a	n/a
Price/sales FY1	1.8x	1.9x	0.7x	n/a	n/a
Price/cash flow	14.5x	13.2x	n/a	n/a	n/a
Debt to EBITDA	0.2x	-0.2x	1.9x	1.8x	1.2x
GVQIM cash flow yield FY1 ¹	8.9%	9.1%	n/a	n/a	n/a
Overseas sales as %	41.0%	26.0%	n/a	n/a	n/a

Portfolio average metrics closer to AIM than FTSE Small Cap. Price to cashflow metrics look attractive

As at 30th September 2016 for SEC; as at 1st October 2016 for Index data

Source: Factset portfolio analysis; Bloomberg; Peel Hunt; *Index is ex loss makers – i.e. valuation and yield is flattered. Harworth Estates excluded from analysis

Note: 1. GVQIM cashflow yield: (12m forward Cash EBITDA minus maintenance capex)/(market capitalisation plus 12m forward net debt)

Past performance is no guarantee of future performance and the value of investments can go down as well as up

Top 10 holdings¹

Company	Vintage	Sector	GVQIM Funds % of company	Return potential ²	Progress vs thesis	GVQIM CF yield ³ NTM ⁴	Net debt/ EBITDA NTM ⁴	12 month catalyst	Market leader ²
Servelec	2013	Technology	>5%	Medium	Behind	11.2%	0.0x	Work begins on Centrica platforms 2&3; clarity on prospects for healthcare market	Yes – UK niches
Clinigen	2014	Healthcare	>3%	Medium	Ahead	8.0%	0.6x	Return to organic growth in Global Access and Managed Access	Yes – niche
e2v technologies	2009	Electronics	>3%	Medium	In line	10.7%	-0.2x	Evidence of returns improving in Space imaging. Improved working capital	Yes - niche
Wilmington	2010	Media	>5%	Medium	In line	10.6%	0.9x	Overseas growth; de-gearing; M&A	Yes - niche
Equiniti	2016	Support Services	>3%	High	Ahead	9.1%	2.3x	Delivery of organic growth and cashflow	Yes in niches
Tribal	2014	Support Services	>5%	High	Behind	3.7%	-0.7x	CEO sets out and delivers improvement plan	Yes - UK
4 imprint	2006	Support Services	<3%	Medium	Ahead	6.8%	-0.3x	Continued US growth. Pension fund buyout completed	Yes - US niche
EMIS	2014	Technology	>3%	Medium	Ahead	8.9%	-0.3x	Traction in secondary care business	Yes – UK
IFG Group	2015	Financials	>5%	High	In line	10.0%	-2.3x	Sustainability of margin in James Hay. Increased interest from London investors	#2 in high end SIPPs
Goals Soccer	2012	Consumer Services	>5%	High	Behind	11.1%	1.5x	New pitch capex and soft comps drive recovery in L4L sales growth	Yes - UK

Balance sheets of top 10 holdings are very strong. Equiniti most geared but due to de-gear materially

As at 30th September 2016. Source: GVQIM analysis; Capita

Note: 1. Top 10 holdings representing c.71% of NAV. 2. In the opinion of GVQIM. 3. GVQIM cashflow yield: (12m forward Cash EBITDA minus maintenance capex)/(market capitalisation plus 12m forward net debt). 4. NTM: Next Twelve Months

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- Low levels of exposure to the UK consumer
 - Goals Soccer (recovery; we believe that good upside exists as new team beds in and replacement pitches roll out)
 - Harworth Group (Deep value regional property company. Low gearing. Low beta/self help. We believe materially under-owned by institutional investors – good scope for enhanced investor relations)
- Strong balance sheets
 - Many net-cash balance sheets and aggregate portfolio company gearing is negligible
 - Company ungeared with significant cash balance
- Targeting/increasing weights in
 - Structural/acyclical growth at a reasonable price. Ideally good earnings visibility
 - Self help
 - Both structural and acyclical growth companies
 - Seek only to retain exposure to cyclicals which offer self-help, and where the upside is not priced in
- Exiting/selling down
 - Cyclicals with self-help where their ratings prices in flawless delivery of improvement
- Avoiding
 - Cyclicals operating at peak margins on high ratings
 - Pension deficits (impediment to corporate activity and cash drain)
 - Commodity stocks (miners; oil & gas etc)

OUTLOOK

- **Positives**

- Fall in Sterling is good for UK companies with overseas earnings
- Government stimulus will keep economy on track. Scope for upside surprise in Autumn Statement
- Market volatility is likely to lead to more mispricing and opportunities
- M&A levels appear very low so far in 2016 - likely to pick up if the market does not re-rate US economy appears to be relatively healthy. US banking sector appears stable (and much better than EU)
- UK banks and UK corporates much better capitalised than in 2008

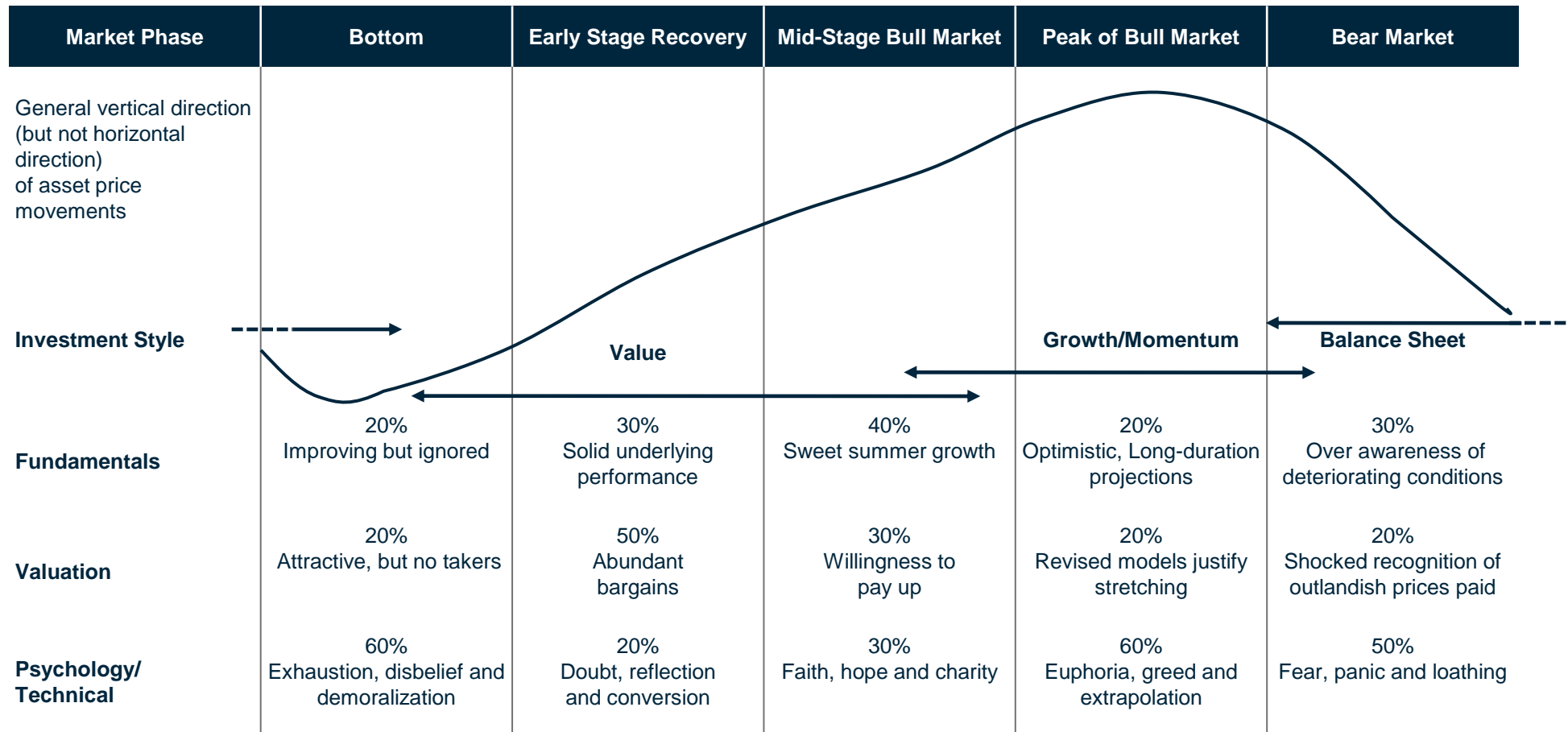
- **Negatives**

- Brexit impact, process and outcome is unclear, and will remain so for some time
- Global macro risks remain unresolved: Eurozone/EU; Chinese shadow banking & equity bubble; public sector indebtedness and persistent budget deficits
- Potential for a European Banking crisis, although we believe that Deutsche Bank is likely to be bailed out
- Geopolitical risks remain e.g. Iraq/Syria/ISIL; North Korea; Russia
- Liquidity in companies <£400m market cap remains poor (although our investment style could thrive on worsening liquidity)
- Aggressive re-rating (on low volumes) of some IHT qualifying AIM growth stocks – “crowded trades”

+ QE – a client recently summarised the situation well *“The difference to 2006/7 is this fundamental problem of where else do you put money...(other than equities)? However, that has led to ever-lower quality assets appearing and a move up the risk scale (and some extreme re-ratings of growth companies) in a search for any return at all. It’s a bizarre mix of the greater fool syndrome and an absence of alternatives”*

Trying to time when the music stops is impossible. Supports selective investment approach and being prepared for volatility

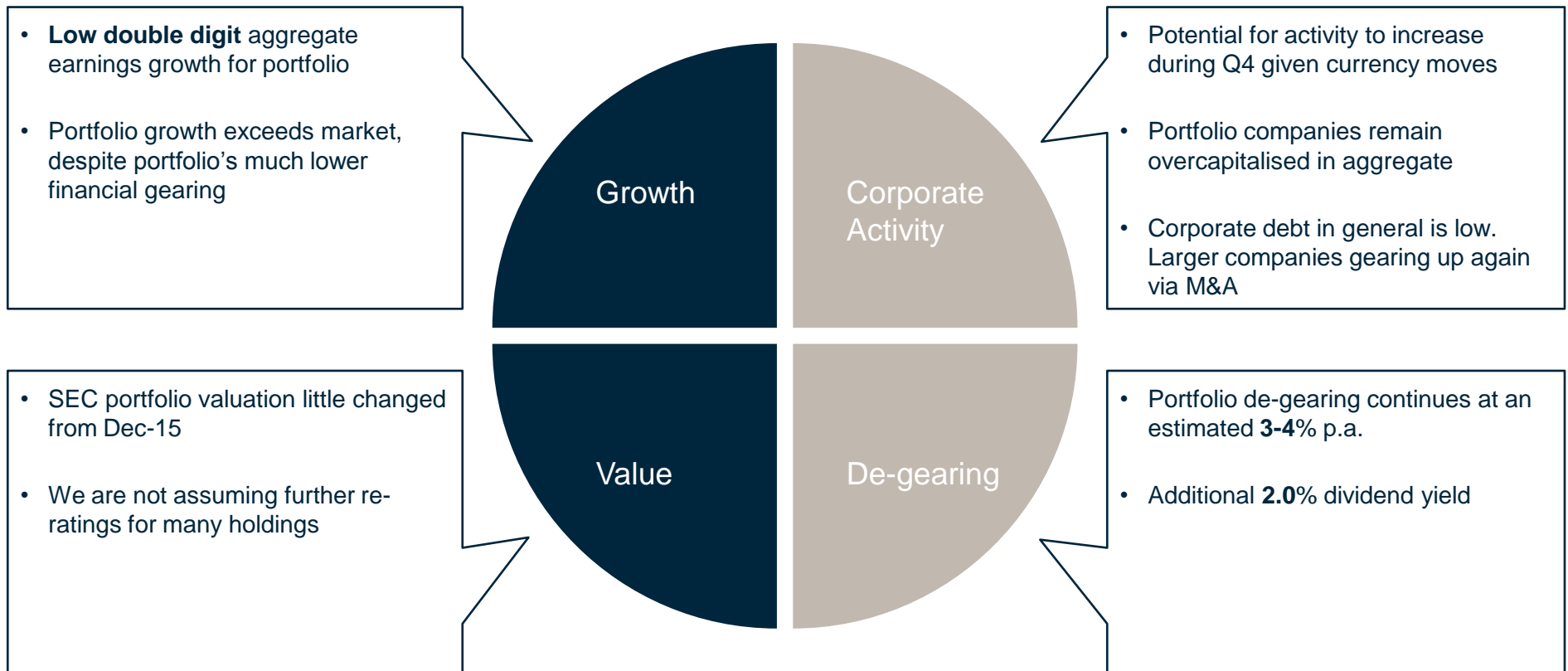
The investment cycle – where are markets now?



Does QE mean this equity cycle is longer/just different? How does slowing growth impact the cycle?

Earnings growth, cashflow and M&A to drive returns

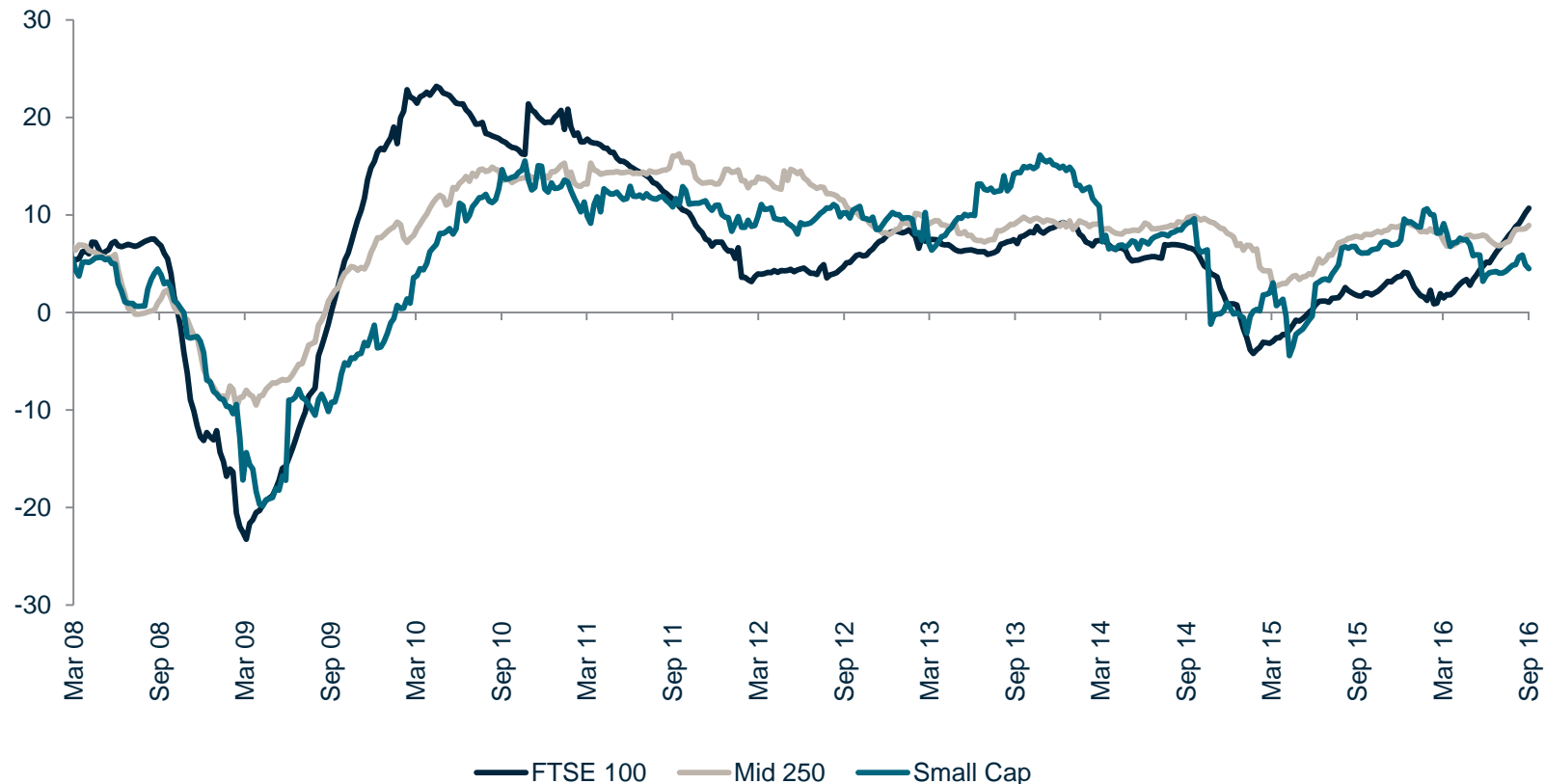
SEC portfolio



We continue to target double digit annualised returns from the portfolio over the medium term

12-month forward EPS¹ growth projections

12m forward EPS growth by FTSE index ex investment trusts March 2008 to date²



Earnings growth forecasts for smaller companies have reduced since the beginning of the year; conversely FTSE 100 companies have seen their prospects materially improve driven by sterling weakness

As at 30th September 2016

Source: 1. EPS = earnings per share 2. Peel Hunt

Note: Index excludes loss makers

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How SEC's portfolio dynamics differ to the market

Valuation and growth metrics of key indices ex oil, miners and ex loss makers and non-dividend payers*

Index	Average market cap	12m forward p/e	12m forward eps growth	12m forward dividend yield	Growth & yield	PEG ratio	PE/(growth + yield)	Net debt/ EBITDA
FTSE 100	£17.2bn	15.4x	6.3%	3.7%	10.0%	2.4x	1.5x	1.6x
FTSE 250	£1.7bn	15.0x	7.8%	3.3%	11.1%	1.9x	1.4x	1.4x
FTSE Small Cap	£308m	12.2x	6.6%	3.9%	10.5%	1.8x	1.2x	1.8x
FTSE AIM	£102m	16.6x	13.7%	2.5%	16.2%	1.2x	1.0x	1.2x
SEC portfolio	£385m	17.2x	12.7%	2.0%	14.7%	1.4x	1.2x	0.2x

Portfolio PE/(Growth & Yield) in line with the market, but enjoys stronger aggregate balance sheets

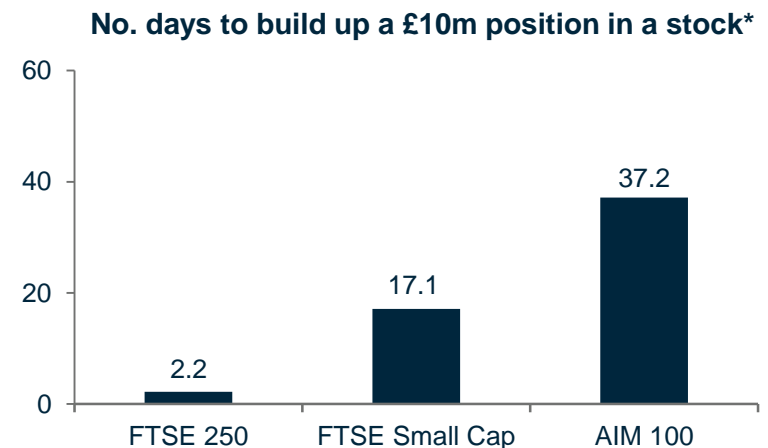
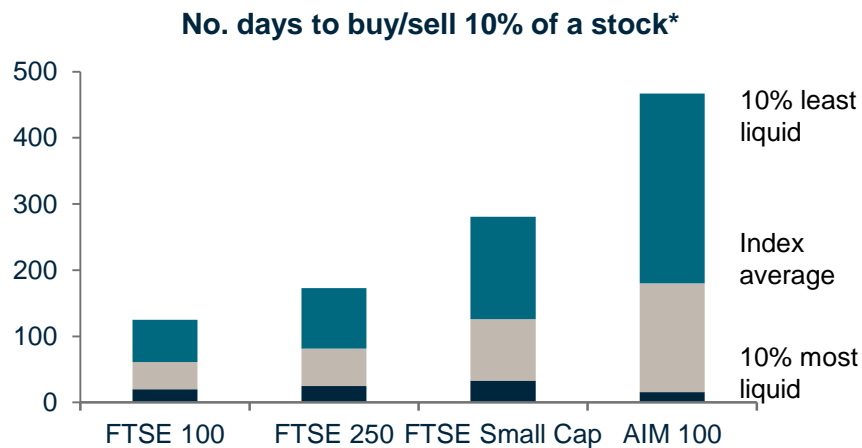
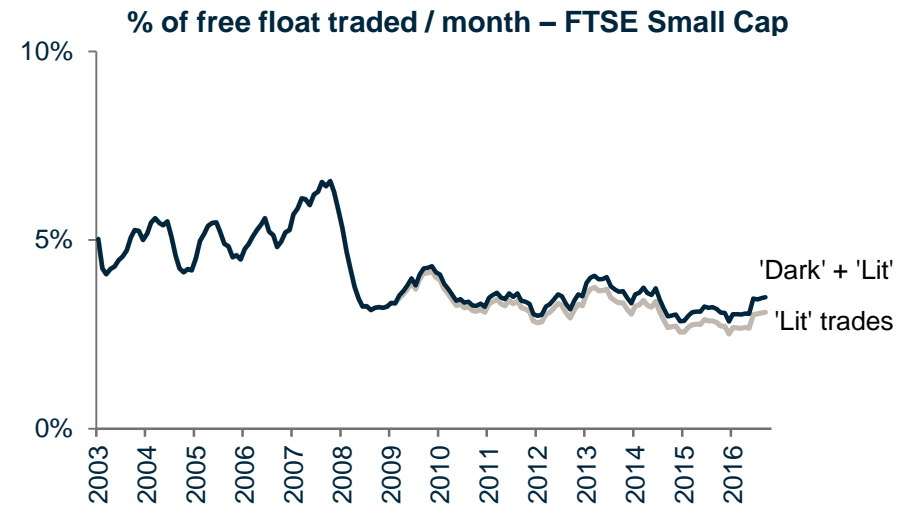
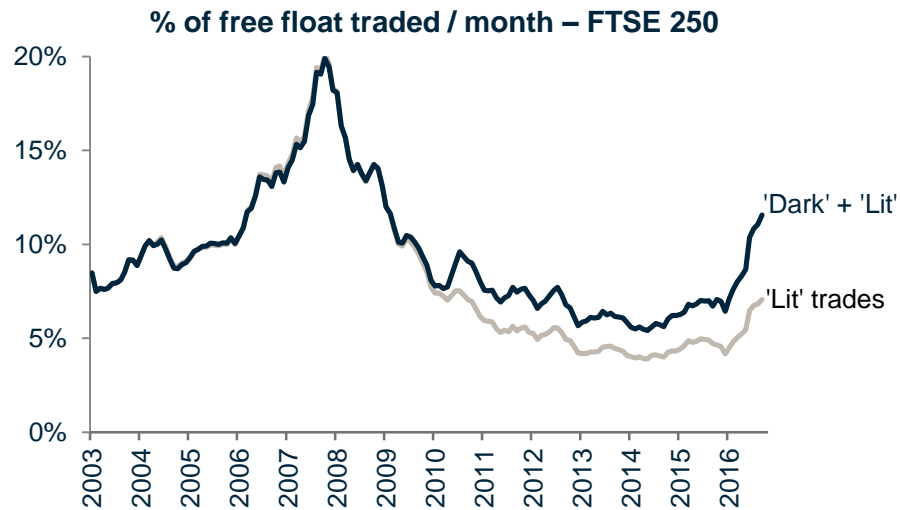
As at 30th September 2016 for SEC and 1st October 2016 for index data from Peel Hunt

Source: Peel Hunt; Capita; Factset; GVQIM

Note: *Indices presented exclude resources, as well as non-dividend payers and loss makers

Past performance is no guarantee of future performance and the value of investments can go down as well as up

FTSE250 liquidity has picked up materially



Unlike the FTSE 250, Small Cap liquidity remains materially below that of 2003-2006

As at 30th September 2016

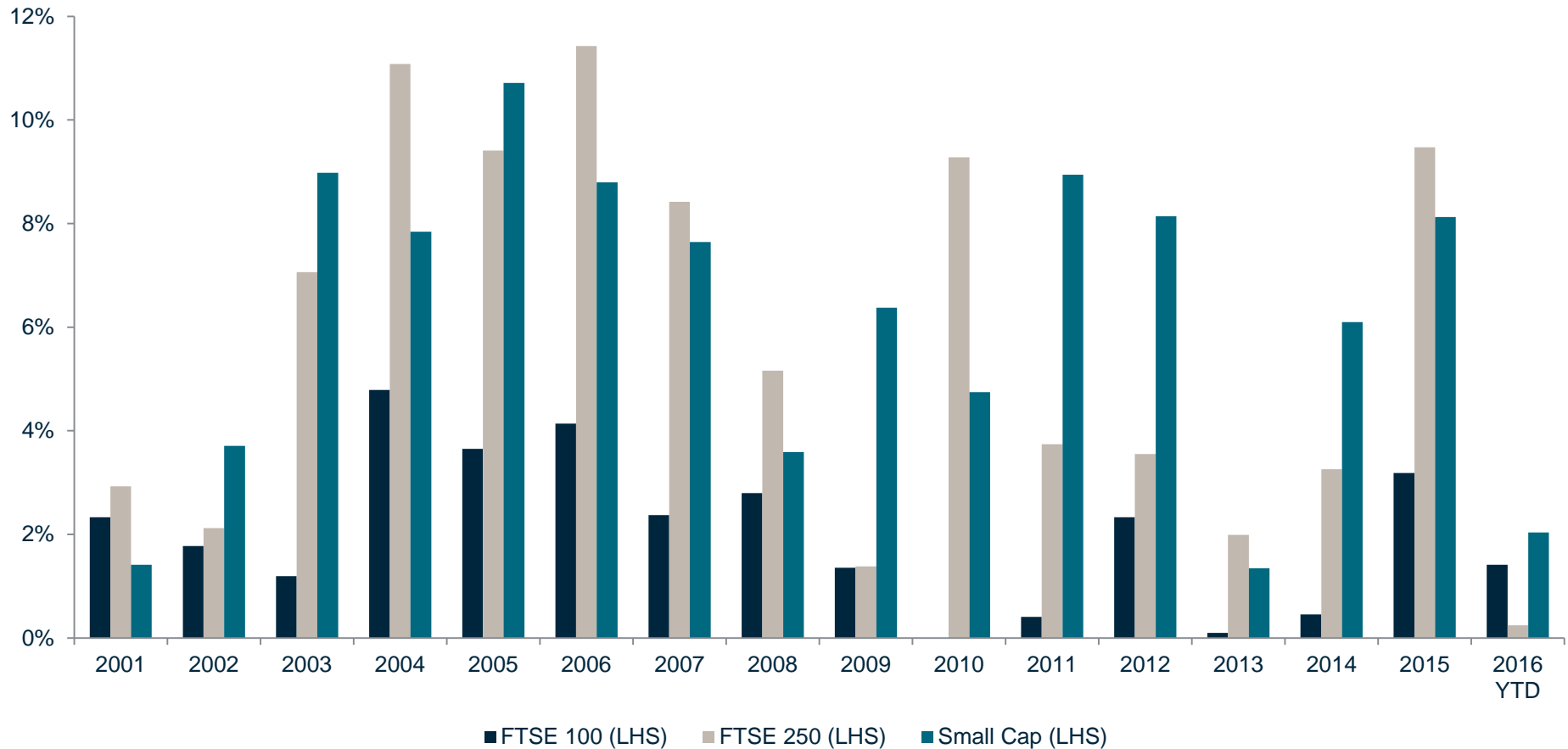
Source: Liberum, Bloomberg

Note: *Assuming 100% of daily volume

Past performance is no guarantee of future performance and the value of investments can go down as well as up

M&A levels appear subdued

Value of acquisitions as % of index starting mkt cap



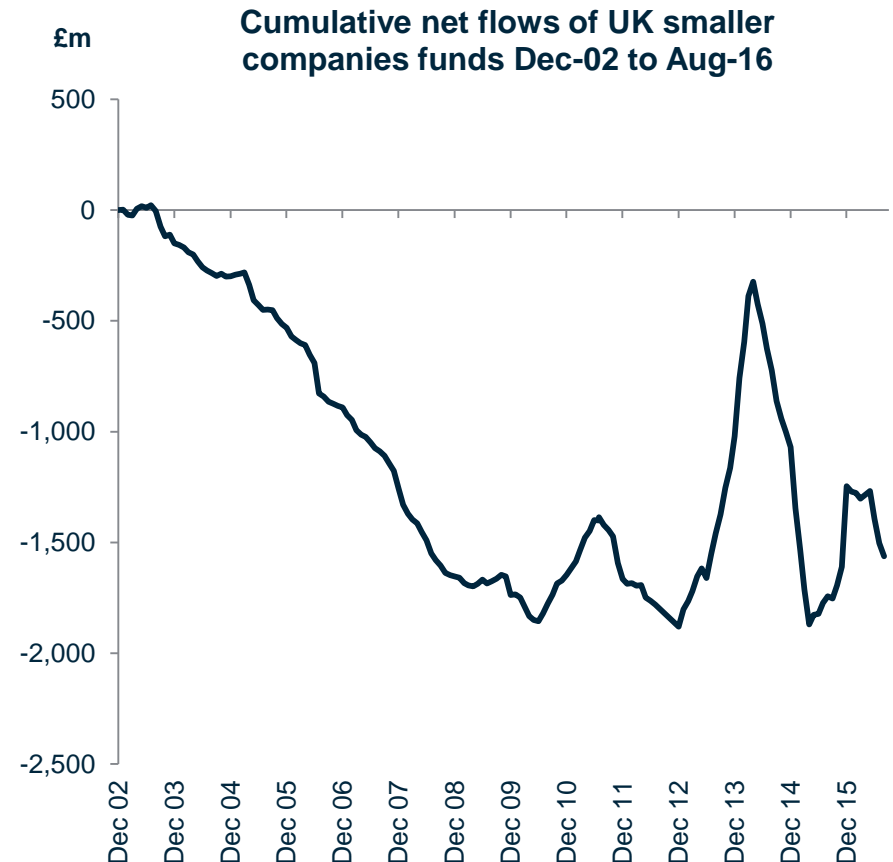
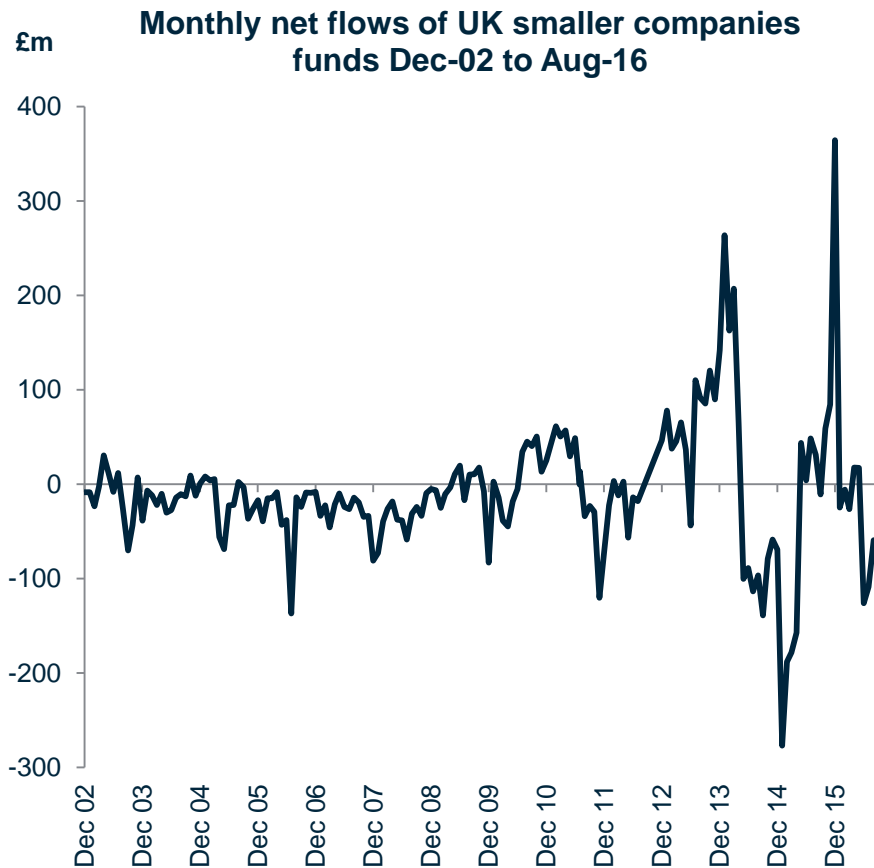
Depreciation of Sterling could attract overseas buyers

As at 30th September 2016

Source: Liberum

Past performance is no guarantee of future performance and the value of investments can go down as well as up

UK Smaller Companies OEIC flows



Outflows through the referendum period and until end August. Market re-rates despite this

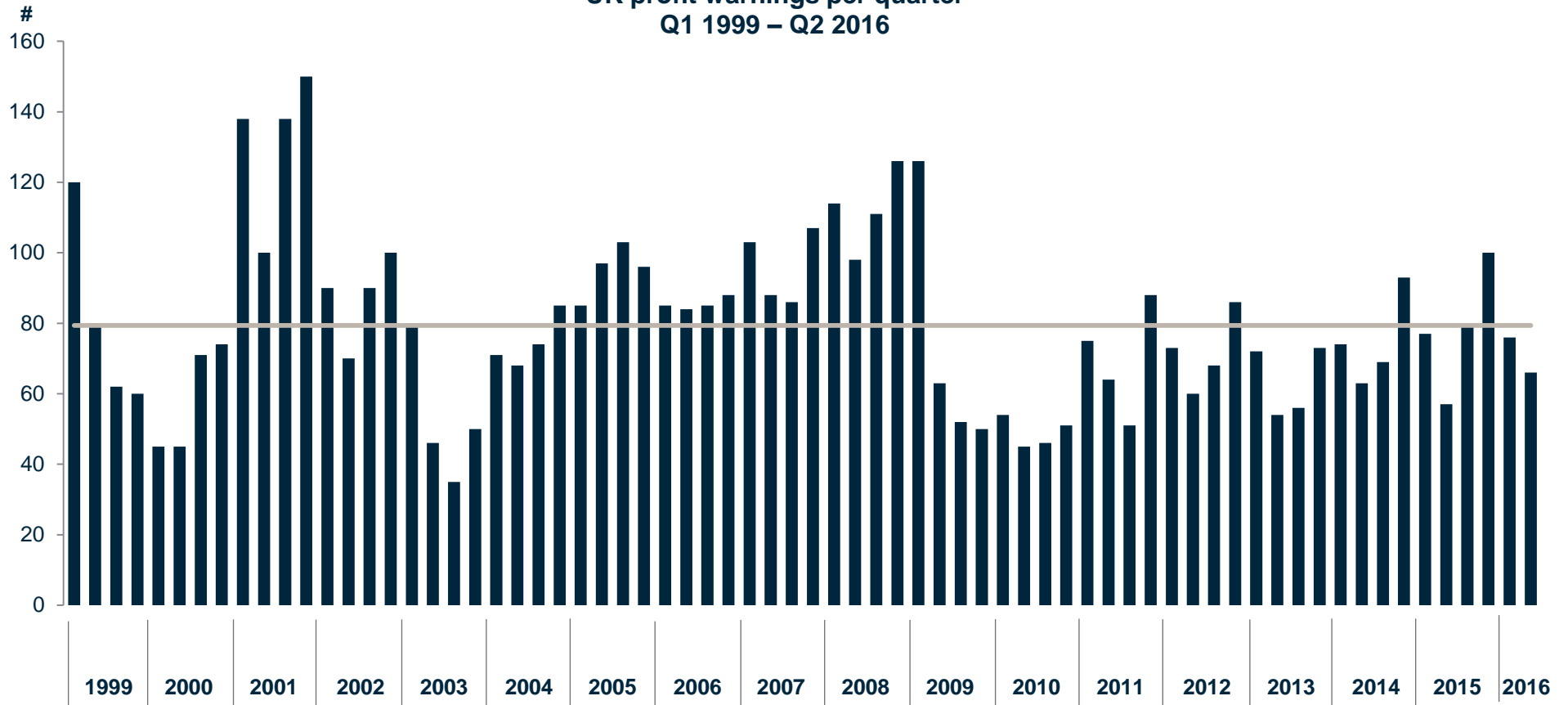
As at 31st August 2016

Source: Investment Association

Note: Total AUM in the IA UK Smaller Companies Sector in May 2016 was £12.2bn

© GVQ Investment Management Past performance is no guarantee of future performance and the value of investments can go down as well as up

UK profit warnings per quarter
Q1 1999 – Q2 2016



Profit warnings were up again YoY in Q2

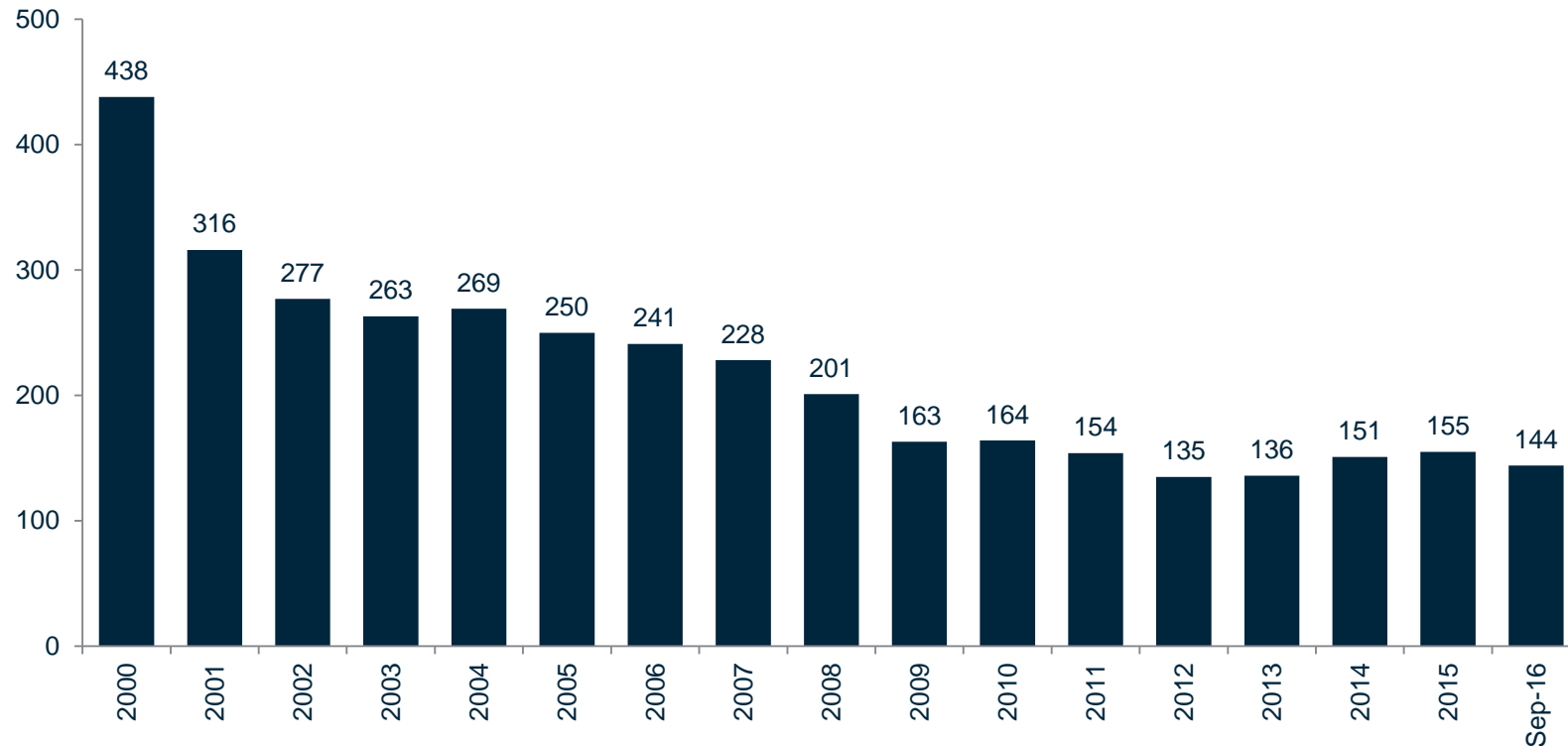
As at 30th June 2016

Source: Ernst & Young

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Growth in number of smaller companies has paused

Constituents of the FTSE Small Cap ex Investment Trusts Index



**Number of constituents of smaller companies index remains well below the middle of the last cycle
Given buoyant market ratings, why is this so low? Perhaps more companies IPO and stay on AIM**

APPENDIX

Calendar Year Annual performance¹

	2016 YTD	2015	2014	2013	2012	2011	2010	2009
Share Price Total Return	-7.5%	14.2%	32.6%	61.4%	25.6%	9.4%	35.1%	252.1%
NAV Total Return	5.0%	12.1%	18.0%	46.0%	21.3%	3.9%	37.1%	63.8%
FTSE Small Cap ex Investment Trusts Total Return	7.6%	13.0%	-2.7%	43.9%	36.3%	-15.2%	16.9%	57.7%
IA UK Smaller Companies	3.8% ²	14.7%	-1.7%	37.4%	22.5%	-9.0%	30.8%	50.1%

Share price return in 2016 impacted by the widening of the discount

As at 30th September 2016

Source: 1. GVQIM; Capita; Bloomberg; Trustnet. 2. Preliminary estimates based on Trustnet & Morningstar data
Past performance is no guarantee of future performance and the value of investments can go down as well as up

There are strict criteria for inclusion in our funds



GVQIM's research process aims to identify high quality coveted assets with attractive cash flows

How we identify coveted assets

We look for characteristics which GVQIM believes potential acquirers value highly

Qualitative	Quantitative
<ul style="list-style-type: none">• Niche market leaders• Orderly end markets, with some growth• Sustainable business model/franchise/uniqueness• Overseas earnings• Able to pass on price increases• Intellectual property• Operational know-how• High barriers to entry	<ul style="list-style-type: none">• High and/or improving ROCE• Strong cash conversion• Limited capex or working capital investment needed to finance growth• Recurring revenues/profits/cashflows• Ideally achieving, or has potential to achieve double digit operating profit margin• Realisable surplus tangible fixed assets and/or working capital

We believe coveted assets retain value even in tough times, and are more likely to be acquired

Our Black List screens out companies with fundamental business risks

Operational

- Excessive reliance on a single product, customer, supplier or distributor
- The primary driver of profitability cannot be influenced by management (e.g. resources)
- Inherently low margins
- Structurally declining markets

Financial

- Poor accounting systems or controls
- Weak cash flows – especially when reported profits look good!
- Excessive gearing

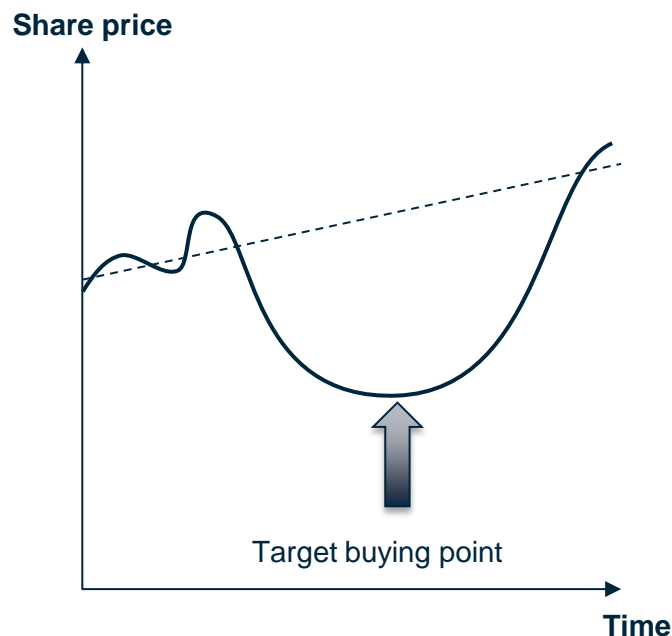
Governance

- Controlling shareholder with misaligned interests
- Below average/deteriorating governance practices
- Stakeholders unwilling to engage constructively

We have learnt what to avoid from previous experiences

Types of market purchases we consider

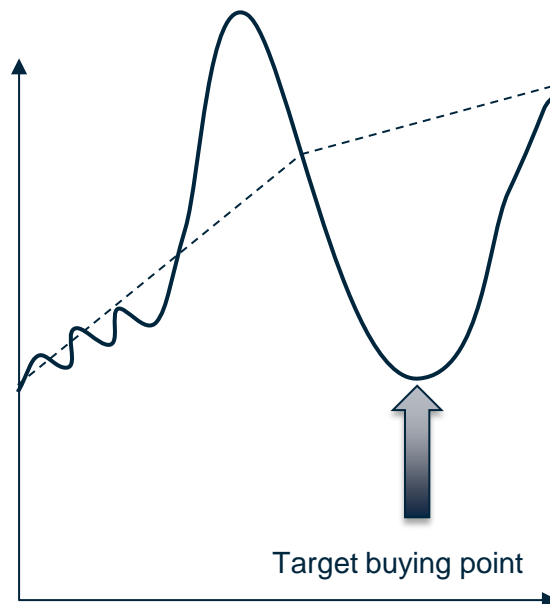
Self help



- Typically low growth businesses
- Some element of engagement required to stimulate performance improvement
- Long term investments

**Identified via deep research.
Require corporate engagement to
unlock value**

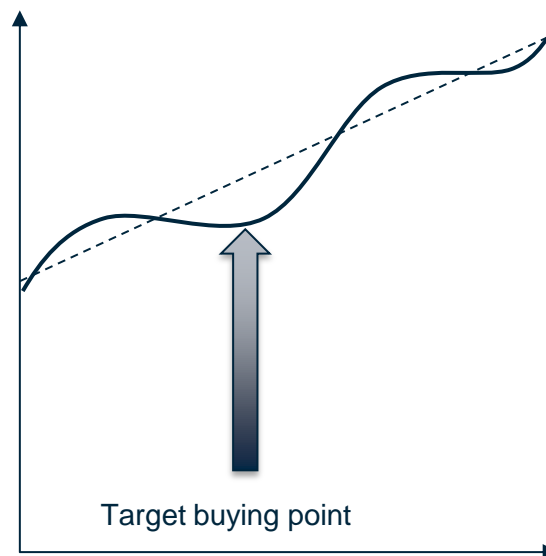
Broken growth



- Momentum stocks, which have gone wrong. Over rated transitions to under rated
- Base investment case attractive even assuming moderate growth
- Often attract corporate suitors

**Shunned by momentum investors.
Some interesting opportunities**

Quality GARP



- Quality, growing, high margin “value compounders”
- Temporary out of favour with investors -> opportunity to buy at a discount to fair value

**Became relatively over valued
in our opinion in late 2015**

Contact details

For further information regarding the SEC please contact the GVQ Investment Management marketing team below, or visit the Company's website: www.strategicequitycapital.com

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