

Client: Chi Med
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Q&A



ANSWERS

RICHARD PENNY

Fund manager, L&G UK Alpha Trust

JAMES CALDER, HEAD OF RESEARCH, CITY ASSET

MANAGEMENT: What is your view on the UK economy and how is this reflected within your fund?

The UK domestic economy is facing challenges. The consumer sector is weak because of rising taxes and public sector employment threats and the government sector is also suffering significant cutbacks. As a result, the fund is positioned towards companies with overseas assets and earnings. Stock selection is fundamentally bottom-up but the macro picture is considered in terms of current challenges and opportunities.

The fund uses two complementary styles, investing in companies with strong growth potential and those we feel are available at a deep discount to their true value, providing the ability to perform successfully throughout the market cycle.

Growth companies are those able to grow sales aggressively at an organic level by exploiting, for example, unique products or services or barriers to entry. Our value holdings, companies suffering subdued valuations and low investor sentiment, are those we believe are fundamentally solid and where we can identify potential catalysts for a re-rating.

The portfolio's tilt between growth and value strategies varies according to the economic environment but is typically 60 to 40, managed to deliver performance through all stages of the cycle.

At present, a greater number of opportunities exist within the value theme, particularly in those asset-backed companies we view as fundamentally undervalued by the market.

WILLIAM BUCKHURST, PARTNER, CHEVIOT ASSET

MANAGEMENT: What was your portfolio turnover rate last year? Why was this higher or lower than average in previous years?

Turnover is such that we will hold stocks for about two to three years. That's been the case for most of the fund's six-year history. We buy shares where illiquidity often creates severe undervaluation but recognise we need to be more patient to follow this strategy. We run the fund as a concentrated portfolio of typically 30-40 stocks, with few constraints on sector weighting or size.

JAMES HUTSON, CHIEF INVESTMENT OFFICER, ARJENT: At stock level, what was your best-performing call of the past 12 months?

The best performer has been Endace, a telecom network monitoring company that is benefiting from the deployment of faster technologies. The company's technology looks to be driving a shift change within the industry. Many of its competitors cannot address the faster speeds that are starting to appear in telecom networks due to the increase in video data. The shares rose 151%

in the year to 31 May 2011. The intention with all our holdings is that they have the potential to double in value over two to three years.

Our idea generation is derived from a number of qualitative sources, including Legal & General and third-party research, directors' dealings and rights issues. We then meet the management of all potential holdings face to face. Ideas are then screened on key financial measures (return on capital, free cash flow, balance sheet strength) and value (price to earnings, enterprise value, price to book). We believe this process identifies competitive companies that are sensibly managed, financially stable, cash generative, and can achieve the aggressive targets we set for all our investments.

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**TOM BECKET, CHIEF INVESTMENT OFFICER, PSIGMA
INVESTMENT MANAGEMENT: How does your risk exposure
compare with the past few years?**

In the 12 months to the end of March 2011, the fund took particular advantage of the deep value and growth styles. This contrasts with 2009 and 2010, where performance was driven from one particular side of the strategy.

In the economic meltdown of 2008/09 there were many value investments available, due to collapsing profits and reduced bank debt availability. The continuing economic recovery helped value stocks, such as 3i and Mecom, to deliver strong performance while investments such as SuperGroup and Hutchison China Mediatech delivered for the growth strategy. Having the value and the growth sides to our investment process has certainly helped over the past few years.

We pick investments from a range of sectors: we have a lot of companies in the mining sector and the technology sector but not too much in any single area, so we have a healthy variety and selection of investments. The fund is now underweight in the oil and gas sector and the domestic retail sector, due to pressures on consumer spending.

**JONATHAN GODFREY, HEAD OF BARCLAYS WEALTH IN
EDINBURGH: : Why should I be investing in the UK now when there
are so many opportunities in better placed regions elsewhere?**

Even if the UK domestic economy is challenging, the FTSE All-Share includes many international companies and UK stocks with significant exports to overseas markets. So an investment into a UK All Companies fund need not be an investment confined to the UK domestic economy. For managers with the freedom to build a high conviction portfolio free from the constraints of the index, we still see attractive opportunities in UK equities.