investment update

2nd quarter 2005

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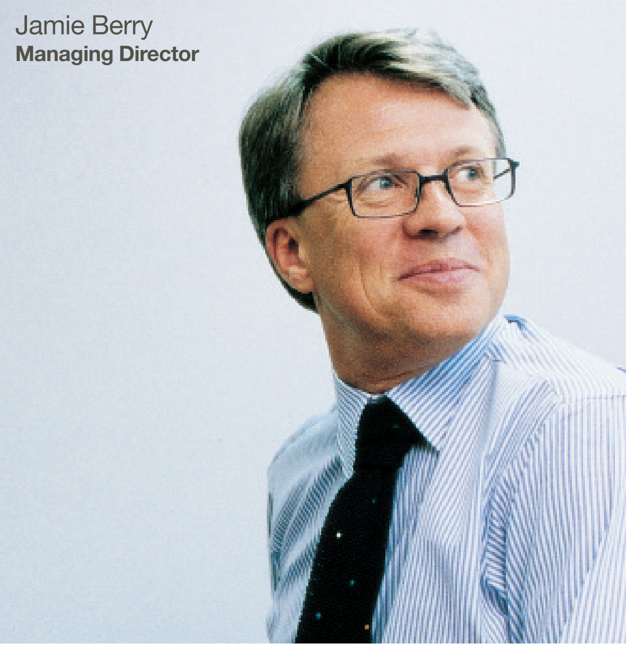
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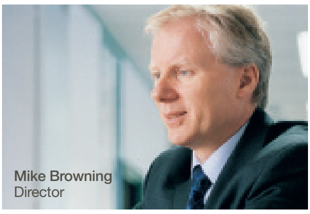

Mike Browning
Director


Neil Kennedy
Director

For once it has been the UK and continental European markets which have offered some of the better returns for equity investors in recent months. The total return of capital and income from the FTSE All Share Index was around 4% in the first quarter, and just under 8% for the past six months. Similar returns were achieved in continental Europe over the past six months in both euro and sterling terms. The US market, by comparison, was virtually unchanged over both periods in sterling terms, with returns impacted by a weak dollar, particularly in the period before Christmas.

The general rally in global equity markets, which began in late summer, finally petered out in early February, since when markets have traded in a very narrow range, reminiscent of the drifting conditions that we witnessed in the second quarter of 2004.

The PAM Awards 2005

In January we were **shortlisted in the category Best Investment Boutique** in the 2005 Private Asset Managers Awards, which is the recognised industry benchmark for private client investment managers. The PAM Awards programme compares the relative performance of the leading private asset management companies who operate in the high net worth arena. The winner is the boutique that is considered by the judges to offer the best overall service covering, inter alia, administration, relationship management, accessibility and product delivery.

Stockmarket review

Medium and smaller sized companies have performed very well over the past year. It is interesting to note that in the UK, the FTSE 100 Index is still around 30% below the peak level it reached at the end of 1999, whilst the FTSE 250 Index, which measures the performance of the next 250 UK companies by size, is around 10% above the level in December 1999.

A large part of this outperformance by mid and smaller companies has occurred in the past two years, propelling valuations in some sectors to very high levels. Energy and natural resources stocks have been in particular strong demand. We are currently seeing some rotation back into larger companies, where less excessive valuations can be found. Managers of the more nimble equity funds that we own have already made a partial shift in emphasis, recognising that it could be time for larger companies to play catch up. On balance, we still favour multi-style, unconstrained funds for the very reason that managers can shift their portfolios to take account of changing market conditions: it is therefore pleasing to see them putting this into practice.

"…markets tend to like continuity. We have seen this in the US after last November's election."

Consumers have played a big part in supporting global economic momentum over the past few years. In the UK, the consumer has not only contributed to, but has also benefited from, the economic expansion during Labour's eight-year reign. The feel-good factor has been high, with cheap credit and a booming housing market contributing to a rise in living standards. However, cracks are appearing at the consumer level, brought about by the turn in interest rates and the real possibility of a housing downturn.

If Labour's two-term record on the economy is the sole determinant of voting behaviour, then a third term in office should be expected after the 5 May election. However, if voting is based on forward-looking factors, then it is easy to see the feel-good factor ebbing away and Labour's re-election prospects put under pressure. For example, tax hikes of previous budgets are already beginning to kick in; rising interest rates are causing a re-think on borrowing habits and the housing market; council taxes and utility bills are increasing at vastly higher rates than inflation; and questions are being asked as to why we are all having to make greater provision for retirement. The demise of MG Rover could also have a big impact on voter sentiment, particularly in some of the marginal constituencies.

From a stability point of view, markets tend to like continuity. We have seen this in the US after last November's election. However, consumers are beginning to notice the squeeze being placed upon them, and even if Labour's policies are not to blame, they are an easy target for any wavering voter visiting the polling booths..

"We are currently seeing some rotation back into larger companies, where less excessive valuations can be found."

Property outlook

Commercial property has been a very active asset class over the past two years and the pace of growth has been maintained in the past quarter. Investors have been attracted by the high income yield afforded by commercial property and its low correlation with equity and fixed interest markets.

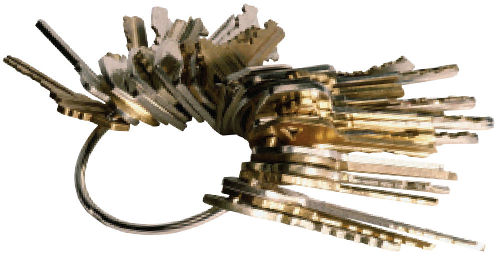
Pension and insurance funds, historically the biggest investors in commercial property, have been slow to increase their exposure to this asset class, largely due to a desire to hold less illiquid investments at a time when pension fund flexibility was becoming more prominent. Strong relative performance from equity markets also diluted exposure and caused pension consultants to allocate less capital to commercial property. This situation is now reversing, and is contributing to the strong demand for this asset class.

“Prices could quite quickly slip to a discount.”

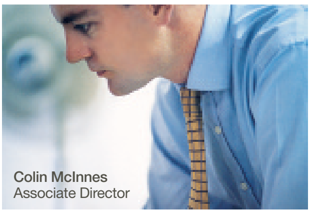
Property investment firms have responded to this growing demand by launching innovative investment structures. Where appropriate, we have invested in certain closed-ended funds to gain access for our clients’ property exposure. These structures have not only seen a good rise in asset values, but their share prices now stand at big premiums to the funds’ underlying asset values. This is probably not a sustainable situation in the medium to long run, and prices could quite quickly slip to a discount if growth in commercial property begins to advance at a more moderate pace, as many expect.

Commercial property remains an ideal asset class in a diversified investment portfolio, but accessing it in the right manner is also important. We may therefore use the current spike in prices to shift some of our property exposure to more open-ended vehicles that trade at asset value, and which are therefore less susceptible to price volatility. Access to continental European property markets is also improving and could offer some interesting opportunities and diversification away from some of the hot spots in the UK market.

“Commercial property remains an ideal asset class in a diversified investment portfolio.”




Mark Robinson
Director
Head of Investment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Oil price worries

There has been a lot of worry and speculation about the price of oil, which at one point was fast approaching $60 a barrel and, according to some commentators, could spike above $100 a barrel during the course of this year. Even the IMF has noted that surging demand and falling supply could cause a "permanent oil shock". It should be noted, however, that the recent rise in oil prices is largely as a result of artificial supply restrictions imposed by OPEC and strong demand from Asia.

For oil to reach even headier heights it will be necessary for Asia's economic growth to remain unchecked by higher oil prices. This seems unlikely. The higher oil prices go, the more likely growth will slow and cause a natural drop in oil demand. This basic rule of economics should come into play long before the price of oil is a major threat to global economic activity. Growth in Asia is already beginning to slow, so one could argue that this self-adjusting process is already underway. Both the UK and European authorities have left interest rates on hold recently, acknowledging the brake that dearer oil places on economic growth. Some of the current headlines surrounding the future direction of oil, and the possibility of a continued surge in commodity prices, are reminiscent of the TMT boom of the late 1990s: several commentators are forgetting some basic economic principles and the fact that the commodity cycle is highly cyclical.

Global GDP is expected to rise by 2.5% this year and by 2.2% in 2006 according to a panel of The Economist's forecasters. This is a slower pace of growth than we have seen in the past two years, but still sufficient to provide reasonable conditions for investing. Of the major global economies, growth rates in the US and UK are expected to be higher than Japan and the eurozone, although this is reflected in the valuations at which the stockmarkets in these areas trade. Growth in Asian economies, excluding Japan, is slowing but the expected nominal rates of growth are still higher than many western economies. We expect to add some exposure to this region in growth-orientated portfolios in the near future, particularly hoping to gain access to those countries and sectors which are prime beneficiaries of global outsourcing and increasing consumerism within Asian economies.

Overall, we are reasonably comfortable with equity market valuations and the prospects for generating positive returns for the remainder of this year. However, diversity in asset allocation and flexibility remain as important as ever.

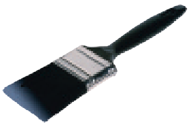
Where next?

In Mark Robinson's longer commentary you will have read that we remain broadly optimistic: the valuation levels of stockmarkets are fair, and the prospects for generating positive returns for the remainder of 2005 seem reasonable. However, we continue to advocate a multi-asset approach to building the portfolios under our management. Over reliance upon equity markets adds to the risk in a portfolio, and we are convinced that successful investment in today's markets needs a much broader cross section of different asset classes than used to be the case.

Our investment team

We continue to strengthen the investment team. In the last few weeks we have been joined by James Calder, who will head our Fund Research function. James, aged 35, previously spent over three years at Bestinvest and prior to this held Fund Analyst positions at Standard & Poor's, Greig Middleton and Gartmore. Within the next month Ian Heap will join the team as an Investment Manager. Ian, aged 30, previously spent three years at Close Wealth Management.

Chelsea Harbour



We have recently acquired additional premises in Chelsea Harbour to accommodate a growing team. The extra space will create two more meeting rooms, as well as further administration and IT accommodation. During the next two months we will be redecorating our existing offices and fitting out the new ones. We hope to move into our new offices later in the summer.

New corporate literature

This is the second edition of the new look Investment Update, and I hope that this fresher look meets with approval. We have also recently refreshed our principal corporate brochure. If you would like to see a copy, or have friends who may be interested in seeing it, please let us know.

Risk Warning, Disclaimer and Authorisation
The value of investments, and the income arising from them, can go down as well as up, and is not guaranteed, which means that you may not get back what you invested.

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