FOR PROFESSIONAL ADVISERS ONLY

R.C. BROWN
INVESTMENT MANAGEMENT PLC

MARKET COMMENTARY - DECEMBER 2011

Bob Brown
Chairman

Welcome to the latest edition of our quarterly 'market update' newsletters, where we share our thoughts on what has been happening recently, and more importantly, what we believe will be the key influences in the near future.

As this is our last newsletter of 2011, may I take the opportunity to wish you all a good Christmas and prosperous New Year.

"The consequences of the credit crunch and the near collapse of the banking system in 2008, and the concomitant sharp setback in economic activity, continue to reverberate around the world. The resulting excessive debt has finished up in government hands.

The standoff between the Democratic administration and the Republicans to raise the debt ceiling was always bound to be resolved at the last minute. The vacillation and squabbling, however, caused Standard & Poor's to downgrade the rating on US debt. This in itself is probably unimportant, and US Treasury yields fell not rose on the news, further reducing borrowing costs for the US Government.

The European situation is more problematic. Over the past eighteen months European leaders have failed to grasp the scale of the necessary action. For example, the bailout packages for Greece, the size and structure of the European Facility Stability Fund and the bank stress tests all proved inadequate. Politicians at least appear to be taking the crisis seriously. After a gargantuan effort by seventeen governments a package to bolster the EFSF, to recapitalise European banks, and the write off of 50% of Greek debt was agreed. Initial market euphoria was quickly tempered by the Greek Prime Minister's decision to seek a vote of confidence and then a referendum. The yield on ten year Italian bonds has risen to an unsustainable 7%. Any resolution will be a slow and painful process against the backdrop of a deteriorating world economy.

While US and European governments exhibited a lack of leadership and ability to control difficult situations the world economy appears to have slowed sharply. There is a real danger of a double dip so soon after the last recession.

In stark contrast the corporate sector worldwide is mostly in rude health. The negligible yield on cash will last a long time. Ten year gilt-edged yield a miserly 2.2% – well below the rate of inflation. The yield on the UK equity market is 3.5% with dividend growth forecasts of 12% both this year and next. As many as 70 of the FTSE 100 constituents yield more than gilts. Although we are exceedingly nervous of short term movements, the market offers a range of diverse opportunities and good value."

OUR INVESTMENT SERVICES

Managed Fund Portfolios (min £25,000)	Direct Portfolios (min £250,000)	Ethical Portfolios (min £250,000)

We have a clear & transparent charging structure:

a. Our fees already include transaction and custody charges
b. We purchase 'institutional' units (where available), and pass on 100% of any rebates we receive
c. Tiered fee structure dependent on the value of the portfolio
d. IFA remuneration is disclosed and levied separately to our own charges

We have our own ISA (at no additional cost), and our portfolio services can also be used through a range of Bond and SIPP wrappers

PRIVATE CLIENT PORTFOLIOS

Glenn Meyer
Head of Managed Funds

Well, hasn't 2011 been eventful. With many Investment Managers facing difficult choices over when and what to buy & sell, we thought you may be interested in what changes we made to our asset allocation and fund selection during the year.

For the most part we have been happy with our fund selection and made only one complete disposal, the Legg Mason US Equity fund. This fund was long run by Bill Miller, who is the only fund manager to outperform the S&P 500 index for 15 consecutive years. However, he went through a period when his value style didn't work around the time of the financial crisis, but when US large cap stocks fell to very low valuations it appeared an ideal opportunity to buy into his fund for a long term increase in value. What I got wrong was the unwillingness of investors to buy US equities with a value bias. Having interviewed Bill and his associate, Mary-Chris Gay and discussed Bill's planned handover of the fund to Sam Peters I could not see that in current market conditions that the fund would outperform and sold it. In recognition that the US equity market is very efficient and therefore difficult to outperform, the fund was replaced by the Schroder QEP US Core fund. This is an institutional only product with a much more broadly based portfolio which uses a quantitative process to identify multiple sources of alpha and is run by a team I have known and respected for some years. So far we are pleased with this fund's performance and believe we made the right decision to change.

Other changes are more incremental in nature. Soon after the Japan earthquake we increased our exposure to Japanese equities by adding an additional fund with a complementary style to the fund we already had. This additional fund, JOHCM Japan, has a hedged institutional share class which gives us the opportunity to benefit from the fund manager's stock selection but without losing value if the Bank of Japan is successful in its plan to bring down the value of the Yen. Before buying the fund I interviewed Ruth Nash (the co-manager) and was able to place a number of questions for her to ask government officials and company management on her forthcoming trip to the area impacted by the earthquake. On her return Ruth reported to me on the low price to book valuation of many Japan stocks and the incremental demand in the region that would come from the reconstruction. I then changed our asset allocation and gradually introduced the fund to our client portfolios and to reflect this.

To fund an increased allocation to selected equity markets after markets fell, we reduced our property exposure, but retained our two preferred property funds.

Our bond exposure was also reduced slightly as conventional gilts became very expensive. We believed the short end of the gilt market to be at great risk of a rapid sell off as a result of political change. Because of the very low yields on offer at the short end we had for some time preferred to increase the duration of our bond portfolio by holding Treasury 4.25% 2027. But this fell to a yield which we felt was unsustainably low and we sold our last conventional bond in late summer. We replaced this by adding to our index linked gilt exposure (I-shares Index Linked Gilt ETF) and an international bond fund, the Templeton Global Total Return Bond fund. This has some exposure to non-eurozone European bonds as well as emerging market bonds in governments with low debt to GDP ratios and the potential for currency appreciation. The fund is run from California by Michael Hassenstab, someone I have known for some years and for whom I have a very high regard.

In the corporate bond area we reduced exposure to the financials sector and bought into I-shares Corporate Bond (ex financials) ETF.