

PERSONAL ASSETS TRUST PLC

DECEMBER 2011

QUARTERLY REPORT N^o. 63

PAT'S LONDON MEETING

Our next London Shareholder Meeting will be at 10.30 am for 11 am on Tuesday 24 January 2012 at the Institution of Engineering and Technology, 2 Savoy Place, London WC2R 0BL (nearest tube stations Charing Cross, Embankment and Temple). There will be a presentation by Sebastian Lyon, our Investment Adviser, followed by Questions & Answers and then by light refreshments. You will find an invitation and an attendance card enclosed along with the Quarterly and the Interim Report. If you require any further information, please telephone Steven Budge on the Personal Assets Trust Shareholder Information Line:

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A SATISFACTORY HALF YEAR

Personal Assets has had a very satisfactory half year. Over the six months to 31 October 2011 our share price rose by 5.9%, from £318 to £336.80, while our comparator, the FTSE All-Share Index, fell by 9.3% — a 16.8% out-performance in capital terms. We continued to outperform in November, by the end of which our share price had risen by 1.1% to a record £340.60 compared to an 0.7% drop in the FTSE All-Share.

We have therefore been succeeding in our primary objective of protecting the per share value of shareholders' funds. Where we are encountering difficulty in today's investment environment is in earning income in a way that doesn't put our capital — our '*sacred savings*' — at risk. As you will have seen, we have just declared a third interim dividend of £1.40 per

share. The fourth quarterly dividend for the year ended 30 April 2012 will be at least £1.40 per share and the total dividend for the year will be not less than £5.55, an increase of 2.8% over the previous year. Our policy remains never to cut the dividend; but, while we still aim to continue to increase it in excess of the RPI over the longer term, we certainly won't manage to do so over the year to 30 April 2012. The Board is convinced that it would be wrong to give rapid short term dividend growth priority over long term capital preservation. For the time being we are prepared, while protecting the level of the dividend in cash terms, to see a pause in real income growth while we inhabit a world of zero interest rates and feel it necessary for capital protection to hold a sizeable sum in non-yielding gold bullion.

DOES SIZE MATTER?

The Interim Report accompanying the Quarterly mentions some other milestones in our progress. During the six months under review we took in £60 million of additional capital through the issue of new shares; we saw our market capitalisation rise from £313.2 million at our 30 April 2011 year end to £393.4 million (it reached £400 million for the first time ever on 16 November); and on 11 October we became a constituent company of the FTSE 250 Index.

Expanding in size through the issue of new shares and then entering the FTSE 250 Index are, of course, irrelevant to Personal Assets' objective of protecting and increasing (*in that order*) the per share value of shareholders' funds over the longer term. Indeed, we are sometimes asked if an increase in size might not be storing up problems for the future — that the bigger we get, the harder it will be to achieve our objective. This we

are confident is not the case. Ian Rushbrook and I often used to discuss it in the days when Personal Assets was a £20 million company growing (*rather to our own surprise*) into a £50 million company and then starting to head for £100 million. Our conclusion then was the same as our settled conviction now — that Personal Assets' investment approach does not depend for its success on the company's being any particular size and will be just as valid however much the company grows or (*if the process reverses*) contracts.

The inflow of new funds has been encouraging, however, because it shows that people must like what we do and that they want to join us as a result. They cannot be doing so under any illusions about what Personal Assets has to offer: in Churchillian parlance, nothing but blood, toil, tears and sweat. We continue to make it plain to shareholders new and old that these are extraordinarily difficult times. On occasion it even feels as if we are in a sort of investment 'Phoney War' in which we daily await a sudden, overwhelming onslaught that always threatens but never seems to come, or are stuck in a stalemate akin to that experienced on the Western Front during much of the Great War.

TRENCH WARFARE

In this investment battle for survival we remain dug into our trenches, sheltering behind our defences of cash, gold, index-linked bonds and solid equities with decent yields. Sebastian and I set out our views and strategy in some detail on page 5 of the Interim Report, but in round figures our portfolio is split 50/50 just now between equities and liquidity. There is no shortage of sound and fury in the markets; but it often recalls the Grand Old Duke of York, marching his ten thousand men up to the

top of the hill and marching them down again. This was true of the gyrations at the end of October and the beginning of November between the announcement of the Euro rescue package and Papan-dreou's subsequent announcement of a referendum, when Barclays — for example — rose by 17.6% and then fell by 9.5%. Patience and calmness are what are needed, and one has to follow Kipling's advice to:

*'Keep your head when all about you
Are losing theirs and blaming it on you'*
while resisting the temptation he holds out later in the poem to:

*'Make one heap of all your winnings
And risk it on one turn of pûch-and-toss.'*
(I find it hard to imagine anything less in keeping with the spirit of Personal Assets than the sentiment expressed in those lines.)

We are long past the stage of lotions and potions. The world is struggling within a gastric band of austerity. Slimming down the flab of debt too quickly might cause a heart attack, but perhaps it is better to have a heart attack and recover than to die of obesity. For the time being, Matthew Arnold in his poem *Dover Beach* sums up better than does Kipling how the markets feel:

*'And we are here as on a darkling plain
Swept with confused alarms
of struggle and flight,
Where ignorant armies clash by night.'*

This sense of darkness, confusion, struggle and ignorance in the markets is what I tried to get across while speaking recently at an investment seminar arranged by *The Scotsman* in Edinburgh. I was invited to give a speech on the rôle of gold on wealth protection, and Sebastian and the Chairman afterwards thought it might be worth reproducing the substance of it for Personal Assets shareholders in general. So, here it is. The fact that it was written to be delivered to an audience explains why in places the style is rather more colloquial than usual for a Quarterly.

THE PROTECTION OF WEALTH

The economic environment these days is diabolical. Many people — indeed, perhaps even *most* people — feel poorer than they did five or ten years ago, and for the first

time for generations we worry that our children will be worse off than we were. Trusting to economic growth has failed. In the USA and the UK there has been little real growth for several years, as opposed to the illusion of growth caused by widespread borrowing against equity assets for immediate consumption. Despite all their ups and downs, the three major world equity markets have done nothing for the last decade. In fact, they've gone backwards.

- In December 1999 the FTSE 100 reached its all time high of 6,950. Now it's some 20% lower.
- The S&P Composite is nearly 20% below its March 2000 high. (It did top its March 2000 intra-day high of 1,552.87 in 2007, but not by much and not for long, reaching an intra-day 1,576.09 on 11 October of that year.)

- And don't even ask about the Nikkei Dow in Japan. In April 2000 it was up at 20,833, having been nearly 39,000 in 1989, and now stands at around 8,500.

Yes, you could have made money during the period. But it's been nothing like the 1980s or the 1990s, when — by and large — you assumed markets would go up and the only question was which markets would do better than others. (And if you were a cautious investor, you had the comfort of knowing you couldn't go wrong by putting all your money into one-decision blue chips, like GEC or Royal Bank of Scotland.)

A 'LAUREL & HARDY' MARKET

And now — well, the world is bust, or as near as damn it. There have never been times like these and today we have no directions to follow or maps to guide us. I call it a 'Laurel & Hardy' market, in which nearly every day one feels like exclaiming to the bankers and politicians:

'Another fine mess you've got me into!'

People still have a childlike expectation of political answers at the moment, not economic ones; but the finance ministers of the G7 and the G20 are out of their depths — gabbling and sweating like a bunch of unsuccessful contestants in *The Apprentice*, bungling their tasks and waiting for Alan Sugar

to give them the sack. They will keep on trying, bless them, in their well-meaning but deluded way. In any conflict between politics and economics, politics always wins in the short term. Sooner or later, however, economics will always take its revenge.

We may well be in a bear market for another five years. I don't usually make predictions of market timing and market levels. Nearly 35 years in the investment business have taught me how little I know, and how unlikely it is that such predictions would be any more than blind guesses. But this evening I *am* going to make you a long-term prediction, and it's this:

*'The next bull market in equities will begin on the day in which the first tram runs in Edinburgh.'*¹

GOLD: THE HOW AND WHY

Personal Assets' investment in gold — approximately 13% of shareholders' funds at 31 October, or around £50 million worth — has been very headline-grabbing. You may even have imagined (*I told the audience*) that I'd be some sort of American-style survivalist, with my rifles and my cases of baked beans and my Sarah Palin Hunting Calendar.² But we're no survivalists — no perma-bears, revelling in gloom. Nor is our investment outlook a stopped clock, right twice a day but wrong all the rest of the time. We're pragmatists, tackling a particular set of problems that face us as investors. All investment decisions should be pragmatic rather than ideological. In a world that was growing fast economically and in which real interest rates were high, we would be behaving differently from how we are behaving now. We would be doing our best to take advantage of that rapid growth and those high interest rates. In the unprecedented situation of a world without growth

¹ The Edinburgh-based audience appreciated this wisecrack, the city council's ludicrous tram project being a major local grievance here. Alas! If the £325 million the Scottish Government promised the city council for the trams in March 2003 had been invested straight away in gold, it would be worth nearly £1,700 million today . . .

² To my surprise and delight, Sebastian and his colleagues at Troy took the hint and presented me a week later with my very own Sarah Palin Calendar as an early Christmas present.

and a world without interest rates, however, our problems are otherwise — how to cling on to what we've got and how to earn enough income from it to live on.

Personal Assets uses gold as a tool, a means to an end, in helping us keep our capital safe. So let's get gold in perspective.

- Objectively considered, gold is just about the worst investment it's possible to imagine. You can't eat it. You can't drink it. You can't smoke it. You can't plant it. You can't make it into anything very useful. It pays you no dividends and earns you no interest. Indeed, it costs you money to store and insure it.

- What's more, gold can be very volatile and very risky. Between its \$800/oz peak in 1980 and Gordon Brown's masterly sale of our gold reserves at \$275/oz twenty years later, it proved to be a rotten long-term investment as well as a terrifying short-term one.

And yet, gold is very remarkable. The thing about gold is that, wherever you went to in the world at whatever period of history, you would have been able to pay your way with a pocketful of small denomination gold coins.

Think of ten sovereigns. (*I actually took ten sovereigns to the presentation as a visual aid and to jingle at the other speakers.*) A century ago, ten quid would have been a week's income for a very comfortably off person. Today, ten sovereigns, now worth around £2,750, would still be a week's income for a very comfortably off person. If Nick Clegg pushes the nuclear button, the Third World War starts and we have to flee to the desert or the mountains, what would we rather take with us? A bundle of banknotes? Some share certificates? Or those ten gold sovereigns?

I'm not saying the Third World War is about to start. Nick Clegg might not even know where to find the button, let alone how to press it. But I *am* saying that in these troubled times I'm happy with gold. Personal Assets' attitude to gold is a sacramental one. As you'll all remember from your Prayer Book Catechism:

QUESTION. *What meanest thou by this word Sacrament?*

ANSWER. *I mean an outward and visible sign of an inward and spiritual grace.*

Gold is the outward and visible sign. The inward and spiritual grace it signifies is Personal Assets' philosophy of protecting wealth in priority to trying to increase it — particularly when times turn nasty.

A MEANS TO AN END

We're not 'gold bugs', although I sometimes enjoy posing as one to tease Keynesians and others who deny either the infallibility of the market or the existence of Original Sin. Would we hold gold in normal times? No. As a matter of fact we wish we didn't have to hold it now and could be bull market investors in growth equities again. But two phrases have tended to characterise our thinking in recent years — '*irreplaceable capital*' and '*sacred savings*'. That's why we're holding gold.

Gold bullion is money that can't be printed — an a-typical holding for a-typical times, and an alternative to holding part of the portfolio in cash.

- It's a time of fear in the financial markets, and fear brings a flight to gold — in which it can be profitable to be a fellow-traveller.

- In a world of currency vulnerability and unprecedentedly low interest rates, gold has a rôle to play in protecting real value. It's an insurance policy against declines in other asset classes. We've seen plenty of those, and we'll see more before we're done.

- Because of zero interest rates there's no loss of income, and holding it is cheap.

- Every other currency is in a 'race to debase'. Gold is the one universally accepted currency that can't be debased.

- There is not a gold 'bubble'. There's been much talk of one — particularly by those who've never owned or recommended gold — but given that only 0.6% of global financial assets are invested in gold compared to 3% in 1980 and the supply of paper money is increasing at an exponential rate, we are way, way off bubble territory.

Don't despise gold and don't patronise it, as so many of the investment intelligentsia have done, from John Maynard Keynes onwards. Never mind if in theory it *should* be an investment of last resort. There are times when it *is* an investment of last resort, and that's what counts, rather than investment theory.

Gold, I repeat, is not a natural long term holding for us. But owning gold makes sense now as one of our weapons for defending what we've got, in readiness for the time we can move forward. Today we are temporarily, but gratefully, holding gold not as an end in itself but as a means to an end — helping us protect our irreplaceable capital, our '*sacred savings*', at a time of financial and economic crisis. And when that yearned-for, once-in-a-generation bull market eventually comes, we won't hold gold any more. But we'll remember that holding gold helped us keep our firepower intact in readiness for that new bull market, and we'll be grateful.

GOLD ON CRACK

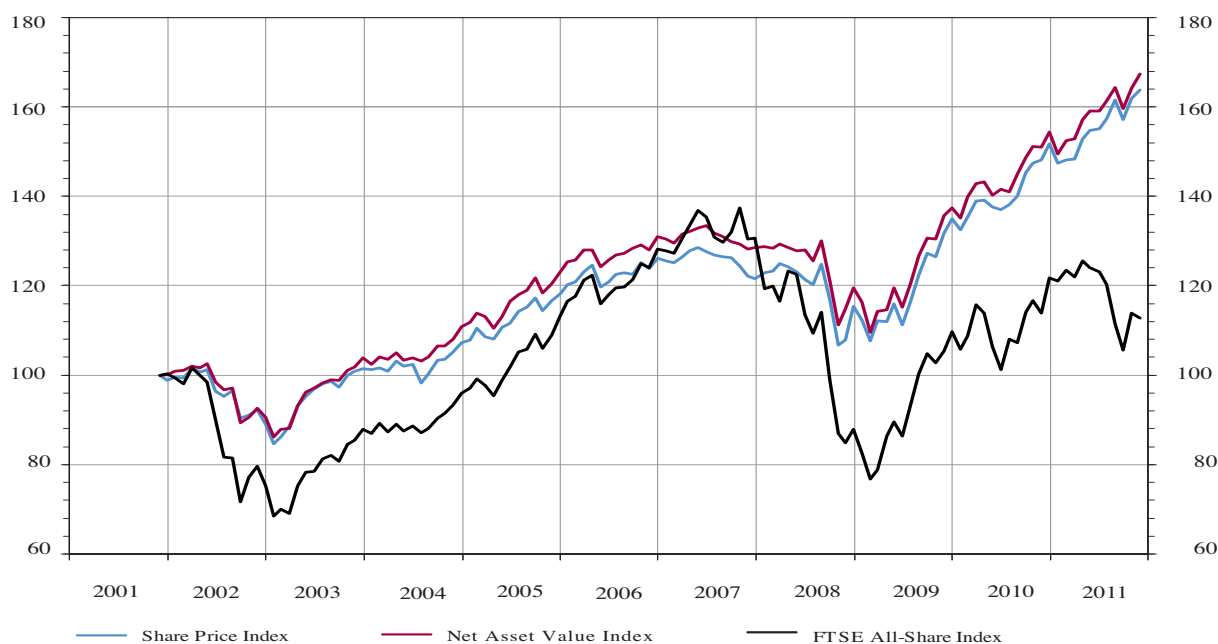
I should add that at the seminar someone asked me about other metals. I quoted Sebastian's view of silver — '*gold on crack*' — while admitting to keeping a 100 troy ounces bar of silver on my desk as a paperweight and for threatening to throw at the Chairman when he annoys me. I bought it in 2003 to tease Ian Rushbrook, paying something below \$5/oz for it (£300 for the bar), and silver is now \$32/oz (just under £2,000 for the bar). I love it and shan't sell.

THE PATIENCE TO WAIT

At the end of the *Scotsman* seminar the speakers were invited to give a very brief summary of their views. As usual when challenged in this way, a Scots phrase sprang to my lips — '*Ca' canny and keep your powder dry.*' But if I had to sum up Personal Assets' approach in a phrase it would be, '*the patience to wait*'. It is frustrating to have to wait, and hope deferred (to quote King Solomon) makes the heart sick. But one day our hope will be rewarded and that bull market will come . . .

ROBIN ANGUS

PERSONAL ASSETS TRUST PERFORMANCE



	Value 30 November 2011	1 Year	Percentage Changes		
			3 Years	5 Years	10 Years
Share Price	£340.60	10.6	51.7	32.1	63.8
NAV per Share	£335.12	10.9	45.8	30.7	67.4
FTSE All-Share Index	2,835.84	(0.9)	32.9	(9.1)	12.8
NAV relative to FTSE All-Share Index		11.9	9.7	43.8	48.4

TOP 10 EQUITY HOLDINGS

Company	Country	Sector	Valuation 30 November 2011 £'000	Shareholders' funds %
British American Tobacco	UK	Tobacco	18,320	4.5
Coca-Cola	USA	Beverages	13,750	3.4
Microsoft	USA	Software	13,565	3.4
Nestlé	Switz	Food Producer	13,480	3.3
Philip Morris International	USA	Tobacco	11,781	2.9
Diageo	UK	Beverages	10,712	2.7
GlaxoSmithKline	UK	Pharmaceuticals	10,593	2.6
Centrica	UK	Utility	10,172	2.5
Newmont Mining	USA	Mining	10,154	2.5
Tesco	UK	Food Retailer	9,413	2.3
			121,940	30.1

GEOGRAPHIC ANALYSIS

	Valuation 30 November 2011 £'000	Shareholders' funds %
UK equities	87,213	21.6
US equities	81,376	20.1
Swiss equities	13,480	3.3
Canadian equities	12,835	3.2
Australian equities	7,878	2.0
Gold	58,616	14.5
Government bonds (USA, Singapore and UK)	134,930	33.4
Net current assets	7,845	1.9
Shareholders' funds	404,173	100.0