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# Portfolios in Focus

selftrade  
research

SUMMER 2007

# Asset Allocator

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# Mark Hall

Lead Manager of the Rensburg UK Select Growth Trust from launch in September 2001 and Joint Manager for the Rensburg UK Managers' Focus Trust from launch in September 2006 talks to Selftrade's Stephen Barber about fund management and his outlook for the market.

### How would you describe your investment approach?

The investment process for the fund is very straight forward. In its purest form we simply focus on delivering absolute rather than relative returns by attempting to identify stocks trading at a significant discount to their intrinsic value. Little or no attention is paid to benchmark weightings and stocks are included in the fund on merit rather than because of the weighting in the index.

We are fundamental investors with a particular emphasis on free cashflow generation and the analysis of balance sheets. This recognises the fact that eliminating the real losers is just as important as getting the winners right. It is all really about the application of common sense, using the experience of the investment team and, equally importantly, that of our network of broking contacts in order to maintain a flow of investment ideas.

We will stand or fall by our ability to wait patiently for the right opportunities to come along and then we must back them with real conviction and have the discipline to sell when our price objectives have been met.

The following quantitative measures are considered relevant, though the list is not exhaustive:

- Price/Book;
- Price Earnings Ratio;
- Price Earnings to Growth Ratio;
- Market Cap/Sales;
- Market Cap/Potential Market Size
- Enterprise Value/ Operating Profit
- Free Cash Flow/ Enterprise Value (%)
- Return on Equity – Specifically for financials.
- Return on capital employed

### If waiting patiently is important, what is your sale discipline and how do you approach holding periods?

Our selling process is determined essentially by changing fundamentals (either stock or sector specific as well as in general economic conditions) or by the attainment of a price target.

### Do you use stop losses?

Within the fund we continue to use 10% relative underperformance as a trigger to review a position.

### What is your outlook for the coming year?

Looking forward, the real opportunity in H2 will be the turn in the financial stocks once the peak in the UK interest rate cycle has been reached. We would expect the rate rises seen thus far to begin to really bite over the next few months and believe that by the end of the summer the current consumer slowdown in big ticket items will have spread to the housing market.

### What would you say are your key concerns, where do you see threats and advise caution?

Current key concern is the oil price and the limitations this will place on the MPC in terms of reacting to a more broadly placed consumer slowdown.

### Where do you envisage investment opportunities in the short and longer-term?

Our ability to add value in small and mid cap emerging growth stocks will hopefully continue. In addition as already mentioned, we see a potential opportunity in financial stocks later this year.

### What themes are you examining for your fund?

The potential of asset backed and interest rate sensitive sectors to bounce back from oversold positions as interest rates peak. Otherwise we remain very stock specific.

### How is your fund positioned to cope with potential market volatility?

As a long only vehicle we are limited in terms of what we can do about market volatility. We do have the ability to go up to 25% in cash but in reality we are always looking to find stocks to buy and are not attempting to use cash as an asset allocation call.

### Mark Hall's CV

#### DEGREE:

BA (Hons) Geography  
with additional Economics (1986)

#### PROFESSIONAL QUALIFICATIONS:

IMC, FSI (Dip)



#### INVESTMENT EXPERIENCE:

Mark trained as an Accountant before joining Rensburg in 1988 as a Smaller Companies Investment Analyst. He subsequently managed private client discretionary portfolios for four years, before assuming control of BWD Equity Growth in 1997 (which has now been renamed as Rensburg Pan European Growth). In addition to the above two funds, Mark also manages two segregated mandates totalling £150m for Russell and Stanlib. Mark has now managed the Rensburg UK Select Growth Trust since launch which continues to enjoy first quartile performance and in June 2004 won an award for the top fund manager for UK larger company shares in the Citywire manager ratio league table over the last 3 years. Mark has also been awarded Top UK Fund Manager by Citywire and best UK All Companies fund manager in March 2005. He is also AAA rated by them. Mark has also been voted best fund manager by Investment Week and is AAA rated by Standard & Poor's.

# Asset Allocation for Fixed Income Investors

Mark Glowrey analyses the case for bonds in a balanced portfolio.

Over an investor's life cycle, savers in the UK have leant heavily towards equity investment, going all-out for capital growth and perhaps shifting the holdings of their portfolio into income producing assets only for the later draw-down year.

However, it is an old adage for savers and investors that the percentage of fixed income in one's portfolio should be proportional to one's age. Thus, even a forty year old man should be holding 40% of fixed income by this measure. Given the increase in life expectancy over the past few decades, this ready-reckoner may be a little too biased in favour of bonds, but the basic theory holds good. All investors should hold some bonds, and the percentage of this allocation should increase as the investor draws nearer to retirement, perhaps reaching up to 75% of the portfolio for older and more risk adverse investors.

## Planning the fixed income exposure of your portfolio.

First consider the overall size of your portfolio. A younger saver who is in the early stages of accumulating his savings might have a total size of £10,000 or less. At this stage of the investment cycle, his or her appetite for bonds will be limited and the focus of attention will be towards high growth equities such as small or mid caps stocks, or to actively managed funds. In such a scenario perhaps only £1,000 would be held in fixed income securities. Holdings in individual bonds would not be viable for this amount, and a fixed income fund would be the best option. Within the fund, the manager will ensure the correct distribution and diversification of holdings, a task that would be impossible to achieve on one's own with this sum of money.

As the total size of this investor's fund rises over the years, so do his options. Assuming our prudent saver has tucked away £50,000 by the early to middle stage of his career, he may wish to tuck up to £10,000 or so into bonds. Again, a well managed (and well priced\*) bond

ISSUE	NOMINAL	PRICE	YIELD	CREDIT RATING
Vodafone 6.25 % 10 July 2008	10,000	99.85	6.4 %	A-
Alliance & Leicester 4.25 % December 2008	10,000	97.15	6.3 %	A+
Experian (GUS) 6.375 % 16 July 2009	10,000	99.975	6.3 %	BBB+
Merrill Lynch 5.125 % 24 Sept 2010	10,000	96.575	6.3 %	AA-
UK Gilt 4.25 % 07 March 2011	10,000	95.4	5.7 %	AAA
EIB 4.75 % 06 June 2012	10,000	94.55	6.0 %	AAA
Kingfisher 5.625 % 15 Dec 2014	10,000	92.1	6.9 %	BBB-
Segro 5.5 % 20 June 2018	10,000	93.8	6.2 %	A-

Prices and yields are shown as of close 24th July 2007

fund may well hit the spot, providing a spread of holdings and automatic re-investment. More adventurous investors will chase the higher yield (and higher risk) offered by corporate bond funds whilst conservatives will prefer Gilt-based funds.

However, with £10,000 to play with, this investor could cut out the middle man and buy Gilts directly. Should this course of action be followed, the investor need not be concerned by diversifying against credit risk (Gilts can be considered free from risk of default). Nevertheless, a spread of maturities should be purchased. This is known as a "ladder" structure and ensures a steady flow of interest and capital repayment back into the portfolio, enabling the investors to buy new bonds as the shorter dated holdings mature and helping smooth the impact of rising and falling interest rates. A simplified Gilt portfolio might consist of the following:

- UK Treasury 4.75 % Jun 2010, priced at 97.6, yielding 5.56 %
- UK Treasury 5 % March 2012, priced at 97.875, yielding 5.53 %
- UK Treasury 4 % Sept 2016, priced at 90.6, yielding 5.31 %

(As at 24th July 2007)

This portfolio contains three bonds, with maturities between three and nine years. The yield on Gilts with maturities longer than ten years falls away, and we would avoid these more volatile instruments at

present. Note that the above bonds are all priced under par, allowing for a gentle capital appreciation and the selection offers a mix of the bi-annual coupons (June/Dec and March/Sept).

For investors in search of incremental yields, the next step is corporate and other non-governmental bonds. Here credit risk must be considered, and a healthy degree of diversification must be maintained. We would suggest ten holdings to be a reasonable portfolio, and these holding should be spread across different industry groups and types of issuer, again taking care to build up the "ladder" structure of short-to-long dated maturities.

The model portfolio constructed by [www.fixedincomeinvestor.co.uk](http://www.fixedincomeinvestor.co.uk) and available on the Selftrade website was started in the early part of this year and has yet to be fully invested. At present we have eight holdings and are looking to add two more before the end of the year.

**Mark Glowrey is a senior analyst for [www.investorsintelligence.com](http://www.investorsintelligence.com) a division of Stockcube Research, authorised and regulated by the Financial Services Authority. Additional analysis on the sterling fixed income markets can be found on the Selftrade website.**

\*A fund's overall charges are important, particularly when viewed against single-digit total returns. The yield on the average Gilt is around 5.4 % at the time of writing whilst investment grade (non-Gilt) Sterling bonds yield a tad more at 6.2 %.

# A Pension for Everyone

Pensions can offer an ideal vehicle for diversified portfolio management with the most flexible being a SIPP says Martin Tilley.

Despite what some journalists would have you believe, pension plans have been a pretty good place to be for the last four years. Rising stockmarkets in general have led to improved values for most. A criticism also levied is that pensions can be “too complicated” but with a little guidance, there are plans to suit all. And for some, a Self Invested Personal Pension (SIPP) is a perfect way of maintaining a diversified portfolio of equities, funds and bonds.

At the lower end, a stakeholder personal pension will provide an opportunity to invest in the pension funds of a single insurer. A stakeholder is a relatively simple pension contract with a simple annual management fee of between 1 – 1.5 %.

Moving up the scale, a platform based personal pension may offer access to several hundred funds from tens of the specialist investment management houses. The annual management charge of the portfolio of funds together with the “wrap” fee will typically fall in the 1.5-2% range per annum.

It is at the next level however that the opportunities to invest widen with the SIPP. To buck a trend, a SIPP can quite often offer a much lower annual fee than either stakeholder or platform pensions.

At its simplest level a SIPP is an approved “shell” within which a wider investment brief may be undertaken. Many of these vehicles can be operated online and can be established for a few

hundred pounds. And if dealing fees are fixed, an experienced investor can run a fair sized portfolio of individual stocks and funds for a fraction of the stakeholder or platform pension costs.

Moving up the SIPP ladder, all investments available through stakeholders, platforms and equity portfolios can be accessed along with futures and options, deposit accounts, second hand endowment policies, unquoted equities and funds and even commercial property. The open architecture of the vehicles really does allow you to build and manage a portfolio of varied assets that combined provide a tailored solution to your needs. Whilst the complexity of investment and administration will increase, it is common for additional structured or time costed fees to apply.

The key feature here is that SIPPs typically do not have a fee structure that is proportionate to the size of the fund. Thus the larger the fund the more economical the SIPP costs can become as a percentage of the overall fund size.

The selection of a SIPP trustee/administrator is a crucial decision, and one that should not be made on costs alone. Ensure that the service selected offers some or all of the features that may become important at a later date. As examples, multi phasing of retirement benefits, the ability to contribute or receive benefits “in specie” or even the ability to invest in some of the wider range of acceptable investments is sometimes prohibited.

Whilst the full features of the SIPP should be thoroughly investigated so too should the charging structure. Headline fees are easy to compare but be sure to delve deeper to see if additional transaction costs apply.

Finally the quality of administration should be considered. Whilst technology can help with the mass markets, the often bespoke nature of a SIPP lends itself to a more personal approach.

Fortunately help is at hand. The Treasury’s decision to place the regulation of SIPPs within the remit of the FSA has added the comfort of an Ombudsman and a compensation scheme to any aggrieved SIPP Member and the implementation of the requirement for SIPP providers to issue key features documents from November of this year should make direct comparison easier.

Irrespective of your investment knowledge, vehicles exist to allow a structured and manageable portfolio of investments to be created, matched specifically to your needs and attitude to risk.

***Martin Tilley is Pension Consultant & Business Development Manager for Dentons Pension Management Ltd.***



# Quick and Easy with ETFs

Asset allocation is an important driver of returns. In the correct hands, portfolio building blocks can be allocated to maximise return for a given level of risk says Adam Gebler.

Anyone who has had consistent exposure to the commodities market over the past few years will vouch for the importance of non core asset class exposure. But the more esoteric end of the investment market – for example, commodities or property – can be difficult and expensive to access. Exchange traded funds (ETFs) can be a cost-effective and liquid way to tap into those markets.

Academic reports have suggested that asset allocation can dictate a significant proportion of investment returns. Specifically, a widely cited article in the Financial Analysts Journal by Gary Brinson in 1986, stated: “Data from 91 large US pension plans over the 1974-83 period indicates that investment policy dominates investment strategy (market timing and security selection), explaining on average 93.6 % of the variation in total return.”

If anything, this has become even more widely recognised over the past few decades. With this in mind, how do investors go about handling asset allocation? They could try standard pooled investments like unit trusts or investment trusts, but this can be relatively expensive.

There has also been much controversy about larger investors trading in and out of funds for asset allocation purposes. For smaller, specialist funds, the addition and removal of large amounts of money can create a real headache for fund managers. Managers are often forced to sell their most liquid holdings. This can have an impact on performance and penalise other unit holders. Fund management groups are getting wise to this and many are threatening to start imposing dilution levies on investors who are not long-term holders.

So how do investors make quick and easy asset allocation decisions? Many are starting to realise that ETFs offer an attractive solution. Investors can take quick exposure to an asset class without worrying about cost or liquidity issues.

ETFs are also commonly used for short-term positions and tactical views. ‘Cash equitisation’ by institutional investors remains the biggest use for ETFs. If a fund has a big cash inflow, it takes time to decide how to invest that money. A manager will want to be in line with his benchmark in the meantime and this is driving demand for ETFs as a means of gaining market exposure rapidly.

ETFs can also be used where investors and fund managers do not have specific competence or expertise. Traditional large investment managers will have capabilities in both equities and bonds. But for smaller, equity-focused groups and many private investors, when equities don’t look good, they may not have the expertise to move into the fixed income Equity hedge funds are some of the largest users of fixed income ETFs for that reason. They are outsourcing a potential problem to ETFs and this is also true for the more esoteric asset classes, like infrastructure and private equity.

The outsourcing argument also holds for smaller allocations within many portfolios. Property and commodities are typical examples, as both tend to have a low correlation to some traditional asset classes and can improve an investor’s returns and lower the risk in a portfolio.

ETFs are also likely to be used when exposure to a region or sector is needed where an active investor finds it hard to outperform the market. One notable example of this is in the US large cap arena, which is very efficient and most investors find it far more rewarding to seek opportunities to outperform elsewhere.

This is also often true for investors operating away from their home market. Institutional and retail investors in

Europe may find it harder to outperform when investing in US stocks and vice versa. Both groups tend to naturally have more local expertise. This may be particularly important when investing in more obscure areas such as emerging markets.

In addition, ETFs are finding a natural home in investors’ portfolios when exposure to specific theme is desired. A highly topical example, which looks set to endure, is the growing demand for products that deliver exposure to the environmentally-related businesses. This demonstrates the increasing awareness of all things environmental, as well as recognition of the strong growth potential that this sector appears to offer. The drivers behind the growth opportunities in this space include increasing governmental backing in the form of rising official targets for renewable energies and subsidies into the sector. Indeed, the Financial Times reported in January this year that \$70 billion of new money was invested globally into clean energy in 2006, up 43 % from 2005. ETFs providing exposure to this global sector, represented by the S&P Global Clean Index comprises 30 of the largest publicly traded stocks in the global clean energy industry, provide an effective route to gaining exposure to this theme.

But ETFs don’t need to be just a ‘filler’ in a portfolio. They can also be used as the entire basis of a fund, if an investor believes that asset allocation is the most significant generator of return.

**Adam Gebler is iShares Strategist, Barclays Global Investors**

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# Regular Investments

Stephen Barber discusses Selftrade’s new Fund Packages Regular Investment Service.

Successful longer-term investing should involve diversification and asset allocation; achieving good investment returns while managing risk. A diversified portfolio should be structured so as to achieve exposure to a range of asset classes, proportioned to meet broad investment objectives. Funds can be useful tools to achieve this both in themselves and in combination. After all, they benefit from being inherently diversified products and having a professional fund manager at the helm. And when funds with different goals are combined, they can create portfolios achieving clear investment objectives.

It is for this reason that Selftrade Research has created a range of asset allocated fund packages to meet a series of lifestyle investment scenarios. Our models select leading funds to match the asset content of each package and allocate these accordingly. Our methodology for selection involves analysing and comparing the individual objectives, performance, fund manager, contents, size, risk profile, annual management charge, rating and other factors of potential funds. These funds are then combined to create the Fund Packages, asset allocated in each case suitable to the lifestyle scenario and guided, where appropriate, by the Association of Private Client Investment Managers and Stockbrokers (APCIMS) and the MSCI.

The service, available in ISAs and SIPP Dealing accounts, invests each month (with no purchase commission until further notice) allowing you to drip feed funds into the market, benefiting from pound/cost averaging. That is, you will buy disproportionately more stock when the market is weak and spreading overall investment risk.

**Stephen Barber is Head of Research for Selftrade.**

The service is available in ISAs and SIPP Dealing accounts. Selftrade offers an execution only service and you should remain actively involved in managing, monitoring and reviewing your investments. You can also invest in any of the constituent funds directly as part of the Regular Investment service. Minimum investment is £50; sales at £12.50.

## Global Growth

The Global Growth fund package is designed to achieve growth over the long-term by investing in a selection of funds across the globe.



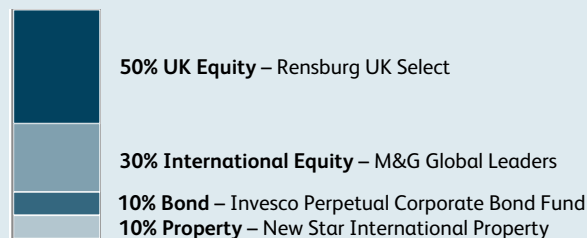
\* BRIC - Brazil, Russia, India, China

## How to invest in the Fund Packages

Full details of the fund packages and an application form are available from the website [www.selftrade.co.uk/fundpackages](http://www.selftrade.co.uk/fundpackages) or by calling customer services on 0845 0700 720.

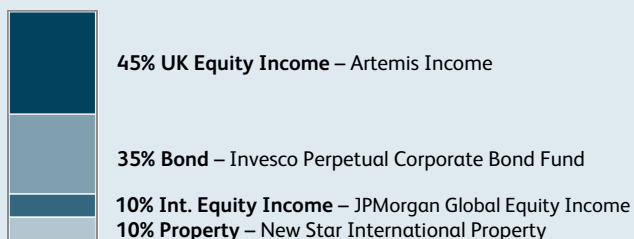
### Balanced Growth

The Balanced Growth fund package is designed to achieve diversified growth over the long-term with some income by investing in a selection of funds which focus on UK equities, international equities, bonds and property respectively.



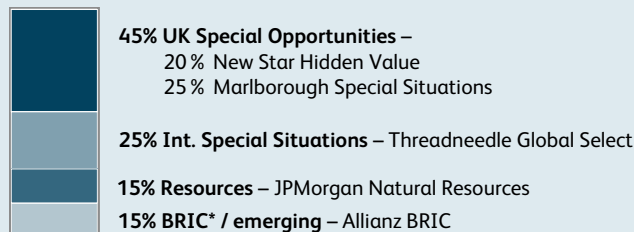
### Income

The Income fund package is designed to achieve diversified income together with some capital growth by investing in a selection of funds which focus on UK equity income, bonds, international equity income and property respectively.



### Opportunities

The Opportunities fund package is designed to achieve higher growth by investing in a selection of funds which seek value and growth opportunities in an international setting.



# Global asset views

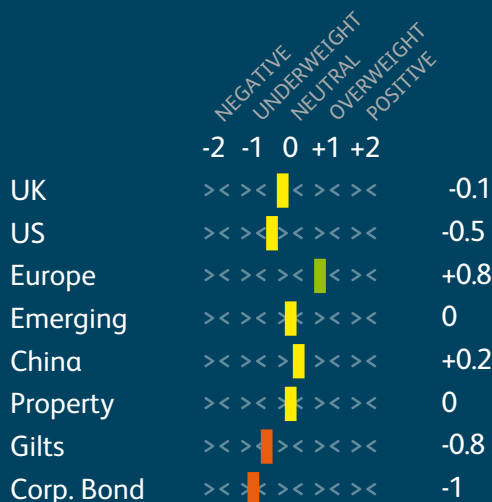
Consensus views on world markets and sectors drawing expertise from fund management groups.

	UK	US	Europe	Emerging	China	Property	Gilts	Corp. Bond
Aberdeen	-1	-2	+1	+1	+1	+1	0	-1
BlackRock Merrill Lynch	0	-2	+2	+2	+2	0	-2	-2
Gartmore	0	-2	+2	0	0	0	-2	-2
JP Morgan Asset Management	0	+1	+1	-1	-1	+1	0	-1
M&G	0	+1	+1	-2	-2	0	-2	-2
Selftrade Research	0	0	+1	+1	+1	0	0	-1
Schroders	-1	+1	+1	0	-	0	0	-1
Société Générale Asset Management	0	+2	-2	0	0	0	-2	+2
Scottish Widows Investment Partnership	0	0	0	0	0	-1	+1	0
Threadneedle	+1	-1	+1	0	+1	-1	-1	-1

KEY:  
 -2 Negative  
 -1 Underweight  
 0 Neutral  
 +1 Overweight  
 +2 Positive

## Consensus

This snapshot view of world market sentiment from some leading fund management groups shows a degree of consensus in continued concern for UK core inflation despite relatively low historic ratings amongst many of the mega caps. Pessimism over gilts and corporate bonds perhaps reflects the corresponding economic environment of rising interest rates. For similar reasons the outlook for property suggests a degree of caution from those surveyed. Elsewhere, there is general positivity towards Europe whose principal markets have enjoyed steady growth over the year combined with healthy economic indicators including falling unemployment. A far more mixed view can be found not only of the more volatile emerging markets and China but also of the United States where a weaker economy contrasts with continued bid activity and strong company earnings.



# Cash in

## No dealing fee on fund purchases Plus discounts on initial charges

Make significant savings when you buy unit trusts and OEICs through Selftrade. Choose from over 1000 funds and pay no dealing fee on purchases in all account types until 28 September 2007. More than 800 funds have an initial charge of 0.50% or less. The table gives examples of how much you could save on the standard initial charge when you buy through Selftrade.

Fund name	Fund Provider's initial charge	Initial charge through Selftrade	Selftrade dealing fee	Selftrade saving on a £5,000 investment
Gartmore China Opportunities	5%	0.25%	Nil	£237
Invesco Perpetual High Income	5%	0%	Nil	£250
JPMorgan Emerging Markets	5.5%	0.50%	Nil	£250
Merrill Lynch UK Smaller Companies	5%	0.25%	Nil	£237
New Star Global Financials	5.25%	0.50%	Nil	£237

Before buying a fund you should read the Simplified Prospectus and familiarise yourself with the fund's charges. A fund's past performance is no guarantee of future performance. Investments can fall in value as well as rise. Fund sales are subject to our standard flat £12.50 dealing fee. We do not provide investment advice.

**Make your money work harder, choose Selftrade.**

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Visit [www.selftrade.co.uk/fundoffer](http://www.selftrade.co.uk/fundoffer) or call 0845 0700 720

Lines are open Monday to Friday 7.45am – 7pm and Sunday 2pm – 6pm. Calls may be recorded.

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