PERSONAL ASSETS TRUST PLC

DECEMBER 2010 QUARTERLY REPORT No. 59

PAT'S LONDON MEETING

Demand for places at our London Shareholders Meeting has proved so overwhelming (over 350 so far) that we have had to change the time and venue. The meeting will now take place at 10.30 am for 11 am on Tuesday 18 January 2011 at the Institution of Engineering and Technology, 2 Savoy Place, London WC2R 0BL (nearest tube stations Charing Cross, Embankment and Temple). It will take the form of a presentation by Sebastian Lyon, our Investment Adviser, followed by Questions & Answers and light refreshments. The Chairman (Hamish Buchan) and several other directors *(not me, alas!)* will also be present. We have written to all those who indicated an interest in coming to the presentation, to keep them informed about the change of timing and venue. If you have any questions, please call Steven Budge on 0131 538 6602 or e-mail him at the address below.

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GROWTH AND EXPANSION

In September 2010, for the first time ever, Personal Assets' share price topped £300 and its stock market capitalisation rose above £250 million. Only 20 years ago, on 31 October 1990, the date from which the Board started measuring performance after assuming direct responsibility for the management of the trust and appointing Ian Rushbrook as the Investment Director, Personal Assets' net asset value per share ("NAV") after adjusting for the 1 for 100 share consolidation in January 1993 was £46.40, our shareholders' funds amounted to £6.9 million, our share price was £35½ (we sold at a sizeable discount to net assets in those days) and our market capitalisation was a mere £5.3 million. It took us until 1998 (the discount having been eliminated from April 1995 onwards) for our market capitalisation to reach £50 million, until 2003 for it to reach £100 million and then until 2009 for it to reach £200 million. As I write (13 December), our share price stands at £311¼ and our market capitalisation is £279 million.

This increase in Personal Assets' size comes from two sources: ***growth*** in NAV; and ***expansion*** in the number of shares in issue. Growth in NAV over two decades has been over six and a half times. Had we issued no new shares since October 1990 our shareholders' funds would today total £46 million. There has also, however, been a six-fold increase in shares outstanding, from 149,313 to today's 897,741. Such expansion, of course, has other implications, notably for our Total Expense Ratio ("TER") and our revenue reserves, and I shall return to these subjects later in the Quarterly.

A PREDICTABLE QUESTION

You may have noticed that the Interim Management Report in our Interim Report to 31 October 2010 opens with these words:

'We are frequently asked what we expect from markets over the next six months. Our response is always the same: look at our portfolio.'

Sebastian Lyon and I phrased it in that way as a deliberately wry response to the exasperating question we are invariably asked:

'What do you think the market will do in the next six months (or the next year)?'

Or, even worse than that:

'Where do you think the market will be in the next six months (or the next year)? Give me a figure!'

I suppose that to ask such questions is just human nature, but I can't help wondering why people do it. Nostradamus is a figure of the distant past, Paul the Octopus has gone to the great aquarium in the sky and even Pope Benedict XVI would claim to be infallible only when speaking *ex cathedra* on matters of faith and morals, rather than about the oil price or the gold price. Let me therefore say with sorrow that nobody, not even Sebastian — and, least of all, I — has foreknowledge of what the level of the FTSE 100 Index, or any other index, or any commodity price such as oil or gold, will be on Christmas Eve 2011.

Every year I attend a reunion Christmas Lunch with some of my old friends and colleagues from Wood Mackenzie (later, NatWest Securities). On each occasion, all 20 or so of us submit our predictions of the level of the FTSE 100 in 12 months' time. All of us are seasoned market observers and practitioners and we each have at least 30 years' investing experience. Every year, our forecasts show a range of several thousand points, the highest sometimes being twice the lowest, and there is virtually never any discernible pattern to them. Heaven help anyone who invested on the basis of such ill-founded predictions; and yet, as New Year approaches, the City and Personal Finance pages will overflow with them. You will find no such contribution from us.

However, avoiding all requests to *'give me a figure'* is not being secretive or obstructive for the sake of it, or trying to keep people in the dark about what we are doing. Our view of the future is always an open book, and the book is our portfolio at any given time.

LOOK AT THE PORTFOLIO!

If you know I have only £1,000 in the world and you see me at a racecourse putting it all on one horse to win, surely the question '*Which horse do you think will win the race?*' will be superfluous? I'm scarcely likely to be betting all my worldly goods on a horse I think will lose. Similarly, it would be strange for Personal Assets to hold the portfolio it does if, on questioning, we admitted to holding views contrary to those implied by our published holdings — say, if we were to 'out' ourselves as covert bears of gold and bulls of conventional gilts. Yet interviewers always seem to be trying to elicit from us such contradictory secret opinions — why, I have no idea. Like most sensible people, we put our money where our mouth is and, in Warren Buffett's phrase, eat our own cooking.

So, just to reiterate, we are still faced (as we noted in the Interim Report) with choosing from within a universe of relatively unattractive asset classes; and our portfolio has changed very little since 31 October. We have (13 December) 13.0% of shareholders' funds in directly-held gold bullion *(12.2% at 31 October)* and 4.4% *(4.1%)* in gold mining shares, 26.1% in US Treasury Inflation Protected Securities (''TIPS'') *(27.7%)*, 51.5% in mainly blue chip defensive equities *(52.9%)* and 5.0% *(3.1%)* in net current assets. The only changes to the portfolio since 31 October are that we have sold out of all our shares in Royal Dutch Shell, added to our holdings of Tesco, Centrica, Greggs and Colgate, and topped up slightly in gold and in Newmont Mining.

THE NATURE OF BOLDNESS

There are two further aspects of being prepared to face the future that I want to mention. The first concerns the nature of boldness. When I was an investment trust analyst in the early 1980s — I was Hamish Buchan's bag-carrier then, so nothing has changed over the last quarter of a century — I interviewed a trust manager who had made something of a name for himself by successful currency hedging. When I asked him how he set about it, his response was:

'It's like driving a car in thick fog.'

What a cop-out, was my youthful thought. How dull and unambitious! Where is the bold stroke, the daring *coup*? In other words, what will the £/$ rate be in a year's time? But today I see what he meant, and I sympathise with it. To quote Cardinal Newman:

'I do not ask to see
The distant scene;
One step enough for me.'

My definition of boldness has also broadened over the years. Boldness, it seems to me, is not only about *making* money through daring *coups* but also about taking determined action with a view to preventing a loss. Our use of liquidity is an illustration of this. We are well known for it — perhaps too well known, because whatever else we may be we are not the perma-bears we are sometimes thought to be, and one day we hope to gear. Managing our liquidity has done well for us over the years. It has been a very significant contributor indeed to our long-term outperformance.[1]

For example, liquidity management was of crucial importance when Ian Rushbrook's death coincided with the market turmoil of 2008. When Ian became fatally ill at the beginning of October and the Board had to run the portfolio directly, we were 40% liquid, having been as much as 100% liquid in June. On 6 October we reduced our liquidity once more to 25% and further reduced it to 15% on 24 October. But then, as we grew more concerned about the short term outlook for markets, we increased our liquidity, in stages, to 45% by 26 February. When the Board took charge of the portfolio, our share price was £245½ and the level of the FTSE All-Share Index was 2,522.12. Over the period during which the Board ran Personal Assets directly, our share price fell 12.0% while our benchmark fell by no less than 27.3%. So, yes, we did lose money during that time — but not nearly as much as the average investor did.

Such absolute losses will happen again. They are the inevitable risk of investing at all, and our aim at such times is to lose as little as possible *and* to lose less than others. There will also be spells of underperformance. Personal Assets will always tend to underperform when the market is rising and outperform when the market is falling. This may seem dull at times, but it is a way of preserving our *'grubstake'* so that we have more funds available to benefit from when markets rise again.

THE LIMITS OF CLAIRVOYANCE

Of course, even if we were clairvoyant there would still be problems. In John Buchan's novel *The Gap in the Curtain*, five guests at a country house take part in an experiment in which each of them is able to glimpse for a moment the newspaper headlines for the day exactly one year later. In each case the information gained, although accurate, proves useless or misleading. Of particular interest in our case is the experience of the financier, Arnold Tavanger, who spots a headline to the effect that there is to be a world merger of all the producers of a rare mineral and tries to capitalise on this cleverly. At the end of Buchan's account, Tavanger is made to say:

'"I saw the announcement of the world merger... I knew with perfect certainty that one thing was going to happen. If I hadn't known it... I would have been content to take my profit... As it is, that infernal atom of accurate knowledge has cost me twenty thousand. But it was worth it... for I have learned one thing which I shall never forget, and which I commend to your notice. Our ignorance of the future has been wisely ordained of Heaven. For unless man were to be like God and know everything, it is better that he should know nothing. If he knows one fact only, instead of profiting by it he will assuredly land in the soup."'

He was right. Had you taken part in such an experiment and spotted in the newspaper for 13 December 2011 that our share price was not £311¼ but £40, you might assume things had gone horribly wrong and rush to sell your shares. But suppose that the price had actually risen — that the equivalent share price to today's £311¼ was £400, but in the meantime there had

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[1] One way of looking at this is that the FTSE All-Share, our comparator, reached its all-time high of 3,478.99 on 15 June 2007, when our share price was £266¾. Had we exactly tracked the FTSE All-Share from that date, our share price today would be £230¾. Similarly, the FTSE 100 reached its all time high of 6,930.2 on 30 December 1999, when Personal Assets' share price was £212½. Had we exactly tracked the FTSE 100 from that date, our share price today would be £178, rather than its current £311¼.

been a share split, giving you nine new shares for every one you already held? You would know the 13 December 2011 price of £40; but, without knowing of the intervening share split, the knowledge would be worse than useless,

EXPANSION OF SHARE CAPITAL

Over the last 20 years our number of shares in issue has risen from 149,313 to 897,741. By the time you get this Quarterly the Board will have taken powers, at the EGM held on 13 December 2010, to issue a further 300,000 shares.

Why have we done this? We have no desire to increase the size of Personal Assets merely for the sake of so doing. Creating new shares, or buying in existing ones, is done as a service to shareholders. It would be a compliment if we were to become a £500 million trust, but if we shrank to £100 million we would manage Personal Assets in the same way, with the same aims and time horizon and for the same sort of investor.

The larger the trust, of course, the lower the Total Expense Ratio ("TER"). I am wary of putting too much stress on the TER. It can be misleading. By definition, it falls if the trust grows, and rises if the trust gets smaller; so the TER can simply be a function of market movements or the issue or cancellation of shares. Some years ago, however, a shareholder did write to me expressing the hope that in the foreseeable future our TER would fall below 1% and I am pleased to record that, for what it is worth, it has now done so!

REVENUE AND DIVIDENDS

After receiving the Interim Report a shareholder wrote to us with a question of general interest which is worth answering publicly here.

'I note that, since May, you have reverted to your former policy of charging expenses to both revenue and capital (in common with many other investment trusts) and also that the demand for PAT shares continues to increase. My concern and question relates to the dividend policy going forward. I wondered whether going forward, you consider there are any circumstances where the stated dividend policy might prove unsustainable or difficult to achieve and if so how you had planned to respond. I feel I should apologise for asking this question as I know that you wouldn't make such a promise without being sure it could be kept, nevertheless I would, if possible, appreciate a better understanding of your thoughts on this matter.'

Our change of accounting policy on expenses, apportioning them 65% to capital and 35% to revenue rather than 100% to revenue, is a return to our practice between 1996 and 2006, when, following the publication of a Statement of Recommended Practice ("SORP") by the Association of Investment Trust Companies, we decided to apportion expenses in line with our expectations of future returns.[2] Over the decade 2000-2010 each Personal Assets share increased in NAV by £86.95 and paid £37.50 in dividends — 70% and 30% respectively of the return received by shareholders who chose to draw their dividends rather than reinvesting them. So the apportionment does seem to be broadly along the right lines, although of course this is not how a statistician would calculate total return.

The issue of new shares inevitably tends to reduce revenue reserves on a per share basis. We are conscious of this, as we are of the strains on the revenue account of paying a growing dividend at a time when cash yields nothing and we have 13% of our net assets in gold. For the time being we believe that, with care, we can continue to increase the dividend in real terms over the longer term, although (as explained in the 2010 Annual Report) not necessarily in each individual year. Accordingly, while it would be a rash Board that said any policy could be set in stone for ever, our revenue objective remains unchanged and no alteration would be made to it without considerable advance warning.

Creating new shares close to an ex dividend date does, however, have an adverse effect on revenue, because such shares are entitled to a full six months' dividend. We are therefore having another look at the possibility of paying dividends quarterly and I shall report back to you on this in the New Year.

[2] *We changed our basis of apportionment in 2006 mainly because we had a short-term surplus of income at the time.*

SPLITTING THE SHARES?

When discussing the inadequacy of foreknowledge, I mentioned the possibility of a share split. This is indeed something that has been suggested to us, and I thought I would mention it here to see how shareholders might react.

In favour of *not* splitting the shares is that our share price is distinctive. It sends out a message as to the kind of trust we are and the kind of people on whose behalf we manage money; and, for myself, I am also fond of recalling Lord Falkland's old dictum that when it is not necessary to change, it is necessary not to change. A share split would not make the market in Personal Assets more liquid. Because of our premium and discount control mechanisms we are already as liquid as a trust can be. It could be argued that a nine for one (giving 10 shares in place of every one currently held) would take us back to the price level at which we started (our share price in 1990 was £39½), although I do remember Ian, at an early AGM, replying to someone who asked about a price target that £1,000 per share would be nice!

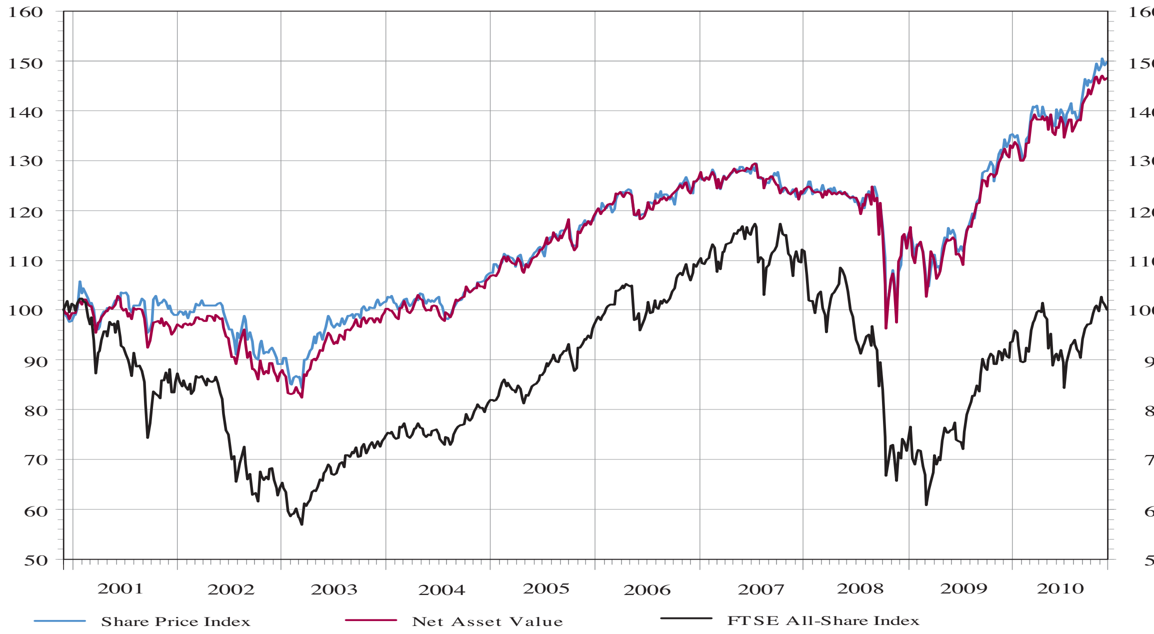
Essentially, if we did split the shares it would be because of the Investment Plans. The minimum subscription is £500 per month, typically leaving up to £200 uninvested, and it would take a holding of some 115 shares, worth around £35,000, to buy one new share through dividend reinvestment. Is having £200 or £300 out of the market for a month, either as a one-off or on average, a problem that would make it worth splitting the shares? I'm open to persuasion either way.

COLLECTED QUARTERLIES

No, you haven't missed the book of collected Quarterlies we are publishing as a tribute to Ian Rushbrook. The delay has been my fault entirely. I now intend that it will be published with the 2011 Annual Report as *'60 Not Out — Personal Assets Trust Quarterlies 1994-2011'*. It will contain 60 Quarterlies and we shall enclose a request form for it along with the Annual Report.

ROBIN ANGUS

PERSONAL ASSETS TRUST PERFORMANCE



	Value	Percentage Changes			
	30 Nov 2010	1 Year	3 Years	5 Years	10 Years
Share Price	308.00	12.4	21.3	26.9	48.4
NAV per Share	302.29	11.3	17.8	25.4	45.5
FTSE All-Share Index	2,861.61	8.1	(12.8)	4.4	(2.8)
NAV relative to FTSE All-Share Index	–	3.0	35.1	20.1	49.7

TOP 10 EQUITY HOLDINGS

Company	Country	Sector	Valuation 30 Nov 2010 £'000	Shareholders' funds %
British American Tobacco	UK	Tobacco	14,507	5.4
Nestlé	Switz	Food & Beverages	13,284	4.9
Coca Cola	USA	Beverages	13,061	4.9
GlaxoSmithKline	UK	Pharmaceuticals	9,151	3.4
Diageo	UK	Beverages	8,998	3.3
Johnson & Johnson	USA	Pharmaceuticals	8,830	3.3
Philip Morris International	USA	Tobacco	8,473	3.1
Vodafone	UK	Telecoms	8,013	3.0
Berkshire Hathaway	USA	Insurance	7,372	2.7
Microsoft	USA	Software	7,336	2.7
			99,025	**36.7**

GEOGRAPHIC ANALYSIS

	Valuation 30 Nov 2010 £'000	Shareholders' funds %
UK equities	69,251	25.7
US equities	58,660	21.8
Swiss equities	13,284	4.9
Australian equities	5,706	2.1
Gold Bullion – Physical	33,782	12.6
US Treasury Inflation-Protected Securities	73,910	27.4
Net current assets	14,851	5.5
Shareholders' Funds	**269,444**	**100.0**

Further information on the Trust can be obtained from the Company's website – www.patplc.co.uk or by contacting Steven Budge on 0131 225 9995.