PERSONAL ASSETS TRUST PLC

JUNE 2013 QUARTERLY REPORT N^o. 68

DON'T MAKE MISTAKES (PART I)

One of the themes of the Chairman's Statement in the 2013 Annual Report is Personal Assets' investment style. We can't deny that it's a somewhat unusual one for a global growth investment trust, but we believe that it not only reduces risk but also increases the likelihood of long-term reward.

Because our investment style can still sometimes be misunderstood, I want to say a little more about it here. Personal Assets must be a tiresome holding for lovers of excitement and adventure, who will find it well-nigh unbearable to see us sitting on the sidelines while Wall Street hits new highs and the FTSE 100 Index climbs tantalisingly to within spitting distance of its 1999 peak.

But as I have so often said before, our aim is to be boring and dependable. If you want a trust that seeks to shoot the lights out in a tempestuous market, give Personal Assets a miss. We're not in that game. *We just try not to make mistakes.* Consider the following performance statistics, which would drive some impatient investors to drink and send others to sleep:

- We underperformed our comparator, the FTSE All-Share Index ("All-Share"), in net asset value ("NAV") terms in no fewer than seven out of our thirteen financial years between 30 April 2000 and 30 April 2013, whereas we outperformed it in only six.
- Not once during the thirteen year period did we outperform the All-Share when it had an up year. The market rose in seven financial years out of thirteen and we underperformed it every time.

To counterbalance this, however, let me point to what may be our most distinctive feature, one which reminds me of a favourite old saying of Ian Rushbrook's that *'you won't win the investment game if you set out to win it — you'll win it only if you set out not to lose it'.*

- We never underperformed the market when it had a down year during the period. The six financial years in which we outperformed the All-Share were the only six years in which it fell.

In this way we preserved our all-important stake money. And each time we held on to our stake money when the market fell, we had it ready to hand and waiting to start working for us when the market began to rise. That is why our style, so uninspiring at first glance, has delivered the goods over the longer term better *(probably)* than would a string of years of outperformance marred by a couple of disastrous ones.

How we did it is illustrated in the chart *Annual Percentage Change in NAV and FTSE All-Share Index to 30 April* on page 3 of the Annual Report, in which we show the NAV of Personal Assets compared to the performance of the All-Share in each of our last thirteen financial years. The chart demonstrates how, despite our underperforming the All-Share in seven out of the thirteen years, *over the period as a whole* our NAV outperformed the All-Share by 56%.

LOOKING BACK TO THE 1990S

What sort of a game are we playing? It's a long game, that's for sure. As I said, *we try not to make mistakes.* From 30 April 2000 to 30 April 2013 may be a lengthy period, but it's still, as the Chairman admitted, an arbitrary one; so let's set those years in the context of Personal Assets' 23-year-long history as a self-managed trust.

If we look back to 30 April 1990, when Ian Rushbrook and the Board took over the running of the trust and Personal Assets as we know it today came into existence, we can detect over our first decade a pattern of performance which, while it is in some ways not dissimilar to that of 2000-13, also contains significant differences which repay careful study. Both the similarities and the differences are of vital importance in understanding what it is that drove Ian Rushbrook and what today drives the Board and Sebastian Lyon, the Investment Adviser.

The 1990s were another world as far as investment was concerned. Over our ten financial years between 30 April 1990 and 30 April 2000 not only did the All-Share rise in eight of them and fall in only two, but even those falls were marginal: in the year to 30 April 1995 the All-Share dipped by just 0.1% and in the year to 30 April 2000 it fell by only 0.9%.

Not to have made money during the 1990s would have been quite an achievement even for perma-bears of the kind we are so often wrongly accused of being. While the long bull market of the 1990s may have climbed a wall of worry as all bull markets do — Greenspan and *'irrational exuberance'* in 1996, the 1997 Asian currency crash, and then the Russian bond default and the collapse of Long Term Capital Management in 1998 — it did so very successfully.

Over the decade the All-Share rose by 187.8%, a stunning feat. Personal Assets, however, did even better, its NAV rising by 252.6% from £56.67 *(adjusted for the 1-for-100 share consolidation in 1993)* to £199.80. Not unsurprisingly given our aversion to risk, we outperformed the All-Share in the two years in which it fell and underperformed it in three of the eight years in which it rose; but our pattern of underperforming the All-Share in up years did not hold good consistently throughout the decade, and that was just as well.

What happened? What was different about the 1990s? The answer is that investment conditions were different. In those days Ian and I were able to be bulls not just in theoretical terms but in practical terms too and we were able to find opportunities for profit which had a far more favourable risk/reward ratio than the ones we saw on offer from 2000 onward.

At least during the first half of the decade, equities were often cheap and were seldom, if ever, priced at higher than their fair value. Accordingly, Personal Assets was not only fully invested in equities until the early months of 1996, but also geared to the rising market until as late as 1998 through our holdings of investment trust warrants and shares in a basket of investment management companies — a form of gearing which we believed was more effective and less risky for us than using borrowed funds would have been. This, together with our success in anticipating the market shift from smaller stocks to large blue chips, was what enabled us to outperform even the heady bull market of the 1990s.

BUILDING ON OUR ADVANTAGE

Again as Ian liked to say, *'Don't try to win it, just try not to lose it.'* Having gained an advantage over our comparator (and hence over the UK market in general) during the 1990s, our next task was to hold on to it during the very different investment environment that was to follow — one in which stocks were very seldom cheap and were often overpriced, and where disasters waiting to happen (the dotcom bubble, sub-prime mortgages and the banking crisis, to name but three of them) were more common than opportunities waiting to be exploited. But despite bloopers like staying with bank shares for too long in 2008, we not only held on to our advantage but managed to increase it.

I described at the beginning of this Quarterly how we managed to outperform the All-Share during the see-saw markets of the last thirteen years. Our net assets of £199.80 per share at 30 April 2000 grew to £351.89 at 30 April 2013, so our stake money — our *'skin in the game'* — increased by 76.1% although the All-Share was up by only 12.9%. *We are hanging on to this increased stake money in order to be able to use it when the long-awaited and longed-for time arrives for us to be bulls again,* because (contrary to what a quick glance at the figures may suggest) our investment style during the 1990s wasn't different from that of 2000-13. It was, I repeat, the investment environment in those days that was different, and presented us with the kind of low risk, high reward opportunities that we found lacking as we tried to avoid mistakes in the years after 2000.

You may be sure that when opportunities with the right balance of risk and reward present themselves again, we shall be more than eager to capitalise on them.

BOARD MEETINGS

Towards the end of last year a shareholder wrote to me:

'Your reply to my original question [about overseas exposure in the portfolio] *made me realise that I have very little idea of what goes on at a Board Meeting for PAT. If you are short of material for a newsletter (admittedly unlikely), could you include an informal summary of a "typical" meeting? I suspect that many readers would find it illuminating to read about the sort of issues that are considered.'*

The Quarterly which goes out along with the Annual Report often provides an opportunity to deal with a more general topic, since what is newsworthy about our recent performance and the investment outlook will already be covered by the Investment Adviser's Report. As it happens, a discussion of what happens at Board Meetings fits in especially well here because this year we give more information about the work of the Board in the Annual Report. On page 19 you will see a diagram highlighting some of the topics the Board has dealt with over the year.

DON'T MAKE MISTAKES (PART II)

My first impressions of the work of a Board came from the popular 1960s TV boardroom drama *The Power Game*. Fortunately for the Directors' blood pressure and the shareholders' peace of mind, the Board Meetings of Personal Assets are nothing like that. Instead, in the same way that much of the Investment Adviser's work is devoted to protection of capital and preventing loss, much of the work of the Board is about protecting the integrity of the Company and its business and preventing problems from arising — in other words, about avoiding slip-ups, mistakes and unforeseen pitfalls.

Each Board Meeting begins with an example of this. The first item on the agenda after apologies for absence is entitled *Directors' Interests/ Conflicts of Interest*, such as directorships of other companies. It isn't that we accept new directorships every day and so risk losing track of which of us sits on which company Board (as an Executive Director I don't accept any at all). But establishing the habit of regular checking and questioning ensures that if a conflict of interest ever did arise it wouldn't slip under the radar but would be spotted right away.

For the same reason, it is important to go through the Minutes — the record of what took place at the last Meeting — to ensure that what was decided then has been put into effect since. Along with the Minutes the Company Secretary[1] compiles a comprehensive list of Matters Arising and Action Points for the Board's consideration, to make sure that nothing is missed. The Board works through this with care, carrying over to the next Meeting any items that have not yet been adequately dealt with.

BOARD COMMITTEES

This theme of regularly checking and examining subjects to make sure nothing is missed is carried over to the Committee Meetings which we hold on a rota basis before Board Meetings themselves.

There are three permanent Committees — Audit, Remuneration and Nomination. Of these, the Au-

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[1] Just as I learned very early on in my career never to underestimate the importance of the Chairman of an investment trust — as well as controlling the Board like the conductor of an orchestra he is the public face of the trust and is highly visible as well as highly responsible, for instance at AGMs and meetings with shareholders — so the importance of the Company Secretary of an investment trust must never be underestimated. All the threads of the trust's activities are in his hands and he has to keep abreast of changes to company law and other regulations and work closely with the trust's principal advisers and with the Association of Investment Companies.

dit Committee has the heaviest workload. Its job is that of scrutinising and checking the annual and interim financial statements (this year, for instance, we were able to correct an error which had gradually crept in to our calculation of the effective yield on our index-linked bonds), our accounting policies and our compliance with financial and regulatory reporting requirements. It also reviews our internal controls and the terms of appointment of the Auditors, including their remuneration.

A further example of checking and examining to ensure that nothing of importance escapes us is our regular examination at each Board Meeting of changes to the share register. Our shareholders are our employers, our colleagues and our partners. We need to know if they are happy with what we are doing on their behalf. We want to know who they are, and who is buying and selling. This is the stage of the Board Meeting at which we discuss meetings that Sebastian, the Chairman and other Directors have had with shareholders and we consider feedback, queries and complaints received by letter, e-mail or through our website.

Management Report

The central business of each Board Meeting is the consideration and discussion of the Management Report. It begins with a report from Troy on the period since the last Board Meeting, describing what changes have been made to the portfolio, what the outlook is for markets and what we should be doing in response or in anticipation. If we have made an investment in a new company, Troy provides for us a comprehensive purchase note which we discuss.

It is not the job of an investment trust Board to pick individual investments. It is, however, very much the Board's job to test the Adviser's thinking — test it to destruction, if necessary. This is no mere academic exercise. Sitting around the Boardroom table are a group of people who have a lot of their own money at stake. The interests of the Board, the Investment Adviser and the other shareholders are the same, and it is as much in the Investment Adviser's personal financial interest for us to test his thinking, as it is in ours!

Red, Amber and Green

Perhaps the single most interesting item in the Board Papers is part of the regular Management Report — the page headed *Investment Universe*. As I mentioned in Quarterly N°. 64 (March 2012), the Board considers asset allocation by using a matrix which has green *(core investments)*, amber *(unlikely to invest — subject to Board approval)* and red *(not currently permitted)* categories in each geographical or size sub-section of the following seven asset classes: Equities; Real Estate; Fixed Interest; Commodities; Currencies; Futures; and Other Asset Classes.

Like a packing list or a Christmas card list, the red, amber and green matrix makes sure we don't forget about anything. Considering it at every Board Meeting prevents us from becoming blinkered. To say that we don't invest in some asset class because we think it unsuitable or unattractive is a very different thing from saying that we don't invest in it because it has never occurred to us to do so. We might have got away with that in the days when we were under £20 million in size but a £600 million company has to be aware of the whole investment universe, even though we can and must be selective investors within it.

Sometimes after discussion we will change an asset class from red to amber or from amber to green. We could also move asset classes from green to amber or from amber to red, but so far we haven't done so — maybe proof of our widening investment horizons?

Complementing the red, amber and green matrix is another matrix of investment bands and ranges, setting out minimum and maximum percentage exposures to equities, gold and liquidity and to the seven currencies through which our investments are currently held. At present our minimum in equities is 33% of shareholders' funds and our maximum 90%, whereas our minimum and maximum in gold are 0% and 25% and we have no maximum or minimum liquidity percentage. These limits can be and are changed after discussion between the Board and the Investment Adviser — as, for instance, in March 2011, when we increased the maximum investment in gold from 15% to 25% (a level we have so far never even come close to reaching).

The AIFM Directive

I've referred already to page 19 of the Annual Report, where you will see a diagram highlighting some of the topics the Board has dealt with over the year. Included there are regular items of business such as dividend declarations; recurring topics such as reviews of Risk Registers, Corporate Governance and Internal Controls; and specific matters like the issue of Prospectuses (necessary in order to operate our premium control mechanism) and, with monotonous regularity at every Board Meeting, the implementation of the Alternative Investment Fund Manager Directive ("AIFMD").

The AIFMD covers all investment funds other than Undertakings for Collective Investments in Transferable Securities ("UCITS") and is a well-meaning but flawed attempt by the European Union to protect investors which ends up delivering no benefits of any kind but instead lumbers trusts with a costly and cumbersome extra layer of unneeded regulation. It will inevitably add to our costs by a few basis points, but we shall do our best to keep this to a minimum.

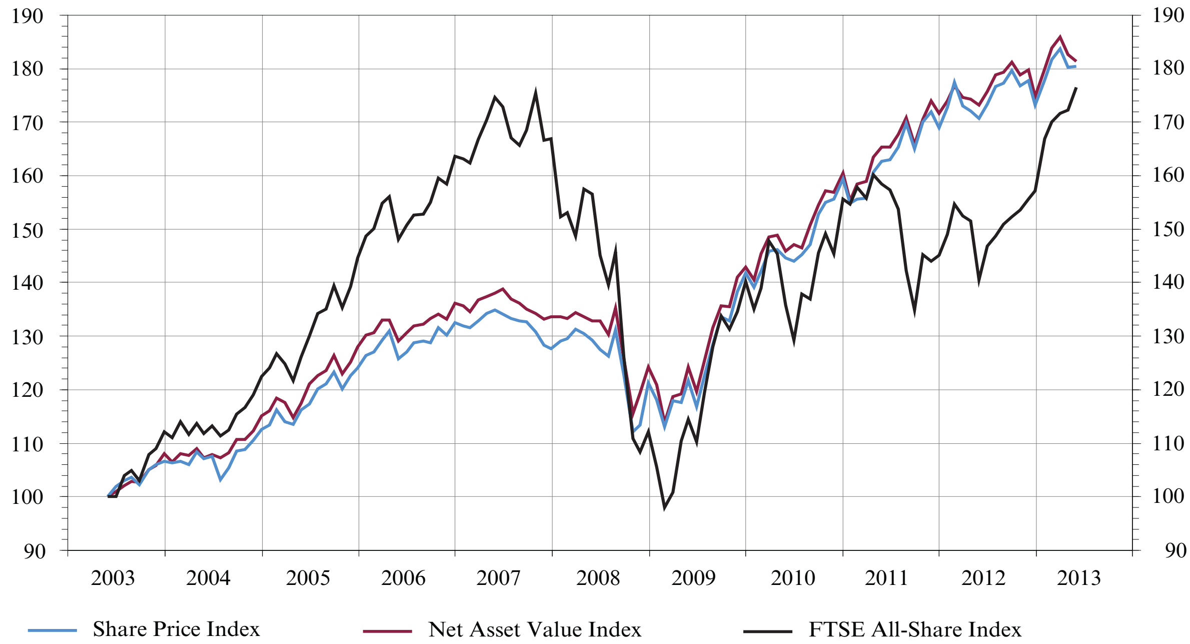
'Ready, aye ready!'

Before Board Meetings the Directors and Adviser often dine together to discuss things in a relaxed and informal way, and we also hold lunches after our Board Meetings as a way of keeping in touch with IFAs, wealth managers, industrialists and the media.

We talk, too, about how Personal Assets might develop. I was about to write that in 1990 Ian and I didn't envisage it would become a £600 million FTSE 250 company, but I think Ian *(deep down)* did. Come what may, we shall guard our stake money and remain, like Camp Coffee, Merchiston Castle School and the Royal Canadian Navy, *'Ready, aye ready!'*

Robin Angus

Personal Assets Trust Performance



	Value 31 May 2013	Percentage Changes 1 Year	3 Years	5 Years	10 Years
Share Price	£357.20	5.7	24.8	39.5	80.4
NAV per Share	£349.36	4.7	24.4	36.5	81.3
FTSE All-Share Index	3,473.82	25.5	30.0	12.7	76.4
NAV relative to FTSE All-Share Index		(16.6)	(4.3)	21.1	2.8

Top 10 Equity Holdings

Company	Country	Sector	Valuation 31 May 2013 £'000	Shareholders' funds %
Microsoft	USA	Software	32,108	5.4
British American Tobacco	UK	Tobacco	25,557	4.3
Nestlé	Switz	Food Producer	20,679	3.5
Becton Dickinson	USA	Pharmaceuticals	19,791	3.3
Coca-Cola	USA	Beverages	16,950	2.8
Imperial Oil	Canada	Oil & Gas	16,764	2.8
Sage Group	UK	Technology	15,334	2.6
Philip Morris International	USA	Tobacco	14,553	2.4
GlaxoSmithkline	UK	Pharmaceuticals	12,937	2.2
Johnson & Johnson	USA	Pharmaceuticals	12,388	2.1
			187,061	**31.4**

Portfolio Analysis

	Valuation 31 May 2013 £'000	Shareholders' funds %
US equities	140,907	23.6
UK equities	73,933	12.4
Canadian equities	20,758	3.5
Swiss equities	20,679	3.5
Australian equities	5,842	1.0
Gold	70,323	11.8
Government bonds (USA, Singapore and UK)	264,317	44.4
Net current liabilities	(1,027)	(0.2)
Shareholders' funds	**595,732**	**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 538 6605