ISA & PEPTalk

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Fidelity Asian Values

After a year in which conventional thinking was often challenged it comes as no surprise that investors have retreated to what they feel are the more tried and tested of markets and sectors. Appetite for niche market segments and overseas geographies is low. Whilst most overseas equities have provided sterling returns influenced by our currency's weakness, less effort seems to be going into pursuing exposure to Asian markets. Not only that, we have seen how even at home investors have approached smaller companies warily. So, it follows that investing in a smaller companies biased Asian portfolio runs counter to trend.

To fill the gap, it helps to have an investment fund that understands the risks for us of venturing off the beaten track. Fidelity Asian Values, managed since April 2015 by Nitin Bajaj, has access to Fidelity's huge research resource but also takes steps to protect the portfolio value by writing put options. This investment trust is particularly attractive to long term growth seekers because it has that bias to smaller companies and value investment themes.

Since taking over the management Bajaj has managed to narrow the discount to net asset value. Over the last 12 months the discount has been as high as 15% but he has succeeded in bringing it down to around 5%, demonstrating that the market has improved its view of the trust.

His stock selection is driven by individual equity attractions and not macro trends. This is not a unique tactic and we have seen Fidelity's investment funds operate this way over the years in a variety of different markets. In this case, the manager is described as *benchmark agnostic* and is entirely focussed on holding stocks that fit valuation criteria. He defines risk as the permanent loss of capital rather than benchmark underperformance. Consequently, he has carefully picked from the 500 companies that analysts are actively monitoring to build a £250 million portfolio that is 57% weighted to companies of sub $1 billion market cap. Exposure to industrial and consumer stocks is high. He does not easily find companies of adequate value in China and is thus underweight that territory. South Korea is also an underweight. India and Australia are the overweight geographies.

Numerous studies have backed up the notion that smaller companies outperform larger companies in the long term but this does mean that investors in Fidelity Asian Values should be looking longer term with it. There is a small yield (1.3%) and virtually no gearing (net -2%). We rate it as **medium-to-high risk** because some of the smaller company stakes will be illiquid but the closed-ended fund structure makes it unlikely the manager is ever going to be a forced seller.

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Economic Overview and Prospects for the Market

	5th Jan 17	4th Jan 16
FTSE 100	7195.31	6093.43
FTSE All-Share	3902.82	3367.42
FTSE 250	18308.23	17122.15
Base Rate	0.25%	0.5%
$/£	1.242	1.469
Euro/£	1.17	1.36

Mike Tattersall

Chartered FCSI Investment Manager

Anne Richards, Chief Investment Officer at Aberdeen Asset Management for 13 years and now Head of M&G was quoted in the press at the beginning of the year saying "It is tempting to extrapolate from the events in 2016 and conclude more of the same is on the way, but if there is anything that investors have learnt in the past 12 months, then it is to expect the unexpected".

Ms Richards believes that politics will dominate 2017 with Brexit, Trump and elections in the Netherlands, Germany and most importantly France taking centre stage. We agree on this point and as political anxieties ebb and flow the financial markets will dance to the tune. Whereas 2016 saw markets brush off concerns and push to new highs the current year can be expected to be more problematic and prone to more volatility.

Inflation

In the US Trump's intended fiscal expansion and tax cut plans will, with little doubt, add to inflationary pressures. Here in the UK sterling's fall against both the euro and dollar will add to import and industrial input costs and send inflation sharply higher.

Interest Rates

In the US, where Mr Trump's plans have, and may continue, to send bond yields higher, interest rates should not get back to anything like the levels seen prior to the onset of the financial crisis.

A point worth making is that Trump does not acquire a dictatorship. So, if he has a problem taking Congress with him, the inflationary threat may prove to be muted.

In the UK, the rise in inflation, as a result of the fall in the sterling exchange rate, can be expected to be one-off (unless Brexit negotiations prove to be a disaster). This being the case, the Bank of England will be careful with interest rate adjustments.

Although bond yields may rise in the short to medium term therefore, they could well adjust back down looking further ahead.

On the 3rd January Ambrose Evans-Pritchard said in the Daily Telegraph that, in his opinion, Trump's reflation rally will short circuit. Rising borrowing costs, he argues, will 'blow fuses' across the world before fiscal stimulus arrives – if it arrives. He sees 'powerful deflationary forces' retain their invisible grip over the global economy leading to bond yields, after ratcheting up, falling to historic lows before the end of the decade.

This may be an extreme view but it should at least dampen expectations that we will see meaningfully higher interest rates in the foreseeable future. Against this background existing or would-be bond investors should exercise caution.

United Kingdom

Despite the weight of Brexit worries the first three PMI (Purchasing Managers Index) declarations for the year have proved to be extraordinarily positive. The Manufacturing PMI, announced on the 3rd January, came in at 54.2 versus a forecast of 52.8 and 52.8 previously. A PMI above 50 indicates growth and one that exceeds the previous one indicates stronger growth. On the 4th January the Construction Sector PMI came in at 56.1 versus a forecast 53.3 and 53.6 previously. Finally on the 5th January the UK Services PMI was announced. Being the largest segment of the economy this was important. The figure came in at 56.2 against a forecast of 54.7. The previous figure was 55.2.

Jeremy Warner, in the Daily Telegraph on the 3rd January said that he expects the UK economy to surprise on the upside with the potential to achieve 2% or more annualised as against 1.4% forecast by the Office for Budget Responsibility and the Bank of England. The main reasons for his optimism are that Brexit concerns already appear to be factored in, the weak pound will boost net trade and, thirdly, consumption will

continue to grow, fed by higher debt and elevated levels of immigration ahead of tougher, post Brexit border controls.

We have to point out that after giving this positive possibility he jumps quickly on the fence saying "All of this could, of course, turn out to be nonsense".

With all of the political uncertainty it seems impossible to say how 2017 will end. From everything I have read Patrick Johnson of Panmure Gordon has, arguably, the most pertinent thing to say and it is this:

"Ultimately quality companies are always "in play" when it comes to mergers & acquisitions and IPOs. The number (of such corporate events) should increase this year building on the late flurry of deal activity heading into Christmas. Everything is 20% cheaper than it was a year ago because of the fall in the pound". Obviously he meant everything is cheaper for foreign predators.

We agree wholeheartedly with this and we also believe that dividends of 3.5% to 4.5% underpinned by solid companies with robust balance sheets will continue to meet the income needs of those investors who can live with some degree of volatility.

Europe

The Wall Street Journal on the 1st January stated "For Europe in 2017, the big question is whether fragile economic growth and unprecedented central-bank stimulus will be overtaken by populist politics". The article went on to say that European equities could have a strong year if the anti-euro populist candidates that have gained traction over 2016 fail to win elections, as polling suggests. If populist candidates triumph in coming elections however, the prospect of a eurozone breakup would return to investors' minds which in turn would weaken market prospects.

On the positive side, assuming the absence of political instability, the weaker euro against the dollar and continuing low interest rates should lead to decent economic growth and stronger performance for banks.

We will have to see what happens as the year pans out.

The United States

By the time you receive this publication the President-elect will have become the President and we will then see how much of the electioneering rhetoric is enacted, or attempted.

According to the most recent FOMC (Federal Reserve's Open Market Committee) meeting on 14th December 2016 GDP growth is expected to rise to 2.1% in 2017, better than the earlier 1.9% estimate. The unemployment rate is expected to drop to 4.5% in 2017 and 2018. Most job growth is expected to be in low-paying retail and food industries. Since many people who have been out of work for a long time cannot expect to return to high paid jobs the Federal Reserve Chair, Janet Yellen, admits a lot of workers are part time though they would prefer full time.

Time will tell if Donald Trump's policies will change this situation and, in his words 'make America great again'.

Global Outlook

Martin Gilbert, CEO of Aberdeen Asset Management sees Asia, as a crucial workshop for the US, benefitting from any American economic resurgence. He believes that on an average forward P/E multiple of 12.4, compared with an average 16 times for the MSCI global index, Asia offers value.

Sir Martin Sorrell, CEO of WPP, sees Donald Trump's proposed infrastructure spending likely to boost both growth and inflation. He says this could potentially deliver a two-to-three year Keynesian type boom. Having made this point he does warn that what is gained on the US swings could be lost on the international roundabouts. What he no doubt alludes to is the threat that rising US interest rates have within the global markets – and in particular in the Emerging markets.

Conclusion

As we move into 2017 we face many uncertainties, most due to a shifting political landscape. Political outcomes will have direct impact on economic and market developments.

Rising inflation and tightening monetary policy in the near term will impact on the bond markets and investors should be cautious.

Equities of the soundest of companies with predictable earnings and well covered dividends should continue to be bought and held in portfolios as should other asset classes such as equity/bond hybrids, most notably solidly established infrastructure companies.

BREXIT, Trump, what does it all mean?
If you would like some professional help with your portfolio we can help.
Our Investment Managers can manage existing portfolios or construct one for you in line with your needs on a Discretionary basis or by you working together with your dedicated manager.
Simply ring **0161 832 6581** for a no obligation chat.

Underperformance at Invesco Perpetual

Nigel Moore

Senior Chartered Wealth Manager

Since the departure of Neil Woodford from Invesco in 2014 Mark Barnett was given responsibility to manage Neil's open ended funds and the three Investment Trusts - **Perpetual Income and Growth Trust, Edinburgh Investment Trust** and **Keystone Investment Trust**.

The performance of these funds has struggled recently and so we have dug deep to try to understand the reasons why and whether the three Trusts are sufficiently different to merit holding.

Looking first at the Trusts, Perpetual Income and Growth and Edinburgh Investment Trust, both employ a similar investment strategy. PLI carries a performance fee and Edinburgh's borrowing costs are higher with a £100m debenture locked in at 7.75% until 2022. It is therefore surprising to find that Perpetual Income and Growth has significantly underperformed Edinburgh. Perpetual Income and Growth has a greater exposure to UK Mid and Small Caps, which evidently has had a material effect, leading to the wider underperformance.

Performance of PLI has been poor on a three year view compounded by a widening of the discount to NAV, currently standing at 8%. I would contend that the NAV discount is an enticing entry point if Mark can re-establish his outperformance credentials.

Both Edinburgh and Perpetual Income and Growth appointed a co-manager in July this year, possibly due to these concerns.

Turning to Keystone Investment Trust, it has more of a growth investment bias and therefore its return last year is especially disappointing given the broader market return. Exposure to UK Mid and Small cap securities has impacted performance with domestic earners experiencing a de-rating.

For clients looking specifically for capital growth they may wish to seek pastures new. One option is **Schroder UK Growth** where performance has improved as the manager's value bias has proven successful.

The Trust trades on an 11% discount to NAV with a low 0.5% AMC. Please note that the trust may employ 'gearing' (borrowing), which may increase returns if the underlying investments perform well but will reduce returns if they fail to do so.

In comparison how well has Neil Woodford fared?

Since establishing his **Woodford Equity Income Fund,** on a total return basis, Neil has outperformed Mark's Invesco Perpetual Income Fund -

28.7% versus 17.8%

(2/6/14-3/1/17 Woodford Equity Income C Inc TR vs Invesco Perpetual Income Y Inc TR).

Over the past 12 months the funds have traded broadly in line with each other whilst also significantly underperforming the FTSE All Share.

Clients who hold more than one of Mark's trusts may wish to look at Neil's fund as a diversifier given his exemplary track record over the longer term and outperformance since establishing Woodford Investment Management.

Prior to any purchase the Key Investor Information Document (KIID) must be read and is available upon request.

Discrete Annual Calendar Performance (%)	2012	2013	2014	2015	2016
Edinburgh Investment Trust	12.9	23.05	12.05	14.44	3.13
Keystone Investment Trust	21.04	34.26	8.86	2.41	-5.23
Perpetual Income and Growth Investment Trust	18.83	34.57	9.84	8.03	-7.58
Schroder UK Growth	28.8	38.02	-16.23	2.06	10.45
Woodford Equity Income C Income*				16.15	3.15
Invesco Perpetual Income Y Income	7.69	26.27	9.72	9.24	2.98
FTSE All Share Index	12.3	20.81	1.18	0.98	16.75
Data Source: FE Analytics *launched in June 2014					

Our Investment Managers Tips from 2016 and for 2017

Please note all our 2017 tips are from the AiM market and are therefore high risk. These stocks may currently be included in our Discretionary AiM portfolio or may be included in the future.

Alistair Hodgson

Senior Chartered Wealth Manager

2016

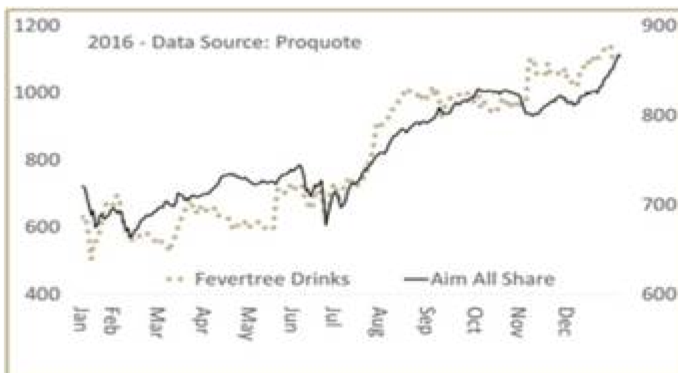
Auto Trader **Buy 435p**

Media **Medium Risk**

Auto Trader put in a credible performance in 2016 but a 6% loss not what I had hoped for. I can blame Brexit but that would be to cloud the picture. The idea with AUTO was to invest in a company where much of the capex was in the past and what lay ahead was delivering on strategy, bringing in the cash and paying down debt. In that respect, I think the story is still intact.

2017 Fevertree **Buy 1105p**

Beverages **High Risk**



For 2017 I am going to do something quite different. In what could be a turbulent year I want to plump for something which has a momentum all of its own. Some people might think I am arriving a bit late to Aim-listed **Fevertree Drinks** which has been making great strides in the premium mixer market. However, the company has several trends working in its favour to justify its heady price.

In the UK, we have seen a revival of gin drinking focussing on quality rather than quantity. Internationally Fevertree has first mover advantage but, relative to UK, that is just getting going. Meantime Berenberg estimates it is about to top 60% of the premium mixer market share, though one would expect competitors to mount something of a fightback in time. With growth still evident in spirit consumption beyond these shores and with a product range now spanning lemonade, ginger ale and cola, there is a lot for this company to go at, justifying their piling up cash instead of enhancing dividends. Unsurprisingly, the *high risk* rating and 48x forward PE ratio for 2017 is a lot harder to swallow than their product but you have to pay up for quality.

Sally Greenwood

Chartered Wealth Manager

2016

BAE Systems **Buy 521p**

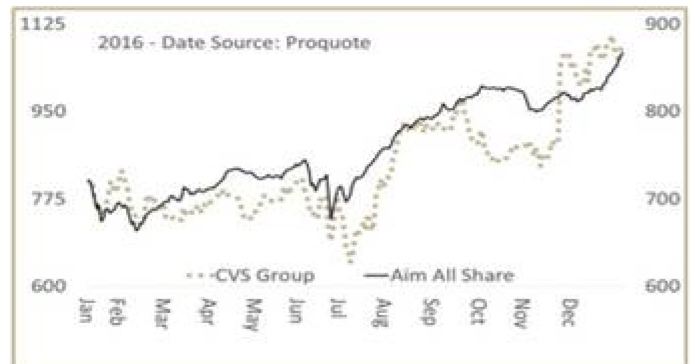
Aerospace & Defence

Medium Risk

At the turn of last year rather than economic concerns, the main worries of the world were geo-political tensions across various countries. For this reason I chose BAE Systems, which has stood me in good stead.

2017 CVS Group **Buy 1062p**

Personal Services **High Risk**



CVS Group is a veterinary services provider that has been steadily buying up practices when they come up for sale, along with diversifying into a vet locum agency, crematoria and own brand drugs.

Its acquisition spree has been gathering momentum over the last 12 months with around 80 surgeries purchased, including its first acquisition in the Netherlands. This is certainly not intended to be a one off event. The group has ambitious overseas expansion plans.

The industry has seen fundamental change over the last 20 years with de-regulation offering practice owners an exit opportunity that did not exist before, and the old idea that to be a vet is a vocation for life, for the practice to then be handed down, no longer holding true in lots of circumstances. This has allowed CVS to consolidate in an unthreatening manner, as any practices which join the fold are allowed to continue to operate under their

original name. They are offered the back office support of CVS whilst being opened up to their hugely advantageous buying power. This has the result of the newly acquired practice immediately seeing an uplift in its profit margins.

A fund raising in December whereby the company raised £30m to fund acquisitions was approximately 2.4 times oversubscribed, demonstrating belief in the business and its strategy from the investment community. At the last update the company gave to the market, sales and margins had improved and profit was running ahead of expectations.

Whilst increasing inflation and the possibility of rising interest rates this year could dent consumer confidence and squeeze household incomes, the growing use of pet insurance should provide a cushion to this. On a P/E of 68 and a yield of only 0.28% the stock is not cheap. It is listed on the AIM market and so must be deemed high risk; but for a pure out and out growth play on an expanding industry that is fully exposed to new medical technology and innovation, I view this as a buy.

Nigel Moore

Senior Chartered Wealth Manager

2016

Next **Buy 6795p**

General Retailers

Medium Risk

Next's decline over the calendar year has continued unabated. Our expectation that the quality of Next's management to navigate the downturn in retail and indeed to prosper ahead of rivals was proven incorrect.

The consumer has curtailed spending on clothing and this can be attributed to several factors including fears over Brexit, reallocation of spend to non-clothing items such as recreational - social spend (food/ beverage) and seasonal events (mild autumn).

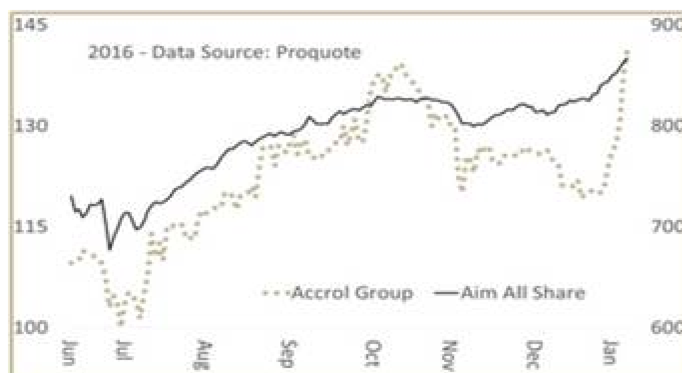
Recent results indicated the slowdown in sales has continued over the fourth quarter of 2016 forcing Next to downgrade 2017 expectations.

It is too early to back management to recover given the consumer headwinds ahead.

The revised dividend policy will generate a 4.8% yield at the current valuation.

Accrol Group Holdings **Buy 138p**

Household Products **High Risk**



Accrol Group Holdings is an AIM listed leading independent tissue converter, manufacturing toilet rolls, kitchen rolls, facial tissues and away from home products to supply retailers throughout the UK.

Accrol imports industrial sized paper reels from around the world and converts them into finished goods at the Company's 350,000 sq. ft. manufacturing, storage and distribution facility in Blackburn, Lancashire.

Accrol currently manufactures approximately 17 million units per week and supplies some of the UK's largest retailers including Tesco and Aldi.

The company issued its maiden first half result on 4th January. Revenue increased 8.8% to £63.9m and gross profit increased 5.6% to £18.2m. Adjusted gross margin improved by 1.1% to 28.4% through significant currency hedging pre and post EU referendum and negotiated parent paper reel pricing.

They have successfully delivered on their strategy of organic growth through discount retailers and by increasing market share through the supply of Private Label products to some of the UK's largest retailers. In addition, management have continued to win new business, including a contract with Lidl which is expected to generate more than the £10m sales per year. The group has increased market share in the discount retail sector to circa 50%.

A maiden dividend of 2 pence was announced indicating a 4.8% annualised yield for the company at the current share price (128 pence 4/1/17).

We forecast continued market and margin growth. Shares trade on an undemanding p/e ratio of 10.9xs 2017 earnings.

Our Investment Managers Tips from 2016 and for 2017 Contd……..

Mike Tattersall

Chartered Investment Manager

2016
Lloyds Banking Buy 71.4p

Banking

Medium Risk

Those who have been to Tattersalls enclosure at the races will be used to experiencing 'naps'. Sadly, despite sharing the name, my 'nap' for 2016 is still coming down the home straight! The lame runner was Lloyds Banking, down 11.7% by the end of the year.

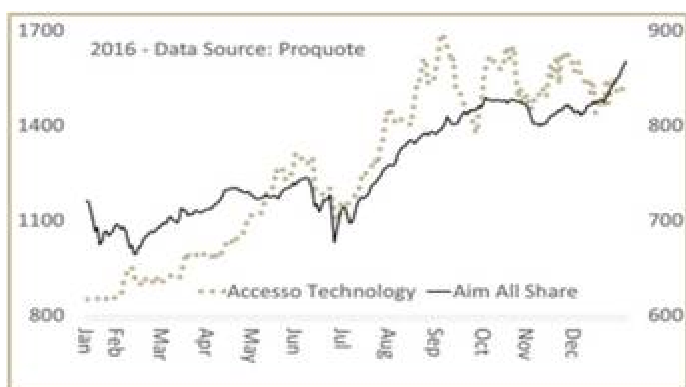
Lloyds during 2016 was held back by poor sentiment engulfing the banking sector generally with mis-selling scandals such as PPI still to the fore of shareholders' minds.

Interestingly, Lloyds Banking is now Investec's top UK banking sector tip for 2017. They say that after the lender's acquisition of MBNA from Bank of America in December it will have a 26% share of the UK credit card market. Couple this with the fact that Lloyds is the largest mortgage lender in the country and it becomes the top provider of consumer finance.

Investec believes that the PPI saga is nearing its end. If they are right in this regard Lloyds' profitability and dividend paying capacity should increase meaningfully and this should result in a share price re-rating. Barclays have Lloyds as an overweight rating with a 75p price target.

2017 Accesso Technology Buy 1555p

Software/Support Services High Risk



Turning to this year I would like to bring your attention to Accesso Technology (ACSO). This is a £345 market cap company operating in a niche market that has the capability of being expanded globally, bearing in mind its lead time advantage.

If you have ever had the misfortune to queue endlessly during a theme park day visit with children who are restless and frustrated you will welcome Accesso as a saviour.

Accesso's Qsmart is a virtual queuing solution that puts virtual queuing straight onto a visitor's smartphone. Visitors get more out of their day by purchasing the service and managing the reservations for their favourite rides. Qsmart waits virtually in line for them and signals when their turn approaches. At this point they access the ride using a priority entrance. Not only is the visitor delighted with this result, so too is the theme park operator since he can maximise the number of rides and therefore his revenue and profits.

Accesso's markets include theme parks, ski-resorts, waterparks, zoos and aquariums, tours and attractions and fairs and festivals globally.

Turnover of £32.22 million in 2013 rose to almost £63 million in 2015 and net profit rose from £1.5 million to £3.62 million. At 1555p the shares are trading on a historic PER of 77.16. On the basis of analysts' forecasts this reduces to 36.31 in 2017.

Accesso trades on the Alternative Investment Market and must be classified as high risk.

Terry Applegate

Chartered Wealth Manager

2016

Bodycote Plc Buy 551p

Industrial Engineering

Medium Risk

Last year I tipped thermal heat treatment company Bodycote.

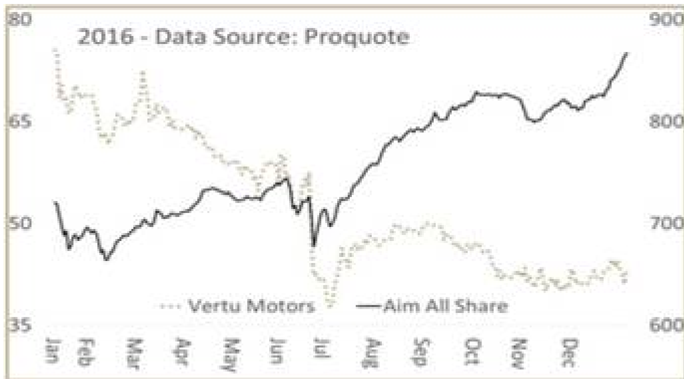
A trading statement released at the end of November 2016 revealed a mixed picture for the group with revenues increasing, although a portion of this was down to recent currency movements in the groups favour.

Analyst coverage on the company has remained positive, and as a result I still feel that the shares offer further upside potential for those clients with a medium term outlook.

Our Investment Managers Tips from 2016 and for 2017 Contd……..

2017 Vertu Motors **Buy 41p**

Motor Dealerships **High Risk**



Listed on the Alternative Investment Market (AiM), Vertu is the UK's 6th largest motor retailer by turnover, with 121 franchised operations across England and Scotland. The group's stable of brands includes Bristol Street Motors and Farnell Land Rover/Jaguar.

Vertu is involved in the sale of new and second hand cars, but also the highly profitable and growing market for service plans, which are seen as a key area for ensuring customers keep returning to the groups garages for both maintenance of their existing vehicle but also the opportunity to sell them a new one when they are looking to upgrade.

The financials of the group have impressed me, with Interim results released in October 2016 for the six months ended 31st August 2016 showing group revenues increasing by 17.7% to £1,454.6m, with record profits before tax up 14% to £18.7m. The group had £12.9m in cash at the end of the period, whilst a £35m fund raising early in 2016 was used to finance further acquisitions.

The company stated that the key September 2016 trading period had been robust and ahead of last year on a like-for-like basis, with recent acquisitions contributing to profit growth. It was also expected that the outlook for the later stages of 2016 would remain positive, underpinned by low interest rates and record high levels of employment in the UK economy.
One of the biggest events of 2016 was the Brexit decision in June, but at the time of the October results announcement, Vertu stated there had been no impact seen from the UK's decision to exit the EU, and the result of the referendum had not materially impacted consumer confidence.

As we move through 2017, future car sales will be closely linked to consumer confidence, but so far, car sales and economic data have remained robust and this gives us confidence in the group moving forward. There are a large number of new high profile models coming out this year and I am sure that there are plenty of people wanting to 'keep up with the Jones's' and have that gleaming new motor parked on the driveway!

Although 2017 may present challenging conditions for the UK economy, I see enough positives within the industry to keep the group motoring ahead! Priced at 41p the shares currently trade on a historic price/ earnings ratio of 7 times, and offer a yield of 3.1%.

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