25 January 2012

New City Energy

12 months ending	Total share price return* (%)	Total NAV return* (%)	Total return S&P/TSX Energy* (%)	Total return S&P/ASX 200 En* (%)	Total return FTSE AW Oil & Gas* (%)
24/01/10	129.2	86.7	37.8	62.5	15.9
24/01/11	83.9	55.4	24.0	21.4	18.4
24/01/12	(31.3)	(20.7)	(7.2)	(6.0)	2.2

Note: *12-month rolling discrete performance; NAV assumes full conversion of subscription shares at 70p.

Investment summary: Energy that works

New City Energy (NCE) is a fund that invests globally in energy-related equities and fixed interest securities. It focuses on small- and mid-cap companies where the manager sees the strongest longer-term growth potential. NCE is invested c 75% in oil & gas but does not invest in renewable sources; in the manager's view it invests in "energy that works". NCE pays quarterly dividends and increased its total dividend for 2011 by 3.125% to 1.65p. It has further capacity to increase the dividend. The manager considers that energy will be crucial to the next decade and, against a backdrop of a diminishing supply of oil and growing energy demand, remains very bullish on the long-term outlook for oil and the energy sector in general.

Investment strategy: Diversified global energy exposure

NCE's portfolio is invested in oil, gas, coal and uranium stocks. It is managed using a mixture of top-down and bottom-up strategies and maintains an extensively diversified portfolio of about 80 securities. The manager employs gearing, when appropriate, to enhance returns over the longer term. NCE's mandate permits it to invest up to 30% of gross assets in companies outside the energy sector.

Sector outlook: Long-term positive outlook for energy

In our view, the long-term demand-supply situation is positive for the oil price. A resilient oil price in 2011 supported the global oil majors but the junior oil and gas sector was subject to near continuous downward pressure, largely reflecting concerns about the ability to finance ongoing operations in a credit constrained environment. Juniors, without the production revenues of the majors and the need to fund development of their assets, are more vulnerable. For this reason New City Investment Managers (NCIM) gives considerable weight to cash flows and the manager is not unduly concerned. Moreover, the cash-rich oil majors continue to look for reserves and may well be attracted by the historically cheap valuations of the juniors.

Valuation: Discount above average since launch

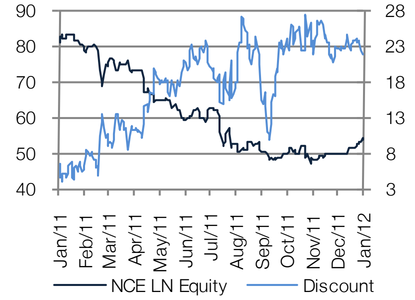
The discount based on the fully diluted NAV, currently at 21.7%, is above its one-, three- and five-year averages of 17.5%, 19.0% and 16.5%. NCE offers a good yield and we believe it may be of interest to long-term investors looking for diversified global energy resources exposure.

Price	54.0p
Market Cap	£29.0m
AUM	£40.2m
NAV	69p*
Discount to NAV	21.7%*
NAV	69p**
Discount to NAV	21.7%**
Yield	3.1%

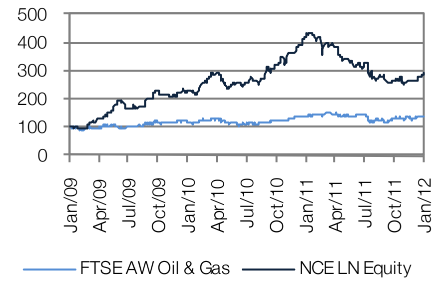
** Adjusted for debt at market value, including income and assuming no further dilution from the conversion of subscription shares. At 20 January 2011.*

*** Adjusted for debt at market value, including income and assuming full dilution from conversion of subscription shares at 70p. At 20 January 2011.*

Share price/discount graph



Three-year cumulative performance graph



Share details

Code	NCE
Listing	CISX, FULL
AIC sector	N/A
Shares in issue	53.6m

Price

52 week	High	Low
Price	83.50p	47.50p
NAV*	89.43p	57.42p

** Assuming subscription shares are converted in full at 70p.*

Subscription share details

Code	NCEA
Subscription shares in issue	24.1m

Analyst

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New City Energy Limited is a research client of Edison Investment Research Limited

Exhibit 1: Trust at a glance

Investment objective and fund background

NCE's investment objective is to deliver returns to shareholders, principally in the form of capital growth, but with some prospect of income. It invests in the securities of companies involved in the exploration, development and production of energy, as well as related service companies. These include, but are not limited to, shares, convertibles, fixed income securities and warrants. Up to 30% of assets can be invested in companies outside the energy sector.

Developments last quarter

23 December 2011: First interim dividend of 0.4p for financial year ending 30 September 2012 declared.

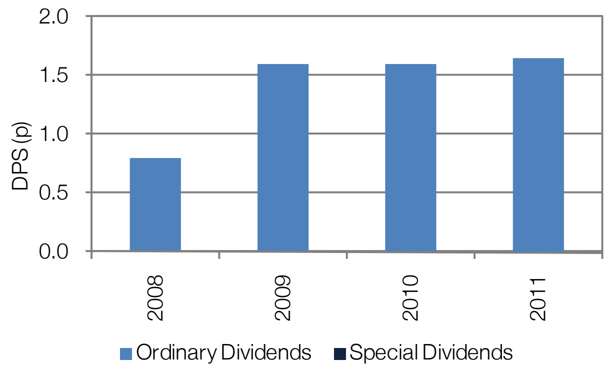
21 December 2011: Annual report for the year ended 30 September 2011 released.

13 October 2011: Will Smith and Ian Francis appointed as co-managers.

Forthcoming		Capital structure		Fund details	
AGM	March 2012	Total expense ratio	2.69%	Group	New City Investment Managers
Preliminary	December 2012	Net gearing	14.8%	Manager	Will Smith and Ian Francis
Year end	30 September	Annual mgmt fee	See pg 7	Address	New City Investment Managers, 5th Floor, 33 Chester Street, London, SW1X 7LB
Dividend paid	Quarterly	Performance fee	See pg 7		
Launch date	February 2008	Trust life	Indefinite	Phone	+44 (0)20 7201 6900
Wind-up date	See Pg. 7	Loan facilities	See Pg. 7	Website	www.ncim.co.uk

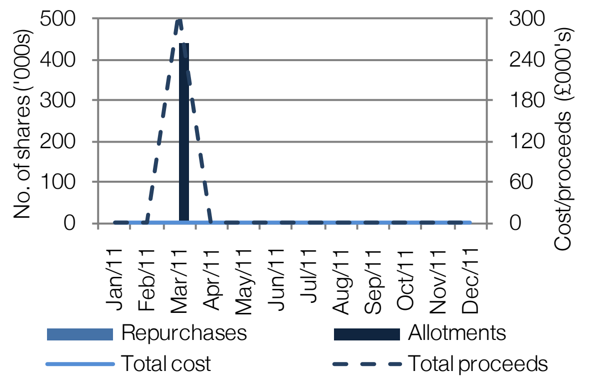
Dividend policy and history

Quarterly dividends paid in January, April, July and October. Current policy is to maintain the quarterly dividend at 0.4p, with a larger fourth interim paid in October of each year.

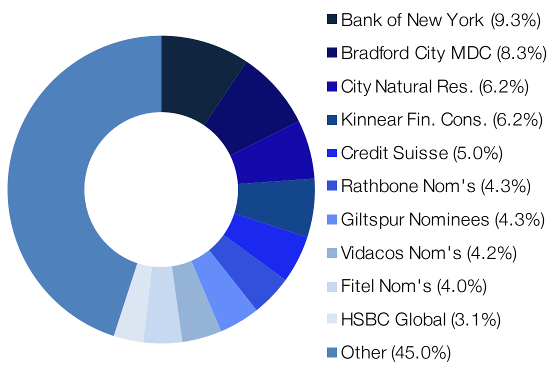


Share buyback policy and history

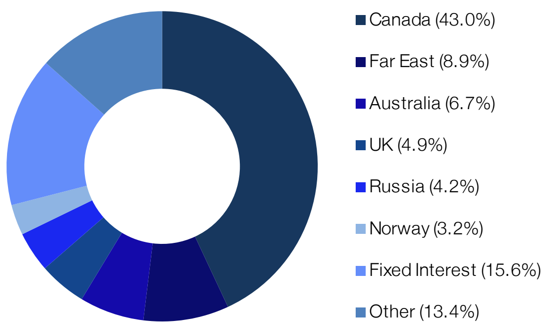
NCE's articles permit it to both allot and repurchase its ordinary shares.



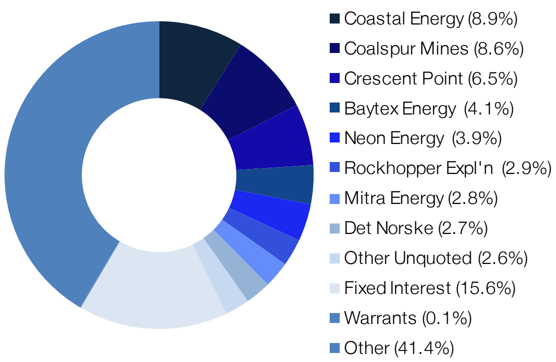
Shareholder base (as at 13 January 2012)



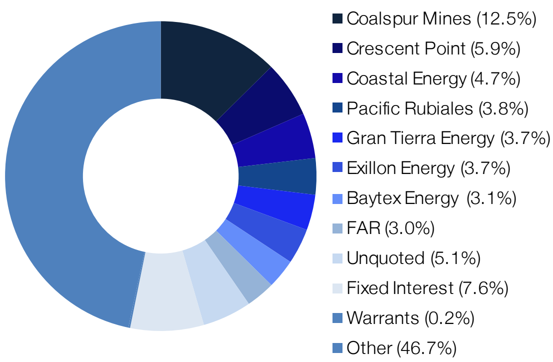
Geographic distribution of portfolio (as at 31 December 2011)



Portfolio composition (as at 31 December 2011)



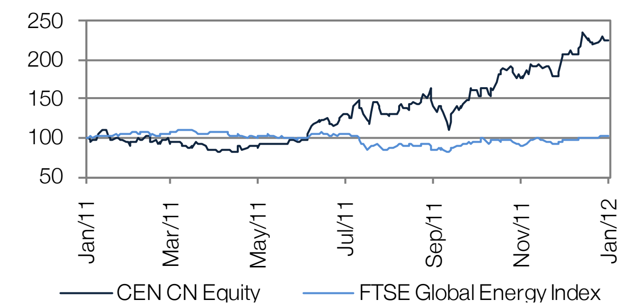
Portfolio composition (as at 30 June 2011)



Sources: New City Energy, Edison Investment Research

Exhibit 2: Top five holdings at a glance

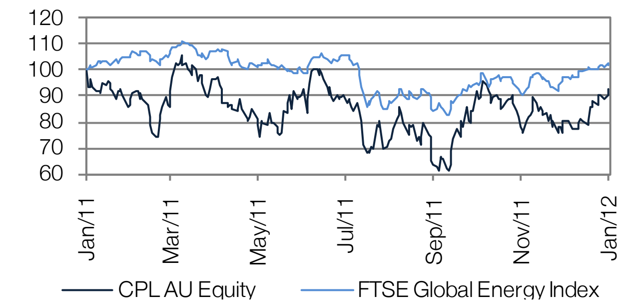
Coastal Energy	Code: CEN CN	Market Cap: C$1,159.4m



Div yield (trail. 12 months)	N/A
Industry/Sector	Oil Comp/Exploration & Production
Listing	Canada – TSX, UK – AIM
Website	www.coastalenergy.com

Coastal Energy (CEN) is an oil and gas exploration and production company, with assets in both onshore and offshore Thailand. As at 31 December 2010, CEN had proven plus probable reserves of 51.0mmboe. As at 30 June 2011, management estimated exploration had added an additional 61.7mmboe. CEN currently has 10,000boe/d average production.

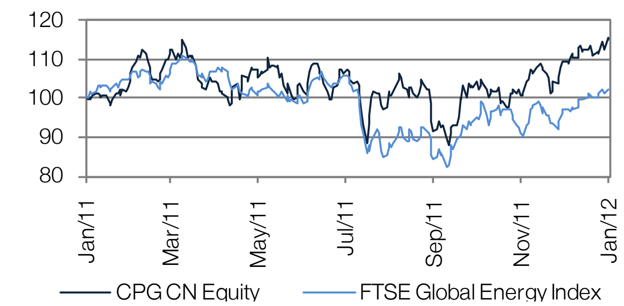
Coalspur Mines	Code: CPL AU	Market cap: A$1,046.5m



Div yield (trail. 12 months)	N/A
Industry/Sector	Coal
Listing	Australia – ASX
Website	www.coalspur.com

Listed in Australia, Coalspur Mines (CPL) is engaged in the exploration and development of its Vista Coal Project (VCP) in Alberta, Canada. The VCP leases cover c 10k hectares and contains a JORC coal resource of c 1,290m tonnes of low sulphur, high volatile, bituminous C thermal coal. CPL also has leases covering c 19.6k hectares in the Vista South Project.

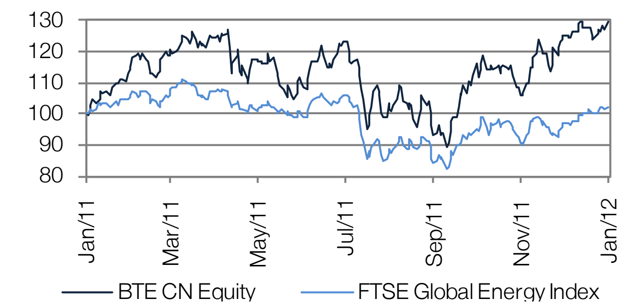
Crescent Point Energy	Code: CPG CN	Market cap: C$13,442.8m



Div yield (trail. 12 months)	5.92%
Industry/Sector	Oil Comp/Exploration & Production
Listing	Canada – TSX
Website	www.crescentpointenergy.com

Crescent Point Energy (CPG) acquires, develops and holds interests in petroleum and natural gas assets. CPG has a strong focus on Western Canada and uses its relative balance sheet strength to acquire assets with long-life, high-quality reserves. Production is weighted 90% oil and 10% natural gas. CPG has a drilling inventory with more than 6,000 locations.

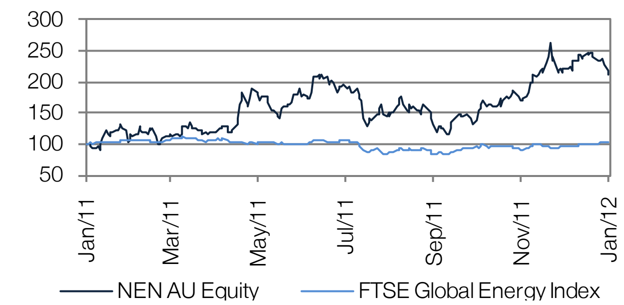
Baytex Energy	Code: BTE CN	Market cap: C$6,873.1m



Div yield (trail. 12 months)	4.53%
Industry/Sector	Oil Comp/Exploration & Production
Listing	Canada – TSX
Website	www.baytex.ab.ca

Baytex Energy (BTE) is engaged in the exploration and development of petroleum and natural gas primarily in Western Canada. As at 31 December 2010, BTE had proven reserves of 140mboe and proven and probable reserves of 229mboe. The manager considers that BTE is well managed and has provided strong growth in production and dividends.

Neon Energy	Code: NEN AU	Market Cap: A$197.5m



Div yield (trail. 12 months)	N/A
Industry/Sector	Oil & Gas Drilling
Listing	Australia – ASX, Berlin, OTC - US
Website	www.neonenergy.com

Headquartered in Australia, Neon Energy (NEN) is an emerging petroleum exploration and production company. Its principal operating asset is the 100% owned, onshore, North San Ardo oil field, in the Salinas Basin, California. It also has exploration interests in California and Vietnam. The manager considers NEN has good assets and the cash flow to fund development.

Sources: New City Energy, Bloomberg, Thomson Datastream, Edison Investment Research

Fund profile

Launched in February 2008, NCE is a Jersey-registered, closed-ended investment company, which invests in the securities of companies involved in the exploration, development and production of energy, as well as related service companies in the energy sector. The investment manager is CQS Cayman, although day-to-day management has been delegated to the investment adviser, NCIM. Merfyn Roberts, lead manager since launch, stepped down in October 2011. However, existing co-managers Will Smith and Ian Francis have moved to take full responsibility for the portfolio. NCE has no formal benchmark and is listed on both the Channel Islands Stock Exchange and the London Stock Exchange. On 5 August 2011, the investment objective was broadened to allow up to 30% of gross assets to be invested in companies operating outside of the energy sector.

The fund managers: Will Smith and Ian Francis

Manager's view

Amid a worsening global economic outlook in 2011, equity markets declined although the oil price held up well. This benefitted the oil and gas majors but not the juniors, as the space became polarised. It reflected concerns about the ability of smaller companies to finance operations in a lower-growth, credit-constrained environment. A precipitous collapse in oil prices seems unlikely; the consensus for world economic growth is lower but still positive and political supply risks remain. Valuations for smaller oil and gas stocks have become more attractive in absolute terms and relative to the oil majors. Adjusted for crude prices, the AIM Oil and Gas Index trades at near-record lows. If companies struggle to move high-quality projects forward for lack of finance they may find themselves to be potential M&A targets for the cash rich oil majors. In addition, our oil& gas team believes that even if there are temporary project delays, the value of oil and gas assets in the ground does not simply evaporate when times are difficult. Decent projects will always be revisited and our team expects this to be very much the case in 2012 as funding constraints ease. This suggests the prospects for better quality junior oil and gas companies are improved in 2012, certainly relative to the oil majors and maybe, as the manager firmly believes, in absolute terms.

Looking to the long term, the manager considers that, unlike other natural resource sectors that have experienced a bear market during the last 20 years and seen exploration cut back, investment in the oil sector has been strong. As such, reserves have been exploited to the point that capacity in the market is not expanding. New production is purely replacing that which is being lost in the Middle East. Against this backdrop energy demands are ever increasing, particularly from emerging economies. The manager considers that, over the longer term, these factors will stimulate the oil price and so the manager is a long-term oil bull. The manager expects that oil will never be exhausted as high oil prices will stimulate investment in alternatives. However, the oil price is expected to move up substantially before alternatives come on stream, particularly given the relative strength of the oil lobby. Compared to oil, natural gas is relatively abundant. However, there is currently a dislocation between oil and natural gas prices. Gas markets, and thus prices, are predominantly local in nature, although as infrastructure develops these can be expected to become increasingly global. The manager considers that nuclear power will be key to meeting future energy demand and still likes uranium as a long-term asset class, but believes that Fukushima has pushed the process back.

Asset allocation

Investment process

In common with other NCIM funds, NCE is managed using a mixture of top-down and bottom-up investment strategies. The process begins with the identification of sectors and geographical areas that the manager favours, to varying degrees. This serves as a guide to the evolution of the portfolio. However, the portfolio is not managed with specific reference to geographic or sector allocation targets or with reference to those of any underlying benchmark. Instead, the New City team focuses its efforts on the fundamental analysis of investment opportunities meeting, on average, 10 energy companies a week. Once included in the portfolio, the New City team continues to assess stocks on an ongoing basis to ascertain whether the level of holding remains appropriate. It is not currently NCE's policy to attempt to hedge currency exposure, and so NCE is exposed to currency risk.

Overview

The overall portfolio is a diversified pool of 68 equity, nine fixed income and eight warrant positions. The top eight quoted equity holdings account for 40.0% of net assets, fixed income accounts for 15.6%, unquoted equities for 5.4%, while the warrant exposure at 0.1% is negligible. The remaining 60 quoted equity investments and other net assets account for 39.0% of net assets. Exhibit 3 illustrates NCE's sector allocations as at 31 December 2011. Reflecting NCE's mandate the portfolio had a substantial allocation to global oil and gas stocks of 74.6%. Bonds, which provide NCE with income, accounted for 14.8%.

Sector allocation

Exhibit 3: Sector allocations, as at 31 December 2011

	Trust weight (%)
Oil & gas (North America and Canada)	26.5
Oil & gas (UK and Europe)	14.5
Oil & gas (Far East)	14.3
Oil & gas (Latin America)	8.2
Coal	7.5
Oil & gas (Africa)	5.7
Oil & gas (Australia and New Zealand)	5.4
Uranium	3.1
Bonds	14.8
Total	100.0

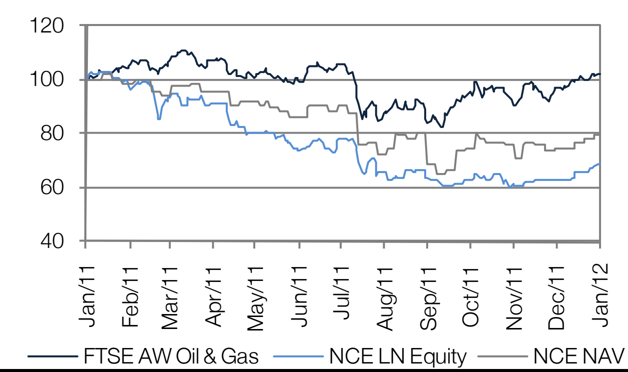
Sources: New City Energy

Recent performance

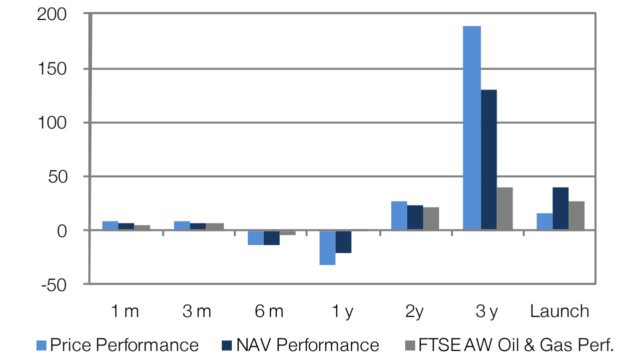
As Exhibits 5 and 6 illustrate, NCE has outperformed the FTSE All-World Oil & Gas Index in terms of of both price and NAV total return, over two and three years. NCE's performance during the last 12 months reflects that of the junior oil and gas sector, in which NCE is overwhelmingly invested. Despite oil price resilience, which acted as a boost to the majors, the juniors were subject to near-continuous downward pressure in 2011, which led to a dislocation in performance. This has largely centred on concerns over juniors' abilities to finance operations in difficult environment. While there remains considerable uncertainty over the global economy, we consider that NCE is well positioned to benefit when the market moves back into a risk on phase.

Exhibit 5: Investment trust performance

Price, NAV & benchmark total return perf., one year rebased



Price, NAV & benchmark total return performance (%)



Sources: New City Energy, Datastream, Edison Investment Research

Exhibit 6: Share price and NAV total return performance (sterling adjusted), relative to benchmarks

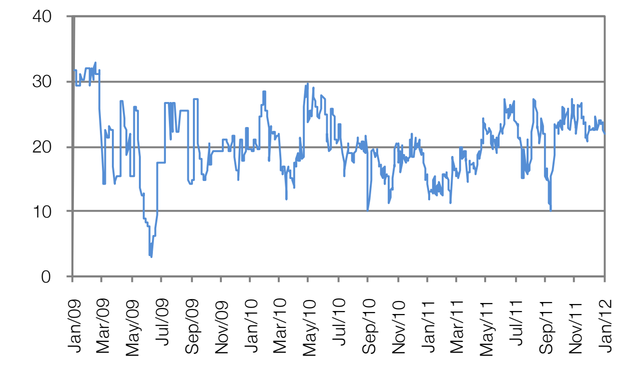
	1 month	3 months	6 months	1 year	2 years	3 years	Launch
Price relative to S&P/TSX Energy	3.9	5.1	(2.0)	(24.2)	11.2	130.8	(5.0)
NAV relative to S&P/TSX Energy	1.9	1.7	(2.2)	(13.5)	8.1	71.4	18.6
Price relative to S&P/ASX 200 Energy	(1.1)	5.7	(6.2)	(25.3)	12.2	104.1	(45.0)
NAV relative to S&P/ASX 200 Energy	(3.2)	2.3	(6.4)	(14.7)	9.1	44.6	(21.4)
Price relative to FTSE AW Oil & Gas	3.5	2.2	(8.8)	(33.6)	5.3	149.2	(11.0)
NAV relative to FTSE AW Oil & Gas	1.5	(1.1)	(9.0)	(22.9)	2.2	89.7	12.6
Price relative to S&P Global 1200 Energy	4.4	2.5	(10.0)	(35.5)	0.9	151.4	(16.4)
NAV relative to S&P Global 1200 Energy	2.3	(0.8)	(10.2)	(24.9)	(2.2)	92.0	7.2

Source: Thomson Datastream, Edison Investment Research

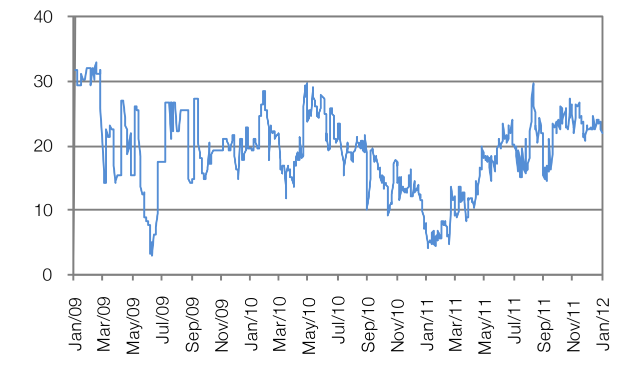
Discount

Exhibit 7: Discount since launch

Assuming all outstanding subscription shares remain unexercised.



Assuming all outstanding subscription shares are exercised.



Sources: Thomson Datastream, Edison Investment Research

NCE has the authority to both allot and repurchase shares, which provides the manager with a mechanism to influence the discount. However, an explicit commitment to maintain the discount at a particular level has not been provided. Since its launch in February 2008, NCE has not used the repurchase authority and the allotment authority has been used three times. The first allotment occurred in May 2008, to address post-launch demand for NCE's shares, and the second and third allotments occurred in March 2010 and March 2011, following conversion of NCE's subscription shares. Exhibit 7 illustrates the discount since NCE's launch. The first graph is produced using par NAVs and assumes that any outstanding subscription shares remain unexercised. The second graph assumes dilution from the full exercise of all outstanding subscription shares at 70p. Prior to September 2010 and from October 2011 the two graphs are identical as the subscription shares are out of the money. From launch to July 2008, NCE frequently traded at a premium. However, from July 2008 the trust moved out to a consistent discount. The discount reached its all-time high of 60.8% in October 2008 before settling down to a discount that has averaged 20.1%, NAV calculated in par value terms, and 18.1%, NAV calculated in fair value terms, over the last two years. With both NCE's price and NAV now back below the exercise price the subscription shares currently have no dilutary effect. However, there is the potential for dilution should these rise again. The discount based on the fully diluted NAV is currently at 21.7%. This is above its one-year, three-year and since-launch average of 17.5%, 19.0% and 16.5% respectively.

Capital structure

NCE has a conventional structure with two classes of security in issue, nil par value ordinary shares and nil par value subscription shares. The latter, which are both listed and tradable, confer the right but not the obligation to subscribe for one ordinary share at any subscription date at a price of 70p. There is one subscription date per year. This is defined as the 30th day after NCE's audited accounts are dispatched to shareholders for the financial years 2008 to 2013 inclusive. The final subscription date will be 28 February 2014. The first conversion was completed in March 2010 under which NCE allotted 3,000 ordinary shares raising proceeds of £2.1k (reflecting that the subscription shares were substantially out of the money and the ordinary shares were trading at a moderately high discount). The second conversion, in March 2011, saw NCE allot 444k ordinary shares raising proceeds of £310k. By comparison, on 17 March 2011 NCE's closing price was 69p, its NAV was 83p and so it was trading at a discount of 16.9%.

NCE's articles of association permit the use of gearing and, accordingly, NCE has a bank borrowing facility with Credit Suisse that can be used for this purpose. As at 31 December 2011, NCE had net gearing of 14.8% of net assets. The management fee, paid monthly in arrears, is 2.0% per year of the net asset value of the company valued monthly, with assets valued using bid prices. The manager is also entitled to a performance fee of 20% of any of the outperformance of NCE's net assets, in total return terms, above an 8% per year hurdle rate. This performance fee is subject to a high watermark provision. A performance fee of £1.5m was accrued for the year ended 30 September 2010. No performance fee was accrued for the year ended 30 September 2011. The total expense ratio (TER), inclusive of performance fees, was 2.69% for the year ended 30 September 2011 (5.08% for the year ended 30 September 2010). Excluding performance fees the 2011 TER is 2.69% (2010=1.85%). The investment management contract with CQS Cayman can be terminated at a year's notice by either side. The investment advisory agreement with NCIM terminates at the same time. NCE has an initial seven-year fixed-life from 8 February 2008 to 8 February 2015. However, from 2014 a continuation vote will be put to shareholders annually, at each AGM, by way of ordinary resolution. As such, NCE's life is indefinite, but with annual continuation votes from 2014.

Dividend policy and record

Dividends are paid quarterly and, for any given complete financial year, the first, second, third and fourth interim dividends are paid in January, April, July and October respectively. From launch to the year ended 30 September 2010, NCE's dividend policy was to maintain the quarterly dividend at 0.4p for all four quarters. However, for the year ended 30 September 2011 and moving forward this policy has been amended. NCE still maintains the quarterly payment at 0.4p, for the first three quarters, but makes a larger payment for the fourth quarter (2011=0.45p). As such, for the year ending 30 September 2011 NCE paid a total dividend of 1.65p (2010=1.6p). This reflects a strong accumulation of revenue reserves, relative to payment, as well as both the board's and the manager's confidence that NCE can provide further dividend growth. Year-on-year growth in the total dividend for 2011 was 3.125%. As at 30 September 2011, NCE had revenue reserves equal to 6.2p per share, or 5.75p after payment of the fourth quarterly dividend. Even without further growth in the revenue reserve, NCE had, as at 30 September 2011 and after payment of the final dividend, revenue reserves equal to 3.48x the increased total dividend for 2011. With income per share for the year ended 30 September 2011 at 3.79p, we consider NCE's guidance that dividend growth for 2012 will be at a comparable rate to 2011, and can comfortably be achieved while retaining considerable capacity to smooth dividends as necessary. The investment management fee and other expenses are charged fully against the capital account which bolsters NCE's revenue reserves and provides greater flexibility in making dividend payments.

Peer group comparison

Exhibit 8 illustrates a peer group comparison across the commodities and natural resources sector. Although there are 18 constituents (a sample is given below), the investment focuses can vary quite markedly. Within this peer group, NCE ranks 16th and fourth over one and three years when considering share price total return, and 16th and fifth over one and three years when considering NAV total return.

Exhibit 8: Commodities and natural resources peers, as at 19 January 2012

Company	Price performance			NAV performance		
	One year	Three year	Five year	One year	Three year	Five year
New City Energy	(32.0)	184.8	N/A	(25.2)	131.3	N/A
BlackRock New Energy	(20.4)	(20.1)	(38.9)	(19.2)	(12.3)	(22.4)
City Natural Resources High Yield Trust	(23.4)	263.2	115.0	(19.0)	189.3	137.7
Close Enhanced Commodities II	(19.8)	68.7	N/A	3.7	59.6	N/A
Ecofin Water & Power Opportunities	(13.0)	7.2	(22.5)	1.5	17.5	19.2
Premier Energy & Water Trust	(32.2)	(9.2)	(23.7)	(31.3)	(10.7)	(24.2)

Source: Thomson Datastrean, Bloomberg, Edison Investment Research

The board

All directors are non-executive and independent of the investment manager: David Norman (chairman), Douglas Breen, Graeme Ross and Craig Stewart (directors). Graeme Ross and Craig Stewart are principals of R&H Fund Services, which provides administrative services to the company. The average length of director service is 3.6 years.

Edison Investment Research

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