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# master investor MAGAZINE

RESEARCH • ANALYSE • INVEST

ISSUE 03 - JUNE 2015
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# HOW TO PICK THE PERFECT SHARE

WE SORT THE WHEAT FROM THE CHAFF IN THE UK MARKET

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# WELCOME

One of the most exciting aspects of working at Master Investor is the opportunity to meet an incredibly varied and smart set of characters. Such can be said, I am proud to say, about the growing team of freelance contributors we have working for us.

Being a highly networked company, we have staff and contributors not just around the entire country, but also abroad. One of them is Filipe R. Costa, our expert on anything relating to monetary policy, macroeconomic issues and behavioural finance. These are subjects that are important for investment success, but which are a closed book for most private investors.

Filipe is one of the rare breed of experts who have both a strong academic background and the ability to explain their subjects in a comprehensible and interesting way to the layman. Besides teaching courses on Financial Markets and Monetary Economics at the University of Oporto, he has made it his passion to help traders maximise profits and manage risk in a better way.

Despite shuttling back and forth between classes and other academic engagements, Filipe is one of our most productive writers. In this issue, you'll find his article about a new monetary system for Greece on page 38. Also, don't miss out on his regular blog posts, where he last explained why central bankers are scratching their heads over the lack of inflation and growth (sign up to our email list so you don't miss them!).

Master Investor is all about breaking complex subjects down into digestible, comprehensible and enjoyable pieces. We are here to inform, educate and inspire investors. So that you have the information available to take your financial destiny into your own hands!

**Until next month, Best regards,**

S. Lorenz

**Swen Lorenz, Editor**

**P.S.: We are still looking for more freelance contributors, both for the blog and the magazine. If you'd like to send us your CV and a few examples of what you typically write about, then email james.faulkner@masterinvestor.co.uk.**


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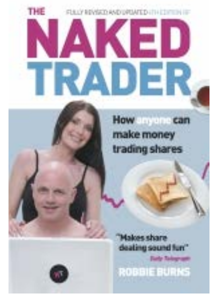


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## PERFECT SHARE SPECIAL ARTICLES











# PROXAMA

## POTENTIALLY A REVOLUTION IN MARKETING

**BY SIMON CAWKWELL (AKA EVIL KNIEVIL)**

*After last month's comment on* ***Proxama (PROX)****, I decided that it would be helpful to expand the comments so that readers could have a better idea as to what is going on. Here I again enlisted chairman David Bailey's assistance and he advises that Proxama's marketing business is focussed on Bluetooth beacons. The beacons "push" a message to passing smartphones.*

Currently there are probably fewer than 4,000 beacons across Britain, nearly all of which are in "closed" environments – i.e. an individual retailer, from a coffee shop to a department store, will deploy beacons on their doorways to alert passing consumers, or internally in the shop to alert consumers to specific offers in a particular department. The retailers control the messages, so only their "messages" will be sent, but the messages only resonate (currently) with consumers who have that specific retailer's app on their phone and are within range. Beacons have a range of 5 to 40 metres.

Proxama's beacons, (they currently have about 1,300 deployed but expect to have around 10,000 deployed by end December 2015), are in an "open" environment, so they are/will be on buses, bus shelters, poster sites in airports and shopping malls as well as in stores, sports stadia and bars. The strategy is to put them in high footfall areas, to create a network that any brand can use to "push" marketing messages, whether general (e.g Sky sending out info about tonight's movie premier) or specific (today's offer at a particular JD Wetherspoon) with target geographies (e.g. within the Oval on an Ashes Test day, or as broad as Norwich, or London, or Britain, or Europe). Proxama intends to create a broad

**"PROXAMA'S BEACONS ARE IN AN 'OPEN' ENVIRONMENT, SO THEY ARE/WILL BE ON BUSES, BUS SHELTERS, POSTER SITES IN AIRPORTS AND SHOPPING MALLS AS WELL AS IN STORES, SPORTS STADIA AND BARS."**

network infrastructure of owned and controlled beacons. Proxama controls the access to that network, collects the data from that network and charges a fee for access to, and notifications and triggers by that network. Any app that the consumer has on his phone can trigger the Bluetooth message.

Proxama has developed its own App, and has deployed it so far in Norwich and Jersey, to support community wide messaging and marketing. It has recently won a £1m grant from the UK Government to roll out this solution to communities across Britain.

It is helpful to appreciate that a beacon is a small device the size of a slug, which is battery powered (though Proxama are working on a solution that would make a mobile phone emulate a beacon which would be useful in taxis for example). The beacon is a Bluetooth device, so it connects with the Bluetooth app on a smartphone, and "pushes" a message to that phone. The consumer has to do nothing bar have the Bluetooth turned on, and (for the moment) have an app on his phone that recognises that the message is coming from a source that is acceptable to the consumer (it could be the Sky app, Dominos Pizza, YouTube, Google, Waitrose... whatever).





**"THIS IS A REVOLUTION IN MARKETING, AND, IF PROXAMA CAN CONTROL THE INFRASTRUCTURE, AND THE DATA, IT WILL HAVE A BUSINESS WHICH WOULD BE VERY ATTRACTIVE TO LARGER COMPANIES, FROM WPP TO GOOGLE"**

Proxama gets paid for "notifications" – i.e. the beacon interfacing with the phone, and also gets paid a lot more for "click through" by the phone user to actually look at the message being offered. Experience so far is that Proxama get a response rate of between 11% and 25% to the initial message, which is clearly a fabulous number compared to flyers etc. where 2% is considered good. Bus-mounted beacons – these have a range of 5 to 40 metres – will be stuck behind the drivers. In airports they will be stuck on billboards and pillars. Proxama control the network across the beacons (they cost about £12 each to buy plus programming costing £3.40 followed by the fitting cost). So no one can send messages across without Proxama's permission. Retailers can devise their own messages and change them several times a day. Therefore a coffee shop could push croissants in the morning, sandwiches at lunch and, in the afternoon, cakes and scones etc.

**"PROXAMA'S SOLUTIONS ARE ALREADY DEPLOYED IN MANY COUNTRIES AROUND THE WORLD."**

Proxama can then send less retailer specific messages across that network (or be geographic specific) pushing an offer from the local theatre, or rugby club or pub chain which may not have beacons, but want to "broadcast" an offer… perhaps because they have spare seats, or because there is a band playing tonight, or just because it is hot weather and it is "Pimms time". The key to Proxama is that they have exclusive, multi-year deals with the owners of the key out of home media sites who see the opportunity to increase the effective inventory of advertising sites by using digital technology, as well as much better information for advertisers as to the success of their campaigns. This should increase the yield from the advertising, as well as make the advertisers keen to use the greater opportunities to change the offer messaging depending on time of day, weather, stock levels, etc. This is a revolution in marketing, and, if Proxama can control the infrastructure, and the data, it will have a business which would be very attractive to larger companies, from WPP to Google.

**"THE PAYMENTS SIDE OF THE BUSINESS ALSO OFFERS A GREAT OPPORTUNITY."**

If beacons are about "pushing" messages, Proxama also offers "pull" technology where, using NFC (Near Field Communication) or QR codes, consumers can "tap" a coil embedded in a poster, beermat, card (an example was the Oystercard) and receive a download of a voucher/recipe/message etc. That is also part of their offering but requires more consumer acceptance and effort and so is expected to take longer. However, that is expected to be a large market before the end of the decade. Again, Proxama will control the "pipe" and charge for access, for messaging and for downloading and redemption of marketing and loyalty offers.

The payments side of the business also offers a great opportunity, as the US credit and debit card industry moved from "magstripe and signature" to "ChipnPin" (EMV) technology, and then through to "cards on mobile". Proxama offers a suite of software products to enable card processors and banks to migrate their cards to the EMV technology, and Proxama's solutions are already deployed in many countries around the world. The current sales pipeline (taken to be five years value) of this division has risen from £18m in February to £31m (unweighted for probability of crystallising) today.

Increasingly banks are looking at ways to differentiate their offerings to the market, and the combination offer of card management, migration to mobile payments capability and access to mobile marketing capability and loyalty vouchers offers and redemption, is attracting great interest.

All the foregoing means that Proxama could be sharply undervalued at 2p.

# ROBBIE BURNS' TRADING DIARY

*Why do most traders lose money? One of the answers I think is the thrill of the chase: trying to chase volatile shares up and down. Shares like Quindell, Tungsten, Plus 500, New World Oil, Xcite Energy, Coms... the list is endless. But all this isn't really "trading" or "investing" - it's pure gambling for pure adrenaline and perhaps to relieve boredom elsewhere in your life.*

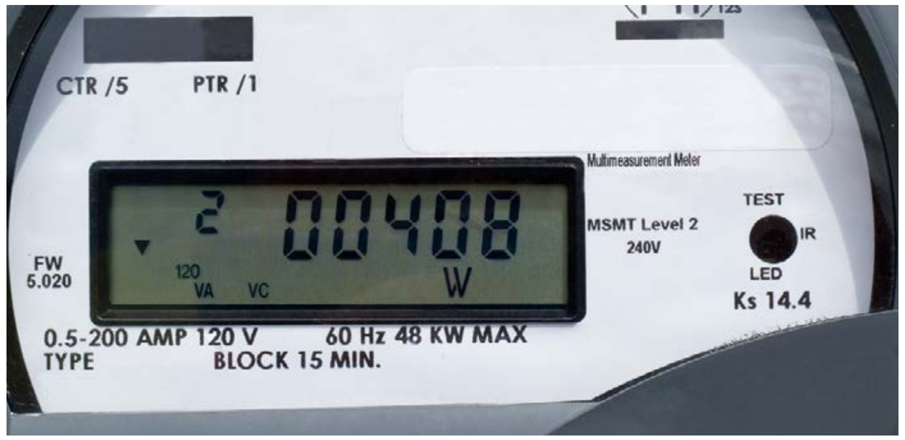
And it there is one thing that's for sure: gamblers always lose, eventually. Sure, there will be big wins too that they'll boast about. But the losses on punts will always stack up, which is why any spreadbetting firm will tell you that most accounts blow out, and many quite quickly.

If you have the gambling mentality, why not just use 10% of your total pot to have fun with in a separate account? Expect to lose it all, have fun, get some kicks; when it blows up you only lose 10%.

But what about the other 90%? Trade properly. Buy really boring stuff - really boring companies where profits are rising, there is a bright future, great prospects, and, hey even a dividend. I would say that being in the lucky position now of having made millions in the market, all that profit has come from boring. None of it at all has come from any "exciting" company - you know, the ones beloved of bulletin boards.

So here are some boring companies I'm in and why. I bet you've never heard of most of them - which is good: the fewer punters in my shares, the less volatile they are. What is ironic to me is I bet you read about these boring ones, nod sagely, but move right along to the next "exciting" volatile share you can find. Now that's odds on!

Starting with a recent buy, **Quantum Pharma (QP.)** (see - told you you'd never have heard of it). Nicely quietly under the radar this one - and I expect to double my money over the next year having bought it at 114p and recently added more at 120p. My target price is well over 200p. Potential for even a treble-bagger, over say three years.




This pharmaceutical maker, developer and supplier actually makes money already. Operating profit soared nearly 200% in the last financial year. A dividend is coming and net debt has come in very low after raising money via a listing a few months ago. With a super pipeline of products, low debt, and the ability to grow by acquisition as well as organically, to me it's a lovely (for now) low risk one to tuck away in an ISA, go on summer holiday with peace of mind and wait for the capital increase.

Another one I bet you never heard of is **Energy Assets (EAS).** I'm already up 70% on my first buy of these and I've bought some more this month. This company is the largest independent provider of industrial and commercial gas metering services in the UK and a provider of electricity metering and data services.





Demand for the installation of advanced utility metering and related services remains high and, as a result, Energy Assets says it continues to experience strong trading and growth.

This area of the market just keeps on growing and Energy Assets is taking full advantage of its position. It just keeps announcing deals too – most recently with City West Homes and Westminster Council. This is another boring one I expect to hold for some time.

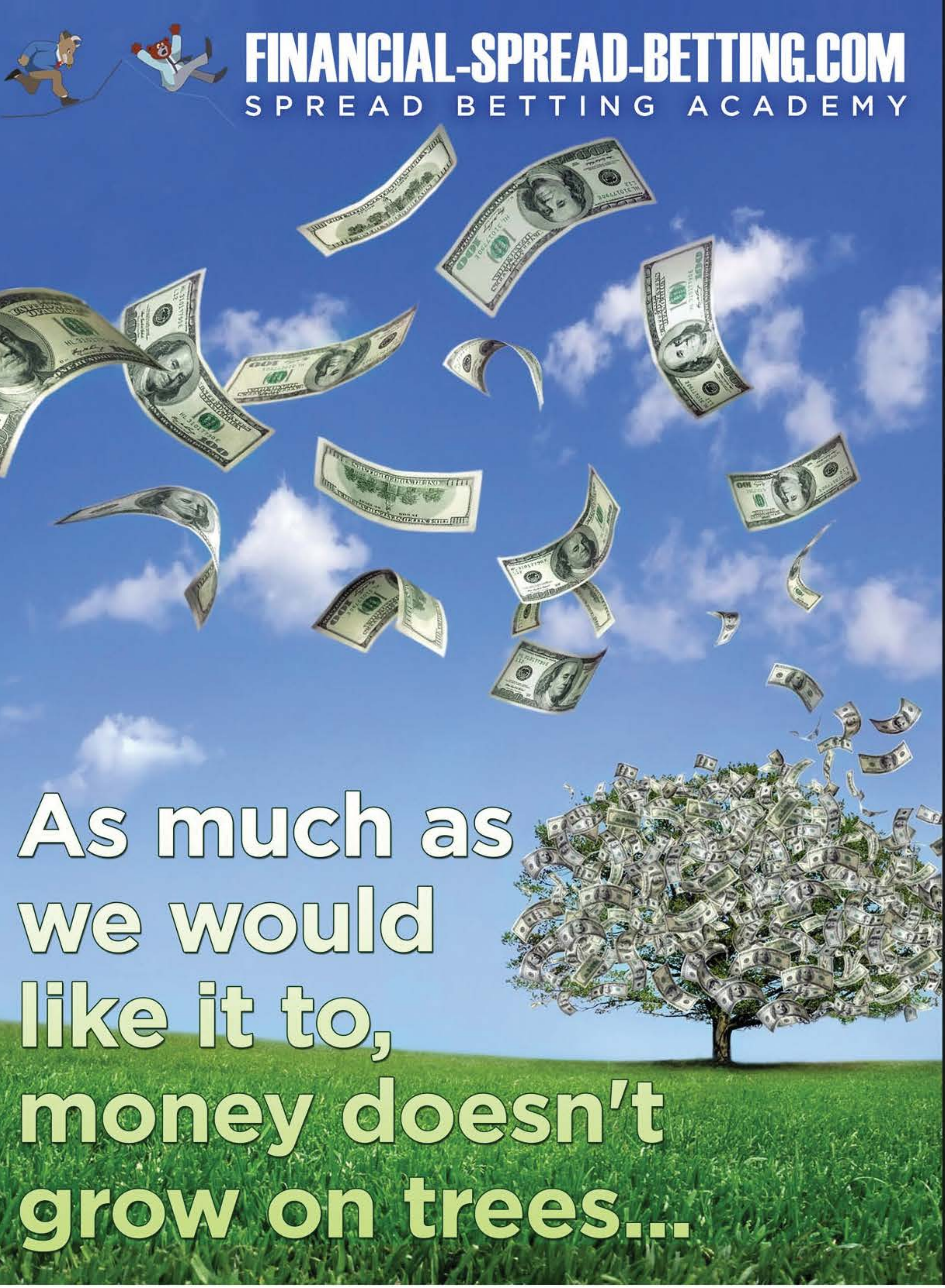
Now one you've definitely heard of **Aga (AGA)!** People might be spending again on bigger ticket items now the election is over and also with the freedom to use up pension money, so I wonder how many pensioners in the country fancy buying an Aga... My desire to buy Aga has been cooking away slowly over the last few weeks after it lost half its value, and I have been building a stake in it starting in the 80p area and buying more as it hit 100p.

Its last results show nice signs of an upturn (it also owns Fired Earth where posh mums buy overpriced tiles – I should know, we have some!) Revenues, profits and cash balances are rising as well. Its AGM statement was interesting and contained the intriguing phrase "we are exploring a number of strategic options". If revenues and profits continue to rise the shares are going to look mighty cheap. Perhaps they might not reach the dizzy heights of 200p - but any recovery statement could see them back up in the 130-150p area.

**"MY DESIRE TO BUY AGA HAS BEEN COOKING AWAY SLOWLY OVER THE LAST FEW WEEKS AFTER IT LOST HALF ITS VALUE, AND I HAVE BEEN BUILDING A STAKE IN IT STARTING IN THE 80P AREA AND BUYING MORE AS IT HIT 100P."**

If any of you are left after reading stuff about boring companies, this one will finish you off! **Empiric (ESP)** specialises in buying sites and turning them into student accommodation. (That's the last reader gone now.) I expect a gradual rise in the share price and some decent dividends and I reckon anyone holding with a three year view will get a lovely "sleep at night" capital rise, even if the main markets tank, and some nice cash in the accounts too via the dividends.

That's it from boring me this time. Next time I'll be back with something really exciting. In the meantime... I really need some sleep. Night night.




## ...but we can give you the opportunity to plant the seeds of your own success!

In our own experience with hundreds of traders from around the world, the 'secret' - if there is one, as to why some of these guys always seem to make money right from the start, is that they keep things simple.

First you must grasp a good understanding of basic market mechanics. Trading with trend lines for example is not rocket science, and is more akin to simple geometry - it does not take a genius to draw a line on a chart. Momentum ndicators require a few more brain cells, but any 10 year old can be taught to recognise a divergence of momentum indicator and price.

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MELLON ON THE MARKETS

# MELLON ON THE MARKETS

**BY JIM MELLON**

*The dog days of the markets are apparently what we face for a while. There is no discernable trend in the equity markets of the West and even Japan seems to have stalled, hopefully temporarily. China is the only major market, (soundly recommended by Merryn Somerset Webb at the recent Master Investor conference), to be making headway.*

**It's pretty speculative stuff though , with a couple of HK listed stocks engaged in solar power, in one case and – wait for it – fine wine and horses, in the other, losing over $50 billion worth of value in two trading days. That's the equivalent of one hefty British FTSE company going up in flames overnight!**

But underneath the drifting flows of the markets, there has been a lot of paddling. At Master Investor 2015 **(and if you weren't here you can see my speech here)** I had a few conviction trades.

One was to short all low yield or negative yield bonds, and in particular the **10 year German bunds.** They were then yielding about 0.2%, and in the past ten days there has been a flash crash in prices taking yields back to over 0.7%. This yield still remains too low and I remain short 10 year bunds, but I would also look at shorting French or Italian bonds for the same

> **"IT MAY AT FIRST SEEM COUNTERINTUITIVE IN THE CONTEXT OF QE THAT INTEREST RATES HAVE GONE UP, BUT IT IS IN FACT ENTIRELY LOGICAL."**

reasons. Risk premia have been distorted by the ECB agreeing to buy vast quantities of sovereign and corporate bonds from Eurozone issuers, hoping to drive peripheral bond spreads down against Bunds and French Oats. This hasn't worked, so I suspect that the ECB will look to do its QE in a different way, buying more corporate bonds, or even bank bonds, to ensure a greater pick up in lending activity in the still depressed Mediterranean parts of the Eurozone.

It may at first seem counterintuitive in the context of QE that interest rates have gone UP, but it is in fact entirely logical. There is a lot of front running of central bank buying to begin with, but then the speculators lose hope, especially with a depreciating currency, and bale out. That is exactly what has happened in the case of the Bunds, and I feel that yields in 10 year German paper should easily exceed 1 per cent in the near future. After all, the asset bubbles caused by QE in property and stocks are potentially inflationary, as is the devaluation of the euro and the recent bounce in oil prices - so why wouldn't interest rates go UP? They are thus up and will continue to rise.

As far as stocks are concerned, we seem to have reached an impasse in the US. Clearly, earnings momentum is being lost, and the US corporate financing gap has now gone negative for the first time in a long while. This means that US companies are not generating enough cash flow to cover their commitments – including cap ex, interest, and most importantly the buyback of their own shares – a trend which has been a major helping hand to indices in recent years.

This bodes badly for the markets, and while I am not signalling a major correction, we are now in pass-the-parcel mode.

We are seeing some evidence of this in more 'glamorous' stocks rapidly turning into fallen angels ; I advocated a short of LinkedIn at Master Investor, and it is now down by a quarter since the show. But LinkedIn is just one member of a cohort of stocks that could easily tumble if their earnings disappoint overheated expectations. I also suggested shorting **Just Eat** in the UK, and although this is down a bit, I would stay short.

Good quality stuff continues to do well; **Galapagos**, another conviction idea is now up 50% since the Show, and I would take half of the table, as the outcome of discussions with AbbVie for its lead drug will be binary.

I would stick with **Synergy Pharma**, listed in the US, which I think will be taken over. It is moving up, and I like the stock action.

In currencies, so far my **Swiss Franc** short is a little against, but it remains a conviction trade. I would hold on to it if you have the stomach for it. **Silver** conversely, is now in profit, and I would run with that. My target for that is at least $20 per ounce before year end, so with some leverage that could be a cracker.

The **Yen** is falling a little against the US dollar, and while it just might go to 125 against the greenback, I would not play it, and wouldn't hedge what should still be a long position in the **Nikkei.** Target there is 22,000.

**Sunny Optical**, another recommendation is up hugely since the show, benefiting from the HK/China speculative bubble that is going on at the moment. I would take profits there. Elsewhere, I would hold onto **Fanuc** and **Kuka** in robotics... they are destined to be long terms plays. I love robotics as a sector and I hope to have a couple more ideas for you in the next issue of Master Investor Magazine.

**"I LOVE ROBOTICS AS A SECTOR AND I HOPE TO HAVE A COUPLE MORE IDEAS FOR YOU IN THE NEXT ISSUE OF MASTER INVESTOR MAGAZINE."**

Since the Master Investor show, of course, the results of the British election have become known. A brief flurry on the FTSE and a bounce in the pound were all too fleeting and it's back to more drift. The scale of the problems that the UK faces, including the fiscal and trade deficits, mitigate against any huge uptick in either stocks or economic activity. Capital investment and savings rates remain woeful, and of course there is the upcoming referendum.

I believe that the UK should leave the European Union, and thus be open to immigration from places which could yield us a healthier crop of talent than the largely unskilled migrants who come "a volonte" from the other 27 members of the EU.

The country has no future as a manufacturer of heavy goods, and we need, as examples, to develop in robotics engineering, in new material technology, in space technology, and of course in the Internet of Things. None of this will happen unless we have sufficient people of high calibre working in these fields. And we certainly don't have enough of them now.

At the moment people from China, India and the US, for instance, are being barred from entering our country to accommodate the tide (one a minute) of migrants from the EU.

If Cameron can't – and by the way he won't – negotiate a better deal, then of course we should leave. As the most important export market for many EU countries, we can negotiate a customs union, and avoid the inevitable decay that comes from being part of a bureaucratic, inefficient and rapacious Euroc-racy.

Now if that happened, I really think the FTSE and broader market could take off, we would be exceptionally attractive to foreign investors and sterling would rise. Until it happens, however, there will be continuous uncertainty, and general stagnation in the domestic financial markets is to be expected. These types almost always get it wrong, and on this issue they will do so again. I think the result of a referendum will be close, as the EU and the UK government will spend taxpayers' money on a campaign of North Korean proportions to encourage the result that they want.

Until next time, when I will have some fresh recommendations...

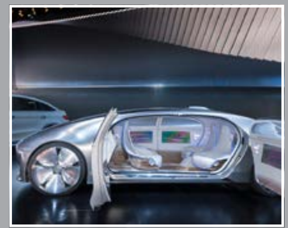
**Happy Hunting!**

**Jim Mellon**





## What Jim read this month...



### Cars of the Future, Today

"The pace of technological advancement accelerates every year"- sound familiar? Mike "Mish" Shedlock takes a look at two prototype cars set to revolutionise the future of transportation: a flying car that wouldn't look out of place on the Jetsons and a two-wheeled self-balancing car that puts even the most pimped-out mobility scooter to shame. The prototypes have a little way to go before they are ready for the consumer market.

**From Mish's Global Economic Analysis - CLICK HERE**

### What Was the Worst Prediction of all Time?

The Atlantic compiles a name and shame list of the worst predictions made by so-called experts over the years, from David Pogue's statement in 2006 declaring Apple will "probably never" release a mobile phone, to the baseless "peak oil" hysteria. It makes for an entertaining, if a little embarrassing, read. Thankfully none of our own writers made the cut.

**From The Atlantic - CLICK HERE**

### Moving to Mars: Preparing for the Longest, Loneliest Voyage Ever

The New Yorker's Tom Kizzia looks at the challenges astronauts will face on the impending (if we are to believe the excitable experts) voyage to Mars. Using the early polar expeditions as example, Kizzia looks at the extreme isolation and arduous journey ahead of any aspiring Martian explorer.

**From The New Yorker - CLICK HERE**


### Uber Fund-Raising Points to $50 Billion Valuation

That's right, Uber is fund-raising again. Everyone's favourite black cab bothering, billion dollar start-up is looking to fund strategic partnerships -not expansion- pointing to a $50 billion valuation. Only one other Silicon Valley start-up attained such a valuation as a private company: Facebook. Hail a cab no-more. All hail Uber.

**From The New York Times - CLICK HERE**

### Zuckerberg, Tech Investors Fund AltSchool Initiative

Unfortunately, the irony that the man who brought us Facebook, heralding a new age of procrastination for the world's disenfranchised youth, has backed a reform of the American education system seems lost on the author... It is revealed a number of tech investors, Zuckerberg included, have pumped a $100 million dollar boost into AltSchool. AltSchool uses tailored software to personalise a student's educational needs and aims to allow teachers to "be their best selves" leveraging technology. With such high-profile backing, it looks to be a welcome solution to America's highly criticised educational system.

**From USA Today - CLICK HERE**

AROUND THE WORLD IN A DOZEN PROPERTIES (PART 2)

## AROUND THE WORLD IN A DOZEN PROPERTIES (PART 3)

# HOW (AND WHEN!) TO INVEST INTO THE WORLD'S FROTHIEST PROPERTY MARKET – HONG KONG

**BY SWEN LORENZ**

*It was Mark Twain who once said, "Buy land, they're not making it anymore." Indeed, had you done so in Hong Kong a few decades ago, you'd now be in a pretty good spot financially. That's despite the fact that in Hong Kong, they ARE making more land.*

Each time I visit the former British Crown Colony, the harbour line of the city has changed slightly. Hong Kong is a master at reclaiming land from the sea, having grown its useable land mass by more than 60 square kilometers. Its new airport and the Disney World Resort are entirely built on reclaimed land, and reclamation in its main harbour area has been so considerable that a discussion started about the risks to the city's natural harbour and its use for transport of both cargo and people.

### One of the most chronically overcrowded cities on the planet

Despite all these efforts, Hong Kong is a territory chronically short of land. Most of its 1,104 square kilometres are mountainous regions and can't be developed at all. Also, business and finance is, of course, concentrated around the central areas of Hong Kong where space is chronically short. Due to the sky-high land prices, Hong Kong became one of the world's most vertical cities, with sky-scraper squeezed next to sky-scraper. Population density is among the world's highest.

It's not just in terms of being built-up that Hong Kong is a city of superlatives. What was a sleepy backwater with just 400,000 residents in 1900 (when Greater London already counted 6.7m residents), has now become the world's 3rd largest financial centre after New York and London. Hong Kong is not just a gateway to China; it is also one of the world's major hubs for trading and financial transactions.

Hong Kong has one of the highest per capita incomes in the world; it has the greatest income inequality of all major cities on the planet; and it's regularly named as the freest market economy by the Heritage Foundation Index of Economic Freedom. It recently ranked fourth in terms of the highest percentage of millionaire households, behind Switzerland, Qatar, and Singapore, with 8.5% of all households being worth at least one million dollars.

No wonder then that property prices have risen to stratospheric levels. In 2014, Hong Kong advertised the world's most expensive home with a price tag of EUR17,000 per square foot. That means a 4,600 sq ft home sells for more than EUR70m! Even London and New York pale in comparison.

The increase in prices in Hong Kong during recent years has been staggering. Demand was strongest for small residential units, driven by the city's growing army of well-heeled young professionals. Since 2003, prices for small residential units have risen five fold.

## Even with land being scarce, there is no guarantee that prices rise in a straight line

Amazingly, Hong Kong wasn't overly affected by the credit crunch. Shares listed in the territory did take a nose-dive in the 2008/09 crash, but property prices didn't. Since 2009, prices in the residential market are up 109%.

Will it continue to rise? And how does one get in on the game without travelling to Hong Kong and putting a million dollars on the table for a small residential unit?

Anyone wanting to invest in Hong Kong property needs to be aware of a number of peculiar factors that are driving the market. Those can, at times, also lead to extreme swings in the opposite direction. Such was the case in the mid 1990s, when property prices fell by 65%. On my recent visit to Hong Kong, I found that prices in the residential sector had recently weakened a bit.

**"WHEREAS THE LOCAL ECONOMY IS A BULWARK OF UNREGULATED CAPITALISM, THE PROPERTY MARKET OF HONG KONG IS ACTUALLY ONE OF THE MOST GOVERNMENT-CONTROLLED PROPERTY MARKETS IN THE WORLD."**

So where will prices be heading from here, and when is the best time for investors to get in?

Incredibly enough, whereas the local economy is a bulwark of unregulated capitalism, the property market of Hong Kong is actually one of the most government-controlled property markets in the world.

A small number of very large property development groups own vast landbanks. It's the government that then determines how much of these land banks is released for development. The process to determine the policies can best be described as an old boys' network consisting of government officials and some of the richest families of the territory. Throw in a bit of corruption, and you basically have a cartel that determines to a large extent how much supply of new properties is being released into the market.

The Chinese being notorious gamblers and momentum investors, there is also a strong element of cyclicality added through both mentality and financial regulation. During downturns, the authorities and the local banking sector loosen lending rules. When the market shows signs of overheating, they are tightened. Nothing unusual per se, but the swings of the Hong Kong market are more extreme than in other localities.

Those with the right feeling for timing were able to repeatedly make a killing in the Hong Kong property market. It's no surprise therefore that of the 20 richest people in Hong Kong, half have made their money in property (and the other half with virtually no exception has had some kind of involvement in the property market). Those who fared best historically were those who combined a vast land bank with a strong balance sheet. They were able to ride out and actively take advantage of weak periods, to expand rapidly during periods of rising prices.

## This property company is the bellwether of the industry

Right among the leaders of this group are the Kwok brothers, Thomas and Raymond. Estimated to be worth $15 billion, they control Sung Hung Kai Properties (SHKP), one of the leading property development groups of Hong Kong.





The company was one of the many non-British owned companies that overtook the British trading companies that dominated the financial order of Hong Kong prior to 1997. It was founded in 1963 and listed on the local exchange in 1972. It specialises in premium-quality residential and commercial projects, with most of its existing rental portfolio focussed on Hong Kong, and only a smaller part of the portfolio now in China. At last count, 80% of its rental income was generated in Hong Kong.

Like virtually all other Hong Kong based property groups, SHKP has recently been branching out to mainland China. In Hong Kong, it owns 28.7m sq ft of completed investment properties with a further 20.8m sq ft of properties under development. In China, it owns 10.3m sq ft of investment properties with a staggering 71.3m sq ft of additional space under development. Property in China is obviously less valuable per square foot than in Hong Kong, but it's clear that the mainland will contribute significantly more to the group in the future. During the past five years, the group's rental income in Hong Kong rose an average of 10% per year, whereas in mainland China it rose by an average of 37% per year.

What initially sounds like potential over-expansion on the mainland is actually built on an extremely solid financial footing. SHKP's balance sheet is currently 85% equity and just 15% debt. The group has some of the highest credit ratings amongst Hong Kong developers – Moody's gave SHKP an A1 rating and Standard & Poor's gave the Group an A+ rating.

**"WITH SUCH A STRONG FINANCIAL FOUNDATION, SHKP SHOULD BE IN A GOOD POSITION TO WITHSTAND ANY POTENTIAL DOWNTURN. AND SUCH A DOWNTURN, IT SEEMS, IS NOW LIKELY ON THE CARDS."**

With such a strong financial foundation, SHKP should be in a good position to withstand any potential downturn. And such a downturn, it seems, is now likely on the cards. In March, property sales fell by 28%. The Hong Kong Monetary Authority passed the seventh round of market tightening measures, and there is a political movement to release more land for residential development so as to ensure that first-time buyers get a chance to get onto the property ladder. Right now, the city has the least affordable housing on the planet, with the median home price 17 times the average house-hold income. From here on, it'll probably be downwards – at least for a while.

## The time to buy probably hasn't come just yet

That leaves SHKP properties an investment that one mustn't get excited about just yet. However, investors are always advised to do some long-term monitoring of quality investments, so that they are ready to invest when the right opportunity arises. In the case of SHKP, such an opportunity last arose in 2008/09, when as a consequence of the global share price rout the stock price temporarily tumbled by 70%, before rising 200% in the following five years.

It's not clear yet if Hong Kong is indeed facing a "perfect storm", as some predict. What is clear, however, is that a combination of new supply hitting the market, monetary cooling measures, and an impending interest rate rise are all in the making. None of this bodes well for the Hong Kong property market in the short term. SHKP, however, is likely going to weather the next storm, too.

For investors, the question will be at what point during the coming downturn will a buying opportunity arise. Master Investor magazine will be on the lookout for you, and get back to the subject when the froth has come off!

# HOW TO PICK THE PERFECT SHARE

# THE SEVEN SECRETS TO SUCCESS

BY JAMES FAULKNER

## What makes a good company?

One of the inherent contradictions within capitalism is its tendency to gravitate towards monopolies. From a capitalist's perspective, a monopoly is the favoured situation, as it removes the competition and enables supernormal profits to be extracted indefinitely. However, in practice, monopolies tend to be bad for the consumer, so most governments take action to break them up wherever possible. At the other end of the spectrum is what economists refer to as "perfect competition", a situation where myriad sellers operate in a market with no product differentiation or barriers to entry or exit. While such a situation may be advantageous for the consumer - ensuring that prices remain as low as possible - it is clearly not attractive from an investment perspective.

The real investment success stories tend to sit somewhere in between these two extremes: close enough to perfect competition in order to remain off the radar of the authorities, but close enough to a monopoly in order to attain a very high return on capital. These companies tend to have achieved a high level of differentiation in their products or services, either through technology ownership or branding. This enables them to compete highly effectively, but not on the basis of price alone. In the words of Warren Buffett, these companies have built an "economic moat" around their businesses, which is very hard for competitors to scale.

> **"IN THE WORDS OF WARREN BUFFETT, THESE COMPANIES HAVE BUILT AN "ECONOMIC MOAT" AROUND THEIR BUSINESSES, WHICH IS VERY HARD FOR COMPETITORS TO SCALE."**

## Competitive advantage

However, it is often posited by economists that no competitive advantage is maintainable in the long term. As new technologies arise, old business models are disrupted and previous market leaders often find themselves on the wrong end of Schumpeter's "creative destruction". Investors must take a view whether or not they believe a firm's competitive position is sound or whether it is about to come under threat. In terms of technological advantages, it is often hard to form a view unless one is highly knowledgeable with regard to the specific technology or industry in question. However, competitive advantages formed by branding power are often much easier to assess - for example, it is likely that the Coca-Cola Company will go on making a very respectable profit for decades, if not centuries to come, unless public tastes alter in some drastic, unforeseeable way.

## ROCE & profitability

We have addressed the qualitative characteristics of competitive advantage, but what are the quantitative characteristics? Companies with a strong competitive advantage usually exhibit two key features: a high return on capital relative to their cost of capital; and high operating margins (profitability). Return on capital employed (ROCE) is a measure of a company's bang for every buck it invests in itself. Companies that are capital intensive tend to have a low ROCE, whereas companies that use an asset-light business model (Domino's Pizza being a very good recent example) tend to exhibit a high ROCE. Meanwhile, operating margins are a measure of profitability and pricing power. Companies that have high operating margins are more likely to be able to increase prices without suffering much by the way of reduced sales – in economic terms we'd say that demand for their products/services is relatively price inelastic.

## Cash generation

Profit is a matter of opinion, cash is a matter of fact, as the saying goes. Companies that claim to be highly profitable but do not generate cash will not be around for very long. Cash generation is the ultimate goal all businesses: it enables them to pay dividends to their shareholders, reinvest in the business, and pay wages to their employees and taxes to the government. Cashflow is also much less easily manipulated by an unscrupulous management team, so investors should get used to looking for a history of strong and consistent cash generation. While there are many measures of cashflow, a preferred one among analysts is Free Cash Flow (FCF), which can be calculated relatively easily by taking Operating Cash Flow and subtracting capital expenditures. This provides an overview of the cash available to equity holders after all the necessary investments have been made within the business.

## Balance sheet

Needless to say, maintaining a strong balance sheet is of the utmost importance for any successful company. Debt is often the destroyer of companies. However, this is not to say that debt in itself is bad. Investors need to learn to understand the requirements of the particular business sector in which a company operates. For example, a company operating in a highly cyclical sector such as the house building sector should have relatively low levels of borrowing; whereas a company operating in a defensive sector such as utilities can probably afford to take on more debt because it has relatively dependable and stable income streams. Looking at the absolute debt burden in isolation probably doesn't say much about a company; investors should look for the interest cover, preferably on a cash flow basis, in order to ascertain how close a company is to getting into financial difficulties. The higher the interest cover, the more financially sound the company.

## Liquidity

If you had no way of exiting your investment, would you sleep soundly? Warren Buffett has often quipped that he only likes to own companies that he'd still feel comfortable with if the market shut down for ten years. That said, personal circumstances may necessitate a sale of an investment, in which case liquidity would clearly be an issue. While most large stocks are easily traded, many smaller ones are not. However, this is by no means a hard and fast rule; there are plenty of small companies that enjoy a very liquid market for their shares.

## Macro backdrop

It always helps to have a tailwind in your sails! Consider the recent experience of the supermarket sector in the UK. Consumers had to endure year upon year of cuts to real incomes, which put pressure on budgets and forced many to 'trade-down' to discounters. At the same time, inflation was relatively low throughout, which made it difficult for supermarkets to raise prices. Growing competition has now led to a price war. These are not conditions conducive to a happy investment outcome. Meanwhile, the pharmaceuticals sector offers a different outlook. The developed world is faced with an ageing population, which guarantees rising demand for decades to come. In addition to this, most pharmaceuticals firms have overcome the so-called 'patent cliff', whereby many of their most profitable patented drugs were opened up to 'generic' competition. They are now rebuilding their pipelines, and new medical advances are promising to yield a string of new innovative treatments in years to come. That is what I would call a tailwind.

**"IF YOU HAD NO WAY OF EXITING YOUR INVESTMENT, WOULD YOU SLEEP SOUNDLY?"**

## Management

This is often a very difficult factor to assess, especially for a private investor who lacks direct access to management. A good starting point is to do a background check on key members of senior management to find out whether or not they have achieved success in previous roles. Are they properly incentivised? This usually means having a significant equity stake in the business relative to their own net worth, or indeed taking a significant share of their salary in stock. The management factor is usually easier to assess in small companies, where management often constitute the largest group of shareholders. However, In larger companies management shareholdings are usually insignificant in relative terms, so an investor needs to rely on other information. Better still, pick a business that can practically run itself. In the worlds of Warren Buffett, "a really good business doesn't need good management - and a poor business can't do well no matter how good management is."

THE LIMPOPO DISPATCHES

# THE LIMPOPO DISPATCHES

## IN SEARCH OF QUALITY

BY ROBERT SUTHERLAND SMITH

*How I came to look like Boris Johnson and later hosted a midnight review of quality share ideas, sending the witch doctor to sleep and Angus MacQuerkie into the night...*

There were the three of us gathered on the veranda of my wooden bungalow which I call home, by the banks of the fair Limpopo River – which, as usual, was making its way quietly towards the distant Indian Ocean, where dolphins and porpoises play, and once the old flotilla lay off Steamer Point, in the Pax Britannica of old British Colony of Aden (now the besieged port of the Yemen Republic).

There was yours truly, together with Milton Tomboya DLit, MA (Cantab), the local witch doctor – and much valued dinner companion – and the local Church of Scotland missionary, Angus MacQuerkie, representative of the Missionary Bible Association of Aberdeen, who modestly describes himself as the representative of the Lord.

We are never certain whether this is a loyal reference to his Highland Chieftain the Great MacQuirkie of the Glens and Islands or merely the Creator of heaven and earth. In the mind of a Highland Scot, the Clan Chief is certainly close to the Creator himself, sitting with the righteous at his right hand, which these days includes Alex Salmond and Nicola Sturgeon as father and mother of the Scottish nation. I suppose. It is curious how in MacQuirkie's theology the righteous are all Scots and probably so is God, which mystifies the Limpopo locals and doesn't give the rest of us much of a chance. That's Scottish Calvinism for you!

Being after dinner, we were each formally attired in evening dress and decorations. Dr. Tomboya sported a Companion of Honour, Croix de Guerre and British Military Cross with bar (though it was never actually revealed by the good doctor, in what circumstances he actually came by these small, diverse manifestations of national recognition and gratitude). The missionary modestly wore the Bible Society Medal only and of course, the clan badge bearing the motto "Sell Early" – a sentiment that the MacRothschild's had once claimed as the source of their success and great fortune in share dealing beyond the glens.

They were both looking deeply concerned, after I had divulged to them my awful condition: I feared I was being transformed into Boris Johnson. Not a thing that a chap hopes to happen to him in a tonsorial and sartorial nightmare.

I continued with my account: "I dread the morning when I awake and stare into my shaving mirror to find that the reflection staring back does not seem to be my own but that of Boris Johnson, looking grotesquely old. Is it some kind of grim prophecy or dire warning? Is it perhaps some sort of inverted example of the portrait of Vivien Grey in the attic plot, where the image never grows old?" I asked these questions with a trembling hand and dry throat. It was as mystifying as it was horrifying! I might want to build an airport in the Limpopo and call it Bob's Island!

**"IN THE MIND OF A HIGHLAND SCOT, THE CLAN CHIEF IS CERTAINLY CLOSE TO THE CREATOR HIMSELF, SITTING WITH THE RIGHTEOUS AT HIS RIGHT HAND."**

"This bad news old man" said Milton Tomboya, the elegant local witch doctor puffing on one of my Cubans, as he lounged in a veranda deck chair marked "SS Titanic" on the back – where it often has the word "Producer" or "Director".

Indeed so!" added MacQuirkie, his black beetled Scot's eyebrows locked in a look of deep consternation.

"It sounds a wee bit like the case of Dr. Jekyll – a respectable Edinburgh physician ye understand – who changed into a ware wolf, from time to time. Does the image you see look like a ware wolf, as well as Boris Johnson, perhaps?"

"Yes!" I replied. "It has crafty looking narrow blue eyes, gazing knowingly from beneath a head of wild, chaotic hair as untamed as our natural Limpopo flora."

"Speaking as a native born Scot", MacQuerkie continued, "I cannae think of anything worse than appearing in the mirror as some unkempt Tory politician from London. It fair makes the flesh creep!" he added gloomily.

"It doesn't speak like a normal human being – merely mumbles and grunts and grimaces – the way they are taught at Eton College I imagine?" I added. Both men looked shocked and downed another Scotch whisky from my diminishing stock of "Auld Heather Malt."

"Och aye mon, ye dinna comprehend a word they say", said the representative of the Lord.

Dr. Tomboya, pointed out that his entire tribe actually spoke with late nineteenth century Old Etonian accent as a result of its originally being taught by a Master of that school who had fled Eton College for not beating the boys sufficiently, but got lost on his way to seek refuge with Dr. Arnold at Rugby School – an easy mistake to make for a short sighted man who taught Latin not geography.

"Hence my own superior and mellifluent diction", added the witch doctor self contentedly. "When we were visited by the late King Emperor", he ruminated, "he felt very much at home amongst the sounds of Windsor on Thames, here on the Limpopo."

"But what about my own appalling condition?" I asked, as they strayed off the subject?

"First", said one of them, "remember it could be worse. You could have found George Osborne staring back at you as you shaved. Think how depressing that might have been? Remember he was the man who talked the UK economy into near double dip backwardness in 2010. You might have gone off your head and done away with yourself, and ended your days hanging from one of our lovely Bongo Bongo trees."

"Second, I suggest that the cause of your problem might actually be you; or more precisely your ageing problem."

"Ageing problem?" I responded. "What on earth do you mean?"

Dr.Tomboyo gave a deep sigh. "Now old Chap" he began "we are all of an uncertain age here, though naturally I will not ask you say exactly how old you are, nor tell my own age! I won't even ask you to write it on a piece of paper".

"Certainly not!" erupted Mac Querkie.

"Consider", continued the good doctor, "that as you grow older, you start to lose control of almost everything. Your eyes, which I see are blue, have weakened and narrowed from your wide-eyed 'salad days'; and your hair has grown pale and wispy, sticking up in all directions, uncontrollably, and most noticeably when you get out of bed in the mornings, I imagine."

The truth began to dawn as he spoke these words of encouragement.

"You mean," I replied with hope mounting in my heart, "that the monstrous creature I see in the shaving mirror each morning is not Boris Johnson – nor even a figment of him – but me?!"

"Exactly", added the witch doctor in his rather pre-Second World War Limpopo Etonian drawl.

"Thank heavens", I exclaimed. "It's me after all! Not Boris Johnson! What a relief!"

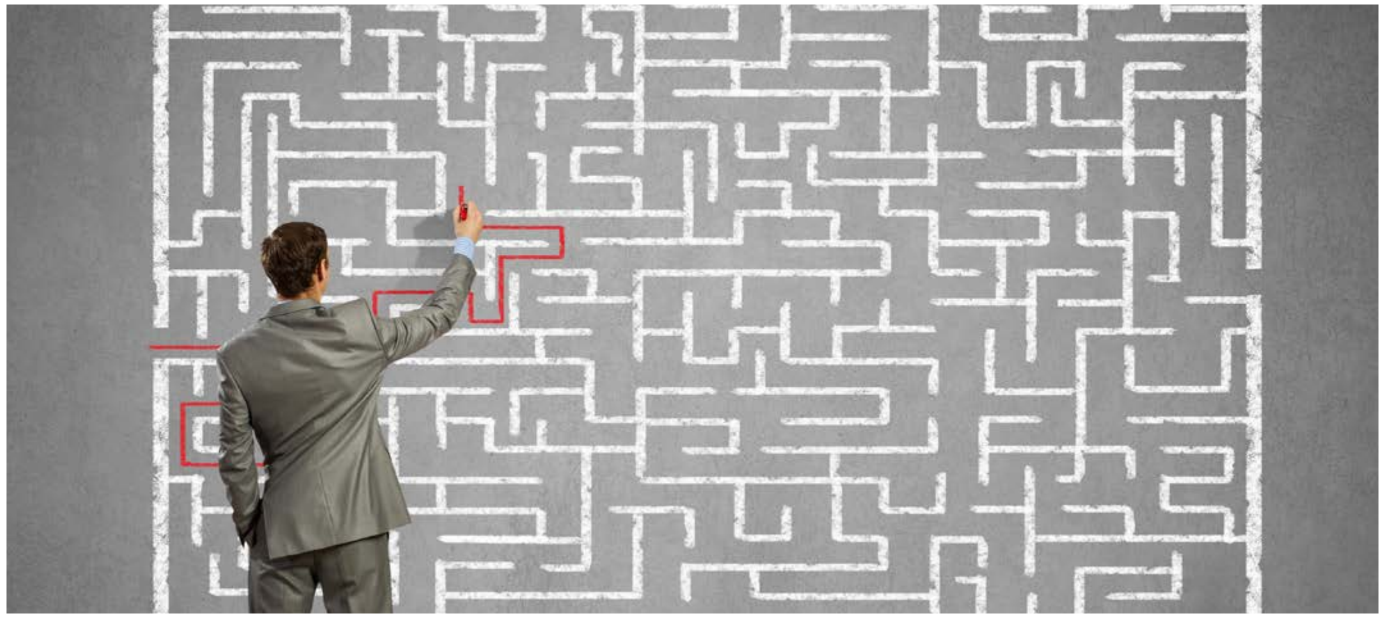
"Thank the Lord", cried MacQuirkie. "I did not know if I was meant to raise my eyes to the heavens or towards the Highlands."

**"THERE ARE NO GIFT HORSES IN THE STOCK MARKET BUT THERE ARE PLENTY OF BLACK HORSES – ONES THAT DO NOT SHOW IN THEIR TRUE COLOURS."**

And the lesson is, dearly beloved, that if you are old and of an uncertain age – a number you will not wish to commit to paper – a bit podgy, with thin, white 'Barnet Fair', you can fluff up into a chaotic hair style with your fingers. Blue eyed? Once round and wide with innocence but now dimmed and narrowed by bitter experience? Then you too may look like Boris Johnson when you get out of bed in the morning and behold your ancient self in the mirror. Which rather demonstrates that King Lear and Sir John Falstaff may have looked like Boris Johnson – or so I guess. They used to say that babies with no hair looked like Winston Churchill; we now know that some, round, podgy old men with chaotic, thin, white hair look like the Mayor of London and MP for Uxbridge. It makes your flesh creep, as Angus might say.







Except, that doing my Boris Johnson imitation last week, when grabbing the hand of a blue rosetted Tory voter at the polling station, was a joy to perform. Fluffing up the Barnet, I grabbed him firmly by the hand and grunted:

"You don't know who I am but I'll give you a clue: my first name is Boris!"

The look of terror was sublime!

Having been saved from worst fears, we later continued our conversation indoors over a glass of V.V.S.O.P. brandy. Tomboya has just returned from a flying visit to London to hand in his thesis to the Hedge Fund Management College in darkest Mayfair, somewhere in Shepherd's Market where scholarship is always marinated in ordinary wine served in very expensive bottles at the Golden Fleece bar and restaurant.

"Tell us", said Mac Quirkie, thinking about how to deploy his newly liberated pension savings contributions (net of a lifetime's tax benefit), "what makes a share right to buy?"

"The first thing to realise is that most shares are second hand", I said. "There are no gift horses in the stock market but there are plenty of black horses – ones that do not show in their true colours. There are two issues to bear in mind: the nature of a company and the value of its equity. They are related but not the same."

Two basic safety first rules: never buy shares over the phone from cold callers; and avoid shares that have been through the hands of private equity practitioners and returned to the market at a much higher price with a reduced (i.e. riskier) range of activities loaded down with risky levels of debt.

The mission is to find companies with a high and sustainable return on assets and high margins. That implies a company with competitive advantage which erects barriers to entry against competitor companies. It also means buying the equity of companies whose return on equity is not too high due to too much debt on the balance sheet – a state of innocence that is very hard to find.

The competitive advantage in competitive markets can come in various forms. It can be intellectual property, operational skills, management ability and reputation, brand loyalty, and of course, scale of operation which provides scale of competitive unit cost advantage. The share valuation attractions include a dividend and reliable dividend growth, good cash flow and net attributable assets – all of which help to give stability to a share's price by providing a floor beneath it.

**"NO COMPANY IS PERFECT. WHEN IT COMES TO GEARING, MOST UK COMPANIES HAVE IT."**

A share which exemplifies the aforementioned characteristics is **Rolls-Royce (RR.).** It had a gross margin of 23% last year and an operating margin of 10%, which is large for a manufacturer and a indication of the scarcity value of its products and services which form part of a barrier to entry to its market and client base. **GKN (KGN)** by way of contrast has an operating margin of only 4.4%. No company is immune from shocks, including Rolls-Royce despite its large order book stretching into the future. It was hit by the sudden drop in the oil price, which reduced demand for it turbine division which serves the oil industry. That provided a wonderful opportunity for analysts to put a downgrade notice over the shares, which normally carry a premium. Consequently, I saw the bad news as an opportunity to buy the shares. The arguments were outlined in my review of the shares in February, when the share price was 900p. It is now, last seen, 1009p. The share price still looks to be on a recovery uptrend and I still regard the shares as good value.

Other shares which I would add to the list of quality companies trading at a reasonable price at the moment include **Diageo (DGE)**, which although far more exposed to competition than Rolls-Royce, has an array of global brands and scale of operations as its qualifications as a good quality business. Having come down, the share price seems to be staging a recovery and carries a decent historic dividend yield of 3%. Note that it is shown to have grown its annual dividend by 7.45% per annum over the last five years. Last year the company reported a gross margin of a handsome 58%, an operating margin of 23% and a net margin of 18%. However, there is relatively high equity gearing and it does not have a lot in terms of assets attributable to ordinary shareholders. No company is perfect. When it comes to gearing, most UK companies have it.

Finally, I recommend a look at **Unilever (ULVR)**, which has come down from a share price peak of 3,087p last month to 2,900p last seen. Although operating in highly competitive markets, it managed to increase its dividend by a remarkable 19% per annum over the last five years. Again it is highly geared, and decidedly so given the markets it competes in. It also has a historic dividend yield of a near 3%.

But remember that like the last Labour Party Manifesto, nothing in the market is written in stone. Even the Financial Times no longer has a Portland stone version for delivery to the West End of London as it did in the Stone Age. **Marks & Spencer (MKS)** is a share which is recovering from the loss of its once undoubted market leadership in UK retailing. It is a share which will, to judge from the progress so far, continue to rebuild shareholder value. That said, after a brilliant year of capital gains and a return to progressive dividend rewards, the share does look to be a little ahead of itself. It is certainly not in the category of shares which never go wrong. Bear in mind that the stock market is never a place where never should be said carelessly. Everything is possible in the equity market.

Another once quality investment that looked as though it could never go astray was the ever growing and ever investing **Tesco (TSCO)**, which are now 219p last seen. I cite it as an example of the fact that the price of market leadership is constant attention and constant vigilance by an always focussed management. It is also in its way an example of the old saying that you learn more from failure than you ever do from success – particularly if you take the success for granted. One does not need to recite the facts of Tesco's decline except to say that it designated its original, successful UK business a sort of museum piece status, a cash cow, to be used in pursuit of new empires abroad. This is a model of business which is always fraught with danger, especially if you are a retail company. Having broken out of its big downtrend, the share has recently been moving sideways in a trading range of 220p to 250p. Shares always break out of trading ranges; it is merely a question of trying to work out whether it will be up or down. That trading range looks to me as though it is operating in the context of a wider downtrend. So in my opinion is that Tesco is not one chase at the moment. I suppose that good news is still a good way off.

**"BEAR IN MIND THAT THE STOCK MARKET IS NEVER A PLACE WHERE NEVER SHOULD BE SAID CARELESSLY. EVERYTHING IS POSSIBLE IN THE EQUITY MARKET."**

I look and see that the local witch doctor has fallen fast asleep, with a half consumed glass of brandy held feebly in one sleeping hand. Angus MacQuerkie has slipped off into the night with my bottle of "Auld Heather Malt". All's well that ends well!





## SMALL CAP CORNER

# SORTING THE WHEAT FROM THE CHAFF

**BY JAMES FAULKNER**

*In choosing this month's small caps I have attempted to sieve through the chaff of the small cap market – and believe me, there is a lot of it – to uncover a selection of what I believe to be the higher quality plays. All the following companies have strong trading records, exhibit strong financials and benefit from competitive advantages that are hard to replicate. In addition to this strong foundation, each stock benefits from considerable macro tailwinds, and each (with the possible exception of Sprue Aegis) has solid trading momentum.*

### Clinigen (CLIN)

Clinigen supplies drugs for clinical trials, many of which compare an experimental treatment with one already on the market. It also supplies unlicensed medicines into markets where a drug is being withdrawn or where there is no alternative. In addition to this, it also buys drugs from other companies, such as AstraZeneca, which sold it the antiviral agent Foscavir in 2010.

The Clinigen Group was formed in 2010 and comprises two divisions - Services and Products. The group manages the supply of drugs into a total of 53 countries, with particular expertise in the therapeutic areas of leukaemia (and other areas of oncology), haematology, transplantation, anti-infective, pain management, gastrointestinal and hospital and critical care, as well as orphan diseases.

**"CLINIGEN IS ABLE TO CHERRY PICK TRIED AND TESTED DRUGS WHERE IT SEES AN OPPORTUNITY TO EXPLOIT ITS OWN INFRASTRUCTURE AND EXPERTISE, THEREBY MAKING IT A LOWER RISK PLAY THAN MANY OF ITS PEERS."**

Clinigen offers investors exposure to a very attractive and potentially highly lucrative business model. Through its extensive network of relationships with major pharmaceuticals firms, Clinigen's specialist Services division offers the perfect forum for the firm's M&A drive to grow its Specialty Pharmaceuticals business, which is looking to replicate the success of peers such as Alliance Pharma, but on a global scale.

CLINIGEN Group plc

This is not your typical pharmaceuticals company funnelling money into drug development programmes that may or may not succeed; Clinigen is able to cherry pick tried and tested drugs where it sees an opportunity to exploit its own infrastructure and expertise, thereby making it a lower risk play than many of its peers.

The Clinigen investment case fits well into the current trends taking place in the pharmaceuticals market. Firstly, under pressure from tightening regulatory requirements and falling returns from R&D, large pharmaceuticals firms are increasingly turning to outsourcing as a means to simplify and streamline their businesses.

SMALL CAP CORNER

Clinigen's expertise lies in helping pharmaceuticals companies navigate these regulatory and logistical hurdles, which become particularly complex when the drugs are unregulated (but required by a critically-ill patient). Meanwhile, the firm's commercial relationships with pharmaceuticals firms (it currently works with 15 of the top 20 pharmaceutical companies) also bring added benefits in that it is kept alert to any potential acquisitions for its Specialty Pharmaceuticals arm.

When some pharmaceuticals products approach the end of their life cycle they can become non-core to a firm's strategy and a drain on resources. Clinigen offers pharmaceuticals firms an exit route, either via management through its GAP business (enabling access to patients reliant on the drug even as sales, marketing and direct distribution is terminated by the pharma company), or through the outright acquisition of the drug by Clinigen Products. Although such drugs may no longer fit with a particular pharmaceutical company's strategy, it does not follow that they are a bad investment for Clinigen: since its acquisition from AstraZeneca in 2010, Foscavir has delivered a four-fold growth in sales under Clinigen's management.

**"SINCE ITS ACQUISITION FROM ASTRAZENECA IN 2010, FOSCAVIR HAS DELIVERED A FOUR-FOLD GROWTH IN SALES UNDER CLINIGEN'S MANAGEMENT."**

In April Clinigen announced what appears to be a potentially transformational acquisition. In a £225 million deal, Clinigen acquired Idis, the global market leader in providing access to unlicensed medicines in over 100 countries, across several therapeutic areas (including oncology, immunology and orphan indications).

Although pricey (Clinigen had to pay c.14x EBITDA), the deal offers some compelling synergies, with Idis strengthening its offering in all three of its main divisions. It also brings Clinigen one big step closer to reaching its goal of becoming the go-to provider of unlicensed medicines – a market which, according to joint house broker Peel Hunt, currently amounts to $2.2 billion, with the potential to grow to >$5 billion. Peel Hunt forecasts earnings growth of more than 26% in FY16, and its current target price for the stock is £10.

## Tristel (TSTL)

Hospital-acquired infections (HAIs) are new infections that patients acquire as a result of healthcare interventions to treat other conditions. Although some high-income countries have national surveillance systems for HAIs, there is less data available from low- and middle-income countries. However, recent systematic reviews have estimated hospital-wide prevalence of HAIs in high-income countries at 7.6%, and in low- and middle-income countries at 10.1%. This is a sizeable and growing problem for healthcare organisations worldwide. HAIs result in prolonged hospital stays, long-term disability, increased resistance of micro-organisms to antimicrobials, massive additional costs for health systems, high costs for patients and their families, and unnecessary deaths. According to the World Economic Forum's *2013 Global Risks Report*, superbugs kill 100,000 Americans, 80,000 Chinese and 25,000 Europeans annually. The UK's Chief Medical Officer, Dame Sally Davies, describes the threat from these "nightmare" antibiotic-resistant diseases as nothing short of "apocalyptic".

Tristel

Enter Tristel (TSTL). Based out of its manufacturing base in Cambridgeshire, the company develops proprietary infection, hygiene and contamination control products used by organisations in healthcare, pharma, personal care, and animal care.

Its patented chlorine dioxide chemistry is clinically proven and deployed in more than 400 UK hospitals. With 96% of its business derived from high-margin consumables (i.e. non-discretionary everyday items), Tristel has strong forward visibility and is therefore a highly profitable business. This also has great benefits for healthcare providers, as it helps reduce capital and operational spend at the same time as raising hygiene standards. Furthermore, more than 70% of sales come from proprietary products, meaning that the bulk of Tristel's business is conducted on the back of its own internally generated technology.

Tristel has created a unique position in high level instrument disinfection in the ambulatory care market as well as sporicidical surface disinfection in hospitals by focusing on chlorine dioxide. Revenues from its instrument disinfectants for ambulatory care have grown at a CAGR (compound annual growth rate) of 49% between 2005 and 2014; and revenues from its sporicidal surface disinfectants have grown at a CAGR of 72% between their first launch in 2007 and 2014. It also anticipates entry into new product segments in the near future. Specifically, the company is said to be looking at airway management (anaesthesia), skin, military medicine, pre-hospital, humanitarian aid and ophthalmology. Furthermore, its chlorine dioxide chemistry benefits from strong intellectual property protection as well as know-how. Patent lives extend up to 2031 and firm continues to invest in a constant stream of new patent applications which are related to both new concepts as well as extensions of existing products. The firm now holds almost 100 patents, and 72% of revenues are now derived from products with IP protection. All this means that barriers to entry are high, and once embedded in hospital routine and best practice, Tristel products are hard to dislodge.

Despite a negative impact from geopolitical issues in Russia and forex headwinds from a relatively strong pound, Tristel reported that both revenues and profit were ahead of budget in a trading update for the 10 months to April 2015. The firm now expects full year adjusted pre-tax profits to be at least £2.5 million, up from £1.8 million in FY14. Management's stated goal is to lift turnover (organically) by at least 50% over the next three years from the FY14 base line of £13.5 million – a move which would entail pushing pre-tax profit margins above 15%. Research house Equity Development sees further earnings growth of 20.5% in FY16 and 19.7% in FY17. Tristel also boasts a clean balance sheet and net cash position of over £2 million, which presumably leaves the company well placed to carry out bolt-on acquisitions should any suitable opportunities arise.

**"SPRUE'S STATUS AS SOLE SUPPLIER TO A NUMBER OF MAJOR RETAILERS IN THE UK PROVIDES SIGNIFICANT BARRIERS TO ENTRY, AS DO ITS 68 GRANTED PATENTS, FURTHER 27 PATENTS PENDING GLOBALLY AND SAFETY CERTIFICATIONS FOR ITS PRODUCTS FROM VARIOUS REGULATORY BODIES."**

## Sprue Aegis (SPRU)

Founded in Coventry in 1998 and listing on the old OFEX market back in 2001, Sprue Aegis has grown over the years to become a leading supplier of home safety products and manufactures one of the world's smallest carbon monoxide sensors for use in carbon monoxide alarms. Products are designed in-house, with the majority of manufacturing being outsourced to contractors in China. From its initial product, the Fire Angel smoke alarm, which fits into a standard ceiling mounted light fitting, the company has built up a strong presence in the UK retail and trade market, as a supplier to the UK Fire & Rescue Services, and has also made significant progress in Continental Europe. Sprue's status as sole supplier to a number of major retailers in the UK provides significant barriers to entry, as do its 68 granted patents, further 27 patents pending globally and safety certifications for its products from various regulatory bodies.

FY14 saw adjusted operating profit almost double to £10.4 million, mainly on the back of positive legislative tailwind in Europe, France in particular. This came on the back of a record sales performance with revenue up 36% to £65.6 million, and notably group profit would have been approximately £1.7 million higher than reported had exchange rates remained at last year's level. Profits were well backed by cash flow, with £8.8 million net cash generated from operations, leaving the net cash position at a reassuring £15.9 million at period end. This also enabled a continuation of the strongly progressive dividend policy, with the total payout of 8p for the year representing a 33% increase on FY13.

Sprue increased its spending on product development to £1.8 million during the period, from £1.4 million in FY13, underlining its commitment to innovation. In December 2014 Sprue launched a new and upgraded UK trade range with cutting-edge value-added features which are intended to increase its relatively low market presence in the trade sector. Also on the cards is a connected home product solution using a cloud-based technology platform, which will allow remote monitoring of alarms – if your house is on fire, you want to know about it, right?! In addition it is gradually installing its miniaturised carbon monoxide (CO) sensor, the Nano-905, into its CO detectors during 2015, which is yet another feature to help differentiate its products from the competition.

SPRUE AEGIS PLC

However, one major factor has taken a bit of steam out of the shares of late. With a significant amount of sales being generated in Europe, the weakening of the euro against the pound is set to have a negative impact in FY15. Although house broker Westhouse expects revenues to grow from £65.9 million to £74.9 million in FY15, profit before tax is expected to come in £0.2 million lower at £10.2 million. Forecasts have also been downgraded for FY16, when profit before tax is expected to fall to £9.2 million, "purely due to the weaker euro", before rising to an estimated £12.4 million in FY17. However, it should be noted that any strengthening of the euro would be likely to lead to forecast upgrades. In any case, Westhouse's 400p price target offers significant upside to the current share price, and there is also a >3% dividend yield for the meantime. Given the short-term nature of currency headwinds, the recent setback for the share price could prove a useful buying opportunity.

## FUND CORNER

# QUALITY WILL OUT

**BY NICK SUDBURY**

*There are many different ways that active fund managers approach the challenge of beating the market. Some are mainly price driven and will buy a stock even if they don't rate the business as long as they think they can make money out of it. Others take a much longer term view and will only invest in quality companies that can deliver superior returns for years to come.*

Unfortunately it is not always immediately apparent which category a fund falls into and you normally have to do a lot of digging around to find out. The best indicator is the portfolio turnover rate, which measures how often a fund manager buys and sells assets. It is usually calculated by looking at the total value of shares bought or sold (using the lower figure) over the course of the year and then dividing by the aggregate net asset value.

You can find the portfolio turnover rate in the fund's annual report. A figure of 200% would imply that the manager has replaced all the assets in the fund twice during the year. It could also mean that they have traded a fifth of the portfolio ten times.

A manager that invests in quality companies and then holds onto them for long periods of time would normally have a much lower level of portfolio turnover.

This sort of buy and hold strategy would typically give rise a turnover rate of between 20% and 30%, whereas anything above 100% would indicate more active buying and selling.

Unfortunately there are a lot of problems with the portfolio turnover figure, with the main one being that it is distorted by client sales and redemptions. Whenever an investor puts money in or takes money out of an open-ended fund, the manager has to invest or disinvest the cash. This forces him to buy or sell assets, which is not something that his closed-ended counterparts have to contend with.

The Investment Association has been looking at this whole area and has proposed a diagram that shows the fund's portfolio turnover rate and how it compares to its peer group along with the relative cost of the transactions. This would make it easier to know what sort of fund you are investing in, but we will have to wait and see whether it is adopted.

## Cost-benefit analysis

The reason they have been scrutinising this issue is because of the lack of transparency of the charges borne by investors. An actively managed fund that trades on a frequent basis would incur much higher transaction costs than one that invests in quality companies and then holds onto them. There may also be more tax on the capital gains, which would be another additional expense.

In the UK All Companies sector, the average portfolio turnover rate across all the funds works out at around 89%. Each time the manager makes a UK share purchase he will have to pay half a percent in stamp duty, there would also be commission payable to the broker and the bid-offer spread, which all adds to the cost of the transaction.


Martin Bamford, MD of Informed Choice, Chartered Financial Planners, says that portfolio turnover seems to have an impact on costs and also on taxation within the fund.

"Funds with higher portfolio turnover do seem to perform worse than those with lower portfolio turnover, as a result of the drag these trading charges have on performance. The Investment Association are still working out a clear way to disclose product and transaction charges, so it can be tricky for investors to see how much they are paying, and portfolio turnover figures are sometimes hard to identify." Higher portfolio turnover is not necessarily a bad thing, it is just that the manager would need to make sure that the additional trades more than justify the higher costs so that the overall performance is not adversely affected.

## 'Buy & hold' open-ended funds

One fund that focuses on quality is **CF Woodford Equity Income.** This was launched in June 2014 and has already amassed assets under management of £5.73bn. The manager, Neil Woodford, uses the same successful strategy that he employed while at Invesco Perpetual. He describes it as investing in good quality companies that can deliver sustainable dividend growth with the focus on the long-term.

CF Woodford Equity Income has a concentrated portfolio with the top 10 holdings accounting for 46% of the fund.

These include: AstraZeneca, Imperial Tobacco, GlaxoSmithKline, British American Tobacco and BT. The fund is currently yielding 4% and is defensively positioned given Woodford's cautious outlook.

Another high profile advocate of this approach is Terry Smith. Smith is a vocal critic of the asset management industry and launched his own fund, **Fundsmith Equity**, to challenge the status quo. It invests in global equities and takes a long-term approach.

Smith targets high quality businesses that can sustain a healthy return on operating capital employed, whose advantages are difficult to replicate and that do not require significant leverage to generate returns. The companies also have to be resilient to change and be trading on an attractive valuation.

Fundsmith Equity has a concentrated portfolio of 20 to 30 stocks. The top 10 holdings include the likes of Microsoft, Imperial Tobacco, Dr Pepper Snapple, Unilever and Domino's Pizza. Since it was launched in November 2010 the fund has generated annualised returns of 17.9% compared to the 12% produced by the MSCI World benchmark.

"Investing in quality companies can play an important part in a portfolio, delivering what should be more stable and predictable long-term returns," says Bamford.

He highlights the **Morgan Stanley Global Quality fund** as one that follows this approach. Its objective is to generate a long-term return by investing in quality global companies in the world's developed countries. The fund is relatively new having been launched in August 2013 and has a portfolio turnover rate of 31%.

"Examples of companies in the portfolio include: Nestle, British American Tobacco, Unilever, Google and Microsoft. Over the past year, the fund has delivered a return of 4.36% compared to a sector average of 11.55%, although we prefer not to judge the performance of a fund until its third or preferably fifth anniversary," explains Bamford.

Another fund with a similar theme is **Sanlam Private Wealth Global High Quality**. It has a small portfolio of 26 high-quality stocks and aims to outperform the MSCI World Index over the medium to long-term. The largest holdings include: Rolls-Royce, MasterCard, Coca-Cola and Philip Morris International. Over the last year the fund has returned 17.6%, compared to the benchmark return of 19.2%.

## Quality closed-ended funds

Closed-ended funds do not have to deal with client sales and redemptions as investors simply buy or sell the shares on the stock exchange whenever they want to increase or reduce their exposure. This makes for a more stable portfolio and cuts down the number of transactions that the manager has to make for administrative purposes.

One of the most successful managers in this area of the market is Nick Train, who runs the **Finsbury Growth & Income** and **Lindsell Train investment trusts.** Both have similar concentrated portfolios and share many of the largest holdings.

Train looks for quality companies that he thinks will be around in 50 years' time and on average he retains them for a remarkable 18 years. He recently said that 'other investors persistently underestimate quality, resulting in unduly low market valuations for the very best companies.'

This suggests that there is an enduring market inefficiency to exploit, which leaves him with the challenge of identifying these companies and working out their intrinsic value so he knows

**"INVESTING IN QUALITY COMPANIES CAN PLAY AN IMPORTANT PART IN A PORTFOLIO, DELIVERING WHAT SHOULD BE MORE STABLE AND PREDICTABLE LONG-TERM RETURNS."**

whether they are undervalued or not. The way he does this is to look for sustainable business models that can generate extraordinary returns for long periods of time and then assess the present value of the future cash flows.

His largest holdings in Finsbury Growth & Income include the likes of Unilever, Diageo, Reed Elsevier, Pearson and Heineken. Over the last five years the fund's share price is up 154% compared to the 65% increase in the FTSE All-Share, yet Train remains extremely bullish. This is because he thinks that factors such as technology, fracking, digital and biotech will push down inflation – thereby raising consumer disposable real income – while also increasing the opportunities for companies to grow.

Simon Elliot, an investment trust analyst at Winterflood, says that Train is an extreme example of a buy and hold manager as he looks for companies that will deliver growth over a long period of time.

"It is an increasing theme as more and more of the managers that we speak to talk about having an ownership attitude towards the stocks in their portfolios. Most tend to have a four or five year holding period in mind, which would imply a portfolio turnover rate of around 20% to 25%."

He says that Baillie Gifford applies this long-term approach to all of their closed-ended funds and also highlights Templeton Emerging Markets. Its manager, Mark Mobius, has a real buy and hold mentality as witnessed by the 15.5% portfolio turnover rate in the last published accounts for the year ended 31st March 2014.

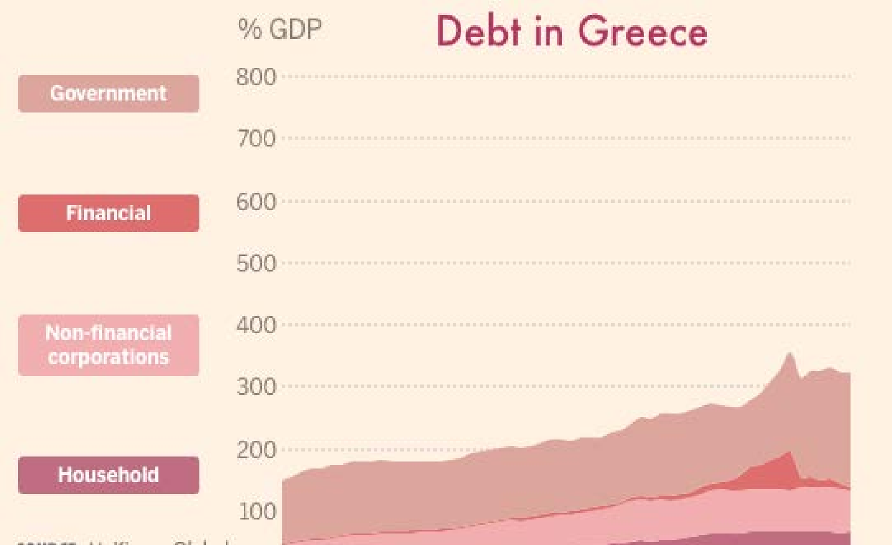
# A NEW MONETARY SYSTEM FOR GREECE

**BY FILIPE R. COSTA**

*"The financial crisis of 2007/08 occurred because we failed to constrain the private financial system's creation of private credit and money" – Lord Adair Turner (former Chairman of the now extinct UK Financial Services Authority)*

## The Greek Misbehaviour

Over the course of many years, and while the global economy was growing, no one really cared about the growing imbalances that Greece was showing. Debt grew to the unsustainable levels seen in 2010, which required the intervention of external entities to help avoid a financial collapse in the country. Exactly five years ago, the Eurozone, the IMF, and the ECB agreed a €110 billion bailout package for Greece to avoid the country's default. One year after, a second bailout worth €130 billion was approved while at the same time they forced private bondholders to accept a 53.5% loss on the face value of Greek government bonds. Another round of €8.2 billion was later approved. Accompanying the bailout money, several austere measures aimed at reducing the country's debt were also adopted by successive governments, but all they achieved was to convert financial turmoil into economic chaos, completely sinking the Greek economy.




SOURCE: McKinsey Global Institute Country Debt Database, Retrieved from FT

**"THE GREEK EFFORT OVER THE LAST FIVE YEARS HAS BEEN ADMIRABLE, I WOULD SAY."**





The Greek effort over the last five years has been admirable, I would say. They were able to turn a huge government deficit into a tiny one, which is now inside the 3% limit required by the EU treaties. So far, so good. But the enthusiasm stops when we look at what happened to GDP. Between 2009 and 2014, real GDP grew at an annual pace of -4.9%. With the denominator declining at such a high pace, the debt-to-GDP ratio is increasing and the country's financial position is looking ever more unsustainable. The "troika" of creditors would say the Greek misbehaved and their effort was not enough. They would additionally argue that Greece needs to implement even more austere measures. Others, in line with Paul Krugman's thinking, would attribute full blame to the austerity itself, claiming that public contraction just leads to a great economic depression and to solve it Greece should have adopted even more fiscal indiscipline. Which one is right? Should we blame Greece for indiscipline or allow them to further expand public spending to boost GDP growth?

## Greek Debt vs. Global Debt

A few weeks ago, McKinsey & Co. conducted a study on global debt that shows growing imbalances around the world, as indebted countries have not been able to improve their financial soundness. Debt is increasing much faster than GDP since the first signs of financial turmoil in 2007, even though several measures were adopted in order to deleverage. Debt is not a Greek problem but rather a global problem. We very well know that the UK, the US and Japan (just to name a few big names) all have unsound public finances. The main reason why they can sustain them for longer than Greece is because all of them retain sovereignty over monetary policy.

Interestingly, the same study shows a path of change in global indebtedness. Some countries that went through the 2007 crisis without suffering much from it, as is the case with Australia, the Netherlands, South Korea and Sweden, are now showing worrying growth in household debt, in particular mortgage-related debt. Why is that?

> **"THE BOE, THE ECB AND THE FEDERAL RESERVE (AND MOST OTHER CENTRAL BANKS) NO LONGER HAVE ANY CONTROL OVER THE MONEY SUPPLY."**

I have several times mentioned the Kindleberger's book *"Manias, Panics, and Crashes: A History of Financial Crises"*. Allow me to make another reference to it, as the book (written in 1978) is so prescient that it suffered several updates prior to its current sixth edition published in 2011 to absorb the latest data. Kindleberger notes that we have been heading from crisis to crisis, with the problem of one country at a certain time being exported to another region at a later time. Starting with the growth in bank loans to governments and government-owned firms in Mexico and a few other developing countries, the wave created a later credit bubble in Japan. As policymakers tried to prick the bubble, it moved on to other Asian countries and led to the Asian financial crisis of 1997. Then a new wave was formed in the technology sector and a new one in real estate at the beginning of this century. It always starts with a large pool of money that can be easily accessed to provide loans, waiting for some positive shock with the ability to create the enthusiasm that leads to credit expansion, asset price rises, and further enthusiasm. Then a self-serviced price loop is created which leads to the excessive leverage we often see and a subsequent bubble burst followed by economic depression.

As long as there is credit waiting to be created, we are able to move from bubble to bubble.

## McKinsey's Solution

The report from McKinsey expects global growth to remain sluggish and as a result debt-to-GDP ratios to increase. To solve the problem they propose:

- **Better risk sharing between borrowers and creditors.** For example, companies should rely more on bond and capital markets instead of bank loans. Mortgages to households should vary according to the household's specific circumstances.

- **Sovereign debt should be restructured.** As debt continues to grow, it should be recognised that the situation is unsustainable and that a hair cut is needed. They propose the central bank should keep the bonds and accept the loss (even though this is forbidden in the EU by its treaties).

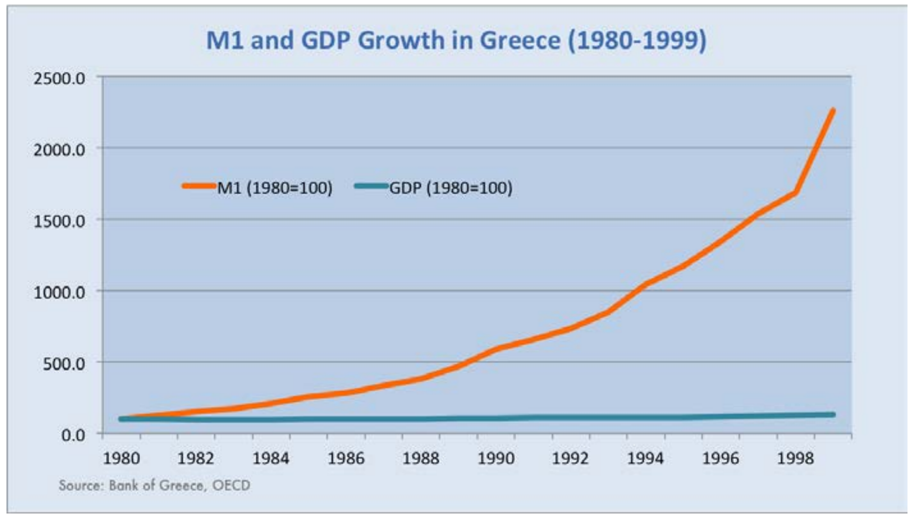
While McKinsey has the courage to state what we all know but still fail to admit - which is that the current global debt levels are neither sustainable nor workable – it still fails to recognise what Kindleberger very well reports in the aforementioned book: the expansion of credit is at the heart of the problem.

In terms of the improved risk sharing McKinsey claims to be necessary, I believe it all starts with removing the state guarantee on bank deposits. That is the most important step towards removing the moral hazard problem that leads banks to externalise risk to society as a whole. One of the main problems that led to the past mortgage crisis was the fact banks were no longer worried with the credit quality of the borrowers as they were re-selling the mortgages as securities. When that happens the bank approves as much credit as possible as the bank receives a commission that is independent of the borrower's payments, because the loan is no longer on its books. Transposing the problem to the state guarantee, when there is such a pledge depositors no longer care for the soundness of the banks and only seek for the best interest rates. On the other hand we have banks that compete with each other to offer the best rate to depositors and capture their money, as they don't bear the full cost of it, because they know the government would bail them out if needed. If there were no state guarantee, risk perceptions would improve and the risk taken by banks would decrease substantially or translate into higher interest rates paid on deposits.

But, the abolition of the state guarantee is not enough. Why? Because our monetary system is based on fractional reserves, under which there's not enough money to repay depositors if even only a small part of them wished to withdraw their cash. Coins and notes make for roughly 9% of the total stock of money, which means that most deposits are backed by thin air. At the first sign of smoke, bank runs would occur and the payments system would be at stake. Governments can't allow this because if a bank run occurs and a bank fails, many other banks can be dragged down too. In the end chaos would set in. So, I must conclude that the fractional reserve system requires a state guarantee.

With the wrong risk sharing that results from distorted risk perceptions (as the state must give guarantees to depositors), banks engage in a credit spree when they want too. The central bank creates electronically issued reserve money and sets the reserve requirement ratio. Then banks wait for deposits from clients, keeping a fraction to comply with the reserve requirement and lending the remainder. Then again, part of it will remain in the bank as deposits, enabling further lending. So, if the reserve requirement is 20, the absolute maximum the high street banks can expand on base money is 5 times.

The above is only correct in textbooks but absolutely wrong in practice. The BoE, the ECB and the Federal Reserve (and most other central banks) no longer have any control over the money supply. The reserve requirement is an entertainment measure that serves for absolutely nothing and it is never a limit on credit expansion for high street banks. Banks lend whenever they please, which creates deposits. They only afterwards look for the reserves they need, which are provided by central banks as and when necessary. For deposits to exist there must also be someone in debt. Under such a system, debt is the engine and one just can't blame a country for accumulating too much of it. The guilt lies not with the government, companies, or households but rather with the monetary system. To solve the problem we need to change the system.




### M1 AND GDP GROWTH IN GREECE

| Indicator | Period | Nr. of Years | Annualised Growth Rate |
|---|---|---|---|
| M1 | 1980-1999 | 19 | 17.8% |
| M1 | 2000-2014 | 14 | 2.3% |
| M1 | 2000-2009 | 9 | 6.6% |
| M1 | 2009-2014 | 5 | -4.9% |
| GDP | 1980-1999 | 19 | 1.4% |
| GDP | 2000-2014 | 14 | -0.1% |
| GDP | 2000-2009 | 9 | 2.6% |
| GDP | 2009-2014 | 5 | -4.9% |

Source: Bank of Greece, OECD

The chart above shows the expansion of both M1 (notes in circulation plus demand deposits) and GDP for Greece in the period pre-Euro between 1980 and 1999. As you can easily spot, the growth of the money stock has largely surpassed the growth in the country's wealth.

M1 grew at an annual pace of 17.8% in that period while GDP only a modest 1.4%. Given the current monetary system, under which deposits are created after credit is awarded to someone, the rise in the country's debt could only be disastrous. The main reason is the power given to high street banks to create money at will, while failing to align their interest with society's.

**"THE ALTERNATIVE IS TO SEPARATE MONEY CREATION FROM THE LENDING ACTIVITIES OF BANKS."**

Even after entering the monetary union, M1 continued growing at 6.6% between 2000 and 2009 while GDP grew at 2.6% per year. Only after 2009 did financial disaster lead to a reduction in M1, which resulted in a severe crisis in the country without allowing it to reduce debt.

## Towards a New System

The old view that banks need some people to save money in order to be able to lend is plain wrong. Our fractional system just doesn't need any savings to be able to lend.

In a speech at Southampton University in 2011, Adair Turner, head of the Financial Services Authority at that time, said the following:

*"Banks it is often said take deposits from savers (for instance households) and lend it to borrowers (for instance businesses) with the quality of this credit allocation process a key driver of allocative efficiency within the economy. But in fact they don't just allocate pre-existing savings, collectively they create both credit and the deposit money, which appears to finance that credit. Banks create credit and money."*

So, it seems possible to create future wealth without saving any part of present wealth. That doesn't sound right. But let's say it is possible. Then banks would lend the money for capacity creation. As a result GDP would grow with M1. But look at our economies. Productivity has been growing at less than 1% per year. The largest part of the credit extended by banks is not for investment activities but rather to buy pre-existing assets, including real estate, and for speculative activities like buying financial assets. Our legislation, under Basel rules, makes this even worse as it favours collateralised loans, which is never conducive to investment.

As you can guess, banks expand credit when they are more confident. The largest part of it goes toward real estate and the equity market. GDP doesn't grow much because these activities don't generate wealth, but asset prices rise. Under such settings there are two significant changes relative to the current system. Firstly, before using the money which in turn generates more demand for credit and further price rises. This creates a disconnection of asset prices from fundamental values. At some point, a crash occurs and we return to the same. High street banks enhance the boom-bust cycle and it is not possible to grow without debt creation.

The alternative is to separate money creation from the lending activities of banks. That is to say, let the central bank regain the power to create money while allowing banks to allocate savings at their will but without generating the current boom-bust. The idea is not new, having been first developed soon after the Great Depression in the 1930s and known at that time as The Chicago Plan. More recently the plan has been revisited by the likes of Ben Dyson and Andrew Jackson in *"Modernising Money: Why Our Monetary System Is Broken And How It Can Be Fixed"* and by F. Sigurjonsson in a report commissioned by the Prime Minister of Iceland and entitled *"Monetary Reform: A Better Monetary System For Iceland"*.





The idea is to limit the action of commercial banks by creating two account types: (1) Transaction Accounts, which are held at the central bank and are risk-free and thus pay no interest at all; and (2) Investment Accounts, which are held at commercial banks and have some varying risk and thus pay interest. Banks can no longer create money. They still have the clients that deposit their money in risk-free accounts (Transaction Accounts), but these accounts are effectively held at the central bank, even if managed by the commercial bank. This means that in case of a bank default this money is fully protected. But banks can still offer time deposits with varying maturities and risk. Clients may opt to transfer their money from the risk-free demand deposits (Transaction Accounts) to these time deposits (Investment Accounts).

**"THE BEAUTY OF THIS IS THAT THE CENTRAL BANK WOULD LOSE CONTROL OF INTEREST RATES, WHICH FINALLY WOULD BE DETERMINED IN THE MARKET AND THUS BECOME AN EFFICIENT ALLOCATION PRICE LEADING TO CORRECT INVESTMENT DECISIONS."**

Under such settings there are two significant changes relative to the current system. Firstly, before using the money from clients to invest, the bank must capture the savings from clients. Secondly, the client needs to monitor bank activities to some degree as these investment accounts do have risk. In such a system, there is no risk of too much credit creation.


But, there's still a missing link - the money creation process. The central bank must create money in a sound way. A committee needs to be created in order to decide on how much base money is going to be created. Eventually, money creation can be tied to GDP growth but there are other options as well. The exact configuration must be debated. In any case money is now a central bank asset that still needs to be allocated. The proposal made by Sigurjonsson and Dyson & Jackson goes in the direction of this money being given to the government, which in a democratised way would then decide what exactly to do with it. It could be used to reduce taxes or to invest in some infrastructure investment projects, for example. As a result, money creation would be under control and much more democratic.

Nevertheless, the incentives to create more money than needed to keep the economy oiled are too strong and inflation could be generated. The system would have to be very tight to avoid being exposed to the political cycle. But in any case, the problem of attributing too much credit would be completely solved.

Unlike the Icelandic case, Greece has an excellent opportunity to get rid of a system that is keeping it zombified for decades. The Eurozone would never agree to cut Greek debt by the necessary amounts for Greece to have a new start, and even if it does, as long as banks keep credit creation under their umbrella, they will move towards the exact same problem in just a matter of years. Allowing a default now is their best chance at starting over from scratch. They can implement a new sovereign based drachma, fully controlled by the central bank. Even if the exchange rate fell at first, it would be a one time, temporary effect. With tight rules regarding money expansion, there's no reason for the currency to revalue over time, in particular when all other banks are using money printing extensively and well above their respective countries' growth rates. The beauty of this is that the central bank would lose control of interest rates, which finally would be determined in the market and thus become an efficient allocation price leading to correct investment decisions.

# ARE PRIVATISATIONS A NO-BRAINER

BY ADRIAN KEMPTON-CUMBER

*I wrote a blog piece recently about Royal Mail Group plc. It got me to thinking about how privatisations had fared in the past. For my own part, it was a government privatisation that first got me into trading and investing. Several members of my family, like many families, applied for privatisations, and of course got scaled down: over-subscription being de rigeur. Then like most people, we had no clue how to sell them!*

I resolved to find out and phoned a broker, Redmayne Bentley, who I still use in preference to an online broker incidentally, and all they needed to know was the number people these shares belonged to, whether or not I had all the share certificates to hand, and my name and address. Got the folks to do the paperwork and that was it. I received a cheque and distributed it myself. A much simpler, and preferable system, in my view. CYK is a load of pointless red tape that just makes it hard for honest individuals to go about their business, while criminals regard getting round it as a normal and fairly cheap part of doing business.

In those days a majority of people were pretty green about all this stocks and shares business, and I remember one of the campaigns, for BP I think it was. "Be part of it", that was the slogan. But then, before the closing date for applications, the market price went below the offer price.

**"CLEARLY YOU COULD JUST BUY THE SHARES ON THE OPEN MARKET FOR LESS THAN THE ONES ON OFFER FROM THE GOVERNMENT."**

Clearly you could just buy the shares on the open market for less than the ones on offer from the government.

There was some guy by a pillar box about to put an application in the post. A TV news journalist approached him and asked if he was posting a share application for the BP offer. "Yes", replied the man. They explained to him that he could buy them for less on the stock market. "I know," he replied, "but I just want to be part of it." Right, this is why not everyone should have a vote, or a job for that matter.

Since Thatch started selling the family silver to inject money into the economy, creating the illusion of a boom for many years to come, there have been some privatisations I'd approve of, and some I wouldn't.

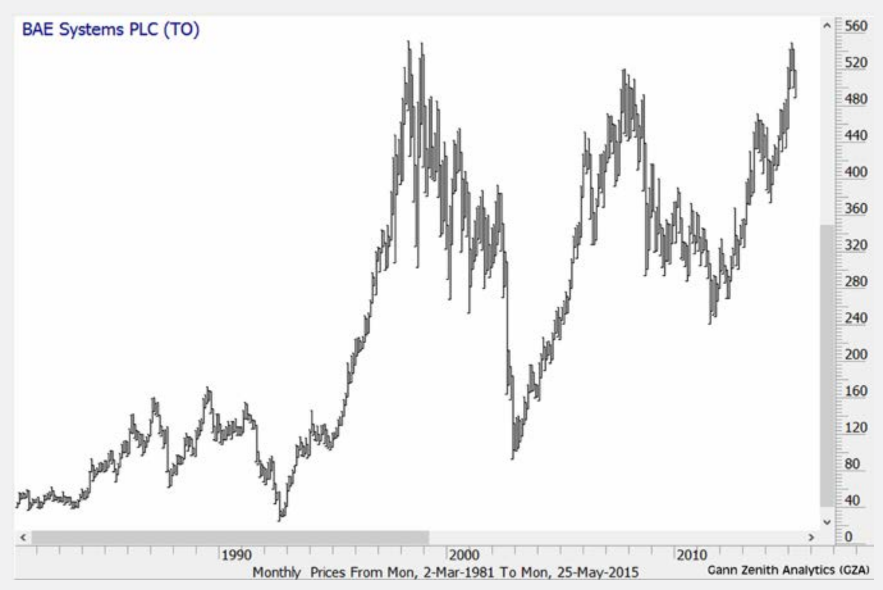
**"SEVERAL MEMBERS OF MY FAMILY, LIKE MANY FAMILIES, APPLIED FOR PRIVATISATIONS, AND OF COURSE GOT SCALED DOWN: OVER-SUBSCRIPTION BEING DE RIGEUR. THEN LIKE MOST PEOPLE, WE HAD NO CLUE HOW TO SELL THEM!"**

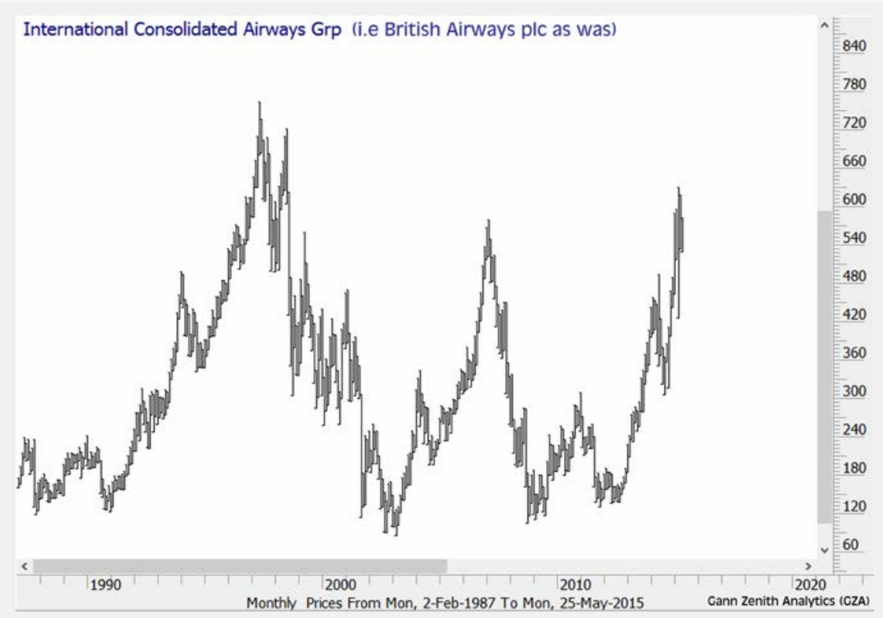
I didn't support selling off, lock stock and barrel, any service which shouldn't be dictated to by economic conditions (i.e. the rail network infrastructure). On the other hand I was very pleased to see BT meet competition, although it took long enough before it was even that viable as competition goes. BT ripped us off so badly when they had a monopoly. I will never deal with them, in the same way one might not choose to go on a date with someone who had previously abused you.

A problem with privatisations is the culture of having been a government corporation, and all the baggage and tribalism that goes with that. I used to work at British Airways and there was a big shadow there of the 'old days'. There was a militant attitude that, given their readiness to strike in spite of being the best paid staff in the airline business, tells you all you need to know about how your privatised company stock could go off the rails when push comes to shove. Employees in most government run operations live in some kind of dream world where they really don't work as hard as those in the private sector, not by a long chalk. They are usually blissfully unaware of it though. Demonstrate this to yourself by mentioning it to anyone who works for the public sector, or a privatised industry. See how defensive they get, and how they 'doth protest too much'. A fun way to ruin someone's dinner party that you don't much care for. So they are likely to be quite a bit less efficient than their private sector competitors, which may explain the delayed gratification with many of these stocks.

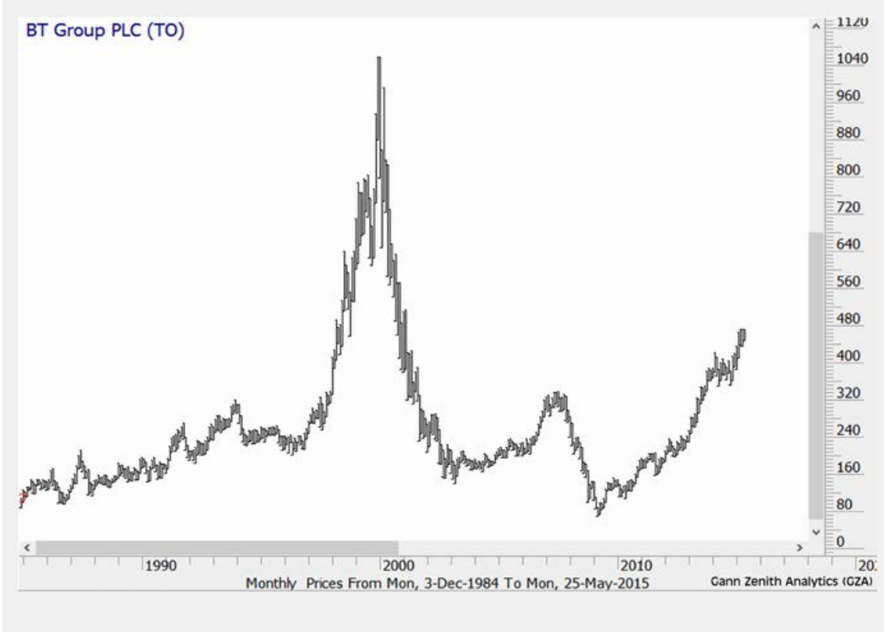
It's accepted that Hayek's economic theories encouraged Thatcher to pursue a policy of privatisation, and a generally deregulatory approach. He was for a much more hands off approach than the reality of what happened. But in true English style she just couldn't do what he wrote, as he has since complained. No, the English way is to half-do something and hope that the results get less flak from critics. This is how we have the situation where it's apparently so dangerous to smoke near your work colleagues that they may expire on sight. So that's illegal. But it's evidently OK to smoke at home with your baby and kids in the same room, and perfectly legal. Because if a thing's worth doing, you can rely on us to half do it.

**"ROYAL MAIL GROUP PLC IS NOW AROUND 18 MONTHS IN, AND HAS REALLY DONE NOTHING MUCH, ALTHOUGH IT MAY BE POISED TO."**




Royal Mail Group plc is now around 18 months in, and has really done nothing much, although it may be poised to. A quick initial move up as successful applicants stagged the issue, while those who wanted in filled those orders. Then a falling off, and now recovered to just above the starting price when trading opened for the first time. Is it justifiable to expect real gains now? Well let's look at some of the major privatisations and see what happened.



What seems fairly typical, looking at the charts, is an initial rise (Rolls-Royce being the exception there). It's many years before these stocks see what you might call 'super-profits' though. Is that really good for your pension? Look at BAE. Yes it has a big rise in the 90s, but if you were retiring in 2002 you wouldn't have been best pleased. If we take these privatisations as a guide then it would seem you need a window of about 15-20 years to ensure you get a really good chance to cash out at a decent top. In the order of six-fold growth from the opening levels is achievable, but then it's highly prudent to cash out into something more stable. They are 'buy and hold then sell' stocks.

When people ask me about what to put in their pension these days I say "if you don't have defence stocks you don't have a pension". Wars seem to be right up there with death and taxes in terms of certainties, and we all love a certainty! There are some brilliantly diversified defence stocks to choose from. I'll look at them another time and explain why there is absolutely no ethical dilemma in owning them for any reasonable person.

If you want the sort of growth you'll need from Royal Mail to make it worth putting in your SIPP, then it seems clear you do need a window of more than 10 years to be confident of pulling down the best gains. Timing your exit may not be so easy. I'm a big fan of 'when in doubt sell half'. It buys you time, and you still don't miss out on further gains (if there are any). Plus you'll be very happy if there's a trade-off and you have already sold half. You can always reinvest.

**A special thanks:** it's hard to get stock data this far back. The LSE offer back only to 1999, ShareScope to 1994, and Yahoo Finance back to 1988. So a big thanks to Gary Stafford at http://www.gann.co.uk/zenithanalytics for providing the charts used in this article. The only source I know of for UK stock data (with data integrity) going back to the early 80s and even beyond. And as an amusing aside, Gary's company is based in Manchester. Epic fail for London here!

# A CLASSIC INVESTMENT

**BY MIKE SUTER-TIBBLE OF WWW.SUITABLECLASSICS.CO.UK**

*A pristine classic car can be an indicator of a successful investor; but can the right set of wheels become a golden investment in itself?*

Cars depreciate. That's pretty much guaranteed as far as the vast majority of cars are concerned. Each passing year, or owner added to the log book, takes it a step closer to 'old banger' territory, and ultimately the scrapyard. However, buy the right car and you could be one of the very few people who manage to sell a car for more than you paid for it (car dealers excluded of course).

Since the financial crisis, traditional investments haven't performed as well as in previous years, leading many investors to look for new opportunities. Art, fine wine and classic cars have all seen increased interest. I don't follow the art or fine wine markets, but certainly in the case of classic cars, this increased attention and competition for the most valuable cars has driven prices up. The classic car market has had its share of bubbles and busts though, so to provide the familiar disclaimer, past performance is no indication of future returns. If and when traditional assets pick up, it's possible that the new investors will have been 'bitten by the bug' and stay in the market, keeping prices buoyant.

> **"THE KEY HERE IS TO EITHER SPOT A MODEL THAT WILL EITHER BECOME A CLASSIC IN THE TIMESCALE YOU'RE LOOKING TO INVEST OVER, OR ONE THAT WILL GO FROM 'UNDERVALUED' TO CORRECTLY OR EVEN OVER-VALUED."**


## About me

Mike Suter-Tibble is a life-long classic car enthusiast who runs Suitable Classics, a classic car upholstery and trimming company. He also writes occasional articles on buying, selling, restoring and driving classic cars on his website **www.suitableclassics.co.uk.**

A CLASSIC INVESTMENT

Alternatively, if they choose to exit the market and sell up, prices might fall quickly. A lot of long-term enthusiasts are priced out of the market at the moment, which might not bode well if prices falter.

So, if you do want to invest in vintage motors, which set of wheels would make the best addition to your portfolio? The choice depends on how much money you have available, and what you mean by 'investment'. Investment-minded buyers usually fall into one of two camps: firstly, those setting out to make a 'true' investment (where the main aim of buying the car is to sell it later at a profit); and secondly, those whose main aim is to enjoy their purchase, but who buy with an eye on the possibility of their classic increasing in value enough to offset at least some of the costs of ownership.

If you're intending to make a short-term investment it's best to go for a model already showing a clear increase in price. The Aston Martin DB6 is the perfect example: prices have risen significantly over the last five years. In 2010 you could bag a good one for about £80k; currently, you'll need to find £130K to £180K for a decent one.

Longer-term investments can be split into two categories: those that are 'undervalued', and those that are 'not quite classics'. The key here is to either spot a model that will either become a classic in the timescale you're looking to invest over, or one that will go from 'undervalued' to correctly or even over-valued.

'Undervalued' cars are those already considered classic, whose price is lower than it 'should' be. Until the last two to three years, the least desirable models from Ferrari, such as the Mondial or 400/400i, had been hanging around at the rock-bottom Ferrari price of £10k. A couple of years ago I'd have said to avoid them as investments, unless you're trying to lose money. Recently however, values for the 400s seem to have increased to around £20K for a good one, so they might be a good buy after all – as long as prices don't fall, leaving you with the Ferrari no-one wants. You'll need to exercise your judgement as to whether the market for an undervalued car is about to take off.

**"NEW FERRARIS, ASTON MARTINS AND PORSCHES TEND TO DEPRECIATE RAPIDLY UNTIL THEY REACH A LOW-POINT IN TERMS OF DESIRABILITY (AND THEREFORE PRICE) BEFORE REGAINING VALUE AS THEY BECOME RECOGNISED AS, THEN DESIRABLE AS, CLASSICS."**

Another strategy is to look for a car that's destined to become a classic, but that isn't quite there yet. By taking this route, you're trying to buy a car when its price nears its lowest point, before it becomes highly desirable and the price rockets. As a rule, these 'not quite classics' are still seen as just 'old' at the moment – the key is to know which ones are likely to attract collectors in a few years. The Mark 2 Escort is one such 'not quite a classic' success story. Nowadays they're worth real money, with just the bodyshell of a two-door likely to set you back £1,000. Yet in the early nineties the self-built 'Locost' kit car (popularised in Ron Champion's *Build your own sports car for £250)* used Escorts as the donor car, because they could be picked up as MOT failures for as little as £50. This strategy requires you to play the long game: it can take twenty years to gain from this increase. Just as with the 'undervalued' moniker, phrases like 'future classic' crop up a lot in adverts for 10 to 15 year old cars. There's almost certainly a lot of wishful thinking involved here, but in amongst the over-hyped old bangers there are a few smart investments to be made.


The big names are a popular bet in the 'not quite classics' market. New Ferraris, Aston Martins and Porsches tend to depreciate rapidly until they reach a low-point in terms of desirability (and therefore price) before regaining value as they become recognised as, then desirable as, classics. Buying near to this low point can return a reasonable profit. However, this isn't a failsafe strategy. Some models from each of these marques haven't seen a rise in prices as they age: the Aston Martin Lagonda of the 1970s and 1980s hasn't seen much of an increase, while Porsche 924s seem forever condemned to be the 'poor man's Porsche'. Four-seater Ferraris appear particularly vulnerable to price restriction, so may be best avoided as investments.

Some classic dealers remember when decent E-types could be picked up for a bargain: today they're worth at least £20,000. They've taken twenty years to increase by that much though, so this isn't always a route to a quick profit. This approach is probably the most long-term of the ones we've described here. Because of that, you should bear in mind running costs could very well wipe out any increase and more.

It's impossible to compile a list of cars to recommend that covers all budgets and investment strategies, but I've tried to pick out some interesting classics to consider, which stand a good chance of increasing in value over the next few years.

At the upper end of the price range there are some sure-fire bets. If you've sufficient funds to be seriously considering a Ferrari 250 GTO, Lusso, or 275 4-cam, you've probably already had a lot of advice from experts. If not you probably should do. For an investment classic like these, dealers such as Talacrest, JD Classics or Tom Hartley Junior would be a good starting point.

The Ferrari 250 GTO is always the one that grabs attention, as it's the one that sets records at auction. This red-blooded sports racer is from a production run of just thirty-nine. Although road-legal, they were very definitely built as track cars – inside the cabin you don't even get a headlining. They come in two body styles: the earlier, fastback style is the prettiest, in my opinion. Although their competition heritage is slightly oversold (they mainly competed against other Ferraris), the 250 GTO is rightly considered one of the purest 'driver's' cars. Prices *start* at around £25 million – a real thoroughbred of an investment. These cars also illustrate the warning about bubbles – at the peak of the '80s boom in classic cars, they changed hands for around $13 million (at the top

**"IF YOU'VE SUFFICIENT FUNDS TO BE SERIOUSLY CONSIDERING A FERRARI 250 GTO, LUSSO, OR 275 4-CAM, YOU'VE PROBABLY ALREADY HAD A LOT OF ADVICE FROM EXPERTS. IF NOT YOU PROBABLY SHOULD DO."**

end of the market, most cars are bought in dollars); just three years later asking prices had dropped to a mere $3 million.

Its cousin, the road-going Ferrari 250 Lusso is a favourite of mine. Ultra stylish and very quick, the Lusso has possibly the classiest, understated interior ever made: no radio (who needs one with that fantastic V12 exhaust note?), and just the right amount of diamond stitching, done before the style became a Range Rover cliché. "Cheaper" than the GTO, prices range from £800K for a project car, to £1.5 million for a really good one.

For a home-grown investment, look to the Aston Martin DB4/5/6. The DB5 was made famous after appearing in 'Goldfinger', and has starred in numerous Bond films since. You'll need at least £100,000 to bag one, even a project car requiring complete restoration. Serious investors looking to target the classic market may wish to look earlier in Aston Martin's illustrious series. Topping the price list is the achingly beautiful DB4 Zagato, valued at around £4 to 5 million.

For an investment with panache (and entry into a lot of exclusive councours events), the Bugatti type 57 could be the classic for you. The Type 57 came in a variety of body styles, including the elegant Atalante. Prices start at £110,000 for one of these, climbing to a shade over £5 million for the best 57S Atalante.

In the middle of the market is the ever-popular Porsche 911, a car with a big following amongst collectors. The value of earlier (1964-1973) cars has increased rapidly over the last few years, with £20k now the entry point. The "impact bumper" models (with plastic rather than metal bumpers) were made after 1973 up to the introduction of the water-cooled 996 series in 1998. If you can't afford an earlier car, these might make a great investment. A couple of years ago you could find pretty decent ones for around £15,000; today that's the bottom end of the price range.

If you really want a 911 and only have £9,000 to £10,000 you'll have to make do with a water-cooled 996 from the early 2000s – and being told you don't have a proper 911 by purists. Air-cooled 911's are pretty tough mechanically, but Porsche parts are absurdly expensive, and 911s can rust badly, so the cost of upkeep might mean they're not such a great investment.

The Aston Martin DB7 is reaching its lowest price around now, and a reasonable one can be picked up for around £15k. They're also around fifteen years old and savvy buyers could benefit from bagging one while it inhabits the 'not quite classic' category. In ten years the DB7 will be about 25 years old – and it has the makings of a classic (even though smug car bores will tell you it's just a 'Jag in drag' as it's based on Jaguar underpinnings).

**"AT THE CHEAPER END OF THE MARKET YOU'RE UNLIKELY TO MAKE HUGE PROFITS, BUT THERE'S THE POTENTIAL TO FIND A CAR THAT WILL INCREASE BY MORE THAN WHAT IT COSTS TO MAINTAIN WHILE YOU OWN IT."**


Nothing whispers class like a Mercedes convertible, so if you're after the feeling of wind in your hair or headscarf, consider the 1989–2002 Mercedes SL (R129 – Mercedes' internal model designation. Confusingly, these don't run sequentially). The beautiful '60s/early '70s 280SL (R113 - Mercedes' internal model number) is out of the price range of many people at around £40k upwards, and a late '70s/early '80s R107 will set you back at least £10k for one that doesn't need work. With its plastic bumpers, pop up roll-over bars and sloping bonnet, the R129s look a lot newer than their metal-trimmed forebears. While they may not have the cache of the 1970s Mercedes, they're tough mechanically (and the electronics seem reliable too) and there are enough of them around to be very choosy when buying one. You'd be wise to track down the most desirable model – the 500 SL – in the very best condition you can find, as the price difference between good and poor means restoring one's not financially worthwhile.

At the cheaper end of the market you're unlikely to make huge profits, but there's the potential to find a car that will increase by more than what it costs to maintain while you own it. Rather than opting for classics from premium manufacturers that have reached rock bottom (such as Porsche 944s) there might be more profit in mainstream models like Fords and Vauxhalls. These marques tend to have strong followings; collectors are often most nostalgic about the models they or their parents owned, or models which have become rare. Cars like the Cortina or Escort that could be picked up for a pittance are increasingly worth a great deal to the right buyer.

Sporting Fords are probably the best bet. XR3is and s from the 1980s are still fairly inexpensive at the moment, but they're harder and harder to find in decent condition. These hot-hatches are front wheel drive though, in contrast to the Escort MK2s that are desirable as rally replicas. A better bet might be the Escort Cosworth; although not in the bargain basement at the moment, they're yet to reach the desirability levels of the Lotus Cortina or Escort Mexico.

Regardless of how much you're looking to invest, if you're new to buying classic cars, there are a few things to consider, and factor into your calculations before you buy. Cars need maintenance - and need to be used if they're not to seize up. So-called 'Barn finds' are all the rage at the moment, but a 40 year old car with 5,000 miles on the clock may not be the safe bet it seems to be. If the car has been sitting around for a while it's likely to need a lot of work to get it back on the road. The to-do list can be both extensive and expensive. Engines have a number of rubber seals which perish over time, particularly if the car hasn't been run regularly. The resulting work might include a total engine rebuild, which on a rarer and exclusive car could easily run into five figures. Bodywork can also get very expensive if you discover rust lurking under the paint or underseal (If you see fresh underseal on a classic you're considering buying that hasn't just had a complete restoration start prodding the metal to check it's solid). While a poor or tired interior may be easy to spot, that doesn't make it cheaper: higher end cars may need seven or eight complete hides (at £800 each) - and that's just for the materials.

As a trimmer, I know how commonly people think re-covering seats is an hour's work on the sewing machine – be warned, it isn't! In the vast majority of cases, unless you can do a lot of the work yourself, or have a competent mechanic who'll work for very little, you'd be advised to only buy cars in the best condition if your main motivation is investment.

If you're new to the world of classic cars, or if you're not but are looking to spend a good proportion of your available capital, you should find someone to help you avoid buying a lemon. The phrase 'Caveat emptor' could have been invented to describe the process of buying an old car. There are lots of garages and mechanics around who'll provide a pre-purchase inspection; if possible, it's a good idea to find someone who specialises in the model you're considering, as they all have quirks and common pitfalls they'll know to look for.


**"IN TEN YEARS THE DB7 WILL BE ABOUT 25 YEARS OLD – AND IT HAS THE MAKINGS OF A CLASSIC (EVEN THOUGH SMUG CAR BORES WILL TELL YOU IT'S JUST A 'JAG IN DRAG' AS IT'S BASED ON JAGUAR UNDERPINNINGS)."**

Just in case I'm putting you off, I should remind you that classic cars, unlike wine, can be enjoyed multiple times, and they're a LOT more fun than share certificates.

## CURRENCY CORNER

# WHY I'M A LONG-TERM US DOLLAR BULL

**BY SAMUEL J. RAE**

*A few weeks ago, we heard HSBC chief economist Stephen King announce projections for the global economy over the next decade. Many reading this will already be familiar with his conclusions, but as a quick outline, he suggested that six years into a recovery, we're likely closer to the next recession than we are from the last.*

He outlined a number of reasons why this recession could be much worse than the others, primarily focusing on the fact that unlike previous downturn we don't have any real tools at our disposal with which we can fend off any economic weakness.

King pointed out that, normally, developed economy interest rates will fall by five percentage points in recessionary times, but of course with interest rates at zero already (or less in Europe) this is not a possibility. Further, he pointed out that with current debt levels unsustainable as they are, an extension of any quantitative easing policy would be merely a temporary solution, and one that would likely lead to far worse trouble in the short to medium term. News media picked up on the story and King's likening of the global economy to the ill-fated Titanic, and our lack of policy tools with which to deal with a recession to the Titanic's lack of lifeboats. He did, however, make one point that, as currency traders, we may be able to take advantage of.

He gave four potential reasons why the global economy might collapse – four potential icebergs, to stick with the analogy. These included the Fed raising interest rates too quickly and plunging us back into recession; non-banking financial services failing to meet future obligations such as pension funds and an ensuing run towards liquid assets that could lead to panic selling; high US wages with a non-concurrent expansion in output leading to a decline in company profits and, in turn, market capitalization; and finally – the one that we're interested in – a weakening economy in China.

Why is it interesting to us? Well, it could present us with a long-term bias in the US dollar. For a long time, Beijing has reportedly maintained a certain level of control over the value of its currency, the renminbi.

In 2005, China scrapped its policy of pegging the currency to the US dollar, and now, every business day, government workers in the country publish the value of the renminbi versus the US dollar. This value tends to increase steadily every day, and as a result today's renminbi is worth about 25% more versus the US dollar than it was 10 years ago. However, this sort of appreciation is only sustainable as long as the Chinese economy maintains a particular level of expansion. If expansion wanes, China may be forced to let the renminbi decline in value versus the US dollar.





**"NEWS MEDIA PICKED UP ON THE STORY AND KING'S LIKENING OF THE GLOBAL ECONOMY TO THE ILL-FATED TITANIC, AND OUR LACK OF POLICY TOOLS WITH WHICH TO DEAL WITH A RECESSION TO THE TITANIC'S LACK OF LIFEBOATS."**

What does this mean? Well, first off, it will translate to short-term dollar buying, and the associated strength this brings. Further, however, Chinese demand for commodities such as oil, agriculture, mining (especially from Australia) and foodstuff from places like New Zealand, strengthens prices for all these commodities considerably. Once the Chinese economy starts to slide, and it weakens its currency, its demand for these commodities will decrease and their prices will follow.

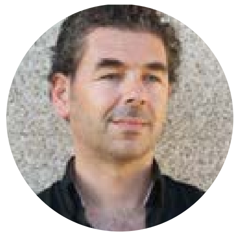
The vast majority of global commodities trading is done using the US dollar as a means of exchange. So, as commodity prices decline, demand for the dollar will increase. This increase in demand will boost the US dollar medium term – and therein lies our bias. We can also pretty firmly say that in the event of a Chinese slowdown the value of the Australian dollar will also suffer, and present us with a bearish bias in the Aussie. This, however, is only the start. As mentioned earlier, normally we would see the Fed raise interest rates in order to counter a strong US dollar (and the inflation this engenders). However, with such a weak recovery, raising interest rates could be extremely dangerous, and again, as mentioned, could simply plunge the US into further recession. For this reason, the Fed may only be able to raise its interest rates very slowly, through gradual increment. This, therefore, could very easily extend our bullish bias from a medium-term to a long-term one. Further, if we get any potential sell-off in the equities markets as Stephen King also predicts, this could add fuel to the fire as far as a strong dollar is concerned.

So, there we have it. In the long term at least, it looks as though the US dollar is set to strengthen considerably versus its major counterparts.

## FUND MANAGER IN FOCUS

# EMMANUEL LEMELSON

**BY FILIPE R. COSTA**



*"The recent financial abuses in housing caused many to suffer unnecessarily. Critical questions ought to be asked – how did it occur on such a massive scale, and in of all places, the US? Many of the greatest minds in finance have either ignored the issue of economic injustice or perhaps don't understand it fully, which is a shame because they have influential voices and could affect change."* - Emmanuel Lemmelson

### A Singular Man

The hedge fund industry is certainly one of the most exquisite branches of the investment world, where one can find the most disciplined, the most skilled, and the most obstinate individuals who hide behind powerful computer algorithms, rely on rigorous analysis, and seek the most mind-boggling opportunities to squeeze alpha from their investments.

No one could imagine that a man, at the age of 47, seeking a mere analyst job after a few failed ones, and upon his third wife, could lead a hedge fund towards "the best trade ever". But that was the case with Paolo Pellegrini who led Paulson & Co. toward multi-billion dollar gains after betting against the mortgage collapse in 2006.

At par with some odd success stories like Pellegrini's, there are some odd ways of making money. We must mention, for example, Carson Block and his Muddy Waters Research. As the name suggests, the company "looks for trouble", selling the shares of companies with suspicious activities before trying to uncover accounting scandals. Muddy Water's targets usually experience a downhill ride and in some cases end up being delisted from the exchange.

But there are even stranger relations in the hedge fund world. What do you think is the connection between Faith, Investment, and Photography? Do you believe that studying Theology can help you run an e-commerce business? And what about choosing a Masters in Divinity to run a hedge fund? The puzzle is solved with this month's focus on Emmanuel Lemelson, the hedge fund manager that is actually… wait for it… a priest!

### From Religion…

Emmanuel Lemelson was born in Phoenix, Arizona in 1976. In fact his name was Gregory M. Lemelson but, as he was ordained as a Greek Orthodox priest in 2011, he was granted the ecclesiastical name Emmanuel.

Lemelson studied in Germany for a few years but returned to the U.S. to attend high school in Washington, where he graduated in 1993. At the age of 18, he went to the Jesuits-run Seattle University to pursue a degree in Theology and Religious Studies.



FUND MANAGER IN FOCUS

**"BUYING JUST FOR THE SAKE OF IT WHILE DISREGARDING ANY FUNDAMENTAL VALUE, IN THE HOPE SOMEONE WILL COME ALONG LATER AND BUY THE SAME AT A GREATER PRICE WAS NEVER IN HENDRY'S VEINS. MOVE FORWARD."**

After graduating he continued his studies in Theology and obtained a Master of Divinity from the Hellenic College Holy Cross Greek Orthodox School of Theology.

As part of his religious tasks he founded “The Lantern Foundation”, a non-profit foundation focused on supporting religious, charitable and educational causes, where he has also served as President. His theological work is centred on canonical issues in apostolic mission and ethics in relationship to commerce, finance and social justice. In November 2014 he was part of the official Orthodox delegation during the papal visit to Turkey and he fostered a vision that Catholics and Orthodox Christians would soon be reunited after the split in 1054 over disagreement on matters including the primacy of the papacy.

## ...towards ecommerce

While still known as Gregory, Lemelson began a retail photography business. When the digital world was still in its earliest days, he envisioned its growth towards a mass market. At that time photography accessories were expensive and mostly inaccessible for non-professionals. His goal was to begin a retail business where he could sell budget accessories. At the beginning he started manufacturing accessories at his dorm room but later founded Amvona, a retail website that derives its name from the Greek world “pulpit”. The popularity of Amvona grew very fast and it soon started generating around $40 million in revenue.

Lemelson was always old-fashioned in terms of business management and adopted a frugal approach to life in general. While many neighbour companies were supported by venture capital and managed by “rich kids” from inside “decorator-stylish offices”, his company was founded by owners' money and his office comprised a simple desk and a large warehouse behind it.

Lemelson always favoured cash flows over outside capital as a way of financing a business. “We've developed our business the old-fashioned way... we sell products, and we bring in more than we pay out”, he explains.

**“WHEN THE DIGITAL WORLD WAS STILL IN ITS EARLIEST DAYS, HE ENVISIONED ITS GROWTH TOWARDS A MASS MARKET.”**

Many companies rely heavily on mortgages, which are often based on optimistic assumptions about future earnings, which most of the time just turn into realised losses. In his view, it is better for the cash flows to materialise first, and only after buy more product and expand the business. This approach inevitably delays growth but can also save the business from being liquidated during tougher times.

Amvona operated as an online retailer between 1999 and 2010 and was once one of the top 10 most visited online photo retailers. It has sold more than 1 million photo accessories to 300,000 customers around the world over its existence. The company pioneered software development, having registered a few patents. At a time when social networking was just a mirage, Amvona was already developing proprietary software to connect its customers through the creation of user profiles, product reviews, exif data and online tracking software. Such technology is now heavily used by online retailers and by Facebook to track user activities.

But it was not only in terms of software that Lemelson pioneered. To offer budget accessories, Lemelson needed to find the lowest cost possible to manufacture the products. At a time many clothing brands were relocating their production facilities to China to cut costs, Lemelson thought about doing the same for photo accessories. But in 2000, no one was doing it with photo accessories. The decision was right and Amvona was able to decimate its competition.

In 2009, Lemelson created a blog providing opinion and analysis on issues of Faith, Investment, Economics and Technology on the Amvona website. One year later, Amvona announced it was discontinuing its e-commerce business. Lemelson's life was about to acquire a new direction, one that would join Religion with Investment.

While there's no official explanation for the Amvona e-commerce business discontinuation, it is very likely that at some point competition pressures were too strong for the business to be worth expanding. By 2010, almost all U.S. companies were in some way connected with China and many Chinese producers were already selling directly to the general public at bargain prices. The only way to compete in the photo accessories sector would be through company dimension. Many of the existing retailers were by then large companies taking on massive leverage in the expectation of growing even more, something heavily opposed by Lemelson. *“The time has come when companies are going to have to reinvent themselves because the old paradigm of the same ideas only with more leverage piled on top of more debt isn't working”*. There was no room for Lemelson here anymore and it was time to go in a different direction.





## An Eternal Hunt For Value

**“AS A SUPPORTER OF A CONSERVATIVE BUSINESS APPROACH, LEMELSON WAS ALWAYS A CRITIC OF THE MASSIVE LEVERAGE TAKEN BY COMPANIES.”**

As a supporter of a conservative business approach, Lemelson was always a critic of the massive leverage taken by companies. In particular, he criticised the behaviour of banks and other financial institutions who contributed to that same excessive leverage and who guided the U.S. economy towards collapse. At certain times there is so much optimism that asset prices reflect conditional events as if they were material realities. Companies like Facebook and others are filled with “users” instead of “customers”, who buy nothing and may eventually disappear, but they're priced as if those “users” were regular “customers” buying stuff and contributing to these companies' bottom line. This observation was seen by Lemelson as a big opportunity to enter the fund management business.

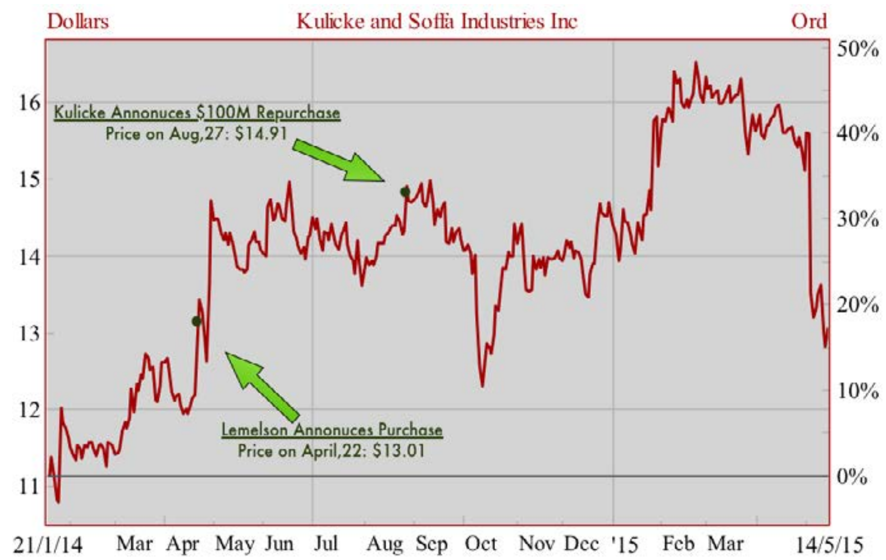
In September 2012 Lemelson founded Lemelson Capital Management and created its flagship fund “The Amvona Fund, LP”. The hedge fund is of the long/short bias type with a focus on deep value and special situation investments. As a fund manager, Lemelson has adopted an activist position in several publicly traded companies and often creates some discomfort to the executive management.

In 2014, Lemelson made a short call on World Wrestling Entertainment criticising the deficiencies in executive management. On March 17, 2013 he announced a short position on the shares reporting fair value to be around $8.25 and $11.88. The shares were trading at $30.37 at the end of that day. Less than two months later and after a worse-than-expected profit statement and a failed deal with NBC, the shares were down 63%, trading at $11.27 on May 5. Lemelson covered the short (and even reversed it to a long position, but ended closing it recently due to the same management problems he pointed out in the past, and which he believed to be unsolved).

Last year, on 22nd April, Lemelson announced the Amvona fund had been


acquiring shares on Kulicke & Soffa Industries while, at the same time, wrote an open letter to the management of the company suggesting a repurchase of the shares, as the company was sitting on a large cash pile with no debt and was not paying any dividends to shareholders.

Four months later, on 27th August the company announced a $100 million share repurchase programme. The shares were up 15% by then.



The Amvona fund has been cited several times as a top performing hedge fund by Barron's and BarclayHedge. Recently, the WSJ published a list with the top 10 hedge fund performers that primarily take long/short positions in US equities. The Amvona fund tops the list with a reported 1-year performance of 58.71% for the interval between January 7, 2014 and January 7, 2015.

While the Amvona Fund does not have a large track record for us to evaluate it properly, its performance so far has been stellar. The fund reports an accumulated net performance of 173.8% since its inception on 1st September 2012 until 30th November 2014, which corresponds to a 56.5% annualised gain, largely surpassing the S&P 500.

**"AS A SUPPORTER OF A CONSERVATIVE BUSINESS APPROACH, LEMELSON WAS ALWAYS A CRITIC OF THE MASSIVE LEVERAGE TAKEN BY COMPANIES."**

### Final Words

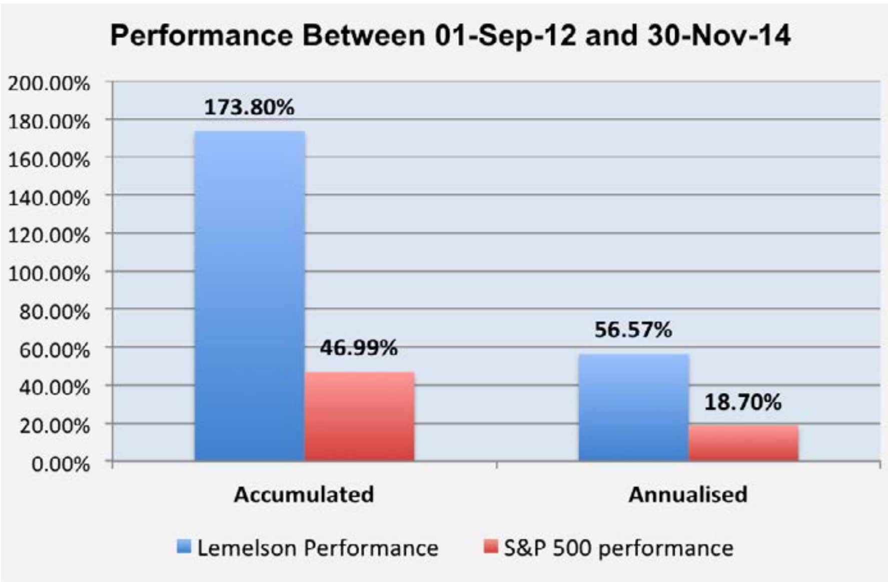
In a world where replicating what others do while taking on some extra leverage seems to be the main game, there are still a few that detach from society in general to seek out value. Lemelson proves that it doesn't matter what you do but how you do it. Be it e-commerce, finance, investment, or theology, a successful individual is one that is able to at some point detach from the herd and start thinking independently.

US LONG/SHORT EQUITY

LEADING 10 PERFORMERS

| Rank | Fund Name | Fund Mngmt. Co. | 1-Yr | 2-Yr | 5-Yr |
|---|---|---|---|---|---|
| #1 | The Amvona Fund, LP | Lemelson Capital Management, LLC | 58.71 | 90.27 | NS |
| #2 | Krensavage Partners LP | Krensavage Asset Management, LLC | 55.43 | 57.33 | 40.46 |
| #3 | Outer Islands Capital LP | Outer Islands Capital Management, LLC | 49.18 | 52.59 | 24.13 |
| #4 | Lycos Value Class O Fund | Lycos Asset Management Inc. | 42.92 | 25.71 | 24.30 |
| #5 | Harvest Small Cap Partners | Harvest Capital Strategies LLC | 41.17 | 24.02 | 16.37 |
| ........ | ........................ | ......... | | | |
| ### | S&P 500 | N/M | 10.20 | 38.54 | 77.40 |

SOURCE: WSJ



ALPESH PATEL ON THE MARKETS

**ALPESH PATEL ON THE MARKETS**

# TRADING ROADMAP

## A DIVERSION FROM SWEAT, TEARS AND PROFITS LOST (PART 2)

*Following up from last month on my series of lessons that I believe are essential for any trader or investor to keep in mind, I am offering the next and final part of my "trading bible". I firmly believe that these bits and pieces of hard-earned wisdom – if I may say so – are equally important to studying technical analysis or understanding the principles of macroeconomics before one trades the markets.*

**"IT'S LIKE LEARNING TO DRIVE A CAR: IT'S NOT JUST ABOUT READING THE CAR'S MANUAL OR TAKING THE TEST; IT'S ABOUT THE DRIVING INSTRUCTOR CONVEYING HIS YEARS OF EXPERIENCE WHILE WE'RE LEARNING."**

It's like learning to drive a car: it's not just about reading the car's manual or taking the test; it's about the driving instructor conveying his years of experience while we're learning. It's an interpersonal experience, but it's the most important part of learning how to trade the markets. So here we go again.

## Don't underestimate the psychological aspect of trading

Trading is as much about psychology as it is about technical patterns and trading setups. It is important that trading decisions are made without fear, doubt or anger. If you like the look of an opportunity and you believe in it, go ahead and take it.

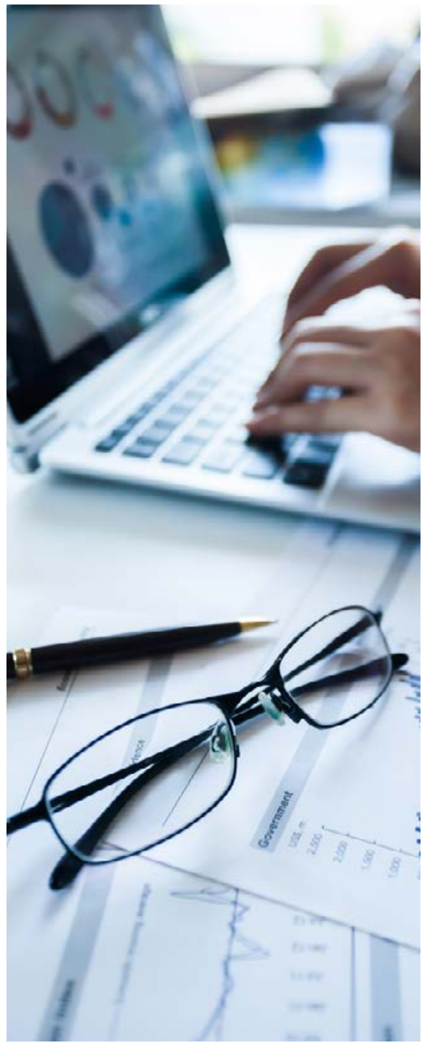
**"IT'S LIKE LEARNING TO DRIVE A CAR: IT'S NOT JUST ABOUT READING THE CAR'S MANUAL OR TAKING THE TEST; IT'S ABOUT THE DRIVING INSTRUCTOR CONVEYING HIS YEARS OF EXPERIENCE WHILE WE'RE LEARNING. "**

This is especially true since trading as an activity can sometimes go against our own human instincts, and our brain is not always wired to perform well when dealing with facts and emotions at the same time. In an ideal scenario trading should be done without any emotional factors taking effect, but we're human and this is not possible.

What is possible however is to develop a system and a set of rules to rely upon and make trading decisions part of this process, of this system. And again, trading decisions should be kept simple and fast. Make sure that you have followed your decision-making rules and just go with whatever conclusion they add up to.

If your system indicates a buying opportunity with set parameters for your target and your stop, then go for it without doubts.

Keep it simple and repeated. If you result in more losses than you'd expect then you might need to tweak your rules or tactics. But always follow them religiously so you find out as quickly as possible whether they're the wrong ones and actually need that tweaking.



## Trading involves losing money as well as making it

Let me blunt here: you will lose money when trading; we all lose and this is a fact. However this is an important thing to digest and it amounts to two principles essentially: first, if you can't afford to lose any money from your trading account then you shouldn't risk that capital at all; and secondly, if you can't get over the fact that you will be wrong numerous times and lose money as a result of that, then maybe trading is not the right thing for you.

The first lesson should really go without saying but people sometimes don't understand the simple truth that losses are inevitable. And they will be frequent – that's inevitable too.

No one can be right all the time, not even more than 7-8 times out of 10 consistently. And usually when it comes to trading, being able to be right just a bit more than you're wrong is enough and most times is the best you can hope for.

So if you can't afford any losses to your capital, then that capital shouldn't be part of your trading account. Find an amount of money that you can comfortably put at risk and trade with that.

And don't ever think that you can trade profitably if what you're looking to get out of the markets is an ego boost, a confirmation that you can be right more times than not.

Losses are to be loved; losses teach us valuable lessons and improve our tactics; losses when cut to a sustainable amount prove to us that we're badly positioned in the markets and maybe we should reposition accordingly.

So losses are not to be feared or fussed over. Losses are to be loved and treated as helpful signs along the road.

## Be informed, trading is all about making informed decisions

Find a reliable source of information, a website or a newsletter that can quickly and effectively let you know what the conditions of the market are and base your decisions on facts and not on instinct or luck.

There is an abundance of news and information sources out there. News and analysis websites like Bloomberg, Financial Times and Reuters can provide a stream of news 24/7. Technical analysis and ideas websites can be found by the dozen and even social media platforms like Facebook, StockTwits or even Twitter can provide crucial insight on the social aspect of trading.





One should be mindful though of two potential pitfalls: one is the credibility of the source and the other whether this source has an agenda or not. More reputable and independent sources can mostly be relied upon whereas market-makers and/or brokers sometimes have their own goals in mind.

And secondly, one should also keep in mind that too much analysis leads to paralysis in the end, meaning that you should look to have as much information as necessary to make an informed decision but no more than that.

Keep it simple, find a source that you understand and that suits your style and give it a fair chance. My site InvestingBetter.com offers a selection of newsletters and reports, which are worth taking a look at.

## Get educated and receive proper training from proven professionals

This is an absolute must. Education should be one of your first concerns. If you skip this step you will run out of money or patience before you get the hang of trading. And that's the number one factor that leads people to abandon trading very quickly and paint a very bad picture of it.

In truth, they haven't given trading a fair chance, as it involves a learning curve like every other activity in life.

The difference here is that every mistake, every bad decision literally costs money and operating capital, while taking away the initial excitement chunk by chunk and leaving frustration in its place.

So don't underestimate this important lesson: there is an abundance of educational resources out there. Invest time

**"IN TRUTH, THEY HAVEN'T GIVEN TRADING A FAIR CHANCE, AS IT INVOLVES A LEARNING CURVE LIKE EVERY OTHER ACTIVITY IN LIFE."**

and money if needed to get yourself properly educated. It's really an investment in yourself, and the most effective capital preservation tool.

And with that I am concluding this small series of lessons. These are mistakes and pitfalls that almost every trader falls into, so there's no shame in being in the same position. Nevertheless we should pick ourselves up, learn our lesson and improve our trading. That's the same thing that seasoned professionals do after years and years of experience, we evolve. The markets are never the same, but that's the beauty – and challenge – of trading.

**Happy Trading!**
**Alpesh B Patel**

P.S. You can find my daily market commentary on InvestingBetter.com. See you next month!

Alpesh is a hedge fund manager who set up his asset management company in 2004. His Sharescope Special Edition has outperformed every UK company's fund manager over the past decade, as well as Warren Buffett. He has written over 200 columns for the Financial Times and presented his own investment show on Bloomberg TV for three years. He is a former Visiting Fellow in Business & Industry at Oxford University and the author of 18 books on investing. Find out more at http://www.investingbetter.com and http://www.inter.tradermind.com

SCHOOL CORNER

# MARIA'S GOLDEN RULES FOR TRADING CFDS

**BY MARIA PSARRA**

*Now ladies and gentlemen, the time has come to continue with my Golden Rules for Trading CFDs, a subject that we started discussing in my last article (May edition of the Master Investor Magazine), where you will find the first four Rules. So starting with Rule five, here are the rest of them:*

## Rule 5 - Have a plan, and stick to it

This is one of the most important rules of trading, and it remains the same regardless of whether you are trading CFDs or any other financial product. Every trader, every investor has different goals, different experience, different risk tolerance, and really a different life and personality. Your plan should be such that it is suitable for you personally, having taken into account all of the aforementioned criteria. ''*Wanting to make money quickly*'' may be something I keep hearing from traders and investors over the years, but I can ensure you that it is in no way a viable trading plan. It is simply and only a wish.

Furthermore, it is not enough to have a plan; you also have to follow it. Otherwise, even the best plan in the world will have zero value to you.

## Rule 6 - Select markets and financial products that are suitable for your risk tolerance, your experience, and your financial situation

These products may or may not include CFDs. I do not have the right answer for you without knowing you, and discussing things with you in person. The FCA's ''Assessing Suitability and Appropriateness'' tests can help you and your advisors assess this one.

> **"IT IS NOT ENOUGH TO HAVE A PLAN; YOU ALSO HAVE TO FOLLOW IT. OTHERWISE, EVEN THE BEST PLAN IN THE WORLD WILL HAVE ZERO VALUE TO YOU."**

What I can and will say however is that you need to fully understand any financial product and the risks associated with it prior to trading it.

No one is born with this type of knowledge: we all have to learn, we all ask stupid questions, and we all get things wrong when first approaching any new product. So do please ask questions, clearly understand the answers, and then choose that which is suitable for you.

## Rule 7 - Only risk money you can afford to lose

This applies to any given moment in time and to any financial product you trade. It is even more so the case with derivatives products like CFDs, Futures, and Options, where you can lose more than your initial investment. To clarify, I am in no way implying that you should not trade derivatives products (I personally tend to prefer them to cash/equities/bonds, as they are much more ''flexible''). I am only repeating the point made earlier that you should understand the products you trade, so that you can then assess whether specific trades will not entail risking more than you can afford to lose.

In reality, the point I am making is the same for any financial product, because I am actually making a point about you. You have to take a view on the amount of funds that, if lost, would realistically not make a change to your life (and by life I do NOT mean your ego; I mean things like your rent, your children's school fees, your retirement plans, etc). This amount is your risk capital, and this is the maximum and only capital that you should put at risk in the markets (and elsewhere, if I may add).

## Rule 8 - Keep emotions out of your trading, and even more so out of your CFD trading

Why? Because to begin with, as we have discussed in my previous articles, emotions simply do not have any place in trading and investing, so do keep them well out of the way. I can ensure you that although most of you will never witness this, I am rather emotional when it comes to my personal life, and yet I am not emotional when trading. I have trained myself to do this, and so can you.

So why the ''even more so out of your CFD trading''? Simply because when you trade CFDs, your exposure to the asset you are trading is magnified, so you may as well not magnify any loss of control issues you have through it. You are better off ensuring you can control yourself before trading anything, including CFDs.

## Rule 9 - Use CFDs to diversify

In other words, do not ''put all of your eggs in one basket''. CFDs allow you to take the same exposure you otherwise would when buying physical shares in a company by putting down just a small initial deposit (otherwise called margin). So do use the remaining funds in your trading account in order to buy/sell other stocks, commodities, or whatever better suits your goal to profit from the prevailing market conditions.

## Rule 10 - Protect yourself, use CFDs for hedging when necessary

Once again, CFDs are a flexible tool. They allow one to go long or short, and as such allow one to profit from both rising and falling asset prices. Take advantage of this flexibility. Nothing goes up or down in a straight line, so there are bound to be opportunities on both sides of the market over any given period of time. Use them to make money.

Furthermore, if you are for example a long-term equities investor, and you are scared that World War Three may just be starting (imaginary scenario obviously), do use CFDs to protect yourself.

How? Go short a related index, buy some ''stress and fear antidotes'' such as gold or government fixed income CFDs, just to name a few options.

> **"CFDS ARE A FLEXIBLE TOOL. THEY ALLOW ONE TO GO LONG OR SHORT, AND AS SUCH ALLOW ONE TO PROFIT FROM BOTH RISING AND FALLING ASSET PRICES."**

Remember, the markets will only ever do to you what you allow them to, so whatever the situation is, just learn to use the right tools to protect yourself and the value of your trading account. CFDs are one of the best products to achieve this so long as you use them wisely.

This concludes my Golden Rules for Trading CFDs. I hope you enjoyed this article, and as always I welcome your questions and feedback.

**Until next month,**
**Happy trading everyone!**

Maria Psarra is a Senior Derivatives and Equities Trader who has headed several Advisory Trading desks in the City over the course of her career. In her most recent role as Head of Trading at Prime Wealth Group, Maria determined the company's trading strategy, supervised a team of experienced brokers, and advised high-net-worth individuals on suitable investment strategies. Maria employs different investment styles in order to construct personalised portfolios best suited to the risk and return preferences of her clients. Typical portfolios primarily comprise UK and European equities and equity indices, and, to a lesser extent, commodities and fixed income exposure.

Maria appears on Tip TV on a weekly basis providing investment tips and market commentary, writes for a number of financial publications, and is often invited to present her views during conferences such as the Master Investor Show, the London Trading Show, and Inside ETFs Europe, Europe's largest ETFs conference.

## EVIL KNIEVIL (AKA SIMON CAWKWELL)

# THE BEST OF THE EVIL DIARIES

*A big man with a bigger reputation, Evil Knievil famously made £1 million by short selling shares in Northern Rock during its collapse. He also uses his knowledge and experience to buy shares, often resulting in the same devastating effect.*

*At least three times a week, Evil provides his thoughts and musings on the markets. Now writing EXCLUSIVELY for Master Investor Magazine at http://www.masterinvestormagazine.co.uk/category/evil-diaries/.*

**He doesn't just pontificate on the financial markets in The Evil Diaries; he also comments on politics, current affairs, his favourite horses/sports bets, and the occasional film and book review thrown in for good measure. Here we take a look back on the highlights of Evil's diaries in the month of May.**

### 6th April

Last week, Jim Slater compared an investment in **Telford Homes (TEF)** with one in **ASOS (ASC).** He is very keen on Telford and he may be right so to enthuse – I myself am cautious about housebuilders since they have always seemed cyclical to me. However, he slates (well, he would wouldn't he) ASOS arguing that a PE for 2016 of 70 is quite ridiculous. I am sure he is right given the declining profit margins and the emergence of competition such as **BooHoo (BOO)** whose results appeared today.

I add that an investment in ASOS is surely an expression of a death wish since not only is a PE of 70 perfectly potty it is held up by sales of ASOS shares being deferred until the owner, seeking that his estate benefits from IHT relief, has done his necessary two years of holding: thereafter the beneficiaries of the will can get out, clear of CGT and IHT. This is an entirely artificial levitation trick. Further I can't think of any good reason to allow IHT relief on an AIM listed stock. That prop could therefore easily evaporate.

### 8th May

About forty years ago, my late father-in-law, himself a by then retired successful soldier and former War Office worker, strongly pointed out to me that the moment the squaddies choose the generals the army is enfeebled. And one wonders whether **Ed Miliband** was chosen just because Len McCluskey and other intellectuals of the trade union movement said so. Further, David Miliband might have been a wiser choice – and he was not adopted since Len and Company said no.

Anyway, I always thought that Labour never offered anything new or credible and the outright refusal to apologise for the appalling mess generated by Gordon Brown and his sidekick Balls was at one level ill-mannered and at another deceitful. Mercifully, the electorate saw through all this.

### 11th May

**Beximco Pharma (BXP)** today announced annual results to 31st December 2014. The statement is fairly upbeat.



> **"IT IS POINTED OUT THAT IF ONE STICKS MICROBIOMES IN A YOGHURT IT SWEETENS THE STUFF, THUS RENDERING YOGHURT MORE PALATABLE, AND CAUSES A MICROBIAL REACTION IN THE GUT WHICH REDUCES WEIGHT. EVEN I CAN SEE THE APPEAL OF THIS SORT OF ADDITIVE."**


**"THE REASON FOR THE PREMIUM IS THE SHEER WEIGHT OF LUNATIC CHINESE RETAIL INVESTORS."**

It begins "Despite prolonged political unrest causing serious disruption to our business activites, especially during the first quarter of 2014....". But the fact remains that EPS came to 4.15p with every expectation that this figure will be bettered in 2015. Provided one is prepared to live with the political uncertainty (just how is it to be assessed at this distance?) Beximco is solvent and TNAV is about 45p. Payday for the dividend of c. 0.8p is in mid July. This is cheap.

**15th May**

The saga continues at **Gate Ventures (GATE)**, now 212p. And yesterday a well known ETF fund manager called by and pointed out that Gate is by no means alone in operating a manipulated share price. For instance he drew my attention to the Hang Seng China AH Premium Index (Google away) which notes the premium that stocks in general quoted in China enjoy over their identical counterparts quoted in Hong Kong. It is currently 33% and has no chance of persisting since the Chinese know perfectly well how to get cash into Hong Kong and invested accordingly. The reason for the premium is the sheer weight of lunatic Chinese retail investors. This is not a permanent condition – the Premium Index stood at a discount of 10% about a year ago. But the premium phase is where we are now.

For instance, take Beijing Baofeng Technology. This was floated about two months ago and has risen thirty-four fold, rising every day bar yesterday. It is capitalised at £2.9bn and is of course absolutely certain to crash. I do not know how to short this stock but, like Gate, it will collapse.

**18th May**

It was surprising that **Chuka Umunna** dropped out as early as he did. He had to start as a front runner since he did not know what his power base would or could prove to be. I suspect that having exposed himself he found a poor response with the result that he decided to plead personal reasons as a basis for packing it in. I have no sympathy since his only guiding principle is to promote Chuka Umunna.

I cannot see Liz Kendall building a power base since she seems not to have union backing – without which she has little chance. Yvette Cooper might be taken on her own merits but she is irrevocably associated with her husband, Ed Balls, and that is surely a disadvantage given that it was he with Gordon Brown who set about deceiving the public to raise money which was promptly applied to reckless massive overspending in 1997 to 2010. Although she has at least had experience (unlike all the other runners bar Burnham) and is not stupid she is unlikely to cut it at a visceral level.

So it looks as if Andy Burnham lands this. However, and as I have noted before, I am not an insider and one really has to be an insider to win at this betting.

Finally, there is quite a time before the final furlong is run since, under a timetable drawn up by the party last week, nominations for leader close on 15th June. Members and supporters who sign up by 12th August will be entitled to vote and the result will be announced on 12th September. Funny things can happen.

**21st May**

There is a disconnect going on here. I mean, this morning's Guardian runs a story on Sadie Frost's damages claim which she has won from Mirror. I hear a figure of £250,000 plus legal expenses. Since this sort of pole-axing amount is to be repeated many times to come, one must presume that Trinity Mirror (TNI) have underprovided for this disaster – they certainly underpaid into Court. Apparently, Mirror's counsel admitted liability to compensate for hurt and then tried to challenge whether the claimant had been hurt. The purpose of this public inconsistency was to try to get claimants to back off. However, I am told that the judge was having none of this and warned Mirror's counsel that each such question was putting up the damages by £10,000 a time. And, of course, Mirror still have to pay counsel. All this could run to many many tens of millions of pounds. And some think that it is sufficiently serious to take Mirror insolvent. I myself cannot comment on the extent of Mirror's problems, but they are clearly vastly more than Mirror has so far publicly announced as in point and provided for. Mirror is now 180p.

**27th May**

Today's RNS from **Plus500 (PLUS)** does not allow hard sensible conclusions. I know that Odey has bought again and I also know that the fund manager in question is not even remotely an idiot – a fact that I established over an extended lunch at Le Gavroche.





However, and starting with the "Group Summary", the facts (Plus500 had better have got these right) there stated are as stated. But no more. All the statistics as regards customer recruitment mean nothing until they reflect what has happened and is happening subsequent to last week's collapse. And it is too early to assemble these on a statistically significant basis.

They refer to "Group cash" of $92.2m. But what happens if people sue for a refund of their money which has been improperly held back? Or regulators compel such refunds? It must be remembered that I am reliably advised that customers who have sought to be paid out have been fobbed off with the advice that since market abuse is suspected their accounts are frozen pending a review (by Plus500 of all parties!). At what point have customers just given up trying to get their money back? How much is thus involved? And how much has been credited to profit and loss account as reported to the market?

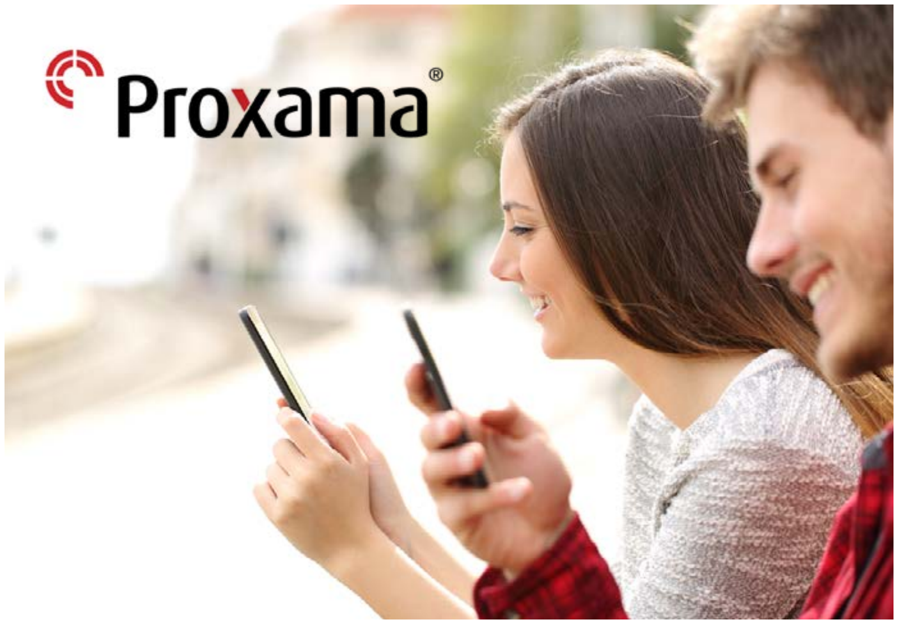
Well, none of these questions have been answered. So anybody who buys Plus500 as an investment is taking a leap of faith which, by generally understood common sense tests, is not justified. I know it is hard to borrow stock. But I keep at it.

**28th May**

I originally subscribed for **Proxama (PROX)** at 5p two years ago and thought it rather disappointing as it kept drifting down. Last week it started to ease back up. A seller has been Richard Griffiths whose judgement I certainly respect but which in this case I have decided to override. Richard has completed his selling.

Were it the case that I have a smart phone I imagine I would have a better idea as to what is going on here. But given that it is clear that many people, particularly young people, are dedicated to inspecting their mobile phones the entire time it would be silly to ignore Proxama's claims to be on the cusp of taking a dominant position in selling this avenue for advertising.

**"THE LIKES OF EXXON AND MOBIL ARE TAKING A CLOSE LOOK SINCE THE POTENTIAL OF MOIL'S ACREAGE IS STRATEGICALLY SIGNIFICANT."**




At December 20 the cash stood at £5.5m. When I spoke to chairman David Bailey yesterday, I had the clear impression that it would not be necessary to raise further cash from shareholders. David is one of nature's enthusiasts and one should therefore be cautious about taking his hook line and sinker. But I am assured that he is honest and I know that he has been successful when developing companies. So I incline to the view that he is very much worth listening to.

Proxama is capitalised at 2p at £20m. Apparently, a company in the USA, Swirl Networks Inc., with which Proxama might be compared is capitalised at £100m. On the other hand it must be accepted that valuations in the USA are often completely mad and that therefore it would be unwise to set much store by this comparison. Besides, this country is very different to the USA as regards its consumers and their way of picking up ideas as to how to spend their money.

As to what the business is, I summarise it as two-pronged. One is payments using one's mobile and the other is proximity marketing (hence the origination of 'prox'). Taking the second activity the punter walks past a pub and is told on his mobile screen that Guinness is on special and that, since it is eleven o'clock, a right thinking punter should pop in. I hasten to add that there are many rather subtler and more varied propositions on this basis – as inspection of Proxama's web site will disclose.

Digital payments means that the punter pays for his/her Guinness on the spot using his/her mobile. Again, I refer you to the Proxama web site. This is a feature/extension of the developing cashless society.

Anyway, Proxama is really confident that it has emerged as a "go to" company and that therefore the commercial success that they have always forecast will now emerge. I bought 2m at 1.8p. I either write off the lot or make perhaps five or ten times that amount.

## MAY 2015

# BEST OF THE BLOG

“AS WE HAVE LEARNED FROM THE PAST, WHEN PRICES DIVERGE TOO MUCH FROM INTRINSIC VALUE, THEY BECOME VULNERABLE TO A CRASH.”

## Bond Mini Crash Uncovers Rising Risks

In my blog **Don’t Fight The Fed, Fight The ECB**, published last week, I said that investors face an epic opportunity to short bonds, as the risks of doing so are very narrow while the upside potential is huge.

Buying an asset just because you believe someone else will buy it from you at a greater price may work for some time, but not forever.

Such a business model relies on the exact same assumptions on which the housing boom was based before the financial crisis. But prices just can’t rise forever without reflecting the intrinsic value of the underlying asset. As we have learned from the past, when prices diverge too much from intrinsic value, they become vulnerable to a crash.

At the beginning of this year, investors, seduced by the ECB bond purchasing programme, forgot about the fundamentals that drive bond prices in the long term and jumped into the market, in expectation that the ECB would purchase from them at higher prices. While the enthusiasm was high, investors were seeking higher risk debt with longer maturities and treating everything as if it was a whole single issue. The lower limit for a government yield issued by a high grade government like Germany was put at the deposit facility rate of -0.2%, as investors thought the huge purchase programme the ECB had in mind would lead the central bank to buy anything up to that limit, no matter how long the maturity was. But the ECB is not purchasing unlimited amounts, nor is it purchasing bonds forever, and sooner or later these bonds need to reflect inflation expectations. We should not forget that one of the aims of the bond purchase programme is precisely to generate inflation. So, with the pursuit of price stability being the sole mandate of the ECB, this would suggest an inflation target of 2%; at buying German 20-year bonds yielding 0.7%, one is either irrational or is simply assuming the ECB will fail miserably in driving inflation higher. In my view, while there is justification for a short-term yield to be lower than the 2% ECB target for inflation, it is not reasonable to assume the same for a 10-year or a 20-year bond.

**By Filipe. R. Costa**

**To read the full article visit...**

**http://www.masterinvestormagazine.co.uk/latest/bond-mini-crash-uncovers-rising-risks/**

## Advanced Oncotherapy (AVO) LIGHTs up

I last looked at Advanced Oncotherapy (AVO) back in the Spreadbet Magazine days, having identified them as part of a crop of "speculative small caps that could be set to surprise on the upside in 2015". Well, certainly haven't disappointed in that regard, having soared from around 4p at the time of my original article to a peak of around 14p in April. They have since settled down to around the 8p mark, but the story isn't over yet...

For the uninitiated, let's remind ourselves of the AVO story. The firm has developed a new slant on the radiotherapy treatment currently used to treat around 60% of cancer patients worldwide. The continued challenge clinicians face is to deliver adequate amounts of radiation to the tumour while sparing non diseased, healthy tissue and vital organs like the heart, lungs, spinal cord, liver, bladder and kidneys. The advantage of sparing healthy tissue is to reduce the risk of secondary cancer from the treatment itself.

**"ADVANCED ONCOTHERAPY'S FOCUS IS TO DEVELOP ADVANCED, COST EFFECTIVE AND PATIENT-FRIENDLY RADIOTHERAPY TREATMENTS WHICH ARE CLINICALLY SUPERIOR TO THOSE CURRENTLY AVAILABLE."**

Advanced Oncotherapy's focus is to develop advanced, cost effective and patient-friendly radiotherapy treatments which are clinically superior to those currently available. The company is a leader in affordable and accessible proton beam therapy which eliminates the need for a cyclotron or synchrotron which alone weigh in excess of 200 tons. This new technology is significantly smaller and thereby reduces capital expenditure, shielding requirements and running costs compared to other machines.

Unlike x-rays, protons do not emit high doses of radiation when they travel through the body. Their killing power comes from the sharp falloff when they stop – this is known as the Bragg Peak.

**By James Faulkner**

**To read the full article visit...**

**http://www.masterinvestormagazine.co.uk/latest/advanced-oncotherapy-avo-lights-up/**

## How Sustainable is the British American Tobacco Dividend?

In anticipation of the first quarter results from British American Tobacco (BATS), I use the hiatus to cast an eye over the last annual results from BAT in order to get some idea of what we should be looking for. I might add that we have a little time to wait, as I understand that the Q1 results to 31st March are published on the 29th of July. The last trading statement said that revenue was down 5.7% in Q1.

I have not been bullish of BAT, being somewhat spooked by the twin peak formation of the share price chart, which according to technical folk law, suggests that the price may have reached a momentous peak. Since then, the share price has come down enough to break the share price uptrend, which according to my observation, has been in place since 2014. You will note that the share price peaked at 3,894p in March. Last seen – having gone through a trend support line – it was 3,569p. The chart now resembles a series of peaks like some alpine vista, which thus constitutes the big overhead resistance to the share price progress. So what should we look for when the next results are published?

The first thing for bulls to hope for is some sign for an improvement in revenue in Q2. Annual sales revenue in 2014 fell 8.45%, depressing statutory reported trading profit, which is an important component of the company's operating cash flow. In fact, during 2014 the operating profit figure was more than a fifth larger than the operating cash flow figure, indicating the crucial importance of operating profit as a contributor to operating cash flow. In contrast, see how small the contribution of depreciation is. That strikes me as a weakness, which needs to be put right.

**By Robert Sutherland-Smith**

**To read the full article visit...**

**http://www.masterinvestormagazine.co.uk/latest/how-sustainable-is-the-british-american-tobacco-dividend/**

**"FGT HAS AN EXTREMELY CONCENTRATED PORTFOLIO OF 25 STOCKS WITH TRAIN JUSTIFYING HIS HANDS OFF APPROACH BY SAYING THAT HE HAS BEEN RUNNING HIS WINNERS AND THAT THEY CONTINUE TO PRODUCE HANDSOME RETURNS."**


## Would you invest in a fund that hasn't bought or sold a share for four years?

I recently came across an interesting comment from Nick Train, the highly regarded manager of the **Finsbury Growth & Income Trust (FGT).** He was quoted in the **Telegraph** as saying that he had not bought or sold a single share for four years and that on average he retains his shareholdings for eighteen years.

FGT has an extremely concentrated portfolio of 25 stocks with Train justifying his hands off approach by saying that he has been running his winners and that they continue to produce handsome returns. This is certainly borne out by the strong outperformance of the fund.

I first came across Nick Train in 2004 when I stumbled upon his **Lindsell Train investment trust (LTI).** At the time it was still relatively new, having been set up in January 2001, but what caught my eye was the investment objective:

'To maximise long-term total returns subject to the avoidance of loss of absolute value and with a minimum objective to maintain the real purchasing power of Sterling capital, as measured by the annual average yield on the 2.5% Consolidated Loan Stock.'

This struck me as exactly what I was looking for and I invested in it, paying the princely sum of £98 a share. Eleven years on I still own them, although they now change hands for more than £450 each.

The reason for mentioning all this is that many of the largest shareholdings in the two funds are the same. These includethe likes of Unilever, Diageo, Pearson, Heineken, and the London Stock Ex change. This made me think about how advisable it is to hold on to such strong performers.

**By Nick Sudbury**

**To read the full article visit...**

**http://www.masterinvestormagazine.co.uk/latest/would-you-invest-in-a-fund-that-hasnt-bought-or-sold-a-share-for-four-years/**

## EVIL KNIEVIL (AKA SIMON CAWKWELL)

# PLANNING TO SAVE

*I am not expert in pension and savings planning. But I console myself with the fact that I've not yet met anybody who knows anything like sufficient about this subject to persuade me that he is worth listening to either.*

However, my eye was caught by an article in the Spectator of 23rd of May 2015 in which the former City editor of the Daily Telegraph, Neil Collins, sets out his views as to how best to save for the long term. He is not a fool. What is really interesting is that he thinks that pension policies are a waste of time and money. I am not sure he's right about that since the general principle behind these pension policies is that tax relief at 40% can be achieved on entering the fund and gains can be rolled up for the duration of operation of the fund free of tax and, when those savings are drawn upon, only income tax at the then standard rate might apply. If that rate is 20% of the coming out bit as against relief of 40% on the going in, there is obviously a theoretical attraction as the law stands. On top of that there is also a lump sum of the order of 25% of the fund which can be taken completely free of tax when retirement eventually occurs. All this is very long term.

One has to be cautious about claiming to know the law that will apply in 20, 30 or 40 years' time since politicians, when they run out of money, have no hesitation in making the law less favourable to savers. And in this particular example I think there is a fair chance that that is exactly what the politicians will do.

Neil says that he thinks the administrative costs of pension pots will rise such that there is a serious impairment of the returns achieved on these funds. I have no way of knowing or guessing the extent of such waste but it seems very likely that it will occur – it is bad enough as it is. Where Neil is emphatic is when claiming that an ISA is the better way to save. As I have earlier remarked, I do not see how he can be certain about this since there's

> **"ONE HAS TO BE CAUTIOUS ABOUT CLAIMING TO KNOW THE LAW THAT WILL APPLY IN 20, 30 OR 40 YEARS' TIME SINCE POLITICIANS, WHEN THEY RUN OUT OF MONEY, HAVE NO HESITATION IN MAKING THE LAW LESS FAVOURABLE TO SAVERS."**

no tax relief going into an ISA and, although the gains are free of tax within the ISA, and there is no tax applied to withdrawals from the ISA my instinct is to bear in mind the possibility that politicians can seek to freeze ISA capital sums at some point. I'm not being cynical. I am merely reflecting upon the fact that the general level of debt – by

> **"THE GENERAL LEVEL OF DEBT – BY THAT I MEAN GOVERNMENT DEBT – IN THIS COUNTRY IS SO GREAT THAT THE TEMPTATION FOR POLITICIANS TO DO SOMETHING ABOUT IT BY RAIDING PEOPLE'S SAVINGS MUST BE OVERWHELMING AND INCREASING."**

that I mean government debt – in this country is so great that the temptation for politicians to do something about it by raiding people's savings must be overwhelming and increasing.

That noted, I think the politicians will have a go at property first. Think of Miliband's insane mansion tax. Neil makes a very good point that savings put into ISAs are free of tax on a pretty considerable scale. Certainly, the amount that can be saved without the annual ISA subscription limits being hit is considerably greater than the average man or woman can set aside. Therefore ISAs must be worth looking at.

A big mistake that savers make with ISAs is that stockpickers for ISAs have historically included funds which have hidden charges applied to them – possibly as much as 2% per annum (the famous "trail"). So although the ISA is on the face of it the cheapest form of investment vehicle to consider, the reality is a hidden accumulating cost which impacts performance on a considerable scale. (I know these hidden charges are supposed to have stopped but I do not trust the providers of these funds.)Also, one should not forget that every taxpayer has the annual tax free capital gains allowance of £11,000 odd. Truly, an astute taxpayer investor will be hard pressed to pay any tax on really quite substantial savings.

THE 2015 MASTER INVESTOR START-UP COMPETITON

2015 masterinvestor

RESEARCH • ANALYSE • INVEST

# START-UP COMPETITON

**BY EMANUIL HALICIOGLU**


*Investing in a successful company earlier on in its business life-cycle can provide greater returns. What's more, start-up companies will likely have a much lower level of market coverage than your more established institutions, thereby increasing your chances of spotting a business gem before anyone else does. Furthermore, with an investment in a start-up company likely to represent a greater proportion of a company's share capital, it provides an opportunity to exercise any entrepreneurial skills you may possess, influencing the direction of the business.*

Manos Halicioglu is an Equity Analyst with extensive experience in research at leading financial institutions, including the European Central Bank and GECR, and is regularly featured in Bloomberg, CityAM and Portfolio Institutional. Manos is a graduate of Imperial College and is a Level III candidate for the CFA Program.

THE 2015 MASTER INVESTOR START-UP COMPETITON

**"TEN START-UP COMPANIES WERE GIVEN THE CHANCE TO PITCH THEIR BUSINESS IDEAS TO A JUDGING PANEL CONSISTING OF FORMER MANAGING DIRECTOR OF GOOGLE UK AND IRELAND DAN COBLEY, HIGH PROFILE INVESTOR JIM MELLON, AND JUNIOR JUDGE ALEX MUSTIER."**

**Last month, I was lucky enough to be invited to the inaugural Master Investor competition. Ten start-up companies were given the chance to pitch their business ideas to a judging panel consisting of former Managing Director of Google UK and Ireland Dan Cobley, high profile investor Jim Mellon, and junior judge Alex Mustier, who will be attending Wharton Business School as a student later this year.**

What were these companies competing for? The opportunity to present at the 2015 Master Investor conference in front of over 4,000 investors, held the very next day in the heart of the City; the opportunity to tap into the networks and experience of Dan Cobley and Jim Mellon (or even obtain funding from them); and the public recognition of having been in the top 10 start-ups chosen for the competition, following the Master Investor team's screening of over 200 start-ups from which the 10 most interesting companies were chosen.

For the benefit of Master Investor readers, I have presented a short summary of each of the start-up companies below:

## 1. Onfido*

Onfido

Founded in 2012 by entrepreneurs from Oxford University and backed by the same institutional investors behind companies like Uber, Spotify, Dropbox and Airbnb, Onfido is a London-based technology company that is revolutionising the way companies carry-out background checks on individuals. With victims of identify fraud rising to 7 million people in the UK alone, it is easy to see why this is such a lucrative area to be in. Utilising its technology-driven platform, its focus is on offering the fastest turnaround times on a comprehensive range of checks and ensuring a fully compliance background checking process, all of which is provided at a very competitive price starting at £39 per check.

**www.onfido.com**

## 2.Gliide

GLiiDE

Headquartered in London, Gliide has developed an app-based chauffeur service with a difference: all its vehicles are 100% electric. Given the ever increasing demand for green products and services, and that the estimated number of licensed taxis and private hire vehicles in England and Wales alone stood at 231,000, its addressable market could be very lucrative. Using its cloud-based dispatch platform, Gliide helps businesses and individuals get around and improve their sustainability efforts without the 'green' premium, with its fares reportedly undercutting the UK's black cab services by half.

**www.gliide.co**


## 3. Virtusize

VIRTUSIZE
FIT ILLUSTRATED

Founded in 2011 and headquartered in Sweden, Virtusize is a fashion tech company with a vision of being the world's leading standard for illustrating fit. With the number of online purchases that are subsequently returned by the buyer at 30%, and improper size and fit accounting for 50% of this, the estimated addressable market is significant. Trusted by some of the most prestigious brands in the industry – including Acne Studios and Monsoon – Virtusize's easily-integrated app helps online retailers to visually illustrate the size and fit of clothing, thereby reducing fit-related returns by up to 50%. It also increases sales, with 20% of shoppers that use Vitusize then going on to make a purchase.

**www.virtusize.com**

## 4. InvestUP

investUP

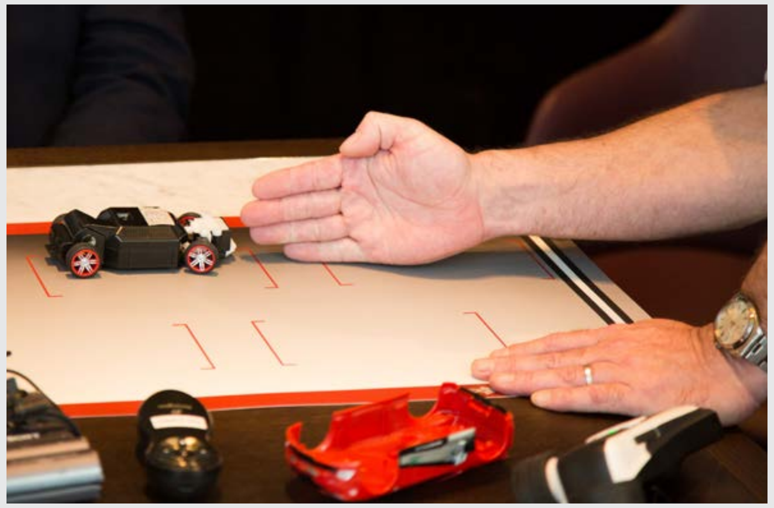
Founded in 2012, InvestUP is a fin-tech company with a goal of simplifying and opening-up crowdfunding for investors. According to the Crowdfunding Industry Report, the global amount raised via crowdfunding is set to double to $34.4 billion by the end of 2015. InvestUP's online platform aggregates crowdfunding sites, enabling investors to access all their favourite crowdfunding sites using just one account, leading to the discovery of more deals and the reduction in time spent sourcing these deals.

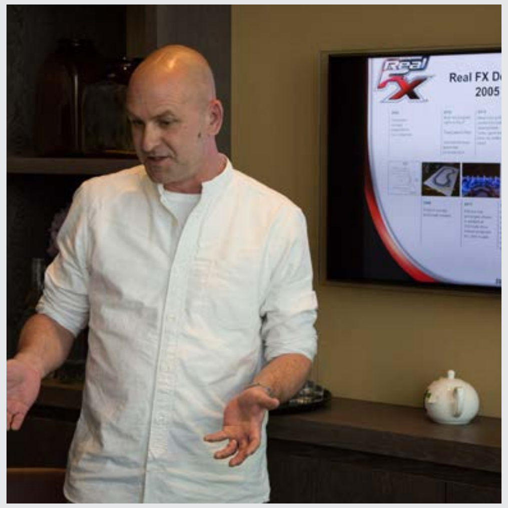
**www.investup.co**

## 5. FX Racing

Focused on creating technology-based toys, Wow! Labs is the architect of Real FX racing, a remote controlled racing car game like no other. Using cars with built-in artificial intelligence, Real FX Racing gives players the rich content of video and digital car racing, but in real life. Click here to see it in action. The demand for toys is certainly significant, with a study, conducting by the NPD Group and the US Department of commerce, estimating the global toy market at $84.1b billion in 2012.

**www.wowstuff.com**









## 6. Business Finance Compared*

business finance compared.com

Headquartered in Nottingham, Bizfitech is a fintech company with a mission of making business finance as transparent, fast and flexible as consumer finance. Its flagship platform, businessfinancecompared.com, is a comparison website that helps UK SMEs to find and compare alternative sources of funding to grow and support their business. With an estimated 5 million SMEs in the UK alone, of which around 500,000 search for new finance every year, the addressable market here is certainly sizeable.

**www.businessfinancecompared.com**

## 7. OpenTRV

openTRV

Founded in 2014 and headquartered in Surrey, OpenTRV is a technology company with a mission to reduce the carbon emission of the UK. Its flagship product, also called OpenTRV, is a sensor-based control system that switches the heating on and off in a room depending on both the temperature and whether anyone is actually in the room, thereby reducing both carbon emissions and energy bills. With heating accounting for 60% of the UK domestic energy use and 60% of people admitting to heating unoccupied rooms, OpenTRV may be the investment we are all looking for.

**www.opentrv.org.uk**

## 8. KweekWeek

KweekWeek
Event discovery & ticketing

Founded in 2013, KweekWeek is a London-based company that has developed a platform which connects event organisers and attendees in a single space. The platform, also called KweekWeek, gives event hosts access to a number of tools to help them manage and promote their event in one place. For event attendees, KweekWeek recommends new events based on location, history, personal preferences and social cues, so that relevant events find an audience – and vice versa. The UK event market is sizeable, housing an estimated 25,000 businesses and generating annual incomes of £42.2 billion.

**www.kweekweek.com**

## 9. Glisser

GLISSER

Glisser is a London-based company that helps make presentations more engaging. Used by Grant Thornton, Bloomberg, i2i Events and a number of Government departments – as well as Jim Mellon at the Master Investor conference this year – its flagship product, also called Glisser, combines PowerPoint or Keynote slides with social and interactive features, engaging audiences through native and web-applications on their smartphones, and collecting data for presenters and event organisers. With more than 30 million PowerPoint presentations made each day, Glisser is certainly worth taking a look at.

**www.glisser.com**

## 10. CityFalcon

Launched in 2014, CityFalcon is a London-based Fintech company that has developed an online platform which provides crowd-curated, real-time financial news. By leveraging more than 200 financial publications and Twitter, its platform helps investors make more informed investment decisions. Around one-in-four investors in the US engage in the equity market, all of which are potential users of CityFalcon.

**www.cityfalcon.com**

## And the winner is...

Ten start-up companies, all of which offered a compelling vision! So which company won the Master Investor Start-Up Competition? Some of you will have already seen the winner present its investment case on the Rising Star Stage at the Master Investor show. If you'd like to see how the individual contestants presented themselves, you can also find our 10 minute video of the presentation highlights on the web: LINK

Following a full day of intense presentations combined with Q&A, the following three companies came out on top:

**1. Business Finance Compared***
**2. Onfido***
**3. Virtusize**

As Jim and Dan agreed, "all 10 of them hold great promise and are worth following." Some of them are currently fundraising, whereas others have fundraisings coming up further down the road. Interested investors can contact these companies themselves through the websites listed above.

*"Such a great event! We not only got to validate our product and get feedback from our potential user base, but we also got some interest from potential angel investors."*

**Ruzbeh Bacha, Founder of CityFalcon.com**

**In 2016, the Master Investor show will take place on 23rd April. Tickets can be booked here. Companies that would like to be considered for next year's competition can email us at swen@masterinvestor.co.uk**

* Brightside Ventures, of which Dan Cobley is a director, is invested in Business Finance Compared and Onfido. Due to Dan's involvement his votes for these companies did not effect the final standing.

## READ TO SUCCEED

# BOLD: HOW TO GO BIG, CREATE WEALTH AND IMPACT THE WORLD

## BY PETER H. DIAMANDIS AND STEVEN KOTLER

### A BOOK REVIEW BY SWEN LORENZ

Simon and Schuster, Paperback GBP 7.69 on Amazon

In order for an investor to make a fortune on the markets, he or she really only needs to strike it big once or twice. Jim Mellon calls them "money fountains", the venture capital industry speaks of unicorns – companies that grow so fast that their investors make 50, 100 or even 1,000 times their money in a really short period of time.

Peter Diamandis' "Bold" explores the technologies that are disrupting today's Fortune 500 companies and that enable start-up entrepreneurs to go from "I have got an idea" to "I run a billion-dollar company" in the space of just a few years.

His book is divided into three sections. In the first section, he provides exceptional and genuinely useful insights into the power of 3D printing, artificial intelligence, robotics, networks and sensors, and synthetic biology. In section two, Diamandis picks the brain of five iconic leaders – Larry Page (Google), Richard Branson (does he need an introduction?), Elon Musk (Tesla), and Jeff Bezos (Amazon). Getting down to practical matters, in section three Diamandis explores and explains how anyone can harness the power of crowd-fundraising, building communities involving a billion users, and making a fortune as an entrepreneur.

**"PETER DIAMANDIS' "BOLD" EXPLORES THE TECHNOLOGIES THAT ARE DISRUPTING TODAY'S FORTUNE 500 COMPANIES AND THAT ENABLE START-UP ENTREPRENEURS TO GO FROM "I HAVE GOT AN IDEA" TO "I RUN A BILLION-DOLLAR COMPANY" IN THE SPACE OF JUST A FEW YEARS."**

Bold is as much a book explaining world-changing trends as it is a manifesto for anyone who wants to become part of it all by becoming an entrepreneur. It's inspiring, informative, instructive. At times, however, it's also hard to absorb.

So enthusiastic is the author for his subject, that he throws a tremendous amount of dense information at his readers. I found myself re-reading some sections on the day after I first read the book in its entirety - both for sheer enjoyment and to look back at some specific points.

What makes the book so authentic is the fact that Diamandis is not writing from the proverbial ivory tower. He has done it himself, through founding more than 15 high tech companies and getting the support from companies like Google to set up the Singularity University, a combined think tank, education facility, and business incubator where smart minds come together to attack the world's toughest challenges. He has personally worked with every single one of the four billionaire entrepreneurs he interviews, and Fortune magazine once named him as one of the world's top 50 leaders.

Bold has already garnered its fair share of publicity, with former U.S. President Bill Clinton declaring it to be a "visionary roadmap for people who believe they can change the world" and the head of Deloitte Consulting recommending it





**"BOLD HAS ALREADY GARNERED ITS FAIR SHARE OF PUBLICITY, WITH FORMER U.S. PRESIDENT BILL CLINTON DECLARING IT TO BE A "VISIONARY ROADMAP FOR PEOPLE WHO BELIEVE THEY CAN CHANGE THE WORLD.""**

as "an essential navigation tool for any proactive CEO who wants to remain relevant."

For investors, too, the book is relevant. Understanding the mindset of entrepreneurs and their approach to creating exponential growth companies is vital for identifying companies that can turn into the aforementioned money fountains.

Being able to analyse a company's figures is only one aspect of successful investing. Spotting promising entrepreneurs early on is another vital skill and can lead to making a killing on the market. This book teaches you how to do that.

**Master Investor rating: Bold is a challenging read because of the density of facts and the authors being so ahead of the curve that it's not always easy to follow them. But the book is all the more recommended for that very reason. It does what it says on the label! I have just sent several copies to personal friends as it's been one of the most useful reads I have come across in months.**

# THE FINAL WORD

# HOW TO SOLVE THE LONDON HOUSING CRISIS

**BY ADRIAN KEMPTON-CUMBER**

*In a two-party political system, like the one we evidently still have in the UK, it could be argued that every policy, every speech, every bit of political posturing, is gerrymandering to some degree. Both of the main parties seek to take away from those that vote for the opposition party, and give to those that (might) vote for them. Since elections are decided by the undecided, they are the ones this behaviour is mostly aimed at.*

THE FINAL WORD

Democracy is not what we think it is. There's a perception that it represents fairness and equality. It doesn't. It's essentially mob rule. And for the last 45 years that's meant the Baby Boomers have, and still do, dominate the polls. It's no accident that the pensions time bomb wasn't defused until all the Baby Boomers had retired a few years back, allowing them to take their lovely final salary pensions, whereas those retiring today are facing down zero interest rates, and thus no chance of buying a decent annuity.

The original Homes for Votes gambit was of course by Moses, and still today homes are a very emotive thing, and no more so than in British society. A castle it may not be, but there is a broad perception that anyone in employment (even unemployed) has the right to get on the property ladder. A sense of entitlement is evidently common to not only the rich, but the poor too, just not the middle.

So I've come up with a solution to the main causes of the property bubble in London and the South East. And as you read, do bear in mind my maxim, borrowed from Einstein: "*If at first, the idea is not absurd, then there is no hope for it.*"

## 1) Raise Interest Rates

The main thing pushing up housing costs is artificially low interest rates. This is disenfranchising savers. It also means that we are subsidising those who bought houses with mortgages they couldn't really afford, and by keeping interest rates low we are basically handing them free money. It's also undermining those who have been saving for a deposit (saving is a very stabilising thing in a modern economy). Instead they're encouraged to borrow a higher percentage to valuation. So a tax on being responsible, you might say, redistributing wealth to the irresponsible.

Raising rates would cause those who wouldn't and shouldn't have been able to borrow, had interest rates been at sensible levels, to be repossessed. And so they should be. Why should we subsidise them? This would soon cause more stock to be available and thus reduce prices.


**"SPARE ROOM? HERE'S YOUR NEW HOUSE MATE. THAT'S HOW THAT WORKS. AT LEAST IT DOES FOR THE REST OF US."**

## 2) Relocate Those Who Don't Need to Be in London

For those of us in the private sector, we are always forced to make economic decisions we don't like. Decisions that never inconvenience those receiving government assistance at all. Many of us are now moving out of London, buying properties in the Home Counties because it's better value, and also a better quality of life. In the interests of fairness we need to apply the same logic to those in public housing. Particularly for those who don't work, and are unlikely to work, or who we are subsidising to a massive degree to live in postcodes most of us can only dream of, or who live in an over-crowded area: move them out of London.

According to a headline on the BBC News site the other day, "[a] third of Londoners cannot afford basic costs". Great. Move somewhere cheaper then. It's not rocket science. (Rocket science, if I'm not mistaken, is the art of creating green salads with lettuce hitherto unknown.)

## 3) Make Council Tenants Share

In the private sector there are hundreds of thousands of us having to share. We don't get the luxury of extra rooms when the other tenants move out, and get to stay on at no extra cost. That's just not how it works. There's a lot of capacity in public housing, it's just being ignored. The problem is the sense of entitlement I referred to earlier. You house someone and subsidise their rent, and they act like they own the place. They don't. Spare room? Here's your new house mate. That's how that works. At least it does for the rest of us. This would take the pressure off the shortage of council houses. Although in the longer term we need to consider whether council housing is meant to be a stop-gap or a permanent solution. Actually it is, practically speaking, a way to reduce crime, but that's another month's column inches to look forward to!

I came up with the sharing idea when having a conversation online with a real lefty. I say conversation but you can't really call it a conversation when he was just responding in a PC way to pre-programmed trigger words and phrases, like a typical social product of a child-minding service thinly disguised as an education system, mistakenly believing that it's more important to try than to succeed in life. And he so nearly does have his own mind. But not quite. Anyway, to wind him up, since he made me think of it, I emailed the Housing Minister with my idea. They don't seem to have done much with it so perhaps a reminder...

## 4) Modify Right to Buy to Include Responsibilities When Selling

Those of us who have not had the chance to capitalise on the free money bonanza that is the Right to Buy would surely not support the policy in any way. We all know since its inception in the Thatcher era, everyone who could 'helped' their dear old mum to buy her council place, and then sold it as soon as possible to reap the cash reward. That's the problem. It's a subsidised purchase. When selling, a pro-rata cut of the profit, at the very least, should be repayable to the council that sold the house.


The Help to Buy scheme is no better in terms of keeping a lid on prices. It too creates imbalance.

To contextualise all of the above, a good example is a bus and a taxi. If you can afford a private taxi then you can sit in it alone. If not then you may have to share. If you're on a bus you cannot expect to have any control over the other passengers. Still you might hear remarks of entitlement, like an indignant "do you mind not reading my Evening Standard over my shoulder?" Your response should be "mate, get a taxi if you want that kind of luxury. Want me to give you something towards the cost of your Evening Standard then, in case my eyes wear it out by looking at it" followed by the obligatory expletive, under your breath. Or imagine taxi passengers that had no money and refused to get out at the end of their journey.

**"THOSE OF US WHO HAVE NOT HAD THE CHANCE TO CAPITALISE ON THE FREE MONEY BONANZA THAT IS THE RIGHT TO BUY WOULD SURELY NOT SUPPORT THE POLICY IN ANY WAY."**

*Notes: for those who aren't Londoners, the Evening Standard is now a free newspaper.*

MARKETS IN FOCUS

# MARKETS IN FOCUS

# MAY 2015

## FOREX

| Forex | May % | YTD % |
|---|---|---|
| USD/JPY | 3.9 | 3.7 |
| USD/CAD | 3.1 | 7.2 |
| GBP/AUD | 2.9 | 4.9 |
| EUR/JPY | 1.9 | -5.8 |
| USD/CHF | 0.7 | -5.4 |
| GBP/USD | -0.4 | -1.8 |
| EUR/CHF | -1.2 | -14.0 |
| EUR/GBP | -1.6 | -7.5 |
| EUR/USD | -2.0 | -9.1 |
| AUD/USD | -3.3 | -6.4 |

## GLOBAL INDEXES

| Index | May % | YTD % |
|---|---|---|
| Nikkei 225 | 5.3 | 17.8 |
| NASDAQ 100 | 2.1 | 6.4 |
| FTSE MIB | 2.0 | 23.6 |
| Dow Jones | 1.0 | 1.1 |
| S&P 500 | 1.0 | 2.4 |
| FTSE 100 | 0.3 | 6.4 |
| Euronext 100 | 0.0 | 17.2 |
| S&P/ASX 200 | -0.2 | 6.8 |
| DAX (Xetra) | -0.4 | 16.4 |
| CAC 40 | -0.8 | 17.2 |
| IBEX 35 | -1.5 | 9.1 |
| Hang Seng | -2.5 | 16.2 |
| Russian Trading System | -4.3 | 25.6 |
| Bovespa | -6.2 | 5.5 |

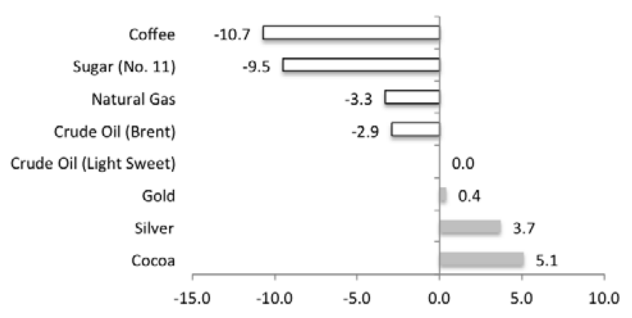
## INTEREST RATES

| Central Bank | Key Rate | Next Meeting |
|---|---|---|
| BOE | 0.50% | Jun 4 |
| ECB | 0.05% | Jun 3 |
| FED | 0.25% | Jun 17 |
| BOJ | 0.10% | Jun 19 |
| SNB | -0.75% | Jun 18 |
| BOC | 0.75% | Jul 15 |
| RBA | 2.00% | Jun 2 |
| RBNZ | 3.50% | Jun 10 |
| BOS | -0.25% | Jul 2 |
| BON | 1.25% | Jun 18 |

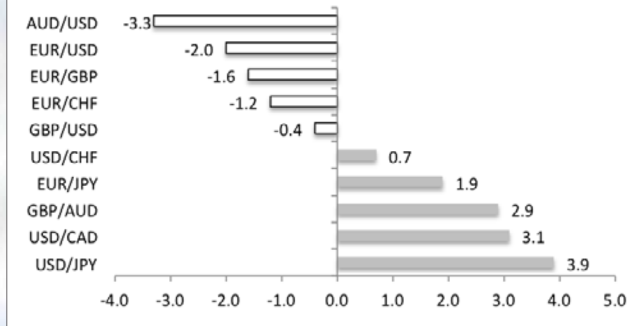
## COMMODITIES

| Commodity | May % | YTD % |
|---|---|---|
| Cocoa | 5.1 | 4.6 |
| Silver | 3.7 | 6.5 |
| Gold | 0.4 | 0.4 |
| Crude Oil (Light Sweet) | 0.0 | 10.9 |
| Crude Oil (Brent) | -2.9 | 12.6 |
| Natural Gas | -3.3 | -9.3 |
| Sugar (No. 11) | -9.5 | -17.9 |
| Coffee | -10.7 | -24.1 |

## COMMODITIES 1M%




## FOREX 1M%




## FTSE 350 BOTTOM

| Sector | May % | YTD % |
|---|---|---|
| Synergy Health PLC | -17.7 | -12.4 |
| BHP Billiton PLC | -11.6 | -0.6 |
| easyJet PLC | -11.3 | -3.7 |
| Evraz PLC | -11.1 | 9.1 |
| Morrison (Wm) Supermarkets PLC | -8.5 | -7.2 |

## FTSE 350 SECTORS BOTTOM

| Sector | May % | YTD % |
|---|---|---|
| Industrial Metals | -11.1 | 9.1 |
| Oil & Gas Producers | -4.9 | 0.4 |
| Mining | -3.9 | -2.0 |
| Food & Drug Retailers | -2.4 | 8.1 |
| Pharmaceuticals & Biotechnology | -1.5 | 5.4 |

## FTSE 350 TOP

| Sector | May % | YTD % |
|---|---|---|
| Bwin.Party Digital Ent. PLC | 26.1 | -10.4 |
| Zoopla Property Group PLC | 25.6 | 37.4 |
| DCC PLC | 25.0 | 46.4 |
| Berkeley Group Hold. (The) PLC | 22.8 | 24.8 |
| Booker Group PLC | 22.7 | 8.6 |

## FTSE 350 SECTORS TOP

| Sector | May % | YTD % |
|---|---|---|
| Software & Computer Services | 13.7 | 23.9 |
| Forestry & Paper | 11.6 | 40.6 |
| Mobile Telecommunications | 9.9 | 15.2 |
| Household Goods & Home Const. | 7.4 | 20.1 |
| Industrial Transportation | 7.0 | 10.0 |