

FUND MANAGEMENT DIARY
Meeting held on 21 February 2012

Long-Term Re-financing!

After the numerous summits of EU leaders, in the early hours of this morning, the news that Greece had secured the €130bn rescue fund was announced to the world. Our diary has covered the lead-up to this event in detail and the deal confirmed that while the money would be provided, it would be covered by the escrow arrangement so that repayments of debt would receive priority. Officials from the EU and IMF will pay the funding for civil servants and government machinery, subject to the austerity terms being met.

The conclusion was that by 2020, the debt to GDP ratio would be reduced to 120.6%, being at the margin and this effectively means that Greece is now on a life support system and there is little chance that a third bail-out would be provided in the future. While the expectation is that the elections in April will result in a complete change in government, the Eurozone seemed to be confident that the agreed arrangements will provide little or no 'wriggle room' for the Greeks to manoeuvre themselves out of the tight fiscal constraints.

While this has bought time for the EU, it is in our opinion, a shame that little has been done to endeavour to engender growth into the Greek economy, so that they at least have some chance of becoming a useful member of the European Community. We have, in a previous diary, stated that when Germany was on its knees after the Second World War, the Allies led by the USA, Canada and the UK, looked to rebuild their economy through the combination of the Marshall Aid Plan and providing the expertise to their manufacturing industries, through secondment of top executives, despite the needs of the domestic economies, especially the UK which had suffered huge war damage. If the Greeks are to get out of their position, then the EU must also help to stimulate GDP growth and to fail to do so, is likely to lead to the inevitable failure with all the consequences!

There is little doubt that the Greek bail-out has only been made possible due to the action of the European Central Bank in making available easy credit to the banks through their offering of credit at 1% over a three year term, subject to collateral. This procedure is now being referred to as LTRO (Long-Term Refinancing Operation) and with the second tranche now being made available for the end of February, it is expected that European banks will be looking to take up between €550-650bn. The announcement is due by around 3 March 2012, with the sum likely to be near the latter figure and therefore the total funding is likely to exceed €1.1tr.

The effect of this quantitative easing by the back door, has applied sharp downward pressure to interest rates in the Eurozone following the leads previously seen in Japan, the USA and UK. The consequences of this are that although banks have now rebuilt their balance sheets the ECB is now a major holder of collateral, while the

retail banks have become further restricted in the amount of money they have available to lend to the private sector. Furthermore, as the banks are no longer holders of the senior bank debt, which is effectively being relegated to junior status, this is adding up to structural subordination. There could certainly be a serious risk in the future that credit lines could dry up. Currently, as corporates have built up their cash reserves, the returns on high yield bonds have dropped to levels below which some sovereign countries are able to borrow, such as: Spain, Portugal, Italy and Ireland. This position is undoubtedly unhealthy for expansion, especially the small and medium enterprises which are being starved of funding and this is the sector which needs to recover, if GDP growth in the main economies is to be stimulated.

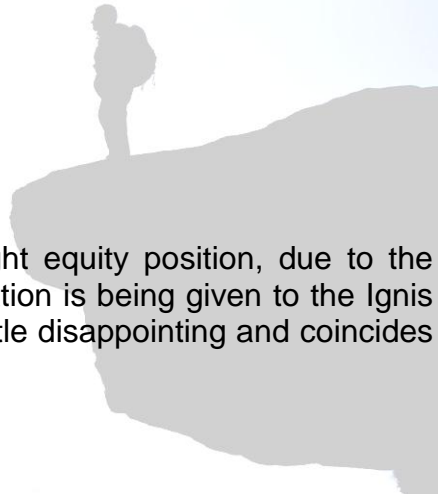
The old fashioned idea that banks obtained their money from savings and then made a turn by lending into the economy, is becoming something of a relic. However, in the opinion of the Margetts Fund Management team, a restoration of traditional financial practices would be desirable, when banks made judgements on the soundness of their lending policies while endeavouring to attract savings deposits, through the competitive market!

The latter position has been thrown all the more into sharp focus following recent abuses in the LIBOR (London Inter-bank Offer Rate) market in which leading banks manipulated the rate by providing false data. This rate is normally calculated from a panel survey of banks, in which the in-built safeguard was provided by exclusion of top and bottom rate estimates. However, as these were estimates, unscrupulous data was provided, with a view to distorting the figures. Given that this is a £30tr market, even a small differential could lead to huge gains and in this case, it appears that there was a downward manipulation, which was against the interests of savers. In view of our above remarks concerning interest rates and savers, the last thing the market needs is this type of behaviour.

The single most important factor required by Western economies at this time is for faith to be restored to the banking system and for a return to be made to traditional values and it is our opinion that this is the area that governments need to work on if they are to restore confidence to the market.

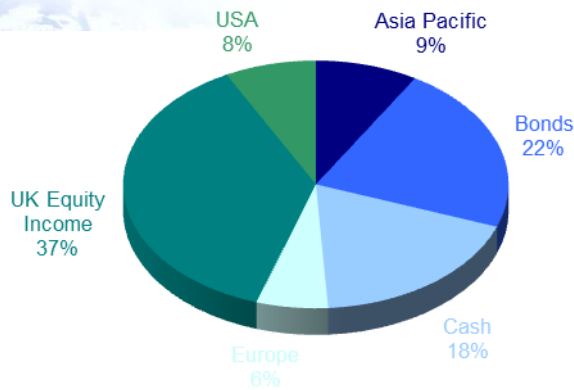
Strategy

We continue to advocate equities as the principal asset of choice, particularly in companies with sound traditional governance in which earnings, profit and value for shareholders is of particular importance. We remain cautious of bonds, given the artificiality of markets at this time, but within certain specialist elements, there are bargains available.



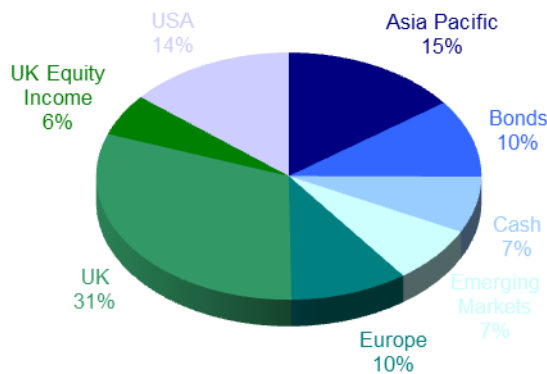
Providence

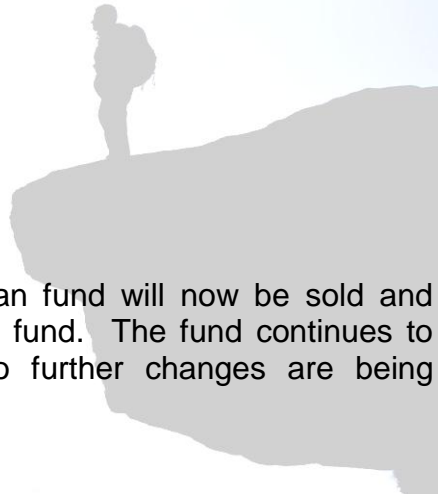
The fund has continued to benefit from an overweight equity position, due to the ongoing recovery in global equity markets. Consideration is being given to the Ignis Argonaut European Income fund, which has been a little disappointing and coincides with a significant change to the group structure.



Select

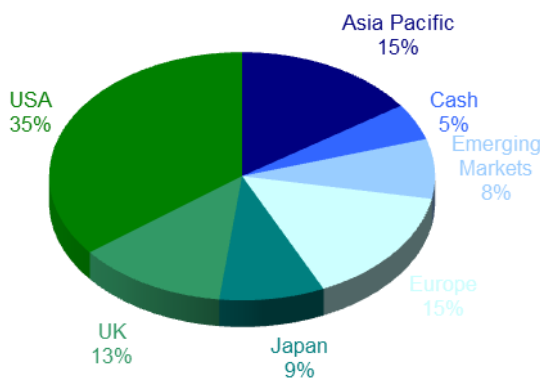
The Blackrock Continental European fund has recovered strongly following the comments made last week, but it remains under review. Consideration continues to be given to the Asia Pacific holdings and specifically the Ignis fund, where we have concerns with regard to the group structure, as commented on previously.





International

Following our previous comments, the M&G American fund will now be sold and replaced with the AXA Framlington American Growth fund. The fund continues to benefit from a recovery in equity markets and no further changes are being considered at present.



Venture

The Venture fund remains fully weighted in all its strategic areas and the underlying funds are performing in line with our expectations. No changes are being considered in the immediate term.

