UKSA

To Shareholders in
Singer & Friedlander AIM 3 VCT Plc

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Analysis of Year End Results and Proxy Voting Advice (S & F AIM 3 VCT)

Dear Shareholder,

You will recently have received from Singer & Friedlander AIM 3 VCT Plc, the Annual Report & Accounts plus a notice of the Annual General Meeting on the 27th June. It includes a proxy voting form at the rear of the Annual Report. You previously responded to a letter from us expressing concerns about the three Singer & Friedlander AIM Venture Capital Trusts (VCTs), so this note is to give you our latest conclusions concerning this company and advice on how to exercise your proxy votes.

Comments on the Latest Results

The Net Asset Value of the company, after the proposed dividends have been paid, rose by 8% during the year. Although this is much less than the AIM index, the company is correct in pointing out that the AIM index is not a good measure for VCT companies, who are restricted from investing in many AIM companies. However the FTSE All-Share rose by 11.6% during the year so the result is still somewhat disappointing. The dividend for the year will be 0.50 pence per share.

The History of the Company

The company raised £33 million in January 2001 (£31.3 million after launch expenses, ie. 95 pence per share). The record thereafter is best examined by looking at the following table.

	Year 1 (Jan 2002)	Year 2 (Jan 2003)	Year 3 (Jan 2004)	Year 4 (Jan 2005)	Totals (£)
Net Assets (£million)	31.4	24.8	31.4	32.6	
Assets per share (pence)	95.5	75.2	95.4	103.4	
Income (£)	1,328,748	999,885	645,846	344,617	3,319,096
Fund Management Fees (£)	512,175	546,226	540,837	603,337	2,202,575
Administration Expenses	253,366	257,295	294,584	309,220	1,114,465
Tax (£)	142,777	81,454	0	0	224,231
Total Costs (£)	908,318	884,975	835,421	912,557	3,541,271
Gains/Losses on Investments (£)	286,688	-6,530,296	6,908,453	3,072,149	3,736,994
Dividends Paid (£)	560,845	263,527	82,227	157,154	1,063,753
Retained Profit/Loss	146,273	-6,678,913	6,636,651	2,347,055	2,451,066

In the first year, the company invested £9.1 million in 13 AIM companies and 10 other unquoted investments. Income mainly came from the uninvested part of the portfolio that was mainly put into fixed income loan stocks and gilts.

By the end of year two, the company had invested £18 million (ie. 56% of the original funds) in 43 companies. However the venture capital investments had declined substantially wiping £6.5 million off the net asset value. This was undoubtedly due partly to the decline in AIM valuations in general in that year, but the investments in Monotub and Recycled Water made in the first year had already been written off in full (the former went into liquidation).

In year 3, the previous year's decline in the portfolio value was reversed, but income was declining rapidly as the funds were invested in AIM and unquoted stocks. At the end of the year, the fund was 77% invested in 55 such companies. But Coinmaster Gaming, Exertis, Firmgrowth, Global Money Transfer, and Stanhope Telecom had also been written off in full during the year.

See comments above for the last year (year 4).

Why the Returns to Shareholders Have Been So Poor

The main reason why returns to shareholders have been so poor in this company is because of the high costs for fund management and administration. For example, in the last year investment gains and income totalled £3.4 million, but total costs for fund management and administration were £0.9 million, ie. 27%. <u>This is a high figure for an investment trust.</u>

Although venture capital funds often have high management charges, the expectation is that they will also have high investment returns, but the Singer & Friedlander AIM VCTs are simply not achieving such returns. Neither are most other AIM VCTs incidentally, and this particular fund seems not to be greatly different to the nearest comparable funds.

If you look at the totals in the right hand column of the previous table, you will in fact see that over the four years of the life of this company, £2.2 million has been paid in fund management fees to Singer & Friedlander, and £1.1 million has been paid in administrative and other expenses (some of which has also gone to Singer & Freidlander although roughly £35,000 per year has gone out in directors fees, and £45,000 per year to the auditors for various services).

Total costs therefore have been £3.5 million, whereas income received by the company has been only £3.3 million, most of which was on the initial fixed income investments which are now a relatively small part of the total funds. Total investment returns over the 4 years have been £3.7 million. That means an average return of £930,000 per year from investment gains which can be added to likely income of £350,000 per year from now on.

<u>If these trends continue, with investment returns, income and costs continuing at similar levels, it will mean that total returns are about £1,280,000 per year, when total costs are £912,000 per year. In other words, almost all the profits will end up in the hands of Singer & Friedlander and other parties, but not in the hands of the shareholders!</u>

Our view is that these conditions, and the associated cost structure, should not be allowed to continue. It is not in the interests of shareholders to persist in continuing to operate the company in this way. Clearly the directors are ultimately responsible for this state of affairs and the fact that the "*board faces the future with confidence*" (see the last Annual Report on page 5) raises the question of what investment returns they expect to achieve that will change this scenario?

In reality the prospects for the AIM market may not be good. For example, the Investors Chronicle in this weeks edition said on page 18 that "*there are some signs that the AIM boom may be coming to an end*" and Martin Churchill of Tax Efficient Review was quoted in last Saturday's Financial Times as saying that "*I am very nervous about AIM companies going forward*". In summary the fear is that investment returns over the next four years may be no better than they have been over the last four years.

It is also worth pointing out that the bid price of your shares at the time of writing this note is 77 pence, so if you choose to sell you will have lost a substantial amount on your original investment of £1 per share, which is only partly offset by dividends received to date.

Our Original Comments and Complaints

In our original letter to you, we raised the following issues:

a - The performance of the company, which is commented on above.

b - The level of audit fees and other fees paid to PricewaterhouseCoopers (PWC). In a letter sent by the chairman, Christopher Moorsom, to some shareholders he stated "*The Directors are reviewing the level of fees paid to the Auditors*". This is welcome news, but as there is nothing in the Annual Report on this subject we advise you to vote against reappointment of the Auditors. Note that it seems that one reason for the higher costs than normal are that an "interim review" is undertaken by PWC which most VCTs dispense with - we think this should be dropped immediately, but even so that does not seem to account for the full amount of the excessive costs in comparison with other such companies.

c - We questioned why the company needed 6 directors, which is more than most VCTs. Mr Moorsom stated in his letter to shareholders that "*In accordance with new 'best practice' one of the Singer & Friedlander Directors will be standing down from the board*" (it is certainly not seen as good corporate governance to have more than one representative of the fund manager on the boards of investment trusts as it reinforces the dominance of the company by the fund manager). However according to the Annual Report, David Lloyd has resigned from the board and Mr Bernays also appears to have left during the year, but two new directors, Mr Page and Mr Wheatley joined on the 1st August 2004 apparently so the number is unchanged. In addition Mr Banks and Mr Ellisdon, both directors of Singer & Friedlander Investment Management, are still listed as directors although we understand that Mr Ellisdon may stand down from the board at the AGM.

Company Strategy and Future Direction

In our view substantial changes need to be made to this company to put it on a sounder footing. Costs must be reduced substantially, either by renegotiating the relevant contracts, or by considering a merger with other similar companies (where the overheads could be reduced in relation to the fund size and income). Clearly two candidates in regard to the latter are the other two Singer & Friedlander AIM VCTs.

How to Vote

As indicated above, our suggestions at this time are that you vote against the approval of the Remuneration Report (motion 2), the reappointment of the auditors (motion 8) and of all the directors except Mr Banks (motions 5 to 7) unless there is some commitment shown at the AGM to change the direction of this company. Note that the Chairman is not up for re-election at this AGM so that would still leave two directors in office. You could of course return the proxy voting form to the company with those votes recorded. However, there may be further announcements at the AGM, so if you are unable to attend I suggest that you appoint me as your proxy to attend the AGM and I will vote according to what is said (or alternatively you can give me specific guidelines). If you wish to do that, please do the following:

- Remove the proxy voting form from the back of the Annual Report.
- Enter your name in the first vacant space.
- Enter my name and the address in the heading of this letter in the second vacant space and cross out "*the Chairman of the meeting or*" in the line above it.
- Leave the voting boxes blank.
- Date and sign the form.
- Return it to me to the following address: UKSA, PO Box 62, Chislehurst, BR7 5YB and I will forward it to the company's registrars after taking a copy. It would help if you can put your address and the number of shares you hold at the foot of the form for my information.

If you have already returned a proxy form to the registrars, but wish to change your vote, please telephone me on the number below and I will send another copy to you.

If you have any questions on the above, please call me on 020-8467-2686 at any time.

Even if you intend to attend the AGM on the 27th, which I would certainly encourage you to do, we advise you to return the proxy voting form as suggested above.

How to Support UKSA

If you have not already become a member of UKSA (and there are many other benefits besides being able to get involved in our campaigning activities), then please consider doing so. More information and an application form are present on our web site at www.uksa.org.uk/Membership.htm or phone 0870-70-60-600 for a form.

Note that UKSA is a mutual organisation owned by its members and we rely solely on our members to fund UKSA operations (we have no government funding and we do not accept funding from financial institutions). The more members we have the better we can represent your interests.

Yours sincerely

Roger Lawson
Communications Director