

Assets:		Equities (Geographic):	
Equities:	➡ Hold	UK:	➡ Hold
Bonds:	➡ Hold	US:	➡ Hold
Cash:	⬇ Reduce (CONS ONLY)	Europe:	➡ Hold
Property:	➡ Hold	Japan:	➡ Hold
Hedge Funds:	⬇ Reduce	Pacific Basin:	➡ Hold
Alternative Assets:	⬆ Increase (CONS ONLY)	Emerging Markets:	➡ Hold
Structured Products:	➡ Hold		
Commodity	➡ Hold		

Minutes

Present: M Jennings, P Smith, F Fulcher, N Kelsall, K Cushway, D Pendlebury, R Hallen.

There are numerous forward looking macro indicators that are showing a consistent positive trend, German ZEW economic expectations are at a 3 year high, and even UK house prices appear to be turning a corner. Recently published data gives an initial indication that the recession is over in France and Germany, both economies grew 0.3% in Q2. The big drag that remains (especially for the UK) is the fiscal deficit which the OECD expects to reach 14% next year, which is why the UK is on S&P credit watch.

Assuming that the UK does eventually get downgraded from AAA, this will throw up an interesting conundrum for the relationship between Gilts and corporate bonds. The IMF recently calculated that the effect of Quantitative Easing (QE) in the UK had reduced Gilt yields by between 40 and 100 basis points.

With the Bank of England recently announcing a further £25 billion of Gilt purchases, yields have fallen again. This has become a drug, and once it stops we would not be surprised to see yields drift higher. Once QE stops, it will be a clear indication that the Bank thinks that we are out of the woods and at that point we should worry about rising interest rates. We therefore feel it is unattractive to hold long dated Gilts. Shorter dated Corporates would seem a better bet all round as credit spreads continue to narrow.

Equities have rallied sharply, with a 46% rally in the US since the March 9th trough, also 46% in Europe, and 30% in FTSE100 to the end of July. We feel that the probability is that March 9th marked the bottom for most major markets. We are still a long way short off the peak and feel we will not get back to the high points reached in 2007 for a few years.

Morgan Stanley's European strategist recently ran some analysis on rallies following bear markets and concluded that 71% was the median rally over a 17 month period. Europe this time has rallied 42% in 5 months.

Valuations have changed significantly having troughed below 10x historic earnings in Q1 and Q2. Earnings have fallen further and prices have risen - the net effect is that the historic global PE is now approx. 18x. This no longer screams out as being cheap. We

must not forget though that at the lowest point in the earnings cycle the PE will look dear as earnings are depressed. We are nearly there. Citi estimate that global earnings have now fallen 42% from their peak and will trough at -50%. If we were to pencil in an earnings rebound in 2010 of say 20%, this would bring the PE back to 15x.

Our valuation conclusion therefore is that the “easy money” in global equity markets has now been made but there is further scope, maybe 20% over the next 12 months. This would more or less tally with the Morgan Stanley strategy view.

Two positive supports to stock markets are that cash balances remain exceptionally high by historical standards (anecdotally, we believe that these are beginning to be put to work into equities), plus earnings upgrades now exceed downgrades for the first time since August 2007.

Generally speaking, analysts are usually too slow to downgrade as the environment deteriorates, and they are also too slow when things improve. A sharper than expected earnings rebound would help the case for valuations. There is also the possibility that the huge fiscal and monetary stimulus floods out into a new bubble in financial assets which is inflationary. This would be very destabilising, especially for bond markets, but good news for equities in the short term. This stimulus is unprecedented in economic history, so the probability of a central bank mistake is high.

We remain positive on global equities as fundamentals continue to improve. Some markets have been overbought recently and were ripe for profit taking. Interestingly, weak days do not last for long as buyers seem to be in the wings. It is highly possible that markets overshoot on the upside, spurred on by large levels of liquidity. Although markets have rallied significantly since March, we are wary to cut exposure too much whilst we are in this sweet spot. Revisions are positive, liquidity is strong, and we have not yet started to worry about interest rates rising.

Portfolio Specific Comments

We have committed £2.5m to a new structured product launched by Goldman Sachs. The product has a one year potential Auto Call structure offering 15% over the year subject to the FTSE100 being at the same level or greater than the initial strike level. If the index is below the strike in 12 months time then the product loses its Auto Call structure and will revert to a 6 year product delivering 175% (uncapped) of the rise in the index from its initial strike. The product has soft protection subject to an 80% barrier and also a 300% reservoir characteristic should the barrier be breached.

The Conservative strategies cash weighting will be reduced from 7% to 2% by the purchase of this Goldman Sachs new issue.

The Balanced strategies will also hold the Goldman product where we are underweight Alternatives. We expect the Citigroup FTSE 23% A/C 7 to redeem in October and proceeds from this redemption may well be used to purchase the new issue.

We are currently underweight commodities and are buying the Schroder Commodity OEIC due to the limited number of structured commodity products available. A newly structured issue would offer very limited geared upside and also link to a narrow range of

commodities. It was felt that a good long only commodity fund manager investing in a wider range of commodities would deliver more attractive returns.

The Premier Capital Builder Portfolio continues to perform well and has made an excellent recovery over the last 6 months. The cover on zero's and synthetics has improved and GRY's of 5% to 7% are very attractive in the current low interest rate environment, especially for tax payers. JZ Equity zero's redeemed in the last quarter which created a 15% cash weighting within the portfolio. There have been two successful new issues of zero's, one by Ecofin, offering a yield of 7% and also by Electra which offered yields of c.6 1/2%. The volatility of the portfolio has been low and is positioned well to demonstrate defensive qualities given any further equity market falls.

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