

## Looking back – looking forward

This, the last edition of FinnFunds Quarterly for 2011, provides an opportunity to look back at what has been a tumultuous year for investors. For much of the past nine months Europe has contributed significantly to investor disquiet. The debt crisis has rumbled on and with it doubts over the sustainability of the single currency zone in Europe. As we go to press, the situation has been further complicated by the failure of Slovakia to ratify the increase in the size of the European Financial Stability Facility – Europe’s bailout fund. Investors do indeed live in interesting times.

Events have been moving so swiftly that, by the time you read this, further developments may well be occupying our minds. In such circumstances, making any forecast will be almost certainly futile. Nevertheless, there are lessons to be drawn and conclusions to be reached from what has been going on in recent months. And perhaps investors can draw some comfort from the fact that globalisation has ensured governments need to act together. Avoiding a return to recessionary conditions is in everyone’s interests.

“At times of rising prices it is worth remembering that history has demonstrated that investors need assets capable of increasing the income return they make to investors.”

So far as the lessons are concerned, it is clear that the increased involvement of governments in the financial sector is unlikely to diminish for some time. The encouragement to borrow has been driven from politicians, anxious to secure re-election through delivering a steadily rising standard of living to the voting populations. Banks accepted the challenge, with the result that the level of indebtedness amongst the developed nations reached unacceptable proportions. Our policy makers will seek to ensure this does not happen again.

But looking forward, this does little to make likely outcomes any more apparent. Political interference adds to uncertainty and thus encourages volatility. This, you may reasonably think, is a reason to steer clear of equities, but there are other considerations to take into account. In particular, the need to rekindle economic growth in countries suffering under austerity measures aimed at reducing debt seems certain to see Western governments continuing to print money. Inevitably this will lead to inflation.

In the short term this could be uncomfortable. Consumers will be faced with rising prices at a time when employment prospects are less good than for some time and wage increases almost certainly non-existent or, at best, below that of inflation. But a rising cost of living does have the merit of reducing the value of debt. While inflation is a genie that it is remarkably difficult to rebottle, providing economic activity in the developing world continues to grow – as seems probable – Western governments seem prepared to stomach a rising cost of living until such time as the debt burden has been reduced to more manageable levels.

And the other merit of inflation is that it tends to favour financial assets. Property and commodities can all benefit and the shares of well managed companies profit also. Nothing is guaranteed in the world of investment, of course, but at times of rising prices it is worth remembering that history has demonstrated that investors need assets capable of increasing the income return they make to investors – like shares.

So, despite the obscurity that the current range of problems has cast over prospects for markets, investors should be encouraged to take a longer view and believe in the likelihood that somehow governments will muddle through – because they have to. The crises present in the economic and financial worlds may take a little while to resolve but, barring a total collapse of the capitalist system, we will emerge from the other side. What does seem certain, though, is that the transfer of economic power from West to East will accelerate. And Africa is likely to emerge as a beneficiary of the overturn of old world orders.

Brian Tora  
Editor

## CF JM Finn Global Opportunities Fund

Markets seem to judge Western politicians as unreliable, which is a major cause of market volatility. However, market forces will instil discipline and volatility should decline as this happens. The private sector is OK. Corporate cash balances are at historically high levels and citizens are retrenching. This cash hoarding will continue until there is some clarity, which defers spending – capital expenditure by companies and shopping by individuals. And that inhibits economic growth, leading to recurring levels of demand but no new demand.

So the problems lie at Western State level. Debts are too high to be repaid in any conventional sense and yet they probably need to go higher if the state is to be spender of last resort. Probably Western central banks will buy in state debts and 'expand their balance sheets'. This dirty little secret is really about printing money as those 'assets' may never reappear. Monetary assets (debt) get diluted through inflation and real assets rise in monetary value – and we all start again.

Meanwhile, the more populous non-Western economies expand – because they can – from the very low levels of GDP per head at which they still sit (about 10% of Western levels), enabling the aggregate global economy to expand.

But a global lack of confidence may keep capital investment down, meaning little change to the installed industrial base supplying expanding global demand. That gives pricing power to incumbent producers supplying recurring demand for all things that the global economy really needs (food, energy, utility) and really wants (global staple consumer brands).

Anthony Eaton  
Manager, CF JM Finn Global Opportunities Fund

### Performance to the last Quarter End\*

Discrete 12 month periods

30.09.10 – 30.09.11	-5.85%
30.09.09 – 30.09.10	+21.6%
30.09.08 – 30.09.09	+14.2%
28.09.07 – 30.09.08	-28.79%
29.09.06 – 28.09.07	+47.5%
30.09.05 – 29.09.06	+19.41%
30.09.04 – 30.09.05	+20.1%

## CF JM Finn UK Smaller Companies Fund

Global economic activity remains uncertain. We are currently waiting on Germany and France to agree on a course of action within the Eurozone, but they have given a deadline for its resolution. In the UK the Bank of England is initiating a further £75bn gilt buyback programme, whilst the Federal Reserve is taking other action. Despite weaker Chinese manufacturing data, exports now represent less of GDP than in 2008. With interest rates believed to have peaked and domestic demand remaining robust, 9% GDP growth is still expected.

In the ensuing stock market volatility many smaller companies are at levels of severe undervaluation against their fundamentals. One global theme within the fund is continued growth of energy demand in the developing world, despite slower economic growth. This will require new oil territories to start supply. China consumes more oil each day than had been originally forecast and developing world demand continues to rise.

An example is Madagascar Oil, with significant reserves of oil worth more than its market cap of only £55m. Another is

Providence Resources, soon to begin drilling existing discoveries and with further exploration prospects.

Meanwhile, the emerging markets, in particular China, India and Brazil, will continue to see the acceleration of urbanisation as part of the modernisation of their respective societies. This will continue to create huge demand for commodities over the long term. Superficially the developed world appears far less attractive, but there are large opportunities in maintaining the basics of life. For instance, the UK will have to spend vast sums over the next dozen years or so to create new power capacity just to stop the lights going out.

Gill Leates  
Manager CF JM Finn UK Smaller Companies Fund

### Performance to the last Quarter End\*

30.09.10 – 30.09.11	-4.32%
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## CF JM Finn Africa Fund

For Africa, as an investment destination, is nirvana delayed? Its economies rely on the health of the global economy. The same applies to its markets, so African asset values cannot really be expected to rise in isolation, unless there is stability in global markets. However the gearing is so great that the wait should be worthwhile. We anticipate that, over the next five year period, growth rates for the principal Sub-Saharan economies will exceed those of Asia.

If it is fair to say that the majority of exported output from that continent will be from commodities, then from around 1975 to the start of the new millennium Africa has seen the value of its output collapse. Since 2002 the situation has turned around completely. The implication is that the earnings stream that exports provide to Africa (most of its output) is compounding at a rate that the word

'unprecedented' barely exaggerates. This is further enhanced by the flow of inbound capital that is attracted by those rising returns.

All of this is lovely fuel to prime the African economic motor – and the gearing is immense. GDP per head in China is now approaching \$4000 annually, but Africa is way behind. The rate of change of economic growth, wealth creation and consumption will be steeper, once it starts, given the lower starting position. A 5% pay rise to a Western employee (which he is not going to get anyway!) changes little overall. A 5% pay rise to somebody on \$1000 per annum is, in aggregate, a game changer.

Anthony Eaton  
Manager, CF JM Finn Global Opportunities Fund

## CF JM Finn UK Portfolio Fund

The third quarter of 2011 has been a torrid one for investors as markets slumped over Europe and global growth as a whole slowed. The UK market came off sharply because of its sizeable resources sector, although year-to-date European markets have fared even worse, this in spite of their very strong first quarter. Given the highly politicised nature of the current situation, there is little we can do, apart from making sure we are happy with the overall portfolio construction.

The UK Portfolio Fund has always had a sizeable exposure to the resources sector, in particular oil, counterbalanced by the utilities and other defensives. Most recently we have seen Tullow Oil recover sharply on favourable drilling results, while BG Group has seen some strength on vague bid rumours, as well as the expectation that they will farm out some of their South American assets. BP is also rumoured to be close to getting permission in the Gulf of Mexico again.

It is likely that the latest £75 billion QE package will maintain the sizeable inflationary pressures on the UK economy, which in turn will be positive for several sectors, including resources and

utilities. Our overriding aim remains the focus on international earnings and away from the precarious state of the UK economy, where latest data suggests that growth is slipping and we could well be heading for a 'double-dip'. Nevertheless, compared to the gilt market, equities look cheap, although short term market performance is undoubtedly bound to our German and Greek cousins.

Mark Powell  
Manager, CF JM Finn UK Portfolio Fund

### Performance to the last Quarter End\*

Discrete 12 month periods

30.09.10 – 30.09.11	-3.75%
30.09.09 – 30.09.10	14.83%
30.09.08 – 30.09.09	0.41%
30.09.07 – 30.09.08	-17.63%
30.09.06 – 30.09.07	7.9%

\*SOURCE: Lipper to 30th September 2011 mid to mid, net income reinvested. Retail class. The value of investments and the income derived from them may go down as well as up and you may not receive back all the money which you invest. Past performance should not be seen as an indication of future performance.

## About JM Finn & Co

Investors and intermediaries interested in our four Investment Funds may like to know that, in addition to this quarterly publication, monthly fact sheets on all of them are available either electronically or in paper form. As the audience for our growing stable of funds increases, we realise that not everyone who receives this document will be a client of the firm, or even have a clear understanding of who and what JM Finn & Co is.

Our origins go back to 1945, when the eponymous stockbroking firm was founded by John Finn as a partnership. Following “Big Bang” in 1986, when many firms chose to incorporate as limited companies and allow themselves to be taken over by other financial institutions, such as banks, JM Finn & Co elected to remain both independent and as a partnership.

In the years that followed, steady expansion took place, with offices being opened around the country, first in Bristol at the end of the 1990s, but followed by Leeds and Bury St Edmunds. Offices were added in Ipswich and, most recently, Cardiff, while our London headquarters, which includes the administration centre for the firm, moved to new, more spacious offices but remained in the heart of the City of London.

In 2006, reflecting the changing nature of the financial services industry in which the firm operated, the decision was taken to incorporate as a private limited company, but outside shareholders were not sought and the firm remained in the ownership of the directors and staff who work in the business. However, recognising that the ability to continue to grow both the business and the service levels for our clients, a decision was taken earlier this year to enter into a strategic partnership with a company that we consider enjoys the same ethos as us.

Ackermans & van Haaren (AvH) is a diversified Belgian investment group which, through its private banking subsidiary Delen Investments, has taken a majority stake in JM Finn & Co, leaving the directors and staff with a substantial minority. Delen itself has operated in a similar field to us since 1936. As the only investment manager in the UK within the AvH group, and sharing similar principles to our new partner, we are convinced that this will provide us with the support that will become increasingly necessary to our business, while allowing us to operate in the manner that we know is in the best interests of our clients.

For our investment funds business this can only be positive news. Our first fund was established several years ago, but this aspect of our business, as well as our traditional role of looking after the portfolios of private investors, continues to grow in a robust manner. Presently we have funds under management or administration of around £5.7 billion, making us one of the most important investment management companies serving private investors, charities and personal pension funds in the country.

With an independent approach, we are able to adhere to our core values of providing a flexible and objective approach, tailored to the needs of individual clients. We do not provide financial planning advice – simply investment management for investment funds and for the portfolios of individual clients. This will not change under these new arrangements.

Brian Tora  
Editor

If you are an existing client of JM Finn & Co, then please get in touch with your usual contact in the firm if you require further information on our investment funds. Intermediaries without an existing contact seeking more information on any of the aspects of our business should get in touch with Layla Fear on telephone number 020 7600 1660, or email her at [layla.fear@jmfinn.com](mailto:layla.fear@jmfinn.com)

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