PREMIER
ASSET MANAGEMENT

Premier Discretionary Team

Asset Allocation - For Professional Adviser Use

12th July 2010

Minutes

Present: F. Fulcher, M. Jennings, I. Rees, N. Kelsall, K. Cushway, D. Pendlebury, N. Sidebottom, R. Hallen.

Assets:

Equities	▶ HOLD
Bonds	▼ REDUCE
Cash	▶ HOLD
Property	▼ REDUCE
Alternative Assets	▶ HOLD
Structured Products	▶ HOLD
Commodity	▶ HOLD
Gold	▲ NEW ASSET CLASS

Equities (Geographic):

UK	▶ HOLD
US	▶ HOLD
Europe	▶ HOLD
Japan	▶ HOLD
Pacific Basin	▶ HOLD
Emerging Markets	▶ HOLD

Overview

During the second quarter of 2010, global equities fell -13.2% in dollar terms and -11.9% in sterling terms[1]. Bond yields in all but the worst economies have fallen sharply in tandem, which can be explained entirely by concerns over slowing economic growth and excess sovereign debt, a text book risk averse flight to safety. The Swiss Franc and Gold, two classic "safe havens", have also been strong as would be expected.

Although consensus data seems broadly fine, momentum has undoubtedly slowed of late so the big macro question now is whether this is the start of a double dip, or a normal breather after the big rebound in data since the summer of 2009?

The worry, of course, is that Europe derails the Global economy; although the evidence for this so far would appear to be slim. It would be very unusual, for example, to have another recession without an inverted yield curve. Taking Merrill Lynch numbers, Euro area GDP has been cut in 2010 from 2.0% to 1.0% and in 2011 from 3.0% to 2.25% so the trend would seem to be deteriorating. Interestingly, reported data from France and Germany has generally exceeded expectations of late, with German unemployment, for example, continuing to drift lower at 7.7%. The worry is in the periphery where, with the more slowly released macro numbers, we have little hard data as yet.

In local currencies, Greece is down 30.4% YTD, Spain down 16.2%, and Italy down 12.1%. Interestingly, China (Shanghai comp) is also down 24.0% in local currency and as current levels of the VIX Index show, fear has risen sharply. Sentiment has become extremely poor with light summer volumes exacerbating stock moves. This may continue through to September.

Taking a look at fundamentals, Bloomberg consensus PE multiples show the Eurostoxx 50 is on 8.4x 2011 expected earnings, FTSE100 on 8.3x, and the S&P on 10.7x. Taking the broader FTSE All Share, we get 8.5x 2011 and the Stoxx 600 is 9.2x 2011. Just a reminder that the historic 40 year average on Global equities is 17.7x (source: Citi), price/book also looks cheap.

In Europe, investors seem to have priced in a fairly ferocious outcome to growth which we believe is misplaced and in both Europe and the UK, equities now yield more than Gilts, thus reversing the reverse yield gap.

With equity yields exceeding bond yields, the implication must be that earnings do not grow for 10 years, dividends will be cut and/or deflation ensues hitting both the above. Yes, macro issues are real, and growth will be severely constrained in the next decade in order to re-pay the indebtedness of the last one, but nonetheless we find any of these outcomes to be only worthy of a very small probability.

The big and unresolved long term risk is that the heart of the problem has not been addressed; debt is excessive and has, so far, been simply passed from private sector to public sector and from peripheral Europe to the core.

The good news is that, for the foreseeable future we cannot see tightening by monetary authorities. So, for now, we have ample liquidity, cheap valuation, and good earnings growth. Once uncertainty subsides, this should be a good time to own equities.

Portfolio Specific Issues

Premier Capital Builder's largest holdings are currently synthetic zeros and have been for a while. One of the main differences between some synthetic zeros held in the portfolio and other typical structured products is that if the barrier is breached, which is only observable at maturity unlike a number of structured products, then the final entitlement gradually reduces rather than incurring a large capital loss. They are defensive in that they have low strikes, liquid secondary markets, senior debt of investment grade banks and are mainly shorter dated, therefore less responsive to rate and credit market influences.

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Premier Capital Builder has been up against a headwind generated by speculation before the emergency budget about a CGT hike and also increased risk aversion during the last few months. Due to the defensive positioning of this strategy, the equity market falls really had limited impact and it was more the CGT fears that caused some weakness. However, with just a 10% CGT hike for higher rate tax payers, the result was very pleasing and zeros have had a nice rally following the budget. The most important result of the budget was that the CGT allowance was maintained and will be increased with inflation. Despite the CGT headwind, the Premier Capital Builder Portfolio typically lost -2.19% over the quarter (up 7.4% over one year to 30.06.2010)[2]. The majority of this fall was due to the CGT fears and final rise which is something we have little control over. However, we have been running the Portfolio with a shorter maturity, making it more defensive to CGT or interest rate hikes. In conclusion, despite the headwind, Premier Capital Builder Portfolio maintains its enviable defensive track record.

The Premier Dynamic Growth strategy recently bought Templeton Emerging Markets and also invested in a company exposed to Timber plantations. 'Phaunus Timber' was bought at around a 30% discount to net asset value. Despite being launched three years ago, it has only recently become fully invested in a diverse range of countries and continents including, South America, North America, Africa, Eastern Europe, China and New Zealand. The company owns well established plantations as well as 'open fields' which they plan to start plantations from scratch.

The Conservative, Balanced and Growth strategies were reviewed and all the current structured products held had been individually assessed. RBS has recently brought some interesting opportunities to our attention which are currently being considered. A discussion took place regarding the credit worthiness of RBS which is currently backed directly by its largest shareholder, mainly the UK exchequer. However, this may change if the company is denationalized as has been muted. It was considered unlikely that the UK government would sell RBS to a new owner which may need to be re-bailed out at some further stage post the sale.

The recently persistent inflationary pressure in the global economy has led us to consider adding an exposure to gold via a bullion ETC / fund (still to be researched). This exposure to gold will act as a risk adjustor against a double dip recession and will be viewed as a non equity correlated asset class. It was agreed to reduce the exposure to property and corporate bonds by 3% and 2% respectively in order to fund a 5% holding in Gold.

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[1] Source: Bloomberg, data from 30.03.2010 to 30.06.2010. Past performance is not a guide to future returns.

[2] Portfolio performance data is calculated by Premier Fund Managers Limited on a total return basis, using a sample portfolio for illustration purposes. Exact performance will depend upon individual stock weightings.

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