Growth Fund Newsletter Issue 46 - February 2012

The Time to Buy and The Time to Sell - by Ross Jones & Tom Winnifrith

The time of maximum pessimism is the best time to buy and the time of maximum optimism is the best time to sell.
John Templeton

As we move into a new year the issues that pulled down 2011 are still firmly with us, but sentiment has, given the Federal Reserve's intentions to pump more sugar into the market, picked up. The EU debt worries do however remain, and the most recent Sovereign credit downgrades were not a shock. As a result of the continued issues in the EU, for the time being, the investment world's gaze has been taken away from the ever increasing debt that the US is running - which is arguably more worrying that the EU situation - the amount of money owed by the US now easily exceeds $15 trillion. This is comfortably more than the value of all of the goods and services produced in the country in one year. But the level of debt is still set to move higher, with current Federal Budget projections indicating that the debt pile will exceed $26 trillion in a decade from now. This means the US economy will need to grow at circa 6% a year to keep pace...

The US's debt position puts the country in the company of stalwarts of debt, such as Greece, Ireland, Italy and Portugal, yet investors continue to flood into US Treasuries. Here in the UK we are not really any better off in terms of lowering our debt, but on the 10th of January 2012, the UK's Debt Management office sold GBP700 million worth of debt securities, set to mature in 2047, which adjusted to exclude inflation, were sold at an effective rate of -0.116%. What this highlights is that investors are actually accepting a small loss in real terms in exchange for lending cash to, in this instance the UK. But on a wider view, this directly applies to US too (this is without even contemplating the long term decline in the value of the Dollar).

However, the madness continues and the US is still seeing relatively strong demand for its debt, but with rates expected to be kept at record lows until at least 2014 following the Fed's most recent comments, investors are effectively paying the US to let them lend it funds - this is clearly good news for the US in the short term, but devastating for its creditors. Rates will however not stay low through to 2014 without continued intervention and this is one reason why we believe that in the first half of this year (if not the first quarter) the US will kick off a further round of what is now commonly termed Quantitative Easing.

A further motivation for the Doves is the US unemployment rate. The fact that it has recently dropped off to c8.5% (clearly nothing to do with increased employment over the relatively busy Christmas period) provides ammunition to continue the monetary policy led assault on the stubbornly high figure. Fed Bank of New York President William Dudley has recently voiced his support for further initiatives to bring down the level of people currently unemployed: *'Because the outlook for unemployment is unacceptably high relative to our dual mandate and the outlook for inflation is moderate, I believe it is appropriate to continue to evaluate whether we could provide additional accommodation in a manner that produces more benefits than costs'*

So when further QE eventually comes what will it mean for you?

Looking back; in the months immediately after the announcement of previous bouts of QE, after a teething period, equity markets strengthened significantly, and the balance of risks perceived by market participants surrounding equities (implied by option prices) became increasingly more positive. That is to say that QE was, from a general equity investor's point of view, beneficial - as can be seen from the below graph which charts the movements of the wider FTSE 350, the AIM All Share, the S&P 500 and the Nasdaq.

Looking ahead; as QE hits, we believe larger players will move their cash away from low yielding asset classes such as Bonds, front running Federal purchases of government debt (and potentially mortgage securities), using the proceeds to pile into equities and higher yielding debt as a means of improving returns. Furthermore, we also believe that looking into 2012, leveraged investors such as PE firms, Hedge Funds, etc able to borrow money at low rates, will look to up their activity and pick up companies/stocks with high earnings/free cash flow yields.

In addition, we expect QE to be executed by the ECB as a means of stemming the flow of Eurozone blood. But as monetarists we know that the above will not come without a catch. In the long run the impact of deployment of untested, loose policies is an unknown. But what we can be sure of is that QE is set to bring significant inflationary pressures.

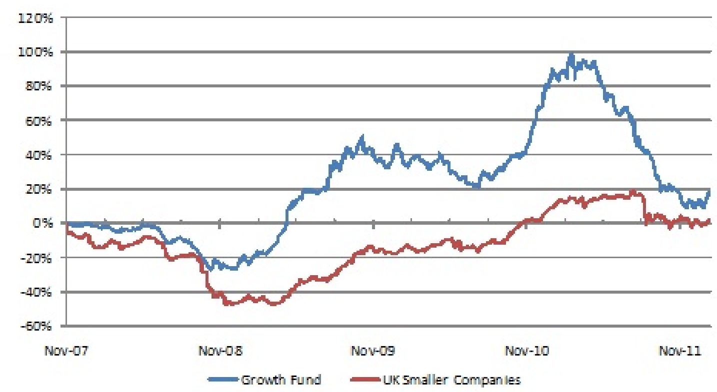
Gold has reacted accordingly - shooting to where it currently trades at circa $1745 an ounce, and in light of the relatively clear intentions of Western governments we have increased our exposure to Gold. We have bought more shares in; the soon to be producing (even after a short delay), small cap miner; **Ariana Resources**, and what we believe to be, currently, the best risk reward play around; Norseman Gold. Furthermore, we have upped our exposure to oil through, notably, **Northern Petroleum** (which was commented on in The Independent recently), and on a wider view continue to invest where we believe above average earnings growth will be delivered. We have recently bought more **Skywest** (see below), and picked up more **Symphony Environmental**. Furthermore, we have also kicked off a new position in a biotech company that has the potential to be a very exciting portfolio member - **Plethora Solutions** - this is most definitely one to watch. Brokers value the stock at c24p, Jim Mellon recently joined as a non exec and we have been hovering up any loose stock we can get at c3.5p.

It is our view that, in what will be a period of high inflation coupled with anaemic growth in the Western world, companies able to offer above average earnings, and strong cash generation, will be rewarded in terms of market valuation - see **Stanley Gibbons** below, where we have also bought more stock recently. Given the current low levels of liquidity within the small cap market it is our view that prices have the potential to move rapidly (a clear example of this is **Forbidden Tech** which has, since releasing news of a cracking deal with Youtube, seen its shares jump by more than 180% to its high). Over the last week we have seen more activity come back to the smaller market and as previously discussed we have seen Directors put their money where their mouth is and pick up stock in the secondary market - **Pivot Entertainment** being one such example. We are happy to see more liquidity returning to the small cap secondary market and believe that we are well positioned moving forward.

Benchmarking

Fund launched 22/11/2007

Cumulative Return Since Inception Source: T1ps IM



Cumulative Performance Table Source: T1ps IM

	1m	3m	6m	1y	2y	4y	Inception
Growth Fund	4.5%	-2.9%	-26.3%	-36.8%	-13.0%	19.1%	17.3%
UK Smaller Companies	7.0%	5.5%	-7.2%	-4.5%	26.7%	24.2%	7.8%

Discrete Performance Table Source: T1ps IM

	0-12m	12-24m	24-36m	36-48m	48m-Inception
Growth Fund	-36.8%	37.7%	72.9%	-20.8%	-1.5%
UK Smaller Companies	-4.5%	32.7%	53.8%	-36.3%	-13.2%

Past performance is not a reliable indicator of future performance

Coining it in... company comment

The combination of record low interest rates, market volatility and future uncertainty has driven an increasing number of investors outside of the box when it comes to wealth enhancement and investing for the future. One of the beneficiaries of this move has been; **Stanley Gibbons** and the company's update on trading, released, on 16th January 2011, confirmed that the financial performance for the year just ended (31 Dec 2011) was broadly in line with expectations showing growth in sales, profit and cash generation.

The company offers investors a route to alternative investments such as rare stamps and coins, and has over the last year upped its marketing push and investment spending as a method of widening its reach, resulting in the recruitment of new high net worth clients and an intensified move out into Asia. As a result Stanley now finds itself with an order pipeline materially better than this time last year (which itself is a strong comparable). Since the first stamp was issued in 1840, what we typically see as everyday items, have grown to be one of the World's largest and best known alternative investments - assuming a Penny Black was purchased in 1840 and held until 2010, this classic would have returned 11.1% per annum.

That said, Stanley Gibbons is the market leader in the stamp collecting world, and out of the company's Strand showroom, it stocks more than 1 million stamps and a range of specialist items from across Britain and the Commonwealth. The main operations of the group involve dealing in, amongst other items; stamps, coins, banknotes, military medals, autographs, and rare records (and related memorabilia), and over the last five years the company has refined its business, and delivered consistently strong revenue, Earnings per Share, and Dividend growth.

For the six months to 30th June 2011, turnover powered ahead, when compared to a year earlier, by 25.5% to GBP14.951 million. But as a result of higher IT costs in support of website development, and an increased non cash depreciation charge in respect of the Strand refurb costs, underlying profit did not mirror the revenue growth exactly - EPS came in up 11% at 6.18p. In terms of pre investment spending cash generation, cash from operating activities came in at GBP1.8 million. But as a result of a number of exceptional buying opportunities during June 2011 (a top quality GB stamp collection became available) the firm buried GBP0.9 million into stocking up its inventory. This saw net cash from operations come in at GBP0.9 million.

The first half of the year itself was a serious building block for the company and has firmly put in place the support needed to ensure future growth in what is a changing and challenging marketplace. Growth in the rare collectibles market is, for a large part, coming from the East, and in terms of the second half of the company's year Stanley focused the bulk of its attention on the opening of its new Hong Kong office and increasing its presence in the region. This is not without good reason seeing that a block of four stamps from the Cultural Revolution recently fetched circa $1.15 million at an auction in HK. As at 16th January it is clear the investment in Hong Kong has already begun to pay off with, over the last quarter, the new office adding a stream of fresh revenue and delivering a profit in its first three months of operations.

Away from the geographical expansion, the company has been developing its online trade offering, which is expected to bring in a completely new area of business. We see the internet and e-communications with clients as a key dynamic moving forward and believe that it will increasingly become the company's primary sales channel.

Currently trading at 179.5p, giving it a market cap of GBP45 million, when the prelims (31st Dec 2011) are released towards the end of March, Stanley Gibbons should report revenues 10% higher at GBP29.4 million, and a c9% increase in both underlying EPS, and DPS, to 17p, and 6p, respectively. This sees the shares currently offering a prospective yield of 3.3% and trading on just 10.5 times FY12 earnings. For a highly liquid (in terms of asset backing), nichey company, that is likely to deliver quality earnings growth in an anaemic growth environment, and that had, as at the half year, almost half of its market cap covered by quality inventory, and wider net current assets of GBP18.76 million, plus no material debt of note, the current valuation is by no means 'toppy'. We recently bought more given that the company adds both good value and liquidity to our portfolio.

As noted in the Editorial we have recently bought more Australian regional airline, **Skywest**. We believe the new Charter contracts, with notably BHP Iron Ore and Bechtel (Chevron's engineering/design partner at the vast on shore gas Wheatson LNG project), coupled with the ten year alliance with Virgin Australia, will, over the next 18 months transform the company's standing and lead to an enhanced level of profitability. Early evidence of the top line impact of the above was provided on 15 December 2011 when the company noted that it expected revenues for the half year to 31st December 2011, to be 20% higher than a year earlier at GBP75 million (S$150m).

Furthermore, on 11th January 2012 the company announced its December Operating Statistics which showed Charter Services up 23.57% to 325. One of the key downfalls previously has been the company's exposure to fluctuating fuel prices, and although this risk still remains with the standard scheduled routes, the increasing number of charter contracts allows the company to partially negate this risk.

In addition to the increased charter contracts the company noted on the 26th January 2012 that a further two aircraft, making up part of the Australian Regional Airline Network (ARAN) with Virgin Australia, had been delivered. This now means that there are six new ATR72-500's in operation, which is key as it simply has only been the lag time in receiving aircrafts which is delaying this project shooting on ahead.

We bought stock ahead of the half year results, which should be published on 10th February, and expect the company to report EBITDAR in the region of (assuming a flat exchange rate) between GBP15.6 million to GBP16.6 million and NPAT (net profit after tax) of between GBP2 and GBP2.5 million, equating to (assuming bottom of the range) 1p of EPS. For the full year we reckon that EPS of 3p are comfortably realisable (it should be noted that our forecasts are below market consensus which the company has neither confirmed nor denied given the unpredictable nature of the airline industry).

At 25.5p Skywest is currently valued at GBP51.6 million and trades on 8.5x this year's projected earnings. For the FY13, given the increasing fly in fly out charter services and the developing ARAN project gaining traction, EPS of at least 4p should be achievable. Underpin this solid earnings grow with a tidy yield of c3.9% and the shares look good value - 10x FY13 EPS (40p) would be a good start.

Tom Winnifrith & Ross Jones

Fund Information	
Size:	**£13,379,100.20 (01/02/12)**
Launch date:	**21 November 2007**
Launch price:	**£1.00**
Current Yield:	**0.00%**
Legal Status:	**OEIC**
Annual Management Fee:	**1.5%**
Initial Charge:	**5.25%**
Minimum lump sum Investment:	**£1000.00**
Minimum monthly investment:	**£25.00**
Sedol Number:	**B28R5W3**
Unit offer price:	**Single Priced Fund Last Dealt Price: 115.99 (01/02/12)**
Unit bid price:	**As Above**

Top Ten Holdings (as at 15/12/2011)	
Stock name	**% Fund**
Pivot Entertainment Group Plc Ord 2.5p	**9.25**
Avisen Plc Ord 1p	**8.32**
Forbidden Technologies Plc Ord 0.8p	**6.19**
Intandem Films Plc Ord 0.1p	**5.62**
ILX Group Plc Ord 10p	**4.87**
Ascot Mining Plc Ord 1p	**4.82**
Rivington Street Holdings Plc Ord 1p	**3.77**
Mirada Plc 10% Secured Convertible Loan Stock 2015	**3.74**
Nexus Management Plc Ord 0.25p	**3.73**
Minoan Group Plc Ord 1p	**3.45**

How to Buy Growth Fund Units

1. You can deal through www.JPJShare.com at the initial fee rate of 2%. Simply call 01624 641 301 or email admin@jpjshare.com for more information.

2. Contact your broker. Most brokers offer the chance to buy units although few can match the JPJ initial rate of 2%. If your broker will not deal please call Sarah Read on 01624 641 318 and she will try to rectify the situation.

3. Deal directly through t1ps and The Share Centre at the initial fee rate of 2.5%. If you want an application form email growthfund@t1psim.com or go to www.t1psim.com.

Once you have made an initial investment (of as little as £1000) you can set up a monthly standing order with The Share Centre to drip feed further cash (as little as £25 a month) into the fund. All existing fund holders can set up such an order.

If you have any questions about investing in the SF t1ps Smaller Companies Growth Fund please contact Sarah Read on 01624 641 318 or email sarah.read@t1psim.com.If you would like a simplified prospectus and an application form please visit our website at www.t1psim.com or email growthfund@t1psim.com.

Risk warning:

The value of your investment can go down as well as up and you may not get back a significant proportion of your investment. Past performance is not a reliable indicator of future results. If you are in any doubt as to the suitability of an investment, you should seek independent financial advice. *Please remember that the tax treatment depends on the individual circumstances of each investor and may be subject to change in the future.

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