JMFinn&Co

PROSPECTS

The JMFinn & Co Investment Newsletter

Fifteen

Summer 2016

London's past revealed

A long history of immigration

China's global influence

Has their game changed enough?

Great Capabilities

The Father of landscape architecture

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IMPORTANT NOTICE
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COVER ILLUSTRATION

Jon Berkeley/Debut Art

Jon Berkeley is a renowned illustrator who regularly contributes to publications such as The Economist.


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WELCOME

In my thirty odd years at JM Finn & Co, I've always been proud to have worked alongside some exceptional colleagues and having to report the untimely death of one saddens me enormously. Sadly it falls to me to report to our readers that our regular contributor to Prospects and Head of Research, Geordie Kidston died at his home in London in April at the age of 52.

This publication was just one of the many ways in which Geordie made an enormous contribution to the business and he will be fondly remembered for his passionate approach to furnishing our investment managers with stock ideas and insights into the mechanics of the world's stock markets. A more detailed tribute to Geordie features on page 8.

I am also sad to announce that David Gibbon, who was head of our Cardiff office, has died following an illness. David, who featured in Prospects in the Summer 2015 edition, had been with us since 2013 following a long and distinguished investment management career of more than 30 years. Our thoughts are with his wife and three sons and colleagues from across the industry.

In the three months since our last edition of Prospects, stock markets have been particularly tricky with general economic conditions mixed. This has very much been portrayed by recent company results which have also been a mixed bag with some being better than expected and some disappointing which continues to make our jobs as Investment Managers more and more difficult.

With prolonged uncertainty, these conditions are set to continue but hopefully, once the European Referendum vote and the American election is out of the way, conditions will become a little clearer and the general economic environment should improve. In the meantime, with current conditions I think it is highly unlikely that interest rates will move.

On a positive note, JM Finn & Co has been the subject of some plaudits of late, having been awarded the "Best Discretionary Service" at the 2016 City of London Wealth Management Awards and having two Investment Directors named in a list of leading industry lights, under the age of 40, as reported on page 20.

These accolades are testament to the hard work we put in and I hope give our clients some comfort that by entrusting their assets to us, whether on a managed or advisory basis, they are in good hands.
In addition, this helps in our quest to grow our business as, when seeking referrals, which is how we have traditionally grown, a third party endorsement can be very beneficial.

I hope the various subjects up for discussion in this issue of Prospects continue to interest our readers. Subjects ranging from the benefits our capital city have received from immigration, to the current situation in China, to a brief look into the life of one of the UK's most influential landscape gardeners on the 300th anniversary of his birth underscore the varied content that we try to achieve.

James Edgedale
Chairman

James Edgedale

THE FUTURE REVEALS THE PAST

John Royden, Head of Fixed Income Research

The other day, as my handkerchief was pulled from my pocket, it brought with it a £2 coin. My coin bounced twice on the cobbles of Bow Lane before plopping down a grid into the drains below. I reconciled my loss with the kind thought that it would give some archaeologist in centuries to come a reason to smile when he found it.

Editorial

I wonder how many of the artefacts that London has yielded were originally lost with a similar wish of benevolence to some future archaeologist. I should guess not many; from the tens of thousands of antiquities that Crossrail's burrowings and the excavators of the new and deep foundations of London's smartest skyscrapers have given us, Bloomberg's new offices on Walbrook and Liverpool Street Station have been the star performers. I gather that the workings at Farringdon Station are a close third.

> Immigration has been London's bedfellow for longer than you might imagine.

Each item is history now shared with the present. Coins, bracelets, plates, lamps and, apparently, a multitude of shoes and boots from the pasts of the Romans, Saxons, Normans and all who followed are now enjoying more salubrious resting places, when compared to the muddy surround from whence they came.

And then there are the bones; Liverpool Street Station's own architectural re-birth and the tunnels of Crossrail have carved slices through the Bedlam Cemetery from the fourteenth century and onwards. The remains of these Londoners, and indeed each piece of jewellery or pottery, is an indulgent invitation to ponder their lives; and to walk your mind's eye around the architecture of our Roman forebears, or perhaps the alleys of Shakespearian London. If you need inspiration and can spare the time, then the Museum of London, not far from our front door, can help. Did they love their families and friends as I love mine? Or, more practically, were they as worried about the national debt and the debasement of our currency as I am today?

The astonishment is that DNA analysis of these 500-year-old bones tells us that half of the skeletons were not London born and bred. Immigration has been London's bedfellow for longer than you might imagine.

We know both the Romans and the Normans brought waves of immigrants with them. London prospered under the edicts of Rome and the Norman arches that support the lofty vaulted ceilings of many of London's cathedrals and churches bear testament to the endowment of William I and those who followed him. But more waves followed; the Flemish crossed the Channel in the fourteenth century, bringing with them industrial craftsmanship that benefited all.

> London's greatness through history has had much to do with its ability to blend the best of ethnic migration from abroad and to harness their skills and expertise for the greater good.

Without wishing to infringe on the bigotry that is so often labelled as contemporary political correctness, I do observe that some 400 years after their expulsion in 1290, Jewish merchants came back to London from Europe in ever increasing numbers; bringing with them their predisposition to expertise in banking, trade and finance. Think Rothschild Bank and Samuel Montagu. David Solomons founded the (now National) Westminster Bank and the Torah and Talmud laid down strict rules for commercial honesty and public-mindedness. Perhaps the eighteenth century Jewish banks, with a prescribed religious template for honourable conduct were more trusted than others?

The massacre of French Protestants on St Bartholomew's Day in Paris in 1572, and more hard-line Catholicism that followed, gave London its fleeing crowds of Huguenots; Cazenove (now JP Morgan Cazenove) was from one of their number.

Each conflict of Europe's muddled warring over the centuries that followed drove more and more to the UK. Asians and Africans soon joined the mix as we progressed through industrialisation.

By and large these immigrants brought new, and different, skills and expertise. But more importantly, the ethnic diversity allowed a culture of foreign ownership to flourish. And that, in my mind, has been behind much of London's success. JP Morgan Chase, Goldman Sachs, Bank of America, Morgan Stanley, Citigroup, Deutsche Bank, UBS, Wells Fargo, BNP Paribas, Nomura, Lazards; all from abroad and all at home and flourishing in our international mix. Where are the English houses of finance? Even Lloyds Bank is Scottish. Is Barclays alone with an all English heritage?

So where is all this taking me? The empirical evidence suggests to me that London's greatness through history has had much to do with its ability to blend the best of ethnic migration from abroad and to harness their skills and expertise for the greater good. After all, it takes a certain amount of gumption and entrepreneurialism to up your sticks and flee from where you lived. Perhaps the immigrants, by the very nature of their choice to venture forth from the known predictability of their earlier lives, are the traders, financiers and manufacturers that we want and need. Newness, freshness and value-creating competition for the local incumbents, as well as an international crowd at ease with international ownership.

I write this note with a copy date that precedes the Brexit vote, which in turn precedes the publication date. Part of the Brexit debate revolves around control of our borders. Immigration, as measured by the foreign-born has risen from 0.6% in 1850, to 1.5% by 1900, to 4.3% at 1950 and then to 13% today. So we are ahead of ourselves from an historical perspective; but even with that in mind, I tread carefully when slamming the door shut on a past enriched, sometimes by the already distinguished wealthy, but also sometimes by the once downtrodden who came knocking at our door.

GEORDIE KIDSTON


Geordie Kidston's sudden and unexpected death has shocked us all here at JM Finn, particularly me having known him personally for many years. A hugely analytical mind, Geordie had been Head of Research for twelve years providing a highly original take on stocks and markets. Ever present across the firm, he would deliver his latest opinions each morning and write intricate and relevant insights for this publication, of which he was hugely influential in its content and style.

Geordie grew up in rural Wales on the Upper Wye where wild trout streams and once impressive salmon runs allowed his lifelong love for all things piscatorial to flourish. He was educated at Eton College and then Exeter University.

He decided to become an analyst whilst at Mercury Asset Management and then moved on to help start up Ruffer Investment Management about 22 years ago. From there Geordie moved to Neville Merriam where he was instrumental in turning the company around and following them being taken over he moved to join us at JM Finn & Co, thus cementing a long-standing connection that goes back to the 1970s when his family first became clients of the firm.

Over the last twelve years Geordie has been the leading light in our Research Department and extremely important in the development of the firm. He made many incisive calls on individual sectors, markets and companies over the years and all the Investment Managers and many clients are indebted to Geordie for his insights. For him, investment analysis was a 24/7 job which consumed much of his life. We will all remember his daily meetings when he'd tell us what he'd discovered at 2am that morning.

It takes persistent bravery and originality to make as many unique calls as Geordie did. His dogged passion for markets meant his meetings were unmissable, even if what he had to say was not always popular. He supplemented his own reading with an extensive network of market professionals and company executives who clearly enjoyed the often abstract questions that he fired their way. In one memorable meeting, Geordie informed an incredulous CEO of a FTSE stalwart that his industry was about to be revolutionised by Bitcoin; looking how far Bitcoin has come since then, this prescience was typical.

Geordie was also a great observer of UK politics and used to talk about situations and people without actually expressing distinct political views of his own, unlike his comments about markets and stocks. Over the years, he has introduced the firm to some very senior politicians and political figures giving us leading insights into the ways of Westminster.

He was a great friend to a number of people and his attentive kindness and generosity often went way beyond the call of duty. His altruism only truly came to light of late, when charities close to his heart, to whom he had been incredibly generous over the years, wrote to me expressing their condolences.

I know many of his friends and former colleagues, and we are all saddened and shocked at what has happened. He will leave a big hole in both our professional and domestic lives. I am in no doubt that evenings at Geordie's clubs, Whites and Pratts, will never be the same without him and I'm sure his fellow anglers at the Piscatorial Society will mourn his passing.

There are few blessed at birth to be tremendous stock pickers but Geordie was one of them. His cerebral capacity for both gathering and assimilating the flows of trade, commerce, finance and politics were matched by few.

His sister, Cath, revealed recently that Geordie always imagined clients of JM Finn & Co as people like their mother – being dependant on being looked after. He often told her how he took that responsibility incredibly seriously. This highlights how Geordie was the very essence of JM Finn & Co and reminds us what a big hole has been left here, and not just in the research team.

James Edgedale, Chairman

CORPORATE INDEX LINKED BONDS

Most of us are fairly familiar with our government's index linked bonds or gilts. Both the capital and the coupon grow in line with inflation. And they fall in value with deflation.

John Royden, Head of Fixed Income Research

Capital gains on many bonds are tax free to UK individuals and this applies to the government's index linked gilts; which is particularly interesting for UK tax payers.

But a number of corporates have issued index linked gilts as well. From a tax perspective the main difference is that corporate index linked gilts have their capital-gains-attributable-to-indexation taxed as income.

I suppose the rationale for this is that to the extent that a company has to pay a greater redemption amount on its index linked bonds, that amount is a tax deductible interest expense in the company's accounts. If HMRC allowed individuals to escape tax on the gain then it would create a tax loop hole for extracting tax free profits out of a company.

An area of uncertainty is what happens if you suffer a capital loss. Presumably it is a deduction against your income tax liability.

In terms of what is out there, National Grid and Severn Trent have issued the National Grid plc 1.25% 06-OCT-2021 ("NG") and the Severn Trent Plc 1.3% 11-JUL-2022 ("SVT").

Tesco Personal Finance Plc trades under the name of Tesco Bank and as such is frequently called the Tesco Bank. It has issued the Tesco Personal Finance Plc 1.0% 16-DEC-2019 ("Tesco"). My mind struggles to find such a correlation between inflation and revenue as exists with National Grid and Severn Trent.

Working out the yield that you get on these corporate index linked bonds is tricky. First of all you have to reverse out the inflation implied by the prices of the various index linked gilts. Then you can use this inflation to predict what the cash flows are going to be from the corporate index linked bonds. Then you can work out what the gross redemption yields on a taxed and un-taxed basis.

All three bonds have attractive additional yields for non-tax payers when compared to index linked gilts. But that advantage diminishes significantly once you move up to the higher rates of personal tax. That is because individuals pay income tax on the capital gain to the extent that it is driven by indexation.

One of the resticting factors for individuals investing directly into corporate bonds is the minimum trade size. For many, so called "Institutional" bonds this is frequently £100,000 nominal. However in the case of these three bonds you can trade them in a "Retail" size of £100 nominal.

One difference between the Tesco bond and the others is that there is no explicit or parent guarantee from Tesco PLC. So, in theory, Tesco Bank could go bust and Tesco PLC would not be under any obligation to bail out the bond holders. And Tesco Bank could get sold as well. That is not true of the NG and SVT bonds which are issued by the quoted PLC and whose bonds have claims over all the assets of National Grid and Severn Trent.

THE PUNCH AND JUDY SHOW OF BRITISH POLITICS

Simon Walker, Director General of the Institute of Directors

As the longest running organisation for professional leaders, with nearly 35,000 members, the Institute of Directors is the voice for UK business. As the Director General, Simon Walker is well placed to discuss one of the burning issues at the heart of British politics.


MIGRATION
IS NOT A CRIME

In the latest edition of Director magazine, Wilfred Emmanuel-Jones, a Jamaican-born businessman, made an argument that is not often heard in the debate on immigration. The children of migrants should be proud, he said, because they had “courageous parents who decided to leave their comfort zone to better their lives. They suffered and they struggled and they had a pretty hard time as a consequence, but my god, what a pedigree to have”.

Every time new migration statistics are released showing net migration above 100,000, the front pages accuse the Government of failing to deliver on their promises. Instead of a realistic discussion of the data and opinions on immigration, we have a political Punch and Judy show, with a steady stream of critical headlines met by pig-headed insistence by the Government that they will hit their target.

Every time new migration statistics are released showing net migration above 100,000, the front pages accuse the Government of failing to deliver on their promises

Emmanuel-Jones is an independent-minded entrepreneur who is not afraid to say what he thinks. After years running a successful food PR firm, he grew tired of working for large companies (too many “big willy boys”), moved to the West Country and started selling gluten-free sausages under the brand of The Black Farmer.

For politicians, on the other hand, immigration is an area full of potential pitfalls – Gordon Brown can attest to that. I can understand that those who aspire to office are nervous about saying the wrong thing, but it has led to a very poor quality of debate on the subject.

Even before it became one of the central points of disagreement in the EU referendum campaign, migration was already seen by the public as the top issue facing the country. The Conservative party’s decision before last year’s General Election to maintain its target to reduce net migration to ‘the tens of thousands’ has ensured that it remains there.

No government can control one side of the equation in a net figure – how many people leave – so by tying themselves to this objective, the Conservatives have entrenched the opinion that politicians have lost control. Politics may often resemble a form of masochism, but rarely do ministers make such stiff rods for their own backs.

While the empty promise remains, it will be difficult to have a serious discussion about migration. But we should try anyway.

Roughly speaking, the fight over the pros and cons of migration is fought on two battlegrounds: economics and culture. The main economic question is whether immigrants are a benefit, or a drain on the UK. It depends slightly on what time period you look at, and whether the migrants come from Europe of further afield, but nearly all of the major studies conducted in the last 15 years find that migrants have a net positive fiscal effect: they pay more in taxes than they take in public services. This is because migrants are normally younger, and are very likely to be working and paying taxes. This is particularly true of migrants from Europe.

The Office for Budget Responsibility, the independent watchdog for the Treasury, also estimated in 2013 that lower immigration would lead to higher government debt in the long term. If net migration was reduced to zero, by 2060, the mountain of debt would be 150% of the size of the UK economy. If, on the other hand, migration continues at roughly the current level, debt will only be half the size, around 75% of GDP.
There are, of course, arguments to be had about methodology, and plenty of people dispute the above findings. However, the weight of academic evidence does seem to suggest migrants are an economic benefit to the UK.

Economics may hold a strong sway over voters' minds, but clearly it isn't everything. David Goodhart, author of The British Dream: Successes and Failures of Post-War Immigration, divides the public into two camps, liberals and communitarians. Liberals value cultural openness and are pro-immigration, while communitarians value the familiar and local, and are sceptical of globalisation and movement of people.

I will lay my cards on the table. As someone who was born in South Africa and spent much of my adult life in New Zealand, I fall squarely into Goodhart's liberal category. I make no apologies for saying that, rather than viewing migration as a threat to be contained, we should champion Emmanuel-Jones and the 450,000 other migrant entrepreneurs in the UK. Rather than fretting about numbers, we should recognise that the determined young people from Europe and elsewhere who come here to work are also enriching us in the process.

Values are not like economic forecasts, they are deeply held and not very susceptible to argument. But I would make one final point: if the UK was an economic basket case, as it was when I left for New Zealand in the seventies, immigration wouldn't be an issue. The question is, which would you prefer – a strong economy attracting hard-working and talented people from across the world, or the opposite?

Simon Walker

Simon Walker became Director General of the Institute of Directors in October 2011 and debates regularly in the media and engages with senior figures from across government and politics.

He previously served as Chief Executive of the BVCA, the organisation that represents British private equity and venture capital and prior to that he worked at Reuters as Director of Corporate Communications and Marketing. He was Communications Secretary to HM The Queen at Buckingham Palace from 2000 to 2003 and earlier served as Director of Corporate Affairs at British Airways. From 1996-1997 Simon worked as a special adviser in the Prime Minister's Policy Unit at 10 Downing Street.

He has been a member of the Better Regulation Commission, a Trustee of The Queen's Golden Jubilee Trust and the New Zealand-UK Link Association. He is a Council Member of the European Policy Forum and a member of the Parliamentary Speaker's Advisory Committee on Public Engagement. In 2015, GQ magazine listed Simon among the 100 best connected men in the country.

Simon was born in South Africa, and has worked as a journalist and consultant in New Zealand, Belgium and the UK. He read Philosophy, Politics and Economics at Balliol College, Oxford, where he was President of the Oxford Union. He was a Knight Journalism Fellow at Stanford University. He is married with two children.

CHANGING THE GAME

Brian Tora, Associate

My brother visited Washington DC recently as a tourist. Amongst the sights he took in was the view of the capital of the United States from a boat on the Potomac River. Aside from himself and his travelling companion, all the other tourists on board were Chinese and the commentary broadcast on the boat's loudspeakers was in Mandarin as well as English.

Perhaps I shouldn't have been surprised at his story. After all, China is the world's most populous nation and the second largest economy on the planet, accounting for more than 15% of global Gross Domestic Product (GDP). It has a rapidly growing middle class and, despite remaining a Communist autocracy, has embraced capitalist ideals, with much wealth being created by hard working entrepreneurs. Spending this wealth must include international tourism, but the fact remains that China has yet to achieve the transition into a Western style society.

The influence that China has had on the global economy is well documented. Commodities and other resources were boosted in value over a decade as China first industrialised and then developed its infrastructure. The construction of new road and rail networks and the creation of a number of "super cities" kept demand for oil and steel high. But such a trend cannot be sustained indefinitely and the inevitable slowdown has left many commodity prices in the doldrums as supply exceeds demand.

The effects are worldwide, of course. Major economies like Brazil have been plunged into recession as demand for their raw materials dried up and prices slumped. Australia has suffered too, with its heavy reliance on the mining industry. And the fall in the price of oil has had consequences for a number of countries. The global economic future is truly intertwined with the outlook for China – which is something of a worrying thought.

> We would do well not to lose sight of what is happening in China.

A little over a year ago markets were rocked by a modest devaluation of the Chinese currency and increasing intervention there by the authorities in financial markets. With growth having slowed from the double digit gains of previous years to a more modest 7.5%, the action in China simply added to the concerns of investors. What China needed to do was to redirect its economy to a slower, higher quality growth engine powered by services and domestic consumption. Achieving such a transition would not be easy, but would be crucial to global economic wellbeing.

Mindful that boosting consumption was key to maintaining growth, the Chinese authorities chose to encourage credit expansion. Unlike the US, UK, Japan and the Eurozone, it did not expand the central bank's balance sheet, instead encouraging banks to increase lending. The debt to GDP ratio ballooned as a consequence and now stands at around 35% above trend. But not all easy money finds its way into the right hands. Speculative activity increased, with the inevitable rise in defaults and non-performing loans, adding to investor's worries.

So we may well see the Chinese authorities pull back from introducing further monetary stimulus, which could, of course, mean that growth undershoots expectations. Certainly, recent data does suggest a continuation of the trend towards slower growth. In April industrial production grew by just 6.0%, compared with 6.8% previously, electricity generation was actually down on the previous year, while retail sales growth dropped to 10.1% from the previous month's 10.5%.

While we might remain fixated on the in/out European referendum in the short term and the outcome of the US Presidential elections in the medium term, we would do well not to lose sight of what is happening in China. The game there is far from over, but there is little evidence so far that the changes that are so crucial to sustaining future growth are taking place at an acceptable pace. The advantage the Chinese have is the command nature of their economy. But set against that is an inbuilt tendency to gamble and a growing desire for more freedom.

As it happens, sharing your sightseeing trip with a group of Chinese holidaymakers should be taken as a good sign. The advantage China enjoyed on the manufacturing front was always unsustainable if living standards were to continue to rise in what was, not too long ago, one of the poorest nations on Earth. There are plenty of signs that manufacturing jobs are returning to those countries which lost them to cheap Chinese imports – including America. But what we really need is for the Chinese middle classes to prosper – and spend.

A SPOTLIGHT ON THREE OF THE KEY COMPANIES WE'VE MET DURING THE PAST QUARTER

Theo Wyld, Research Analyst
James Godrick, Research Assistant

We met the companies below and you can learn more on any of these by contacting the person at JM Finn & Co with whom you usually deal.

BASIC MATERIALS
Coats Group, Rio Tinto Plc, BHP Billiton

CONSUMER GOODS
Barratt Developments, Carr's group, GKN, Imperial Tobacco

CONSUMER SERVICES
Whitbread, Saga, Kingfisher, Greene King, Enterprise Inns, Pearson, GVC Holdings, RELX

FINANCIALS
Barclays, Lloyds, British Land

INDUSTRIALS
Howden Joinery, Cobham, Spectris, Carillion, Equiniti

OIL & GAS
Hunting

TECHNOLOGY
Sage Group

UTILITIES
SSE

ENTERPRISE INNS

PRICE: £0.99
52 WEEK HIGH-LOW: £1.35 – £0.69
NET YIELD: 0.0%
HIST/PROS PER: 5.8 – 5.2
EQUITY MARKET CAP: £496m

CONSUMER SERVICES
Simon Townsend, CEO and Neil Smith, CFO

Enterprise Inns (ETI) boasts a portfolio of over 5,000 UK pubs. The majority of the estate is operated under what is known as a 'tied and tenanted' model. Under this arrangement, a publican pays below market rent to ETI and in return is bound by contract to sell the beers that the company buys in bulk and at a discount from various breweries. In this model ETI has their predictable rental income supplemented by a share of sales.

The market is changing however, with legislation brewing known as the Market Rent Option (MRO). Although not finalised yet, it is anticipated that under this new ruling publicans will have the option to break the tie to the ETI-provided beers in exchange for higher rent. Although the latter benefits ETI, they lose their economies of scale in bulk ordering the beer which eats into their margins.

As well as navigating the upcoming legislation, the relatively new management team undertook a strategic review of the business with a fine tooth comb and have communicated their five year plan. This involves disposing of c. 1,000 pubs whilst diversifying the remainder of the estate across tenanted, leased, managed, and commercial models. Clearly, this is not without considerable execution risk, however the benefits to be reaped, should they pull this off, could be extensive.

The story prior to the strategic review had been all about paying down debt. ETI remains highly geared, as EBITDA has fallen off concurrently, but in absolute terms Net Debt has reduced by c. £1.4bn since the crisis. The company is now in a position to invest in the business itself and is at a c.70% discount to NAV.

KINGFISHER

PRICE: £3.75
52 WEEK HIGH-LOW: £3.86 – £3.12
NET YIELD: 2.7%
HIST/PROS PER: 20.9 – 16.0
EQUITY MARKET CAP: £8,412m

CONSUMER SERVICES

Sarah Levy, Investor Relations Director

Kingfisher operates as a home improvement retailer under well-known brands such as B&Q, Screwfix and other European brands. The Group has over 1,100 stores across ten European countries including a major presence in France, Poland and the UK.

Since the appointment of the current CEO, Véronique Laury the Group has begun its new 'One Kingfisher' strategy. This is a five year plan aimed at unifying their international offering whilst improving digital capabilities and operational efficiency. Through this they expect to deliver a £500m sustainable annual profit uplift by the end of year five over and above 'business as usual'. They also expect to return £600m of capital to shareholders over the next three years and are targeting a total cash cost of £800m.

At the heart of their decision to reform is the quite disparate running of each of their individual businesses. This manifests itself in the group wide offering of 393,000 different SKUs (stock keeping units) of which only four items were sold across all five of the Group's brands. During our most recent meeting we were given the example of the Group's lightbulb offering which has been reduced from 2,824 to 498 SKUs and has seen a 20% cost price reduction as a result.

Clearly this is a quite major shift in the Company's strategy and culture. The unification of nine separately run companies into one Group will be quite a challenge but the potential for increased operational efficiency and significant cost savings means that I believe this is a project well worth taking on. Both Kingfisher and the market are well aware that this fundamental change in strategy carries significant risk and the concern remains that Kingfisher may have bitten off more than they can chew.

SAGE

PRICE: £6.04
52 WEEK HIGH-LOW: £6.39 – £4.82
NET YIELD: 2.1%
HIST/PROS PER: 38.0 – 23.0
EQUITY MARKET CAP: £6,616m

TECHNOLOGY

Simon John, Investor Relations VP

Sage provides business management solutions to small and medium sized enterprises (SMEs) predominantly in Northern Europe and the US.

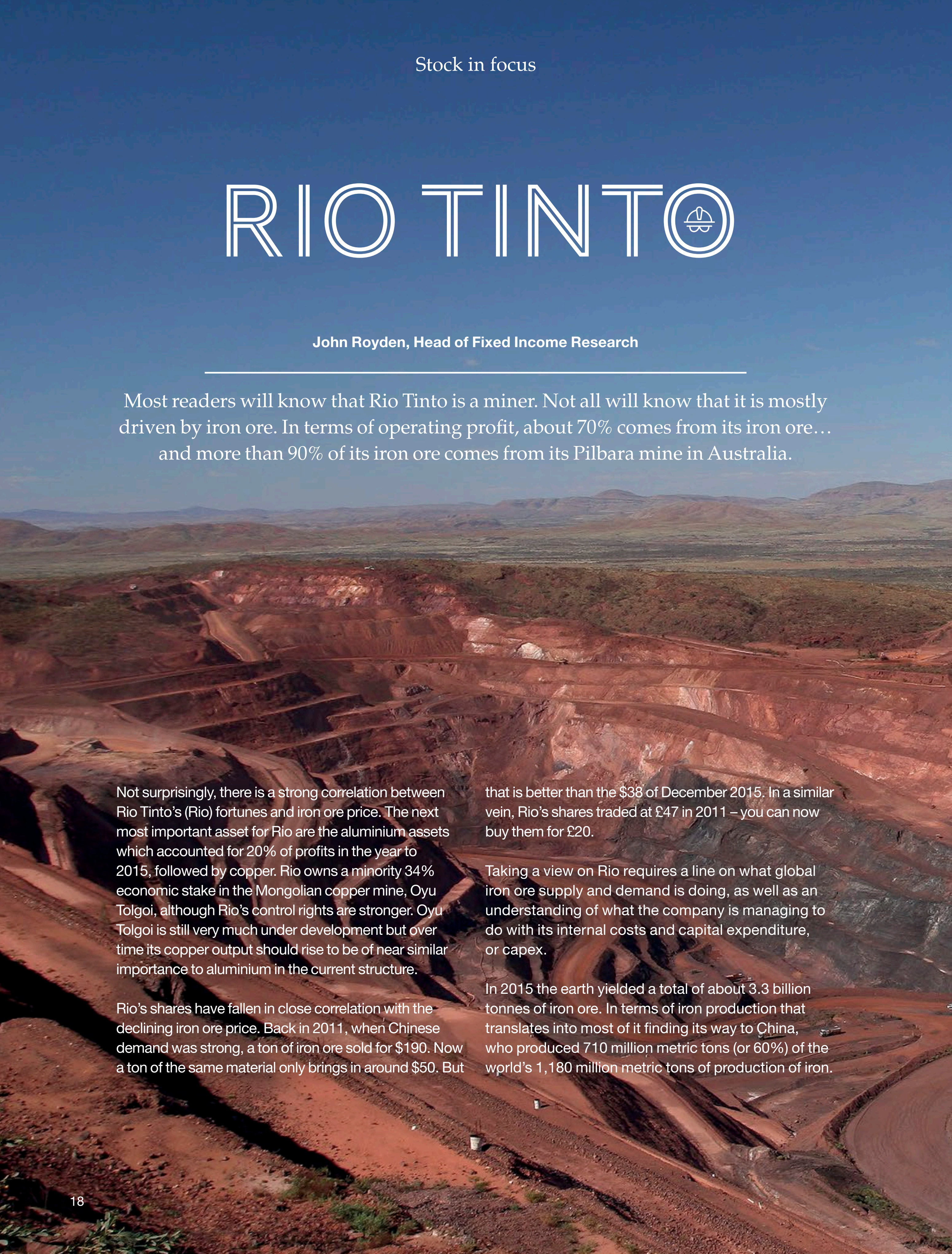
Sage has a niche product offering in business management software and a high level of recurring revenue that has delivered multiple years of organic sales growth ahead of inflation whilst increasing margins and returns on capital; an encouraging indicator of persistent pricing power.

The relatively new management team announced their strategy in June last year. It became evident during the meeting that departing management had done a good job picking up assets but a lesser one on centralising the process and generating efficiencies. Sage are focussing heavily on concentrating their product range to a suite of three main subscription offerings that cater for the complete range of SMEs of which there are circa 75m companies.

Sage are firmly number two behind Intuit in the US and struggle to compete. However, they believe the sheer size of the addressable market justifies their presence. In France it is a case of keeping up with the strong local players, however most recent numbers out of the region have been more promising. Sage see cloud-based products as the future and despite having been slow to enter this market, the new management team are heavily focussed on moving in this direction.

Our recent meeting with representatives from the company was informative and reassuring. I see a lot of easy wins in terms of centralisation and efficiencies to come in the medium term. The business plan is to move towards recurring service revenues and the cloud, which could help them address the market needs.

Please read the important notice on page 2.



RIO TINTO

John Royden, Head of Fixed Income Research

Most readers will know that Rio Tinto is a miner. Not all will know that it is mostly driven by iron ore. In terms of operating profit, about 70% comes from its iron ore… and more than 90% of its iron ore comes from its Pilbara mine in Australia.

Not surprisingly, there is a strong correlation between Rio Tinto's (Rio) fortunes and iron ore price. The next most important asset for Rio are the aluminium assets which accounted for 20% of profits in the year to 2015, followed by copper. Rio owns a minority 34% economic stake in the Mongolian copper mine, Oyu Tolgoi, although Rio's control rights are stronger. Oyu Tolgoi is still very much under development but over time its copper output should rise to be of near similar importance to aluminium in the current structure.

Rio's shares have fallen in close correlation with the declining iron ore price. Back in 2011, when Chinese demand was strong, a ton of iron ore sold for $190. Now a ton of the same material only brings in around $50. But that is better than the $38 of December 2015. In a similar vein, Rio's shares traded at £47 in 2011 – you can now buy them for £20.

Taking a view on Rio requires a line on what global iron ore supply and demand is doing, as well as an understanding of what the company is managing to do with its internal costs and capital expenditure, or capex.

In 2015 the earth yielded a total of about 3.3 billion tonnes of iron ore. In terms of iron production that translates into most of it finding its way to China, who produced 710 million metric tons (or 60%) of the world's 1,180 million metric tons of production of iron.

That illustrates the importance of China in terms of the supply and demand equation and why investors are still “all eyes on China”. In terms of Chinese demand, I am more inclined to a benign view on their prospects going forward; Chinese growth has been slowing for the last decade and it continues to slow, but I don’t think it is crashing. Even if it did start to crash, I feel the Chinese have a free get-out-of-jail-card in terms of additional infrastructure spend.

Others look at the high levels of debt and take the opposite view. Officially, Chinese corporate, household and government debt stands at 250% of GDP, compared to Japan at 380% and the USA at 245%. Unofficial estimates of Chinese debt however are much higher and lead to the conclusion that paying the interest on the debt just about mops up all the spare cash which takes the economy into a recession that can only be avoided by allowing the renminbi to fall in order to stimulate demand.

I side with the optimists and don’t see China imploding. Attempts to finely predict the balance of the supply and demand of iron ore, and its effect on price have not, in the past, proved particularly fruitful. But there is a view that higher cost producers will have to exit at some stage.

So my conclusion on the topic of iron ore price is that whilst others have been predicting chaos in China for a year or so, it has not materialised; and I don’t think it will. At the same time, I see that iron ore prices at c$50 per ton are more than 30% off the December lows of $38. It looks as if prices going forward will be more range bound than before.

This all then begs the question of what happens to Rio’s finances if we hold these iron ore prices? Much of that is driven by what happens to the dividend.

In February Rio announced that “The board expects total cash returns to shareholders over the longer term to be in a range of 40 to 60 per cent of underlying earnings in aggregate through the cycle.” They also said that they would commit to the full dividend for 2016 of $1.10 (76p). That compares to $2.15 (£1.48) in 2015.

A raft of analysts swiftly applied the “range of 40% to 60%” to 2017’s earnings and looked for more cuts. I think that was misplaced as the analysts missed the “through the cycle” element of the announcement. My analysis shows that I think Rio can hold the dividend going forward. They will be post-dividend cashflow positive this year, cashflow negative in 2017 and broadly neutral thereafter. Having one of the strongest balance sheets amongst the miners should help avoid rash decisions being made on account of short term iron ore price volatility, or indeed capex requirements at Oyu Tolgoi.

The price of iron ore is critical going forward and a fall back to $40 per ton could prejudice the dividend, but going forward, I would look for the price of iron ore to hold.

PRICE
£19.64

52 WEEK HIGH-LOW
£29.23 – £15.57

NET YIELD
7.6%

HIST/PROS PER
42.8 – 18.3

EQUITY MARKET CAP
£36,090m

John Royden is a beneficial owner of Rio Tinto.

Please read the important notice on page 2.

JM FINN & CO WINS PRESTIGIOUS AWARD

The award for Best Discretionary Service at the 2016 City of London Wealth Management Awards was presented to JM Finn & Co at a ceremony at The Guildhall.

The City of London Wealth Management Awards, which are unique in that winners are determined by an online public vote, were presented by the BBC's Sophie Raworth.

Stephen Pinner, MD of Goodacre UK, the company managing the Awards, said: "Winning a City of London Wealth Management Award is significant proof of distinction for the best companies and individuals providing services for private investors. The fact that winners are determined by individual votes is a huge endorsement for all winners".
The award was collected by Sarah Soar, Head of Investment Management, who commented: "We've always known that we offer a high quality discretionary service, something that was supported by last summer's client survey results, and to receive public acknowledgement of this is tremendous."

The purpose of the City of London Wealth Management Awards is to recognise and promote quality of service from Wealth Management companies and individuals. The public online vote took place over a two week period in March 2016 and was reviewed by an independent panel of judges.

COLWMA
CITY OF LONDON WEALTH MANAGEMENT AWARDS
WINNER 2016
Best Discretionary Service

JM Finn & Co hires two **Investment Managers**

JM Finn & Co has hired Edward Hagger and Harry Burnham to join the firm as Investment Managers in their London office.

Harry, who joined the firm in May as an Investment Director, was previously at Ashcourt Rowan Asset Management (subsequently acquired by Towry) and prior to that he was an Investment Director at Brewin Dolphin.

Edward Hagger, who joined in March, has spent over 30 years in the investment management industry since graduating from Oxford University in 1984, the majority of which was at Brewin Dolphin.

Commenting on Harry and Edward's arrival, Sarah Soar, Head of Investment Management said:
"We are delighted to have secured these two highly regarded Investment Managers to our team. I know both will be a huge asset to JM Finn & Co."

Investment Directors named in **industry leader's list**

PAM Insight, a leading independent provider of specialist news, analysis and comparative data for the wealth management industry, has released the latest list of the PAM Top 40 Under 40. This comprises the leading private client investment managers under the age of 40.

JM Finn & Co Investment Directors, Simon Tufnell and Charles Ramsay were both named in this year's list which is drawn up based upon the qualities that the nominees were deemed to have. Contributing factors included the career trajectory, industry feedback and the reputation and performance of the firm, supplemented by PAM Insight's experience and knowledge of who is rising to the top and why.

Congratulations to both Charles and Simon for being nominated (for the second time in Simon's case), which we believe is testament to the quality of Investment Manager at JM Finn & Co.

Celebrating 10 years in East Anglia with **new office**

The firm has marked the tenth anniversary of its presence in East Anglia, by developing a new office and merging the Bury St Edmunds team with the Ipswich team.

The new office incorporates the ground floor space at the existing site on Abbeygate Street in Bury St Edmunds and will provide our enlarged staff with a much improved working environment and a first class facility in which to meet clients.

"Bringing together the two teams will provide additional benefits on all levels," said Brett Bayliss, Head of the East Anglian Branch.

"Our clients will have a hugely improved site in which to meet with us in Bury, and for those clients located in Ipswich, we will retain an office with meeting space. Our Investment Managers will benefit from sharing administrative resources and a wider breadth of intellectual capital to bounce investment ideas off, and in addition, we will be able to provide a more coordinated approach to servicing the flourishing intermediary community across the region. We very much look forward to welcoming clients in the region to our new office."

EQUINITI

James Godrich, Research Assistant

PRICE
£1.86

52 WEEK HIGH-LOW
£1.94 – £1.27

NET YIELD
0.4%

HIST/PROS PER
N/A – 12.7

EQUITY MARKET CAP
£577m

Equiniti Group plc is principally a provider of share registration, pension payment and administration services to a range of organisations. It also benefits from various cross-selling opportunities in its offering, which includes employee and investment services as well as specialist business and technology solutions.

After its October 2015 IPO the Company had a difficult initial trading period. Since then though they have produced a very strong set of year end results which included (a) a 26% increase in revenues, 7% of which came from organic growth and (b) a material reduction in net debt – one of the major concerns for the market since IPO.

Equiniti have a remarkable level of stickiness in their contracts with a 100% retention rate of FTSE350 registry contracts for each of the past four years and an average contract length of 27 years, some of which date back to the 1800s. They currently boast around a 50% FTSE registry base market share and are winning more than 50% of IPO mandates.

Greater broker coverage, continued reduction in levels of gearing and consistent in line results are all hurdles that the Company must clear in order to build long term value for shareholders.

Please read the important notice on page 2.

THE SEARCH FOR YIELD

Chris Bowie, Partner, Portfolio Manager

The Holy Grail for any fixed income investor is an attractive level of income, or yield, with little or no capital losses and very little capital volatility along the way. Chris Bowie, Portfolio Manager and Partner at TwentyFour Asset Management describes their back to basics approach to fixed income investing.

Not surprisingly, achieving consistently risk adjusted returns is harder than it sounds! Whilst we certainly don't claim to have found that Grail just yet, we have come up with an approach that we believe seems to stack the odds more favourably towards the investor in terms of the risk/reward trade-off, and this approach is our guiding principle.

Since the financial crisis, many investors have turned towards bond funds seeking absolute returns in the belief that it can generate superior risk-adjusted returns through the investment cycle. Sadly, the reality has not lived up to the promise in all cases, with frequent comments from investors that I meet calling it "the absolutely negative return sector". Some of these criticisms are valid, as many funds in the sector have struggled to achieve positive returns over reasonable time frames, and often with higher levels of volatility than are appropriate for their return targets.

So when we set about designing an absolute return product, we went for a real back-to-basics approach. We asked ourselves, what if we let fixed income do what it should be best at doing? Simply put, getting your capital back with a decent level of income for putting that capital at risk. That means having income as the dominant driver of those returns, and rejecting other strategies that are harder to be

When it comes to stock selection, we add in some more special sauce; this time in the form of our custom designed stock picking system, called "Observatory". What this system does is take a stock level view of just how volatile every single bond that we could buy actually is.

consistently great at; such as shorting, using leverage or complicated derivative overlays. However, in order to keep capital volatility contained, we would need to find the bond market segment that was best at returning income and which consistently kept capital volatility low – and our suspicion was that short dated bonds were the best fit. But would a simpler, short-dated approach consistently work, and work with a high enough level of return to make it attractive?

We found that it would, and often does. The evidence we have for that assertion is twofold: firstly, our extensive quantitative back-testing confirmed what we had long suspected, that short-dated bonds had the lowest volatility, but also surprised us in how good the returns could actually be; and secondly, that experience of running the Fund through some challenging markets we feel the strategy actually works, even within a period when the US Federal Reserve has raised rates for the first time in nearly ten years, and the credit markets had one of their worst months for five years. So, how have we managed to achieve this, with such low volatility?

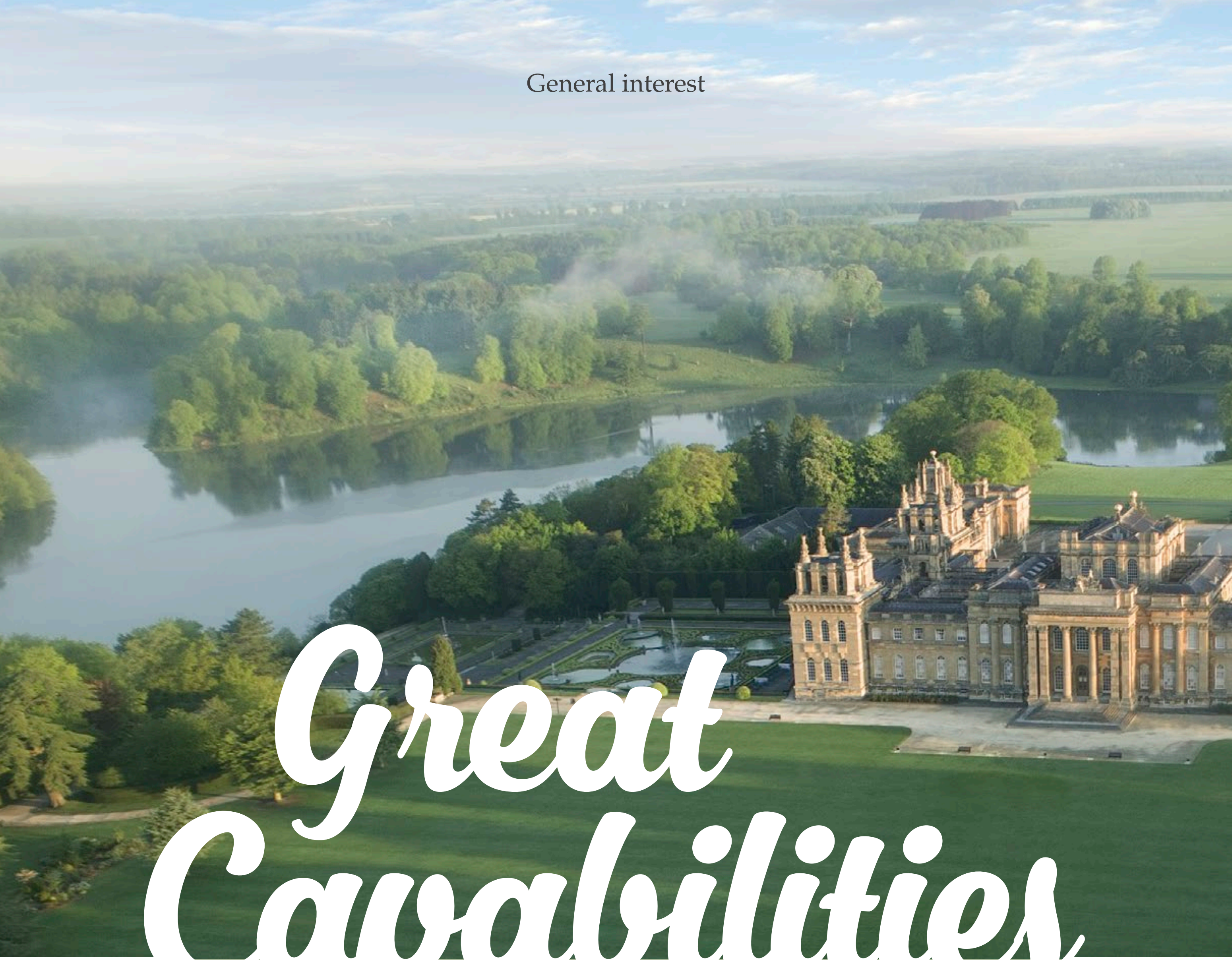
We spent months designing and then fine-tuning what we invest in, and where it can take the limited risks that it is allowed to take. By looking at daily returns from all areas of credit since the turn of the century, our in-house testing work looked in detail as to where the drivers of volatility reside, and from that we work out how to try to avoid them. But more than that, we also knew from the data where the best returning opportunities were too, and how to exploit them. That critical work, of seeking the very best returns with the lowest volatilities, led us into finding the best Sharpe Ratios (a measure of risk-adjusted return) – and then hard-coding that into our investment process.

The second part of the answer relies on a little bit of our TwentyFour special sauce of course. This is where we use our in-house asset allocation preferences, within a much defined low volatility universe, to attempt to elevate returns whilst lowering risks even further than the core product design itself would bring. When it comes to stock selection, we add in some more special sauce; this time in the form of our custom designed stock picking system, called "Observatory". What this system does is take a stock level view of just how volatile every single bond that we could buy actually is. Before we buy anything, we know what its spread volatility and cash price volatility is – and not just for that bond and company, but the average for its peers in that sector, that country, that currency, that rating band, that maturity, that level of subordination etc.

So when we set about designing our absolute return fund, we went for a real back-to-basics approach. We asked ourselves, what if we let fixed income do what it is best at doing?

Right now we think this approach of maximising return in a low volatility context is crucial, as lots of risks and opportunities remain in credit, and fixed income in general. As I write, some hawkish commentary is starting to come out from the Federal Reserve suggesting rate rises may come earlier than many were expecting, and that is pressuring capital values on longer dated bonds. Of course, closer to home, the Brexit referendum later in June could well be a source of volatility, not just for UK fixed income markets, but possibly even more so in the exchange rate.

You should contact the person at JM Finn & Co with whom you usually deal if you wish to discuss the suitability of any securities mentioned.



Great Capabilities

By Ceryl Evans, Director, Capability Brown Festival and Fiona Davison, Head of Libraries and Exhibitions at Royal Horticultural Society.

Lancelot"Capability"Brown, often called the 'father of landscape architecture,' changed the face of the British landscape. He worked in the English Landscape style, creating the rolling vistas and serpentine waterways that have come to epitomise the English countryside ideal.

Thought to have worked or advised on around 250 landscapes in England and Wales, with his work covering an estimated 200 square miles, about the same land mass as the island of Mauritius, his name will be familiar to anyone with an interest in gardens or historic landscapes. Yet beyond his inimitable nickname, derived from his habit of telling owners of large estates that their land had “great capabilities” for improvement, Brown remains something of a mystery. We don’t even know if he was called “Capability” to his face.

His exact birthday is unknown, but his baptism was recorded at St Wilfrid’s Church at Kirkharle in Northumberland on 30 August 1716. His parents worked on the Kirkharle Estate but it is unclear how well off they were, but many see Brown’s rise to Royal Gardener as something of a rags to riches story.

Capability Brown’s name is used as a badge of quality on advertising material for days out at country estates, but what makes the landscape a Brownian one, and what he caused to happen there is not usually explained. “Wasn’t he some sort of gardener?” was the standard response received when we asked visitors about him at one Brown site last year. Not a bad place to start, but we think Brown deserves to be better known and his work understood, hence the development of the Capability Brown Festival 2016, funded by the Heritage Lottery Fund, with 21 partner organisations. The Festival’s ultimate ambition is to give historic landscapes as much prominence as the country houses which sit within them.

Looking at his achievements, in an age when communication was by letter and the fastest means of travel was by horse, the natural question to ask is how on earth did he manage it all? Given the scale of the impact he made upon the British landscape, Brown has left surprisingly little documentary evidence of his working practices for us to study. One of the few quotes we have from Brown on his methods is in a letter and sums his mantra up as "Hideing what is disagreeable and shewing what is beautiful."

Unlike his successor Repton, he did not write a book on his 'Theory and Practice', he did not supply picture books of his proposals and a frustratingly small number of his working plans have survived. Evidence is scattered in the family archives of country houses and there is always the hope that a new letter, contract or drawing may surface from a dusty attic somewhere. However we do have two important sources of information that throw light on Brown as a consummate entrepreneur and businessman. One is his set of accounts with his bank Drummonds (now in the RBS Archive) the other is his personal Account Book, one of the treasures of the Royal Horticultural Society's Lindley Library.

The Account Book is a long slim volume, apparently custom made for Brown to fit in his frock coat pocket so that he could take it with him on the road. The book came to the RHS Lindley Library in the 1950s via the Morrice family, descendants of Brown's younger daughter Margaret. It has recently undergone careful conservation in preparation for display at the Library in the RHS headquarters at Vincent Square for the first time ever this September as part of the Capability Brown Festival.

The book contains the details of 125 clients and reads like a 'Who's Who' of the English aristocracy, boasting The King, six prime ministers and half the House of Lords. Brown clearly had no trouble drumming up business. These clients had the wealth, enthusiasm and long term vision to commit huge sums to improving their estates. It has been estimated that when translated into modern terms, his annual turnover in the 1760s averaged over £36m.

> "Hideing what is disagreeable and shewing what is beautiful".

However the book is not just a dry accounting record and the exhibition will explore some of the fascinating things it can tell us about how Brown operated, such as the frenetic amount of travelling he did and the team of specialist subcontractors he relied upon to deliver his vision. Little glimpses of Brown's personality also creep in, such as the incident in 1765 with Ambrose Dickens of Suffolk over an unpaid bill. The book records 'Mr Brown could not get the money for the Extra Work and tore the account before Mr Dickens' face and said his say upon that Business to him.'

Brown was buried at Fenstanton aged 66, which he bought for £13k (today's equivalent c. £29m) in 1767 from a client who could not afford to pay his bill. It is the only place he is believed to have owned any property. The exact location of his body in the churchyard of St Peter and St Paul has been lost in time. The Brown family memorial is in a prominent position by the altar, but his sons' inscriptions are given far more consequence. The University of Cambridge holds maps illustrating what he planned to do with his holdings in Fenstanton but which never came to fruition.

THE CAPABILITY BROWN FESTIVAL

The Festival has two key aims. The first is to open up Brown landscapes to as many people as possible. We want to encourage new visitors, people who may never ordinarily think of visiting a Brown site, to go along, learn about, explore and enjoy the landscapes on offer. We have commissioned Brown sites and other organisations across the country to run specific projects as part of the Festival, to attract different audiences to Brown's sites, and use new and innovative ways to explore and engage visitors with their surroundings, including exhibitions, art based projects, exploratory trails of landscape and much more.

Our second aim is to discover more about Brown's work, and how he created his amazing landscapes. Brown was known to ask workmen to dig lakes, move hills and occasionally even entire villages to make way for his designs. This would be a daunting prospect now, but truly impressive with the manpower and hand tools available in the 18th century.

For more information on the Capability Brown Festival, please see **www.capabilitybrown.org** or contact us via **info@capabilitybrown.org** or **@BrownCapability**

The exhibition, entitled 'A Capable Businessman' will run from 5th September – 28th October and details can be found on the RHS website **www.rhs.org.uk**

The conservation of Capability Brown's Account Book was one of the first projects to be supported by the RHS's Treasures of the Lindley Library Appeal. Details of other similar treasures the Library hopes to restore can be found on the RHS website: **www.rhs.org.uk/about-the-rhs/support-us/making-a-donation/support-rhs-lindley-libraries**

EXPERIAN

Theo Wyld, Research Analyst

PRICE
£12.91

52 WEEK HIGH-LOW
£13.04 – £10.17

NET YIELD
2.1%

HIST/PROS PER
23.7 – 20.1

EQUITY MARKET CAP
£12,440m

Experian is an information services firm best known for providing consumers and businesses alike with credit reports, but they are also engaged in fraud prevention, targeted marketing offers, and automated processes. Experian generates roughly half of earnings in North America; the remainder is spread relatively evenly across the globe.

Experian is a niche business with high barriers to entry and a strong balance sheet. It is well positioned to benefit from the structural growth in data usage and associated services; the products and services that Experian offer have the potential to materially enhance a given customer's business and are likely to see significant demand over coming years.

The strategic success story at present, particular in the UK and the US, is the idea of 'One Experian'; a push to cross-sell within their all-encompassing suite of products, the range of which is not available from competitors.

Alongside implementing 'One Experian', the relatively new management team have been effective in returning Consumer Services to growth, and building out a well invested, profitable franchise across all geographies.

Please read the important notice on page 2.

CAN I HELP MY CHILDREN GET ON THE PROPERTY LADDER?

Ian Gray

Ian Gray, Senior Partner at Property Finance specialists, Kinnison Limited discusses how it is getting easier to use your home equity to assist your children.

Much has been written about the difficulty young adults have making their first home purchase. It's true that without substantial help with a larger deposit, it's almost impossible to save much of a deposit whilst paying rent along the way. Imagine someone on a £60,000 salary, with a £500,000 flat purchase. The most they can hope to borrow is likely to be around £300,000, meaning they must find £215,000 to cover the deposit and Stamp Duty alone.

> So if you've assumed that you're too old to get a mortgage, or couldn't afford to service a larger mortgage, you might now qualify.

Traditionally, parents might have had to liquidate investments to pass on enough to make a difference for their child's first house purchase, or to help with that second step on the ladder when they start a family and must upsize.

In the past, it's also been common for parents to "guarantee" the child's mortgage – signing a Deed promising to make the payments if they were called upon to do so. However, since the credit crunch, many lenders have banned "guarantor" mortgages altogether.

Recent changes to several lenders' criteria mean that it's now easier for older homeowners to remortgage their homes to provide that assistance. So if you've assumed that you're too old to get a mortgage, or couldn't afford to service a larger mortgage, you might now qualify.

Increased Maximum Age

Many mortgage lenders will now extend the term until the borrower's 80th birthday, rather than the maximum state retirement age which has been the norm. So, someone aged 64 today could potentially remortgage over a 15 year term to release cash, and not have to worry that they must either sell investments or be forced to downsize until well after their retirement. As long as they can show they have sufficient income (from sources including earned income and pensions) to support the payments, lenders have become more flexible on age. There are also options for asset-rich, income-poor borrowers, and they tend to be for larger mortgages over £1,000,000.

What if you don't have enough in other assets? Some lenders will allow you to borrow up to 50% of your house value providing you have a sensible level of equity and have real plans to downsize prior to the expiry of the mortgage term.

Interest-only is Easier Now

Interest-only mortgages have recently been somewhat controversial, but we are of the opinion that it has a place for certain clients. Most lenders have begun to agree, and we're seeing it in recent changes to their lending policy. If you have in excess of the amount of the desired mortgage held in other investments or in other property assets (i.e. buy to let property) then it's usually possible to release up to 75% of your home's value, all on an interest-only basis. For example, a £500,000 mortgage against a house value of £670,000 could be secured on an interest-only basis if you had at least £250,000 in stocks and shares, and equity in a let property of £250,000, and you're willing to liquidate both to repay the mortgage before the end of the term. This is assuming, of course, the interest payments are deemed affordable.

What if you don't have enough in other assets? Some lenders will allow you to borrow up to 50% of your house value providing you have a sensible level of equity and have real plans to downsize prior to the expiry of the mortgage term. A few will even go higher than 50%, but the plans to downsize must be robust and the equity in your home substantial.

Rates are at Historic Lows

It's possible to remortgage your home on rates as low as 1.39% today. This would be on a two-year "tracker" variable rate, so it should be noted that it could increase over time. For example, a £500,000 mortgage at 1.39%, on an interest-only basis would result in initial monthly payments of only £579.16 per month. The deal comes with a £995 lender's arrangement fee and the APR is 3.7%.

As long as you have either income or assets to deal with the risk that your payments will increase in the event of an interest-rate hike, you may consider taking advantage of these extremely low mortgage rates. It's never been more affordable.

Readers of the financial press will know it's not easy to get a mortgage today, and tight regulation has imposed rules to prevent lenders from allowing us to become overextended. The spirit behind these rules is right and proper and we mustn't allow the market to veer back to how it was before the credit crunch. But in cases where borrowers have either income or assets adequate to support a sensible level of borrowing, there are new, "challenger" lenders out there who will take a common-sense view of your case. It's easier for us to secure lending for older clients where it wasn't available before.

As a last resort, your home may be repossessed if you do not keep up with payments.

Kinnison Limited of 23 Hanover Square, London W1S 1JB is an appointed representative of H L Partnership Limited, Pharos House, 67 High Street, Worthing, West Sussex, BN11 1DN, England, which is authorised and regulated by the Financial Conduct Authority. H L Partnership Limited's FCA number is 303397.

KINNISON
PROPERTY FINANCE EXPERTS

JM Finn & Co is not able to give individual property or borrowing advice. Clients who wish to explore the points that this article refers to should seek advice from a specialist in relation to their own personal circumstances.

US GAAP AND IFRS

John Royden, Head of Fixed Income Research

There are two sets of accounting standards which dominate the world. The IFRS Foundation has oversight of the International Accounting Standards Board who publish the IFRS or International Financial Reporting Standards. In the US, the FASB, or Financial Accounting Standards Board, publish US GAAP, or US Generally Accepted Accounting Principles.

As a general rule most companies around the world can choose whether they want to report under US GAAP or IFRS. US companies based overseas can use IFRS and overseas companies based in the US can still use IFRS rather than GAAP.

Much of US GAAP and IFRS is very similar. My impression is that where there are differences, US GAAP is more prescriptive than IFRS, which allows more choice.

For example, the cashflow statement divides into (a) operations, (b) financing and (c) investment. US GAAP tells you exactly where to put items like dividends and interest, whereas IFRS allows you a choice of one or another cashflow category. IFRS allows the balance sheet to better reflect market values by allowing companies to revalue their properties and long lived assets upwards. US GAAP does not.

Both US GAAP and IFRS have different approaches to incorporating pension related changes into the Profit and Loss statement, which are equally complex in both cases.

Minor differences persist in terms of tests for qualifications, such as when an operating lease (renting an asset) is taken onto a balance sheet as an asset and a debt (to avoid off-balance sheet financing being disguised).

US GAAP uses the LIFO (Last In First Out) method to value inventory, whereas IFRS compels the use of FIFO (First in First Out). Most of the time this allows US GAAP companies to make lower profits and so pay lower taxes.

RENISHAW

James Godrich, Research Assistant

PRICE
£19.70

52 WEEK HIGH-LOW
£25.50 – £15.77

NET YIELD
2.4

HIST/PROS PER
14.6 – 22.2

EQUITY MARKET CAP
£1,427

Renishaw is a United Kingdom-based, specialist electronic engineering company operating in three segments: metrology, healthcare and additive manufacturing, more commonly known as 3D printing.

The business model centres on finding a problem, patenting a solution and using the high margin sales to enable them to offer excellent customer support and to invest in their next project. The Company continues to drive future growth through its heavy investment in R&D. In the last year 18% of their revenues were reinvested in R&D resulting in 54 patents being granted and a further 32 filed.

The Company is not without its problems: a six week order book, spikes in demand caused by an ever changing product range and lumpy cash flows make guidance difficult. All of this means that the Company will likely continue to experience short term volatility, exacerbated by its 47% free float and limited communication with the market.

Renishaw has shown impressive organic growth with both average revenue and pre-tax profit growing at c.13% and c.12% respectively per annum since 1983. An exciting pipeline of products combined with continued R&D suggests that a long term growth story may also lie ahead.

Please read the important notice on page 2.

Asset Allocation focus

As part of our focus on providing a high quality, personalised investment service, we look to support our investment managers in their decision making when it comes to constructing client portfolios. Our asset allocation committee is one example of this, via their monthly output.

FIXED INCOME

UK Government Bonds	Having been positive on conventional gilts relative to index-linked we now find that the risk reward profile is balanced. We are inclined to favour maturities in the four to twelve year range for both.
UK Corporate Bonds	
UK Indexed Linked Bonds	We prefer to hold five year duration BB bonds via funds for diversification, spread compression and tax reasons. We remain alert to liquidity risks in the bond markets. Spreads at the quality end of the spectrum have widened to a point where we think the reward is now commensurate with the risk.

UK EQUITIES

UK Financials	Banks are being impacted by exposure to Oil & Gas so default rates are possibly set to rise. Within the sector, we favour the Life Insurers for their secular growth.
Consumer Goods	Wage inflation and momentum in UK economy should continue to benefit the sector.
Oil & Gas	Given the unfavourable supply/demand dynamics we do not expect any improvement until we see concrete production cuts announced.
Consumer Services	Some interesting opportunities in Media and Leisure exist; we are still positive on consumer spending.
Industrials	Slowing global manufacturing continues to weigh on the sector for the time being. Overseas earnings could be a potential hedge on sterling.

OTHER EQUITIES

US	We remain concerned by extended valuations and slowing earnings momentum as QE matures and the headwind of recent USD strength is felt. The threat of a forced rate reversal may cause short term volatility.
Europe	We continue to see some upside in the Eurozone generally; Europe is currently enjoying the tailwinds of QE and depressed borrowing costs and so we favour this region over the US.
Japan	We have little conviction as to Japan's economic outlook as QE appears to have achieved limited long-term benefits for the underlying economy.
Asia/China	We continue to remain cautious on the Chinese economy as it undertakes a cyclical deleveraging, post an extensive domestic property boom and overcapacity. Any further devaluation of the yuan would trigger similar devaluations elsewhere in Asia.
Emerging Markets	We remain wary of EM currencies given the ongoing rally in the USD, although indecision by the Fed over future interest rate moves might see a relief rally.

ALTERNATIVES

Property	We are increasingly wary of bull market characteristics in the UK. There is anecdotal evidence of pent-up demand and signs of cyclical maturity.
Absolute Return	Exposure might be appropriate given current market conditions. We suggest caution on the "yield hunt" and are wary of lower quality products.
Infrastructure	As with absolute return, investors should be cautious when looking for yield and pay close scrutiny to the quality of the investment product.

ASSET ALLOCATION: A SNAPSHOT

The Asset Allocation Committee, which consists of three members of our research team and a number of investment managers, aims to provide a view on the asset allocation that seems most suitable in current macro conditions. The output of the monthly meetings remains a suggested stance and it is important to note, that the views expressed are not those of the firm but rather those of the committee and that the views expressed may not necessarily be those of your individual investment manager.

KEY

Positive Neutral Negative

SMITH & NEPHEW

Theo Wyld, Research Assistant

PRICE
£11.79

52 WEEK HIGH-LOW
£12.20 – £10.41

NET YIELD
1.8%

HIST/PROS PER
37.6 – 19.8

EQUITY MARKET CAP
£10,544

Smith & Nephew (SN) is a global medical devices business operating in three main segments: Orthopaedics, Endoscopy and Advanced Wound Management (AWM). Traditionally SN relied on demand from the developed markets, and whilst they continue to deliver mid-single digit revenue growth, which is no mean feat in these markets, management are concentrating on the emerging economies. Integral to SN maintaining its high rating is tackling the issue of the loss of market share experienced in its core hips and knees segment over the last two to three years. Here, SN has launched a lower cost, streamlined and potentially price disruptive new range in Syncera.

Elsewhere in the Group, their Sports Medicine division is beginning to reap the benefits of the recent acquisition of ArthoCare after some subdued performance throughout most of 2015. AWM has been mixed of late with double digit growth in Devices entirely offset by volatility in Bioactives. I believe the core business to be robust throughout the cycle and the shares enjoy support from a reasonable yield and ever-present bid rumours.

Please read the important notice on page 2.

CHARLES RAMSAY

LONDON

Born Edinburgh

Lives Farnham, Hampshire

Education Exeter University

Started at JM Finn & Co 2003

Current Position
Investment Director

Interests Golf, Gardening, Fly Fishing

First job Tesco Shelf Stacker

Golf handicap 16

Congratulations on being named in the PAM Top 40 under 40 – what do you think makes your approach to managing clients' portfolios stand out?
Like all investment managers at JM Finn I believe it is important to ensure that the service all clients receive is as personal as possible. Perhaps a difference is that unlike some I get great pleasure in developing spreadsheets to assist in my day to day portfolio management. The combination of our pricing software and Excel provides the ability to access and review a wealth of data about the companies and trusts in which we invest. I also feel comfortable investing in large overseas equities which may offer a more attractive valuation than the UK listed equivalent. Many of the large FTSE 100 listed companies are truly global and I believe that when contemplating an investment you must look at them in comparison to their global peers.

You input into the WMA indices – the industry standard comparators; is your current thinking about markets on a par with your peers?
The WMA indices attempt to reflect the average positioning of firms across the industry and inevitably covers a great range of underlying asset allocations from the very bearish to the very bullish. Whatever your confidence level, there is little doubt that low, let alone negative, bond yields have created a very difficult environment in which to invest and all asset classes appear expensive. I believe it is important to have half an eye on the potential for a market setback; at present however, given the choice between a 10 year bond providing a static and low yield and a well-financed, defensive equity with a progressive dividend yield, I know where my preference lies. Equities are inevitably a more volatile ride however over the long term they have outperformed.

What do you see as the biggest long term threat to the markets?
Debt.....it stimulates growth up to a point and then stifles it. A low interest rate environment has undoubtedly promoted the misallocation of capital and we will only discover how significant this is when rates rise, or demand falls. As ever it is the timing that is the unknown. Financial strength is all important in this environment as a move to rising interest rates could quickly prompt investors to review debt levels and shun those sectors and companies that are treading a fine line.

How have you positioned your discretionary portfolios to account for this, whilst meeting your clients' individual investment objectives?
I have tried to focus on high quality companies with strong balance sheets. For quality I look to companies that have consistently managed to grow revenues, free cash flow and dividends over a sustained period of time. When it comes to balance sheet strength, I try to consider the necessary expenditure such as interest, capital expenditure and dividends versus the underlying cash earnings. I have also gradually increased non-equity weightings through infrastructure funds, strategic bond funds and index linked gilts.

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