JMFinn&Co

PROSPECTS

The JMFinn & Co Investment Newsletter

Fourteen

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CONTENTS

IMPORTANT NOTICE

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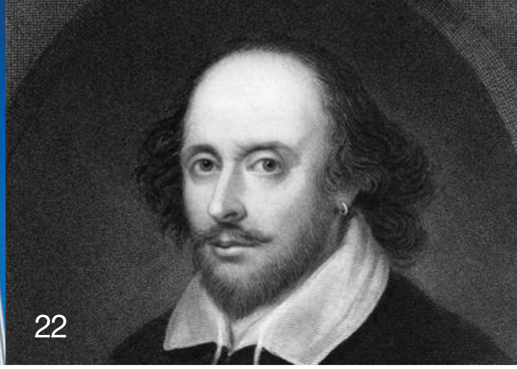
COVER ILLUSTRATION

Jon Berkeley/Debut Art

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



WELCOME

I was asked recently whether we should just sell everything in light of the uncomfortable first quarter we've just experienced, but rather than shut the door after the horse has bolted, I'm always minded to look for the positives, whilst remembering a lesson learnt early in my career: time in the market is often better than timing the market.

The FTSE 100 index has suffered since its high of over 7,100 last year for a variety of reasons, many of which have been hyped up by the usual sensationalist media, the root cause of which, in my opinion, is a huge sell off of the equity markets by the Sovereign Wealth Funds, as a result of the low oil price.

However, amidst the gloomy global macro picture, there are positives which mustn't be overlooked; the falling Pound has been good news for UK stocks who export and overseas investments; interest rates are likely to remain low, somewhat longer than previously expected; and the relative valuation of companies is now below long-term averages.

Even oil at around $30 a barrel, which affects multiple industries, has a positive knock-on effect, with less spend at the pumps creating the potential for an improvement in discretionary consumer spending, despite there being little evidence of this so far. Additionally, it's worth remembering that institutional investors and hedge funds are selling a variety of asset classes and these monies are likely to find their way back to the markets.

So amongst the plethora of bad political and economic news from around the world, including a struggling London residential property market, I'd suggest that not only should investors not sell everything, but the recent sell-off offers a buying opportunity for those investors willing to take at least the medium-term view. And of course, if you are not invested the likelihood is you'll miss the turn when it comes.

Our priority, as ever, is to ensure we retain the service levels for our clients; key to this is providing appropriate support to our investment managers allowing them to stay focussed on events as they occur. Clearly our firm's earnings are directly linked to the stock market and clients' portfolio valuations so we share the anxiety at times like these. At a management level we have to ensure we maintain suitable cost controls, which is tough in an environment when the cost of doing business is on the up, so that we have the necessary resources to continue delivering on our promise of providing a top quality, personalised investment management service.

This edition of Prospects provides some commentary on the possible effects of a Brexit and I would also like to draw readers' attention to the article on page 19 about the recent change in taxation on dividends, which has started to bite already, further compounding investors' plight. Let's hope a change of season brings with it at least a renewed sense of calm.

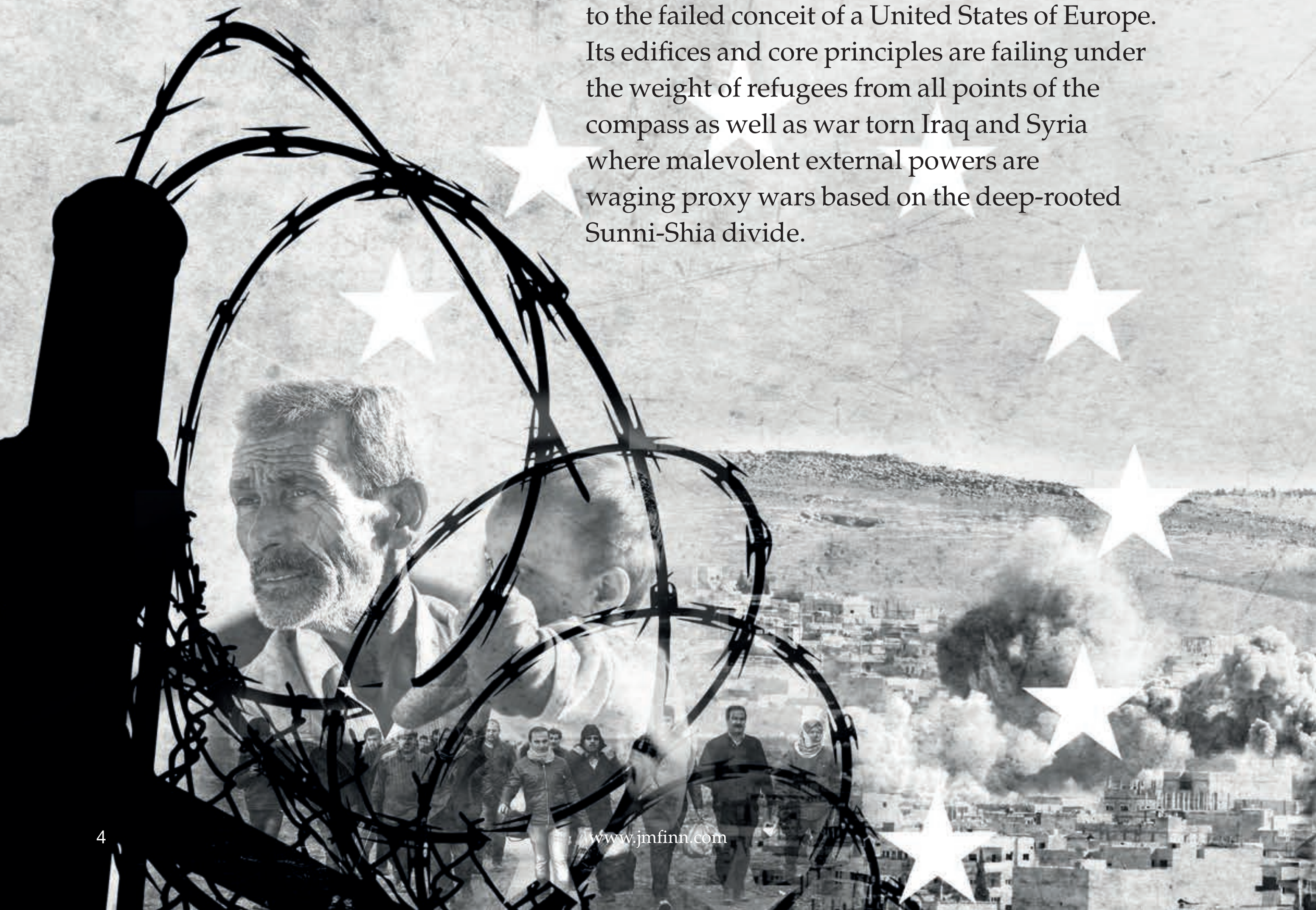
James Edgedale

James Edgedale
Chairman

A CRISIS OF SELF IDENTITY

Geordie Kidston, Head of Research

David Cameron chose to offer the British electorate a vote on their future with a Europe that seems to be rapidly unravelling. Europe itself appears to be groping for an alternative to the failed conceit of a United States of Europe. Its edifices and core principles are failing under the weight of refugees from all points of the compass as well as war torn Iraq and Syria where malevolent external powers are waging proxy wars based on the deep-rooted Sunni-Shia divide.



Some have compared this with the Thirty Years War that raged between Protestants and Catholics in Europe between 1618 and 1648 and which left Germany devastated. With all its sectarian hatreds, no easy solution presents itself to the vortex of violence in the Middle East.

The contemporary world is a multipolar one and so far it has no stable overarching order, as Henry Kissinger has wisely said. China is increasingly encroaching upon the maritime domains of its Asian neighbours, to growing US concern, for Washington will never accept being extruded from the Pacific either. Russia has created a semi-frozen conflict in Ukraine to join those it created in Georgia and Moldova. The very survival of a united Europe looks to be the central question for 2016. With the US increasingly unwilling to fund European defence efforts that themselves show a lack of resolve, it is that bit more difficult to discern a concerted European purpose. Several of Europe's post-communist border states are succumbing to nativist chauvinism as they repel migrants, of whom they have no historical experience, never having been colonial powers themselves. Russia's Putin is using his growing power to disrupt a Europe that cannot decide its own fate.

The very survival of a united Europe looks to be the central question for 2016. With the US increasingly unwilling to fund European defence efforts that themselves show a lack of resolve, it is that bit more difficult to discern a concerted European purpose.

Conflicts over migration have been seen as many parts of Europe resist any central diktat to become multi-ethnic or multi-confessional in character. Tensions have grown in Poland, for instance, since the conservative Catholic Law and Justice party was elected in December, with wider anxieties as they assert control of the courts and media. With the UK solipsistically tied up in Brexit, and France wrapped up in a unilaterally declared "war" on Islamic terror, it has fallen to Germany to maintain the banner of unification. But there Angela Merkel's open armed welcome to migrants has caused bitter divisions, notably after sex-starved migrants ran amok in Cologne and elsewhere.

European problems with Greece may also only be deferred as pension and other structural reforms may yet again put the country on a collision course with its northern creditors. Grexit may also cause beleaguered Finland to seek an exit as its EU membership has caused economic constraints. Brexit would be all the more likely if Grexit were to occur. Last November's terror attacks have made the UK more isolationist, and the timing of the referendum may actually be synchronised with meteorological forecasts from the Aegean and Mediterranean. Cameron may well pull off a Remain majority, but at what price for Conservative party cohesion, for there will be much talk of betrayal? ▶

Already these pressures are seeing the rise of populist parties on both the left and right that share a hostility to free trade, migration, Muslims and globalisation generally.

If Brexit follows, Scotland might decide to leave the UK. This might encourage separatist regions such as Spain's Catalonia to press for independence, with Belgium's government falling shortly, over whether to recognise the new state or not, as the Flemings but not the Walloons wish. The EU's Nordic members might then choose to exit too; risks of disillusionment are rising.

The influx of over one million migrants does little to sustain the future of the Schengen Agreement of 1985, a borderless zone of free travel and trade. Continued migration from large parts of West Asia or Africa leaves open channels for the 20 million or so currently affected and displaced by Islamist violence, civil war, state failure or corruption and plain economic collapse. Already these pressures are seeing the rise of populist parties on both the left and right that share a hostility to free trade, migration, Muslims and globalisation generally.

These pressures are also being seen in the Balkans, the main corridor for mass migration. These areas saw under investment in the post-Communist era and are now reeling under the pressures of the collapsed regimes in Iraq and Syria.

Europe had hoped that its idealistic free market, humanitarian values and social welfare-based culture would have underpinned these newer members and been a beacon to the wider world. However, one can see that following the Cold War, Russia is now able to destabilise the region with its incursion into Crimea and Ukraine. Russia is no longer an institutionally weak state as it was in the post-Soviet era and the US is no longer the sole hegemon as it was after 1989–90. The strongman Putin is not without his admirers among both left and right populists and separatists in Europe either.

At a time when European ideals are floundering, Europe itself clearly needs greater cooperation, integration, risk sharing and sense of common purpose. Instead it appears to be embracing nationalism, Balkanisation, divergence and disintegration.

I am sure that David Cameron wants to stay in Europe. But maybe the referendum was unnecessary, except by the lights of narrow Tory party concerns? We are being asked to vote on the merits or demerits of membership of an entity that seems to be disintegrating, and that may occur much faster if Britain leaves.

Understanding finance

INDEX-LINKED GILTS

John Royden, Head of Fixed Income Research

Index-linked gilts, or "Linkers", are sold by the Debt Management Office (DMO) on behalf of the UK government and have both the coupon and the capital elements linked to inflation.

I'll use the following Linker as an example: 1.25% of 2032 index-linked Gilt. If this were a conventional Gilt, this would pay the holder 1.25% interest (or coupon) of the issue price (or par) until 2032, when the redemption value would normally be the same as the issue price.

A Linker has both the coupon and redemption value linked to inflation, so using the above example, if it was issued at £100 and inflation was 5%, the redemption value increases to £105 and the coupon, which is paid twice yearly, would be £0.656 ((1.25% /2) * 1.05).

The measure of inflation used is the Retail Price Index, or RPI, which is typically 1% per annum more than the Consumer Price Index, or CPI. RPI is thought to be a better measure of the inflation that we actually experience living in the UK. With the main difference being that the CPI excludes house related costs, such as mortgages and council tax and the way that they get calculated. For those with a stronger understanding of maths, the CPI's calculation is more geometric than the RPI.

A point to note about Linkers and contrary to often quoted opinion, index-linked bonds can mature below par if you suffer from deflation. Likewise, deflation can push the coupon to less than the original nominal amount.

The price at which you can trade linkers is primarily driven by two factors: a) future expectations of inflation and (b) future expectations of interest rates. Investor demand, or lack of it, may have a short term effect on price as well.

Equity prospects

SHAFTESBURY

Geordie Kidston, Head of Research

PRICE
£8.58

52 WEEK HIGH-LOW
£9.75 – £7.80

NET YIELD
1.6%

HIST/PROS PER
5.1 – 59.8

EQUITY MARKET CAP
£2,366m

Shaftesbury represents a unique cluster of London based retail assets, backed by extremely high management ability within this sector and locality. As the company highlights, this collection of assets is irreplaceable. Shaftesbury duly re-rated strongly over 2014, outstripping most analysts' expectations of yield compression. The good news continued throughout 2015, culminating in full year results which revealed Net Asset Value growth of +22% for the year mainly driven by an +18% increase in capital value. Shaftesbury capitalised on these favourable markets with like-for-like rental income growth of +9%. These positive trends have continued into 2016 with footfall driving demand which in turn is generating rental growth. Shaftesbury's impressive growth and yield compression reflects the very strong consumer environment in London's West End. Despite the ongoing tight letting background for retail, the trading performance implies peak cycle conditions, with no material room for any bad trading news. I am cautious on the property sector as a whole, given the nature of the shallow interest rate cycle. I acknowledge the unique characteristics at play here but highlight the inherent medium term risks.

Please read the important notice on page 2.

THE CHANGING SHAPE OF EUROPEAN STATE SECURITY

Michael Burleigh

The world seems very bleak at present, and that only includes the threats that are known. Vladimir Putin has used covert 'hybrid' force to seize Crimea and eastern Ukraine, and unarmed means, including energy policy, the media, and funding political clients, to subvert European unity.

This should not be a major surprise to us since the West used exactly these 'hybrid' methods from Cuba via Iran to the Philippines to subvert governments throughout the Cold War. But Russia's resentful kleptocrat secret policemen are not our only problem. Europe faces a major internal threat from Islamist terrorism, edging nearer now that ISIS has relocated fighters from Syria and Iraq to Libya, about 120 miles south of Lampedusa.

Many of the 3,000 ISIS fighters are recruited from the adjacent Sahel states or sub-Saharan Africa where Nigeria's Boko Haram is affiliated with ISIS. Across Africa, thanks to proselytism by Saudi Arabia's Islamic University of Medina, a benign Sufism that incorporated traditional animist beliefs and which joshed along with Christians, has been supplanted by hardcore Wahhabism, from which it is a small leap to violent jihadism. Sub-Saharan Africa's Muslim population of 250 million is projected to grow by 60% in the next three decades, and if Islamist-inspired war zones proliferate, many of them will seek to come to Europe.

In this bleak world, Europeans should not assume that the US Cavalry will ride to their rescue. Failed foreign wars, a growing non-European demographic, and a long-term strategic decision to 'pivot' towards Asia-Pacific to prevent Chinese domination, mean that regardless of who is in the White House after November, US attention has migrated elsewhere.

A US military, whose much reduced budget of $580 billion is equivalent to that of the next fifteen largest nations combined, will indeed still respond to invocations of NATO's Article 5, up to and including use of the nuclear deterrent. But America expects Europe to get serious about defence expenditure (only Britain and Greece currently meet the 2% of GDP decennial aspiration proclaimed in 2014 at the Newport Summit), and to derive a proper bang for its buck. While the US can deploy 200,000 troops from the 1.1 million total under arms, Europe's 1.5 million uniformed personnel can only muster 60,000 for expeditionary operations, and as we saw in Libya in 2011, they would depend on US surveillance flights, air-to-air refueling and stocks of precision munitions.

Although the freedom of Europe remains a vital US interest, Washington expects its European allies to either defuse or deal with security crises, not just on their immediate peripheries (from the Balkans to North Africa) but on the peripheries of the peripheries. Potentially this means deep Africa as well as the Gulf or Caucasus. France is the most active power, with ground interventions in Mali (2013) and the Central African Republic (2014), as well as a ferocious bombardment of ISIS in Syria.

France is the most active power, with ground interventions in Mali and the Central African Republic, as well as a ferocious bombardment of ISIS in Syria.

For years, Europe has also taken the lead in Operation Atalanta against Somali pirates. But these operations do not indicate the actual and potential scale of European defence cooperation, routinely travestied in Britain via Jean-Claude Juncker's daydream of a "European Army", odd coming from the former PM of a country that has no national strategy document. ▶

Not all our European partners regard NATO as a good fit – Finland, Ireland and Sweden come to mind. It was the UK and France which pushed through the 1998 EU Common Security and Defence Policy to help devise a coherent EU grand strategy, even though the UK subsequently cooled on the project, opting instead for closer ties with the robust French.

the Framework Nations Concept. Smaller countries cluster around Germany (logistics), Britain (high intensity expeditions) and Italy (stabilization and reconstruction). In addition, the Belgian and Dutch navies have virtually merged, while the Dutch and German armies have a common Corps based at Münster. As in the case of all such initiatives, this is complementary

Canberra's finest was doubtless vital to spying on North Vietnam, it is far from certain whether it is helpful in knowing what jihadists in Amsterdam, Brussels or Milan are plotting. The first director of the recently re-launched Europol, which gathers information on organized crime and terrorism is Robert Wainwright, a British former MI5 intelligence analyst.

> There is a European Defence Agency, whose purpose is to develop costly projects like drones, heavy lift and air refueling tankers, which declining national defence budgets no longer make cost effective for 'national champion' defence contractors

Likewise, there is a European Defence Agency, whose purpose is to develop costly projects like drones, heavy lift and air refueling tankers, which declining national defence budgets no longer make cost effective for 'national champion' defence contractors. Tie-ups between Dassault, EADS and Finmeccanica will produce the Euro drone, while France's Nexter and Germany's Krauss-Maffei-Wegman will synthesize the best features of their rival tanks.

But more is afoot than eliminating the proverbial corrupt inefficiencies in this sector. European nations adopted a NATO proposal called

rather than competitive with NATO, and in reality is at its disposition in a crisis. While NATO will endure as the ultimate safeguard of our security, something resembling the polyglot armed coalitions of the 18th century are having a comeback.

The British always stress the paramountcy of their "Five Eyes" signals intelligence alliance with the US, Canada, Australia and New Zealand. Sometimes there is talk of this evolving into 6, 9 or 14 eyes, but the US's National Security Agency's refusal not to spy on, say, France or Germany, has proved an obstacle. While the cooperation of

NATO will continue as the ultimate guarantor of our security, and will organize many military operations, but forget the dimwitted clichés about Italians being cowards and hippy Dutch troops who say "Hoi' without a salute (in reality it is the fearsome Germans who are most loath to fly at night and whose equipment is falling apart) and get used to us fighting alongside our 27 EU partners.

Michael Burleigh
CEO, Sea Change Partners LLP

PEER **TO** PEER **LENDING**

In the current low yield environment, some investors have been looking for an alternative. Here, John Royden, Head of Fixed Income Research at JM Finn & Co, explores the growing online P2P market.

Peer to Peer (or P2P) lending is a fast–growing alternative finance practice of lending money to individuals and/or businesses via an online platform that matches lenders directly with borrowers. Attracted by yields higher than most conventional high quality bonds, it has sparked the imagination of many an investor.

I invested small sums with four of the leading UK P2P websites to get a taste: Funding Circle, RateSetter, Wellesley and Zopa. At the outset I was struck by the lack of clarity over the bid / offer spread, thus rendering it unclear what margin the P2P lenders were making; Zopa was the only platform that showed a tight bid / offer spread of 3.8% to 3.9% for three year money and 4.8% to 5% for five year money.

Some of the P2P websites appeared to be offering amortising loans where your cashflow is driven by interest, plus monthly repayment of capital, whereas others appeared to be interest only loans with a repayment of capital at the end of the term. This does make comparing the rates more difficult.

If you want to sell your loans early, then the P2P websites achieve this by selling your loans to new investors, which is by no means guaranteed and exiting loans can sometimes take days, with varying levels of early exit fees charged. If interest rates go up and the value of your loan goes down, you get charged a fee, but you don't get a credit if the opposite occurs.

Zopa and RateSetter both have default funds which compensate investors for defaults by lenders. So far they have covered defaults, but in the event of a large-scale default my main concern across the sector is that they might fail.

The best measure of success in my opinion would be looking at default statistics, but unfortunately, these cover a benign period of economic stability from the 2009 lows of the previous recession. If the current stock market weakness is foretelling another recession, I doubt that the statistics of the past will match what could be about to come.

My main concern is that the lack of transparency means that rates being offered to investors don't reflect the underlying risk. If you earn 10% for five years and then lose 40% on defaults in a recession, you are up a net 10%. But if you only get paid 5% for five years and lose 40%, you are down 15%.

The Armageddon scenario is a tsunami of tweets and Facebook status updates which act to crystallise a mass default by borrowers; which then bankrupts the P2P websites and leaves them unable to finance recovery litigation.

More than 1 million people in the UK invested, donated or lent using P2P lending or crowdfunding platforms in 2015

Source: Nesta, Cambridge University & KPMG

I think successful P2P lending requires plenty of time and some expertise in risk pricing and the ability to control your lending on a case by case basis. In addition, the lack of clarity and transparency suggests care should be taken to ensure you understand the risks in their entirety. It is also worth noting, that whilst the peer-to-peer industry adheres to standards set by the Financial Conduct Authority (FCA), depositors do not qualify for protection from the Financial Services Compensation Scheme (FSCS).

SHOULD WE STAY OR SHOULD WE GO?

It is a once in a lifetime opportunity and one that will dominate the news until the summer. With MPs, business and commentators seemingly split on which way to vote, we asked economist Neil MacKinnon to sum up his thoughts.

So the 23rd of June is the date for the Brexit referendum. The Prime Minister, David Cameron, has concluded a deal with the EU that, although not a "game-changer" in terms of Treaty revisions, it is certainly non-trivial in that the concessions go a long way to protecting the UK's financial services industry. There are also important concessions in ensuring that the UK is not on the hook for any future

Eurozone bail-outs. As such, it would be premature to play down the significance of the Prime Minister's deal as it may well mark the peak in the process of EU political and economic integration. Over the last 50 years, EU leaders and policy-makers have used periodic crises to strengthen the integration process but now the situation is less clear. It is interesting to observe that other EU countries are now looking to seek UK-style opt-outs and special treatment. This threatens to fracture any "progress" in terms of further EU integration. As it is, the tortuous negotiations recently involving the Prime Minister and 27 other heads of state show how cumbersome and bureaucratic reaching any sort of deal can become.

The surge in capital flows from the "north" to the "south" at the inception of monetary union sowed the seeds of the eventual Eurozone banking crisis and exposed the imbalances between the core and periphery.

The debate in the run-up to the Brexit referendum is certainly hotting up. The "in" camp argue that being outside of the EU would threaten the economy resulting in damage to trade, investment and jobs. It would be the proverbial "leap in the dark" so best to stay in the EU, the argument goes, and work to ensure progress towards a reformed EU. The "out" camp insist that far from being apocalyptic, leaving the EU would take back political and economic control of the country and free it from excessive EU regulation and the primacy of EU law. The "out" camp argue that the Eurozone has hardly been an economic success story and since the inception of monetary union the main economic features have been a double-digit unemployment rate, anaemic economic growth and fiscal austerity. Even prior to the onset of monetary union, many academic economists, especially from the US, argued that the Eurozone was not an "optimal currency area" and was entirely unsuited to a "one-size-fits-all" interest rate policy.

The surge in capital flows from the "north" to the "south" at the inception of monetary union sowed the seeds of the eventual Eurozone banking crisis and exposed the imbalances between the core and periphery. The end-result was a bail-out of the French and German banks who had lent to the periphery and financed an unsustainable debt bubble in countries like Greece. For every reckless borrower, there is also a reckless lender. These increasingly periodic debt and banking crises, which compelled the European Central Bank to adopt Quantitative Easing, and negative interest rates has created a division between the core and periphery and between creditor and debtors.

In addition, many economists have pointed out the design flaws in monetary union which increasingly looks eerily reminiscent of how the 1930's Gold Standard operated.

Germany, as the leading creditor and surplus economy, continues to pursue a policy of balanced budgets but is not helping to facilitate the adjustment process for debtor and deficit economies. The upshot is that Germany now has a current account surplus that amounts to 7% of GDP, three times the size of China and a major imbalance in the global economy. The periphery has had to endure so-called "internal devaluations" which have crimped domestic demand and deflated the economy. This is not a recipe for a healthy economic system.

It also has to be said that a key feature of the global economy over the last 10 to 15 years has been a shift in the centre of economic gravity from west to east. Beijing is where it's at, not Brussels. The challenge for the EU is to transform itself into a much more vibrant economic system that can keep pace with China. Emerging markets now account for 60% of global GDP and have contributed to a significant part of global economic growth in recent years. Is the EU capable of serious reform or, as the migrant crisis makes clear, does the EU start to crumble?

The rise of anti-euro political parties throughout the EU threatens to radicalise the political landscape especially bearing in mind the French and German elections in 2017. But as of now all eyes are on the Brexit referendum.

The opinion polls and bookies' odds appear to favour the "in" vote. UK voters, as much as they are uncomfortable with the EU, may decide to stick with the status quo. The interesting issue is that an "in" vote does not necessarily let the EU off the hook. Without reform the EU may wither on the vine and just become increasingly irrelevant in a changing global economy.

Neil MacKinnon is global macro strategist at VTB Capital in London. He is a founding supporter of the Vote Leave campaign and a co-author of Business for Britain's Campaign or Go economic assessment.

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

Theo Wyld, Research Analyst

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
Croda International

CONSUMER GOODS
Diageo, PZ Cussons, Victoria Plc

CONSUMER SERVICES
Compass, J Sainsbury

FINANCIALS
Big Yellow Group, Lloyds Banking Group, LondonMetric Property, Market Tech Holdings, NewRiver Retail

HEALTHCARE
Genus, Smith & Nephew

INDUSTRIALS
Alumasc, Avon Rubber, Berendsen, Porvair, Ricardo, Smiths Group, WS Atkins

OIL & GAS
Premier Oil

BERENDSEN

PRICE: £11.29
52 WEEK HIGH-LOW: £11.59 – £9.46
NET YIELD: 2.6%
HIST/PROS PER: 22.6 – 19.5
EQUITY MARKET CAP: £1,993m

INDUSTRIALS
Kevin Quinn, CFO

Berendsen is engaged in the laundering and maintenance of textiles and provides service solutions for sourcing, cleaning and maintenance. These textiles range from high-visibility workwear, to floor mats, to hospital linen. Customers are primarily based in the UK, Germany and Scandinavia.

The main story for Berendsen of late has been the implementation of its so-called 'best practices', originating in the Nordics, into their laundry businesses across Germany and the UK. The new processes, given the catchy name of the 'CL2000 system', essentially involves moving from the traditional model where each staff member is wedded to a specific task, to small groups of teams responsible for delivering on an order from start to finish. This encompasses everything from deciding when garments are beyond repair and replacing such items from either stock or ordering, to folding the sheets whilst still warm to avoid creases. This change has given the employees more independence, variety and sense of completion than their previously repetitive roles, driving an uplift in morale and subsequently productivity.

As well as productivity gains, there has been consistent improvement in the quality of textiles delivered to customers and volume capacity. Circa 40% of the Company's EBIT comes from the Workwear division, where the CL2000 roll-out is taking place, and therefore these margin improvements have a marked effect on the overall profitability of Berendsen.

The company is seeking to take market share from independents, which make up 45% of their £6.8bn addressable market. In addition, they are looking under-geared at 1.1x Net Debt/EBITDA, which leaves room for potentially accretive acquisitions and/or share buybacks in the short-term.

PZ CUSSONS

PRICE: £2.59
52 WEEK HIGH-LOW: £3.76 – £2.40
NET YIELD: 3.1%
HIST/PROS PER: 20.4 – 15.2
EQUITY MARKET CAP: £1,108m

CONSUMER GOODS

Alex Kanellis, CEO and Brandon Leigh, CFO

The previous edition of Prospects featured PZ Cussons as the Stock in Focus. Since publication, Alex Kanellis (CEO) and Brandon Leigh (CFO) were kind enough to sacrifice a morning and walk myself and a colleague around their innovation centre in Manchester.

The first topic of conversation was the ongoing currency pressures in Nigeria. Roughly 95% of the US Dollar supply in Nigeria comes from oil and, crudely speaking, the drop in the oil price has shrunk this supply by 90%. The official rate has remained at circa 200 NGN throughout, whilst the parallel rate (what you would expect to pay on the street) has moved up to nearer 300 NGN. It is this dichotomy that is putting increasing pressure on the government to devalue the currency. PZ Cusson's willingness to inventory hedge at the parallel rate and worse has been the main driver behind their outperformance of late, relative to peers importing into Nigeria.

PZ Cusson's inability to outspend the likes of Unilever has meant they have looked to product innovation and turnover to gain market share. The dangers with this strategy include product cannibalisation, inventory management, efficient distribution; all of which must be managed carefully. It became clear throughout the morning how they are able to be so nimble.

The state-of-the-art innovation centre contains every stage of the manufacturing process; from an in-house perfumery to all but fully automated production lines. The constant flow of new products created on the back of incipient market trends, when coupled with a production facility working off four hour inventory and minimal downtime, makes for a flexible and efficient supply chain.

SMITHS GROUP

PRICE: £9.73
52 WEEK HIGH-LOW: £12.43 – £8.58
NET YIELD: 4.2%
HIST/PROS PER: 15.6 – 12.9
EQUITY MARKET CAP: £3,842m

INDUSTRIALS

Andrew Lappin, Director of Government Relations

Smiths Group is a holding company that owns a selection of industrial businesses each operating with reasonable autonomy. The largest business is John Crane, which supplies products and services to the energy sector. Smiths Medical sells specialist devices into the healthcare sector and Smiths Detection, Interconnect and Flex-Tek make up the remaining c.30% of Group earnings.

John Crane, is suffering from the downturn in oil and gas expenditure. However, the business is focussed primarily on the downstream aftermarket which positions the Group towards the healthier end of the troubled sector. A potential silver lining for John Crane is that the end demand for gasoline and distillates is still growing implying the refineries can not hold back on maintenance and repair spend for any prolonged period.

The Medical business is largely stable at present. A forced product withdrawal from a competitor bolstered sales last year but it is expected that the division will revert to more normal levels of moderate underlying growth in 2016. There have been two failed efforts in recent times to dispose of this asset in a consolidating sector. Whether a third attempt is made or not, the new management will have to dedicate significant time to stabilise returns and cut costs.

Elsewhere in the Group, Detection remains troublesome as the four global players vie for market share and Interconnect was impacted by a large order deferral by Apple. However, Flex-Tek, the lead supplier of specialist hosing, has remained resilient and boasts a solid order book. Smiths Group remains a true conglomerate and the new management will have to evaluate whether it is worth more than the sum of its parts.

Please read the important notice on page 2.

THE PURSUIT OF ALL WEATHER INVESTING

Arabella Cecil, Chief Investment Officer

BACIT Limited is an investment trust with two very specific aims: to deliver superior investment returns via a multi-manager approach to long-only and alternative investing and, secondly, to contribute to the UK's leading research centre into cancer treatments, the Institute of Cancer Research. Here Arabella Cecil explains why an alternative approach to investing might be considered in today's disrupted markets.

The recent histories of the FTSE 100 and the FTSE All Share eloquently describe the challenges facing investors. Investing in these indices just over 16 years ago on 1st January 2000 would have generated a compound return, including dividends, of less than 2.5% in the case of the FTSE 100 and just under 4% for the All Share.

In our experience, inflation in investors' cost of living runs substantially higher than RPI, but even if we accept RPI as a valid factor of purchasing power, an investment in the FTSE100 would still have eroded during that time. The FTSE All Share would have fared better, but still compounded below 2% per annum. And all of this after seven years of QE, and before fees and tax.

Asset allocation, for us, is driven by the opportunities that present themselves, rather than a pre-determined set of weightings. So whilst we approach investing globally, BACIT's investments are not proportionate to any independent metric of global activity, such as GDP or size of equity market. They are rather a balanced and risk-adjusted representation of the most attractive opportunities we believe we have encountered to date, given the medium-term horizon. We currently see opportunity in areas as diverse as relative value commodities, interest rates, foreign exchange, tech venture capital, and infrastructure investing. Each of these has its own idiosyncratic drivers which should allow it to perform on a trajectory uncorrelated to equity markets.

Which brings us to perhaps the greatest challenge facing investors who value the security of regulated listed markets: that so much of the growth of this 'new economy' is taking place in unlisted companies, and destabilising the listed companies that tend to represent the incumbent industries. One of the most visible examples is in power generation, where coal-fuelled power is being replaced by solar and wind. The problem for investors is two-fold. Firstly that the former are well represented by listed companies, but most of

THE INSTITUTE OF CANCER RESEARCH

The Institute of Cancer Research, London, is one of the world's most influential cancer research institutes, with an outstanding record of achievement dating back more than 100 years. Today, the ICR is ranked as the UK's leading academic research centre, and leads the world in isolating cancer-related genes and discovering new targeted drugs for personalised cancer treatment. The ICR employs leading scientists from over 50 countries around the world. Since 2005 alone, 16 drug development candidates have been discovered based on ICR research, 6 of which have progressed to phase 1 clinical trials. The ICR has charitable status and relies on support from partner organisations, charities and donors to fund its research and innovation.

the latter are not; and secondly the rate of growth of these new technologies. The thing about exponential growth is that when you're at 1% you're halfway to 100%. For an industry doubling each year it takes less than seven years to grow from 1% penetration to market saturation.

The level of innovation, driven by the explosion in data processing power seen in the last few decades, is materialising in a series of parallel digital revolutions in medicine (genetics), energy (alternatives) and technology. The resultant increase in the quality of life for so many people simultaneously, was perhaps last seen in the West in the early 20th Century.

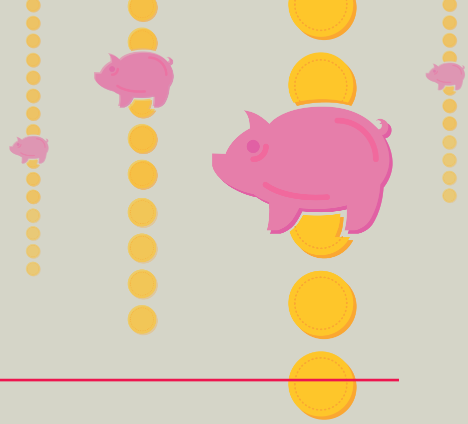
Finally, the secondary impacts of these mini-revolutions are as yet unknown, but will be significant: evidence the oil price collapse seen over the last eighteen months, effectively a global fiscal stimulus worth around $1.5tn to the world's consumers, or 2% of global GDP. There are far fewer oil producing than oil-consuming countries, and many of these producers rely heavily on oil revenues to fund programmes that maintain regional stability. These factors have contributed to the geopolitical instability that has burgeoned in the last three years. The continuing EU crisis, the aftermath of the Arab Spring in the Middle East and Europe, and the posturing of World Powers in the South China Seas all remain tail risks for now, but the scope for a policy mistake has grown significantly.

The opportunity set is now far richer than is typical at this advanced stage in the conventional economic cycle, but taking advantage of these opportunities is only possible by embracing short-selling within your investment strategy as investors cannot buy into unlisted companies. Developed, liquid equity markets remain an attractive way to play both long and short opportunities and we look for fund managers who exercise greater control over the destination of their portfolios by the use of shock-absorption and shock-evasion: a margin for error has a value, as does the option to change your mind, and given a landscape that is dominated by disruption, the ability to short has come into its own.

BACIT

BACIT gives 1% each year to charitable causes: 0.5% to the ICR and 0.5% to the BACIT Foundation. BACIT also has the ability to invest up to 1% of NAV each year in early oncology drug discovery candidates and med tech opportunities. To this end BACIT has committed £20m to the CRT Pioneer Fund, a joint venture with Cancer Research UK.

CAN NEGATIVE INTEREST RATES WORK?



John Royden, Head of Fixed Income Research

Andy Haldane, Chief Economist of the Bank of England, has recently flagged the real possibility of a negative interest rate strategy. John Royden, Head of Fixed Income Research, explores what this really means for the economy.

Negative rates are effectively a tax on deposits, and as such are intrinsically contractionary and therefore a form of financial repression. The starting and simplistic view on negative interest rates is that it discourages bank deposits and encourages people and companies to invest or spend their money; and that gets the economy going again.

At the same time however, it encourages banks to lend their money rather than deposit it at a cost, which also helps get the economy going. And if savers move their money to another currency which actually pays a credit rate of interest, then your currency falls and that helps exports……which generally gets the economy going.

This starting premise ignores the fact that the clearing mechanism for borrowers and savers is banks. Bank profitability is substantially driven by their Net Interest Margin, or NIM. In normal circumstances a bank might pay, for example, 3% on deposits and lend money at 7%, so earning a 4% NIM. If a bank's Central Bank charges them for deposits (negative 0.5% for example), or lends them money at 0.1%, then that means that banks should really quote their clients something like -2% on deposits and 2% for borrowing; thus preserving their NIM of 4%.

The trouble is that depositors don't like being charged for their deposits, so retail investors might hide their cash under the mattress or buy other interest bearing instruments, such as bonds. If banks then have to move their rates to 0% for depositors to stop them leaving and 2% for borrowers, then their NIM has shrunk to 2%, their revenue halves and their profits probably disappear. If a bank needs a NIM of 4% to make a profit after provisions for bad debts then you could find that a NIM of 2% means the bank is losing money after provisions; so it just stops banking.

So one conclusion you could reach is that negative interest rates might cause lending to shrink, when the whole idea designed to do exactly the opposite.

So if negative interest rates are fraught with problems, what are the alternatives? One option is "helicopter money" which involves metaphorically throwing newly printed money out of a helicopter, in the hope that people will spend it. In my opinion, a better way would be to reduce taxes, which encourages people to work, rather than hang around waiting for passing helicopters.

The trouble is that the more wily of us realise that less taxes means unbalanced government books, which in turn means more government borrowing, leading to more government debt to be paid back (from the people via higher taxes eventually); this actually encourages us to save to pay off the future debt, rather than spend the cash.

So as long as banks choose to absorb the tax that is negative interest rates themselves, it can work; but if banks choose to pass that tax on, it will be savers and borrowers who end up paying. I cannot see that the increased economic activity that negative interest rates may generate will be sufficient to offset the effect of this tax.

Alternatively, if we think of negative rates as a monetary operation rather than a tax, we can say that the central banks drain back a small proportion of the reserves they add to the system through Quantitative Easing, which is effectively monetary tightening. Again, I question the benefit of this, leaving me unconvinced that negative interest rates are the right course of action.

TAXATION ON DIVIDENDS

As covered in the autumn issue of Prospects, the Government has brought in sweeping changes to the taxation of dividends, which take effect in the new tax year, which starts on the 6th April 2016.

These changes mean that anyone receiving annual dividends in excess of £5,000 will be liable to this tax, which is payable via your annual tax return. The key points are as follows:

- The government will abolish the Dividend Tax Credit from April 2016 and introduce a new Dividend Tax Allowance of £5,000 a year.

- The new rates of tax on dividend income above the allowance will be 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers.

Some clients of JM Finn & Co may have noticed this change already in your Investment Portfolio Reports, as UK dividends payable after the 5th April are already being announced in their gross form, to reflect the removal of the 10% tax credit. This can result, in some cases, in a reduced “gross income” figure quoted in your report. However, it is important to note, the actual cash amount of the dividend received will not change, it is only the tax treatment which changes.

There has been no change to the tax treatment on interest payments for Bonds and Bond Funds.

To discuss any aspect of your Investment Portfolio Reports, please contact your investment manager, however, JM Finn & Co is not permitted to give individual advice regarding taxation and therefore we would encourage you to seek specialist tax advice in relation to your own personal circumstances if you have any queries regarding the taxation on dividends.

AMEC FOSTER WHEELER

Geordie Kidston, Head of Research

PRICE
£3.49

52 WEEK HIGH-LOW
£10.03 – £3.21

NET YIELD
12.7%

HIST/PROS PER
11.3 – 5.8

EQUITY MARKET CAP
£1,330m

Amec made the major acquisition of US peer, Foster Wheeler in 2014. This effectively doubled Amec’s global scale, mainly in downstream oil services and onshore US. The timing of this deal was unfortunate, with the oil price collapsing upon completion. Amec’s equity value has been similarly weak with cash flow issues now seeing a cut in the dividend of 50% for 2016. Service companies are struggling on the back of producers continuing to announce deep cuts. It still appears that the acquisition was strategically pragmatic, improving both customer offering and barriers to entry. Our concerns over the balance sheet are somewhat protected by the dividend reduction which appears a prudent re-basing. I am concerned that an extended cycle, coupled with refinancing difficulties, will result in a rights issue. The market is pricing in this re-financing risk and that a bolstered balance sheet will, in time, allow the group's operations to participate in any recovery. Amec is a high quality operator suffering concerted attrition in several areas of operation. With some re-financing expected, progress may have to wait until we see either a supply cut from OPEC or a supply/demand rebalancing.

Please read the important notice on page 2.

Diageo is a major international distributor of spirits and a significant brewer of beer, primarily Guinness. It has a strong international distribution capacity and brand profile. Premium spirits are under-penetrated globally and Diageo should deliver secure and consistent growth as the world continues to shift from locally sourced spirits to Western style liquors.

Geordie Kidston, Head of Research

As has been experienced in post-war Japanese society for instance, rapidly Westernising societies have an established tendency to alter their drinking patterns towards established Western brands. Considering the fragmented and localised drinking patterns seen in China, this could prove, in my opinion, lucrative and exciting.

Diageo holds sway over some of the world's strongest brands in key categories of premium spirits. For instance, Johnnie Walker whisky is nearly 150 years old with a high aspirational positioning in the minds of many new consumers. This type of pricing and distribution mechanism is powerful, allowing Diageo to establish an escalating price architecture of products that Emerging Market demand has fed into. Globalisation and the emergence of middle class societies off the maturing wage structures in Asia and Latin America have driven this trend.

It is true that localised economic and corruption measures have interrupted the process recently in China but, longer term, the pricing, penetration and demand for branded Western liquor could be a growth dynamic.

Internationally, the ongoing demand for brown spirits, such as Scotch whisky or North American whiskey/bourbon, is proven. The sector has seen regular consolidation in recent decades and management teams clearly have to plan around long term demographic and social change. Diageo's brand positioning in key categories is important. It has an array of specialist whiskies beyond Johnnie Walker, spanning all aspirant price points. In vodka, it produces the key Smirnoff brand, a high volume seller, and in dark rum, Diageo markets the fast growing Captain Morgan brand, often towards a more youthful demographic. In liqueurs, it owns Baileys and in Canadian whisky, Crown Royal. Within the other major British export category of gin, the group owns Gordons and the super-premium Tanqueray. All of this is supplemented by the somewhat anomalous, historic ownership of the Guinness stout brand. This asset is important and has been subject to speculation that might thrive more and release value if spun out or sold off. The historic links of Empire-based distribution networks for Guinness into Africa are important. This under-developed market place has notoriously poor distribution infrastructure and the Guinness legacy presence is an important and valuable entry point into this vast and early stage market.

Innovation in brand structures and launches plays an important role in developing and growing an international drinks presence. Variants on traditional formats are regularly tested, with flavours for whiskeys and vodkas being seen in such categories as black cherry, vanilla and green apple, all exploring volume growth opportunities among new customer bases. Size availability is also a factor with African consumers being introduced to leading brands through smaller 20cl bottles or cheaper blends. Diageo has also extended its international distribution presence by acquisition, with Mey Icki in Turkey and Ypioca in Brazil being recent examples that leverage its international distribution structure into new growth markets.

> The sector has seen regular consolidation in recent decades and management teams clearly have to plan around long term demographic and social change.

In India, Diageo has a dominant and important network, gained through its shareholding in United Spirits. India is a generation behind China and recent reform patterns underwrite strong long term growth patterns in this major market as its democratic base develops. This market is one where culturally Diageo has an important presence and aspirational drinking volumes and demand patterns are already well established.

Many aspects of Diageo's business mix underwrite its long term growth. However, lacklustre volume delivery and a somewhat cluttered corporate structure leave Diageo's senior management under pressure to perform. The hiatus of demand in the Chinese market has seen growth momentum stall in the short term. Speculation that the acquisitive Brazilian brewing interests of the fast-growing 3G, might be interested in Guinness and have underwritten share price performance in recent months. Finally the historic link between Diageo and LVMH over purchase options on the mutual Moet Hennessy stake could see a resolution, with either a disposal of this valuable asset or a move, albeit at eye-watering levels, to enter the international champagne and cognac arena. At some stage, investors will expect a management decision here.

Diageo represents a fundamentally important example of under-leveraged distribution. Interruptions to global growth aside, these assets and their management are under long term pressure to deliver growth off this proven and defensive growth category.

DIAGEO

PRICE
£18.28

52 WEEK HIGH-LOW
£19.79 – £15.92

NET YIELD
3.1%

HIST/PROS PER
18.9 – 21.2

EQUITY MARKET CAP
£47,108m

Geordie Kidston is a beneficial owner of Diageo

Please read the important notice on page 2.

SHAKESPEARE'S 400 years

This year marks the 400th anniversary of William Shakespeare's death – an event that will be celebrated across the country. Tei Williams, of Propeller, an award-winning, all-male Shakespeare company which seeks to find a more engaging way of expressing Shakespeare, reviews the variety of celebrations of the world's greatest playwright.

Tei Williams, Propeller

Who was Shakespeare? We know little of his background and much of what we do know is a cause of debate. He was born in Stratford in 1564, and he died 23 April 1616, making this year the 400th anniversary of his death. William was the third of eight children but his schooling is a mystery with no record of his attending university. He married Anne Hathaway in 1582 but then is lost to history for several years until he pitched up in London as an established actor and playwright. Described in a pamphlet of the time as an 'upstart crow' by playwright Robert Greene, it seems there was much jealousy of his talent, a feeling that he should not be compared to established writers like Christopher Marlow and Greene himself.

It is thought his career started in the mid-1580s, and certainly after 1594 his plays were only performed by the Lord Chamberlain's Men, soon to be the leading company in the capital (and after Queen Elizabeth I's death known as The Kings Men). As a part-owner Shakespeare was a member of the consortium that in 1599 built The Globe on the south bank of the Thames. That shrewd move into part-ownership made Shakespeare a wealthy man, now able to purchase the second largest house in Stratford, New Place, dividing his time between it and London.

By the 1590s, although Shakespeare's success meant his name was to be found on the title page, he was still acting in his and other's work. His canon consists of 37 plays, 154 sonnets and two long narrative poems. Though some think his authorship questionable, there is no doubt that his work has been translated into every major language and performed more than any other playwright, living or dead.

Shakespeare died in Stratford, one month after signing his will which stated he was in 'perfect health'. The reason for his demise, at 52, is not known, though there were accounts of his succumbing to a fever following a drinking session. Buried in Holy Trinity Church, Stratford-upon-Avon there are numerous memorials to his talent around the country, including Poet's Corner in Westminster Abbey.

Ben Jonson, a Shakespeare contemporary, saw something in his work that led him to write a most prophetic statement, 'He was not of an age, but for all time!' His appeal endures to this day for several reasons; he wrote great stories that have transcended time and culture, which were insightful tales of the human condition that ring true even now. His subjects ranged widely and encompassed comedy, tragedy, romance, adventure, ambition and history touching on great passions, deep jealousies, ambition and questioning minds. And when we find ourselves deep within these emotions, do we not find ourselves quoting Shakespeare? We talk of "the green-eyed monster", we state "It's all Greek to me", we think of foiled romances as "star crossed lovers." Have you ever felt "The world's mine oyster" or been "Eaten out of house and home"? These were all spoken by Shakespeare characters whose traits we can identify with today. And of course there is the language, poetic and beautiful, written in rhymes and rhythms which, when spoken properly, make perfect sense of the sentiments.

His appeal endures to this day for several reasons; he wrote great stories that have transcended time and culture, which were insightful tales of the human condition that ring true even now.

This year there will be endless opportunities to capture the essence of the man's work in the anniversary celebrations including world tours by The Globe, a BBC drama with Dame Judi Dench and Benedict Cumberbatch, an exhibition at the British Museum and a variety of operas. Whatever your preference, it will be hard to escape the joys of Shakespeare this year.

In April **The Globe** is soon to complete the largest ever world tour, to 193 countries, with Hamlet finishing back where it started. The theatre is also showing all 37 of Shakespeare's plays on film in a pop-up cinema on 23 and 24 April; each play condensed to 10 short minutes which presents an opportunity to see the complete work over 6 hours. ▶

BBC 2 has several interesting propositions; a new sitcom from Ben Elton, 'Upstart Crow', about Shakespeare's life and works, starring David Mitchell as the playwright and Harry Enfield as his father, while Benedict Cumberbatch and Judi Dench will star in the next instalment of BBC2 drama, The Hollow Crown.

The **Royal Shakespeare Company** will be curating a new exhibition of 100 years of Shakespeare at its Stratford home and, working in conjunction with BBC 2, will broadcast 'Shakespeare Live', an evening given over to live events, hosted by David Tennant on 23 April. Maybe the most extraordinary production of the year will be its highly anticipated production of The

Tempest, with Simon Russell Beale as Prospero. In a collaboration with Intel, it is hoping to redefine theatre using the creative process to inform the innovative uses of technology. Sounds like one to see.

Shakespeare400 is a consortium of leading cultural, creative and educational organisations, coordinated by **King's College London** offering an extensive range of opportunities. Through a connected series of public performances, guided walks, live screenings, music programmes, exhibitions and creative activities in the capital and beyond, its partners will celebrate the legacy.

In Oxford the world renowned **Bodleian Library** will be presenting 'Shakespeare's Dead' – a major Shakespeare exhibition curated by Dr Emma Smith and Professor Simon Palfrey of the University of Oxford's English Faculty, exploring themes of death in Shakespeare's works.

Windsor Castle, the site where Shakespeare himself read and performed to the Royal Court, will be exhibiting material in the Royal Library, including works of Shakespeare collected by the royal family, accounts of performances at Windsor Castle, and art by members of the royal family inspired by Shakespeare's plays.

The Inigo Rooms, in **Somerset House**, are the place to discover the stories behind key moments in Shakespeare's life, from the birth of the Globe Theatre in London, to his last days in Stratford. 'By me William Shakespeare' offers a once-in-a-generation opportunity to explore Shakespeare's will, alongside other unique documents that witness his life. Through original research, scientific analysis and a new digital installation, the exhibition looks at why these documents were created and what they tell us about the world's most famous playwright.

Propeller will be delivering a Pocket Tour, with support from Arts Council England, continuing with its valuable and wide reaching education programme: Pocket Dream will be touring from 1 February – 31 March 2016.

The **British Library** is offering ‘Shakespeare in Ten Acts’ showcasing over 200 unique and rare items such as the only surviving play-script in Shakespeare’s hand, an authentic Shakespeare signature, the earliest printed edition of Hamlet from 1603 and Shakespeare’s First Folio.

If music is more your forte then a trip to **Glynebourne** will reap rewards for its revival of Sir Peter Hall’s ‘A Midsummer Night’s Dream’ by Britten.

The **Royal Opera House** has Christopher Wheeldon’s three-act ballet adaptation of Shakespeare’s ‘The Winter’s Tale’, a story of love, loss and reconciliation with music by Joby Talbot.

One of the more unusual touring productions this year comes from **Spymonkey**, ‘The Complete Deaths’, a show which draws together all 74 onstage deaths for a strange and bloody Shakespeare-inspired evening.

HUNTING

Geordie Kidston, Head of Research

PRICE
£2.92

52 WEEK HIGH-LOW
£6.77 – £2.32

NET YIELD
6.3%

HIST/PROS PER
8.4 – 67.2

EQUITY MARKET CAP
£460m

As with all the oil services sector, Hunting shares sold off significantly on the back of weakness in the oil price. Hunting typically has limited visibility on its order book, which has historically been volatile. Guidance is that earnings will fall 85–90% in 2015. This is supported by recent reports of significant cuts to the US rig count; the acquisition of BG Group by Royal Dutch Shell implies a troughing in the oil sector and a pick-up in M&A activity. The emergence of the North American gas export market should be a material driver of cyclical recovery in the medium term. Hunting may well be a target for a major oil field services group wishing to integrate into downstream areas. Hunting is expected to directly address the covenant worries by providing a clearer outlook on liquidity. Analysts also believe that working capital outflows will drive year end 2015 debt down sequentially to $126m. Hunting will not be acquiring during this cycle, due to balance sheet constraints, and I continue to believe them vulnerable to ongoing consolidation within the North American shale sector. Despite depressed trading, their broad technological template remains a significant asset.

Please read the important notice on page 2.

ARE YOU BUYING A SECOND HOME?

APRIL FOOLS' DAY MAKES IT A LOT MORE EXPENSIVE…

Patricia Milner

The Government has announced an additional rate of stamp duty land tax (SDLT) adding 3% to existing rates where a second residential property is purchased. Patricia Milner, co-head of Withers Worldwide Wealth Planning practice, explains the complex detail that awaits new purchasers.

As so often with something that sounds simple, the proposed new rules are staggeringly complex with the proposals run to 31 pages. Confirmation of the rules will be announced in the Budget on 16th March (only two weeks before the rules come into effect), however, as it stands today, the new rate applies to purchases where completion (not exchange) takes place on or after 1st April.

Following the abolition of the 'slab' system, the new rates will apply to the relevant value band, so that a property costing £250,000, will be taxed at 3% on the amount paid up to £125,000 and 5% on the balance. The rates apply only to properties in England, Wales and Northern Ireland, not Scotland, but properties held in Scotland and elsewhere will count in determining whether or not several properties are owned for SDLT purposes. Properties costing up to £40,000, caravans, mobile homes and house boats are all excluded. The intention is not to charge the additional rate on replacement of a main residence; so if you own your home and another property, then sell the home and replace it, additional SDLT will not be payable provided, no more than 18 months elapses between the sale and purchase. If the new home is bought before the old home has been sold, the additional SDLT will be payable but can be claimed back on sale of the old home within 18 months.

As with Capital Gains Tax (CGT), a married couple or civil partners can only have one main residence for these rules while they are living together, and will not be treated as separated for these rules, unless there has been a Court Order or Deed of Separation, so an informal separation would be insufficient. Unmarried couples will be treated separately.

What counts as a main residence? Apparently, this will be treated as a question of fact. It will be possible, therefore, to have two properties, both of which are used for residential purposes, one of which you have elected as the main residence for CGT, but the other one being regarded as the main residence for SDLT purposes.

In difficult cases, HMRC may make extensive enquiries as to the circumstances, including where the owners spend their time, where their children go to school, where possessions are kept and which is the correspondence address. Therefore, it may be necessary to keep good records where there are two properties, both of which are used as homes and it is not obvious which is the main one.

The new rules will affect joint owners if any one of them has another property. If a couple owns their home and buys a property jointly with their children, the whole value purchased will be subject to the additional rate on the purchase. If the parents merely assist the children with a loan or guarantee and do not own a share of the equity, the additional rate should not apply. Where a property is held in trust, the additional rate may apply.

Any impending purchases of second homes should be completed before 1st April, wherever possible.

If a beneficiary of the trust has a right to occupy it, this is treated as ownership by the beneficiary. So if the trust or the beneficiary acquire a second property, that property will be liable to the higher rate (whether or not the beneficiary uses the trust property as his residence).

Where none of the beneficiaries have a right to occupy a trust property, then the trustees will be subject to the higher rate even though the trust owns only one property. The trust property is then ignored in looking at whether the beneficiaries have one property or more. Purchases by a partnership means each partner is a joint purchaser of the property so the additional rate may apply; and purchases by companies of a residential property will be subject to the higher rates even for the first purchase. There are however some exemptions for large scale corporate or fund purchases.

It is important to note that the points made above are based on a consultation document only, so the proposals may change. Clearly, however, any impending purchases of second properties should be completed before 1st April wherever possible.

Patricia is co-head of the Wealth Planning department in Europe for Withers Worldwide. She focuses on tax, trust and estate planning for both UK and non-UK resident and domiciled individuals and their families and has significant experience in advising family businesses and landed estates on succession and capital tax issues.

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withers LLP

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

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**

ROYAL DUTCH SHELL

Geordie Kidston, Head of Research

PRICE
£15.60

52 WEEK HIGH-LOW
£22.23 – £12.61

NET YIELD
8.4%

HIST/PROS PER
71.8 – 18.0

EQUITY MARKET CAP
£127,434m

Shell point out the highly complementary overlap of BG Group, particularly in Liquefied Natural Gas and BG's deep water assets in Brazil. Gearing is likely to rise to circa 20% in the short to medium term, with disposals to reduce this a priority. The group talks of a £30bn disposal programme emanating from this transaction, with assets departing from both businesses. The group insists that the BG acquisition has been triggered at a low point in world oil prices, given Shell's historic long term base case range of oil trading at US$70 to US$90 per barrel, albeit somewhat optimistic in the near term. All long term (that is to say twenty years) planning criteria are calculated off this base case, driven as it is by accelerating consumption arising out of growing globalisation and natural depletion rates. Increasing efficiency is seen as entering the shale industry, where some project deferral has already been announced. The dividend is regarded as sacrosanct for now, reiterated yet again in the recent Q4 results. The re-introduction of a scrip alternative during this shorter term period of depressed oil prices is likely to garner appeal; the 4th Quarter dividend saw $1.2 billion of the $3 billion dividend taken as scrip. Management continues to be high grade and long lasting and the income stream that the current oil market weakness grants, remains superior.

Geordie Kidston is a beneficial owner of Royal Dutch Shell

Please read the important notice on page 2.

MATTHEW MCENEANEY

LONDON

Born	Derby
Lives	Barbican, London
Education	Oundle School, Nottingham University
Started at JM Finn & Co	1992
Current Position	Investment Director
Interests	Golf, Motorsports, Fine wine
First job	Blue Button, London Stock Exchange
Favourite gadget	Naim NDS Network Player

With a 20% drop in the FTSE 100 over the last 12 months, this has been an exceptionally difficult time. As chairman of JM Finn & Co's asset allocation committee, what has been your reaction?
This past year has been particularly challenging for making judgements about where we are in the global economic cycle, as the Federal Reserve showed in its arguably late rate increase in December. At this stage in the cycle we would normally have been looking to lower weightings in fixed coupon bonds and higher-yielding, defensive equity but the QE-driven recovery has been patchy and muted. As a result, and given that most of our client portfolios are generally positioned to perform over the long term, with many having income requirements, we have made only small and gradual adjustments to the weightings, primarily to account for the increasing risk of the deflationary impact of China's restructuring.

Maintaining your fundamental investment philosophy must be hard in these markets – what are the key disciplines that you try and stay true to?
In volatile market conditions, when sentiment is a bigger influence than any change in the facts, it is helpful to have experienced previous market cycles, to take a step back and consider the fundamentals, of which perhaps the most important is that investment of this nature is long-term. However tempting it is to trade short-term market movements it is my philosophy to buy high-quality, well-managed and well-capitalised businesses and hold them over the full cycle. That is not to say that taking some profit, or cutting an underperforming stock, isn't necessary from time to time.

With multiple factors contributing to the rout, what are your biggest long-term fears?
The big question that we are all asking ourselves at the moment is what comes after the increasingly ineffective programme of QE, itself arguably the last phase of a 60 year credit expansion cycle. How is the debt paid off and who suffers in the process? It seems to me that deflation and possible negative interest rates, weakness in the commodity cycle and pressure of dividends in those sectors, and the prospect of Brexit, to name the most aired, are all very real concerns; but the elephant in the room is debt and what happens to growth if or when the credit cycle turns and tightens.

As a seasoned investor, what advice would you give to a young graduate embarking on a career in investing now?
It has been said that one isn't truly taken seriously until one has some grey hair; there is no doubt that experience of market cycles and understanding how and why stocks react in different circumstances is vital, to complement the technical skills and knowledge to manage investments. Today the industry is very professional and new entrants to firms such as JM Finn & Co can learn from hundreds of years' worth of collective experience. It helps to have an enquiring mind, enthusiasm and conviction for the stock market. The grey hair comes naturally!

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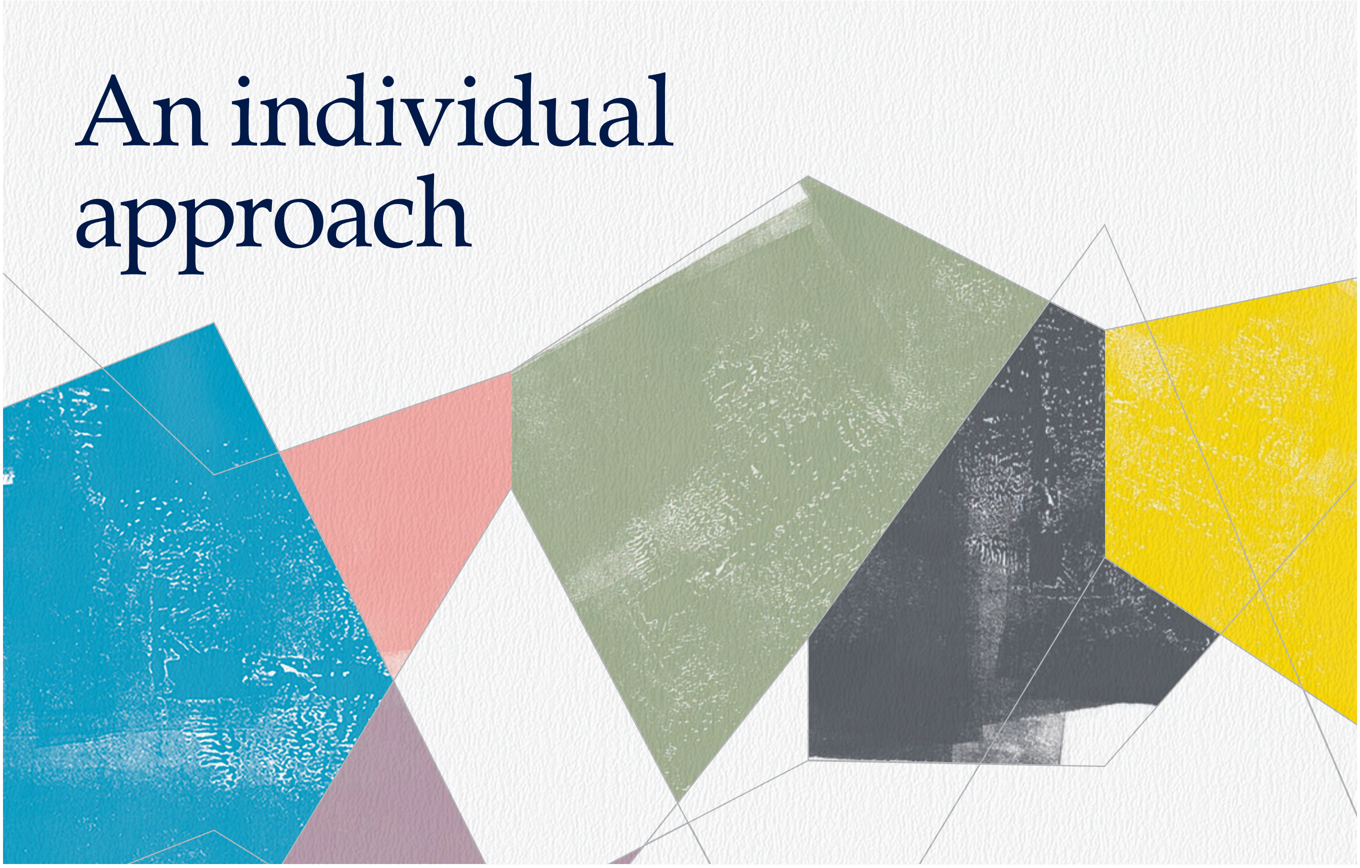

Treating each client as an individual is at the heart of everything we do.

At JM Finn & Co we have over 90 investment managers specialising in providing personalised portfolio management services.

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An eye for investment

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