UKSA
UK Shareholders' Association

FRC - Sue Milton's take

FCA's Investment Market Study

Investment Trusts: more from Roy

The Private Investor

Chairman's Comment

In terms of UKSA's main aims the two months since the last TPI have been the most active in my experience. The lid on corporate governance that Theresa May opened in her first statement as prime minister allowed all sorts of issues to crawl out of the box, many close to UKSA's heart. It impelled the department of Business, Energy and Industrial Strategy (BEIS) to produce a Green Paper: Peter Parry reports on UKSA's response on pages 14 and 15. The Financial Conduct Authority (FCA) issued a consultation document on the practices of the fund management industry, again raising long-standing UKSA issues, and Martin White reports on UKSA's response on Pages 4 to 7. Martin was also in the happy position of being able to point out that many of the points raised had been covered in a private paper he submitted to the FCA in 2012, which had not even been acknowledged and which certainly generated no discernible action. Now, five years on, they are presented as fresh and new. Martin took full advantage of this irony in his UKSA submission.

The Financial Reporting Council (FRC) – the body actually responsible for corporate governance regulation – woke up and promised a major review of the Corporate Governance Code, to include input from a 'Stakeholder Advisory Panel'. This comprised a long list of stakeholder organisations, some only thinly relevant, without mention of private investors at all. This wonderful Freudian slip (the regulations and guidance notes themselves always refer just to 'investors' without defining what the word means) enabled me to write a blunt letter to the FRC Chairman, Sir Win Bischoff, that extracted a grudging response inviting a joint representative of UKSA/Sharesoc onto the Panel.

And that's by no means all. The FRC (which also regulates the audit profession) is beginning to respond to suggestions that all is not well (see Sue Milton on page 8); Martin White signed for UKSA a Green Paper submission from Sarasin Partners that included a forensic attack on modern developments in accounting standards; and various initiatives from various bodies show they are beginning to grasp the fact that increasing regulated disclosure tends to decrease usable information.

You will have received the AGM papers, including the survey questions on our future relationship with Sharesoc. I am extremely keen to get a wide and honest response to these, and that you do not just save your comments for the AGM. Attendees are inevitably mostly fit Londoners. The Board will make its decisions based on the views of *all* members, as expressed for the survey, and not just on the views of those who attend.

These decisions will also be based on the practicalities. UKSA is short of the volunteers necessary to do all we want to do, and this includes people willing to serve on the Board. I shall be stepping down as Chairman at the 2018 AGM, and also as Finance Director; the existing directors cannot consider the chairmanship without a substantial reduction in their existing roles.

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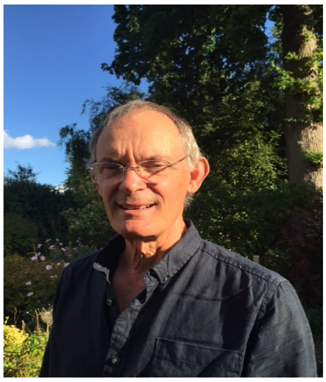
In this issue…

I would welcome a discussion with any of you who are interested in joining the Board, or taking up any volunteer roles, without commitment. The availability of suitable resources within UKSA will affect any decision we may make on involvement with other organisations.



John Hunter Chairman

Just room to congratulate Helen Gibbons on her appointment to ESMA's Consultative Working Group (see below). She continues the UKSA involvement initiated by Roger Collinge. As those of you with email will know Helen has also taken on additional work within UKSA – the notice below went out from me in January.

On the debit side I regret that Paul Waring, who has helped UKSA in different ways for a number of years, has asked to step down from looking after the NW region. This is for the best of all possible reasons – his business is developing faster than expected. Julian Mole of NE region has volunteered to look after NW region for the time being.

The following email went out from me in January:

'I am delighted to inform members that Helen Gibbons - who is UKSA Director, Europe, and our representative on the board of Better Finance - has agreed to additionally become Media Director. She will manage all aspects of UKSA's media presence, including design and content and with particular emphasis on social media, and be a contact point for media briefings. This function has been conspicuously absent from UKSA's armoury.

For those expecting instant miracles I would remind you that Helen works full-time as a self-employed translator of European languages into English in the fields of finance and governance. We are extremely grateful for whatever help she can give us.'

There are many references to UKSA papers in this edition. The easiest way to find them on the website is to look at the news stories on the front page and click on the relevant links.

Good luck!
John Hunter
Chairman

Helen Gibbons

Helen Gibbons, UKSA's Europe and Media Director, has been selected to serve on ESMA's Consultative Working Group (CWG) for the ESMA Corporate Reporting Standing Committee (CRSC). Helen succeeds UKSA member Roger Collinge, who has served on the same working group over the past two years.

ESMA is an independent EU Authority, based in Paris, that contributes to safeguarding the stability of the European Union's financial system by enhancing the protection of investors and promoting stable and orderly financial markets.

The CRSC carries out ESMA's work on issues related to accounting (under IFRS), audit, periodic financial reporting, electronic reporting developments and storage of regulated information. CWG members are expected to provide assistance on the CRSC's activities, such as providing input on its working programme and projects, the draft regulatory technical standard on requirements of the Transparency Directive, the establishment of common enforcement priorities, application of Guidance on Alternative Performance Measures, issuance of comment letters on new IFRS, etc. Membership of the working group is open to nationals of an EU member state. The position requires attendance twice a year at the working group's meetings in Paris.

The FCA's Asset Management Market Study

by Martin White

Martin White
UKSA Director

In November last year, the Financial Conduct Authority, FCA, published a very substantial 200 page "interim" report, and the annexes are in addition and even longer. But, in spite of the length, we welcome it!

The report was the outcome of a large research project into the operation of the asset management industry, primarily from the perspective of the customers – us. The conclusions were what we already know – that the industry is massively profitable, but that the customers generally get a poor deal and, most importantly, are significantly poorer in retirement as a result. They also concluded that active management was generally not worth paying for, that investors in cheap passive vehicles did better, and the fact that the FCA had come out saying this caused consternation throughout the industry.

So well done the FCA. Using colourful language of my own, I would say they have exposed the world's most profitable con trick, the asset management industry, for what it is. There was a fair bit of press coverage of the report following its publication in November, so you might have noticed the story back then.

Now before I get into more trouble, there are a few things I must say. I'm not criticising the good intentions of individuals working in the sector. And I'm not saying there is no place for employing investment managers to make decisions for you, which is what active management is. There clearly are a few investment managers who outperform the overall market. But they are few, and what happens with them is they get so much money to manage that they either stop outperforming, or they have to close their fund to new money.

Incidentally, some of us believe that it makes huge sense for us to dodge the financial sector as much as possible, make our own investment decisions, and avoid paying an annual percentage of our wealth to anyone. But the financial sector puts out the subtle message that it's all too difficult for individuals to manage their own affairs. And all arms of Government seem to ignore the role and importance of the individual as investor. But we are definitely not giving up on this. It was one of our criticisms of the FCA's recent study, as you will see later in this article.

You can find the FCA's report at https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf Responses to the report were requested by 20 February 2017.
As a member of the UKSA policy team, I was the main author of UKSA's response to the FCA's interim report, and you can find this response in full on our web site at http://www.uksa.org.uk/sites/default/files/2017FebUKSA_AssetManagementStudyResponsePDF.pdf

Our response: two parts

There are two parts to our response, which I need to explain. The first takes the form of a 6 page letter signed by me as an UKSA director. And "we" in this letter means UKSA. But as part of the response we also attached a nine page document which I personally had submitted to the FCA before it was formally in operation and signed by me; "I" in that other document means me. I was not an UKSA director at the time, and as the entire thing was to express my personal views I was very careful to emphasise that I was not speaking on behalf of anyone else. Members' comments to the editor would of course be very welcome!

A few words on my personal submission of December 2012

This current article would be too long if I were to say much on it now. Back in October 2012, the document "Journey to the FCA" was issued, all about the plans and aspirations of the not-yet-live FCA (somebody must have had a sense of humour: the go-live date in 2013 was 1 April). This can still be found at https://www.fca.org.uk/publication/corporate/fsa-journey-to-the-fca.pdf. It was all well-meaning stuff, and comments were invited. On the front cover were the words "to make financial markets work well so consumers get a fair deal". I felt it was OK, but naïve in places and missing some important things, and I was worried that unless they had the necessary clarity of thought and courage, there was a risk of their being outmanoeuvred by the industry. So I put in a big effort and produced my submission.

I didn't even get an acknowledgement. I was very cross. I chased them up, to be told that it had been passed to someone in PR! Were they frightened by what I was saying? Anyway, I gave up on it at that point. I had been really keen that what I had said should get into the public domain, but none of the submissions received in response to the "Journey to the FCA" were published.

However, looking on the FCA web site more recently, I discovered that only 3 private individuals had put in responses in 2012, and it did look as if some of the points I had made were noted. And now looking at the 2016 Asset Management Study, I would argue that my 2012 response was totally vindicated and I would say that it is entirely valid today. Hence the decision to include it with the recent UKSA submission.

I will write more about the 2012 submission, which was much more wide ranging than the 2016 Asset Management Submission, in a future edition of TPI. I believe it does contain some ideas for UKSA in this David and Goliath world of individual savers and the financial sector.

Back to the 2016 Asset Management Study Report

Below I reproduce the general section of our report:

"First we would like to congratulate the FCA for shedding a light on both the profitability of active management today, and the poor outcomes for customers. We welcome this Report and generally support the analysis and the conclusions. The measured style of the published material makes the starkness of the conclusions very powerful.

The fact that journalists such as Anthony Hilton in the Evening Standard are referring to the current Report as "controversial" is a good sign that there may be a will to tilt the balance more in the interests of individual customers, or consumers.

The nature of the analysis carried out, concentrating as it has on the fund management sector, does mean that the full impact on the outcomes for ordinary savers of the way in which the financial sector works – and we mean here the total costs including advice, distribution and investment management – was not brought out in the Report. However, it is very clear from the Report that the FCA recognises this and is minded to take the issues further.

We believe that the issues identified in the Report are part of a wider set of problems in the ownership chain that lead to sub-optimal outcomes not only for individual savers and investors but also for individu-als as employees and for the economy as a whole. For those wanting a really good understanding of these problems, we recommend two books by John Kay, *Other people's money* and *The long and the short of it (the subtitle of which is "a guide to finance and investment for normally intelligent people who do not work in the industry").* The way these problems manifest themselves is perhaps best captured as follows. There are three stages in the ownership chain between most individual savers and the underlying companies which they own. The first is financial advisers, the second fund managers, and the third is the senior executives and boards of the underlying companies. The way each is remunerated is effectively by taking an annual percentage of the individual savers' wealth. This is what the methods of "incentivising" senior executives and boards of companies now amount to, and since fund managers with the votes to control company behaviour use the same model themselves they can hardly be expected to reject the theory of incentives on which executive pay now rests.

The only way to achieve fundamental change is to tackle the basic "take an annual percentage of the clients' wealth" model at each stage in the ownership chain. **This model is directly contrary to the principle of stewardship, which is what acting in clients' interests should amount to.**

The scale and the scope of the underlying problems are outside the scope of the FCA to tackle alone. But the FCA may still be the most important regulatory body here, since its scope covers both retail financial advice and financial services generally, including investment management.

Overall, we believe this is a strong and effective analysis, and we agree with the Report's main conclusions. In this letter we touch on both these conclusions and the Report's proposals for the way forward. For us, the most important conclusions of the Report are that competition is not working and that retail savers and investors in particular are getting a poor deal. It would have been helpful, however, if the Report had included at least some analysis of the opportunities available to retail investors as a whole. We believe that a "self-select" service, where you just pay the stockbroker a fixed annual charge, plus a fixed charge for each trade, and where you do not pay any fund percentages to investment advisers either, is the smart option for those with the knowledge and confidence to use it. Under this route, you don't have to select individual company stocks; you can instead buy ETFs if you wish. The trick is to avoid anything that pays a commission, in other words pretty well all the funds "promoted" on the major platforms.

The big question is how to help people make sensible choices; something is needed alongside the current "advice" model. It is our belief, given the inherent conflicts of interest between the customers and the financial sector as it currently works, that "help" is not going to come from the financial sector and it is also difficult to see how regulators can do it unaided. We think there is scope for considering how savers and investors can help each other; it is difficult to see who else there is that they can trust to act in their best interests. At the UK Shareholders Association, we will be directing some of our policy thinking in future to the theme of "savers take control of their own financial future".

UK Shareholders' Association: our perspective and motivations

To conclude, it may help to set our own perspectives and motivations in relation to the subject matter. The UK Shareholders' Association was founded in 1992 in recognition that there was no organisation to represent the interests of private investors. We are a voluntary body, modestly funded by members' subscriptions. Our members tend to be relatively sophisticated investors in that they take their own investment decisions; they tend to use investment funds, especially actively managed funds, less than the general population. We exist to help our members in the investment process, and we provide a network through which people with shared interest in investment can communicate with each other and represent their interests with outside bodies, government, etc.. However, in most of our representation activity we aim to take a more general public interest stance. There are two themes to this. The first theme is that we would like to see all individuals better informed and empowered in relation to their personal financial management, especially their long term financial planning. We believe that the scope for improvement here is considerable. We also believe that investing directly in shares would make sense for many more people than currently do so. This first theme is completely fundamental to the Asset Management Market Study. The second theme is the proper stewardship of companies, which is now very much in the political agenda (excessive executive pay, short termism, etc.), as reflected in the BEIS Green Paper. We believe that that the more people are interested, as long term investors, in the behaviour of companies, the better for society as a whole.

We believe that the operation of the asset management sector is more of a negative than a positive in relation to both of the two themes we explain above. First, it operates as a wealth extraction industry rather than as an agent working in the interests of its principals. And second, because the business model is based on taking an annual percentage of its clients' wealth rather than being truly aligned with their long term interest, there is little by way of incentive for the asset management sector to take a real interest in the quality of stewardship achieved by the boards of the investee companies. It is very important to note that there are a number of investing institutions who are exceptions to this latter point; some focus on the identification of high quality companies and holding them for long periods. Others focus on the behaviour of companies in terms of their impact on customers, the environment, their employees etc.. So there are instances where we, representing individuals as investors, work alongside investing institutions.

As well as this letter, we also attach as part of our submission a document written in 2012 addressed to the FCA in response to the document "Journey to the FCA" that was published in October asking for comments".

What Next?

Stepping back for a moment, the asset management sector is only part of what the FCA is responsible for regulating. There is the financial advice sector too. Together they affect people's lives in terms of financial outcome, but it is not sufficiently appreciated how they also affect people's lives as employees because of the short term pressures they place on companies generally.

So I would regard addressing the many problems as potentially transformative for our society. I see the corruption inherent in commission-based (especially trail commission) sales, and indeed the whole sales-driven "how much money can we make out of x", or "how can we achieve our high target return on capital" approach of the industry, leading not only to systematic customer detriment, but also leading to our whole ownership chain falling short of its potential to generate wealth and deliver it to the underlying owners. The "ownerless corporation" coined by Paul Myners exists because there is self-seeking where stewardship and fiduciary duty should be.

We will be determining what part we at UKSA should play in this essential transformation.

by Martin White, BSc, FIA
Director
UK Shareholders Association

What Does the FRC's 2017-2018 Priorities Mean for Private Shareholders?

Sue Milton

'News flash': The Financial Reporting Council will engage with readers of the Sun newspaper!
'Confession': The Public just might be right in expecting more from Auditors!
Humility in a regulator is rare but this was part of the experience when 50 or so people had a conversation on the 1st February with the Financial Reporting Council (FRC) on its proposed priorities for 2017-18. (The priorities can be found at https://www.frc.org.uk/Our-Work/Publications/FRC-Board/Draft-Plan-Budget-and-Levy-Proposals-2017-18-File.pdf, pages 5-6.)

The priorities stem from the belief that trust in business has declined to such a degree a rethink is necessary to address public concerns whilst complementing work already in hand such as corporate culture, the Corporate Governance Reform green paper and the behavioural failures akin to Volkswagen and Bhs. Somehow business and auditing professionals have failed the Public in at least two areas……

The FRC is concerned about the expectations gap between what auditors do and what the Public think they should be doing. Accessible communication that explains the role of the auditor without needing a PhD is vital to laying the foundations for trust. The aspiration to engage with Sun Readers is therefore inspiring and will help remove misperceptions.
The quality of some audits is poor. Whether produced by accounting professionals or from business assurance, mistakes and misrepresentations have been overlooked or condoned by weak challenge. It is time to listen to the Public and increase the level of professionalism in independent assurance.

This is a real opportunity for the private shareholder and UKSA. We are the Public who has both a foot in the corporate door through our share ownership and an opportunity to influence through our engagement with the CEO. The most relevant of the priorities for private shareholders are the FRC's desire to promote effective investor stewardship, encourage clear and concise corporate reporting and build confidence in auditing. Taking these one-by-one:

From a private shareholder perspective, *promoting effective investor stewardship* is the one negative element. Improving investor shareholder engagement is to be supported but, once again, the barriers to engagement faced by the private shareholder and the private investor, who is not the true owner of their shares but simply the beneficiary, is being overlooked. Nevertheless, should the FRC update the Stewardship Code, we private shareholders should review and comment, and see how we can turn proposed enhancements to our advantage to improve access and accountability. The FRC has to be applauded in
e*ncouraging clear and concise corporate reporting*. It should make producing, reading and understanding reports quicker and easier. Keep those Sun readers in mind and we will all benefit. But this is no easy ask. A reporting rethink is necessary and UKSA's collective expertise may have solutions to propose.
As the UK's Competent Authority, the FRC can now be a more proactive regulator. Enhanced monitoring, balanced by appropriate enforcement will *build confidence in auditing.* We, as private shareholders, can only benefit from improvements in audit and assurance.

To sum up, we need to use the FRC's priorities as an opportunity to create a virtuous circle. Rebuilding genuine trust is important for UK plc as it provides us with a competitive advantage. BREXIT intensifies that need. If we play our part, not only can we support UK plc but also enable UKSA increase its influence on companies for the benefit of private shareholders and the wider private beneficiary community. Power to the People!

By Sue Milton

William Bernstein

by John Hunter

I am a great fan of William Bernstein (www.efficientfrontier.com). His book 'The Intelligent Asset Allocator' (TIAA), now some 20 years old, turned the light on for me when – post-retirement – I was attempting to turn my professional understanding of investment analysis in the corporate world into what I discovered was the very different science of personal investment. I was encouraged in my admiration by the fact that he was (and to some extent still is) a practising neurologist, i.e he has a scientific training but his advice is unconnected with the means by which he makes a living. Translation: he's not trying to make money out of me. Further translation: he's not a part of the financial services industry. He also lives in Oregon, encouragingly remote from any well-known financial centre.

TIAA is about one leg of the investment process, but one that he shows is ten times as important as stock selection or market timing. But it also contains the seeds of his total investment beliefs which he has since encapsulated in a series of books, but also condensed into a simple (well, fairly simple) road map for savers, most completely explained in 'The Four Pillars of Investing' – described as 'aimed at the liberal-arts major seeking investment competence' (revised edition 2012). He has since turned his attention to advice for millennials in a snappy 20-page pamphlet 'If You Can: how millennials can get rich slowly' which re-presents his four pillars as five 'hurdles', the new first hurdle being something so obvious it didn't need stating in the 'Four Pillars' but possibly does for millennials. In his own words these are:

If you can't save you'll die poor
Finance isn't rocket science but you'd better understand it clearly
Those who ignore financial history are condemned to repeat it
We have met the enemy and he is us
The financial services industry wants to make you poor and stupid

Bernstein has a weakness for the aphorism (which on the plus side makes him fun to read) and another weakness in that he writes in American so I would translate these, less catchily, as:
The first stage in the investment process is to spend less than you earn
There are some technical matters that you have to learn
You need a knowledge of the history of finance to learn certain essential lessons
(I'm not totally convinced by this. You can certainly learn a lot from the history of the great market cycles but I suspect you can get along without it – I wouldn't put it on a level with the other four hurdles. I suspect Bernstein was persuaded by his great interest in financial history to give himself an excuse to write about it)
We have behavioural biases that work against us making good investment decisions
The financial services industry can only make money out of YOU – it redistributes the wealth created by others and therefore collects rent; it does not create wealth.
If you are not stupid you can avoid paying the rent

In my own primer on investment basics I have my own set of nine key facts. They are:
Investment principles are immutable but implementation is a personal matter.
The difference between saving and investment is a false distinction; both are just an absence of spending.
Return and compound interest: small differences in return matter.
Risk is a consequence of uncertainty and is personal to the individual investor - a measure of personal disappointment at unfavourable outcomes.
Every 'investment' is a choice between alternatives and a bet on relative outcomes.
The market delivers a return premium to the investor for taking on uncertainty.
For every buyer there must be a seller; therefore the market is a zero-sum game as between total participants.
Identify misinformation before making a decision.
Diversification is the only free lunch.

I can just about persuade myself that Bernstein finds a place for these thoughts under each of his five headings. I certainly hope so. What are *your* investment basics? ***by John Hunter***

Investment Trusts - a Primer Part 3

by Roy Colbran and George Miller

In the final part of the series on Investment Trusts we are, as promised, providing a few brief notes on individual investment trusts with which we are familiar. These are just a few ideas for ones that you might like to look at if you are thinking of beginning a portfolio of investment trusts. They are, of course, not in any way investment recommendations and there is no particular significance in the inclusion or exclusion of any trust. They are just an attempt to give you a selection of various types. We have split them into general trusts which we would expect you to look at as a starting point and specialist trusts.
Portfolio distribution figures are at the last year, or half year end, whichever is the later. Although comments on performance are included, do remember that past performance should not be taken as a guide to the future.

A. GENERAL TRUSTS

Foreign and Colonial

We are starting with the oldest and first-ever of all the investment trusts, founded in 1868 and among the really large ones. It's a global trust and had only 6.6% of its portfolio in the UK. It has performed steadily over the years almost but not quite matching the MSCI World index and well ahead of the All Share. The management fee is only 0.365% of asset value (although this gave rise to a charge of £9 million in 2015). Despite this ongoing charges were 0.80% largely because of the cost of managing the private equity portfolio which is 9% of the total. Despite strenuous buying back of shares it still trades at a significant discount.

City of London

In contrast this large trust had only 13% in shares listed on overseas exchanges and concentrates on FTSE 100 shares although biased towards international companies. It prides itself on low charges with an ongoing charge of only 0.42% - one of the lowest now available. Although ahead of key UK indices, performance has been nothing like that of Foreign and Colonial yet it regularly trades at a small premium. This is possibly because it's a good safe fund to have in one's portfolio and cheaply run.

Bankers Trust

Another global trust with just 27.5% of its assets in UK shares and one that keeps costs low with an ongoing charge of 0.52%. In the last financial year it expanded somewhat as another trust run by Hendersons was liquidated and one of the options that shareholders were given was to move into Bankers Trust. Performance has been distinctly better than City of London if not quite as good as Foreign and Colonial. It tends to trade at a small discount.

Alliance Trust

Readers can hardly have failed to notice all the activity surrounding this Trust in the last few years. Performance on a self-managed basis had been somewhat lacklustre and the fund traded at a large discount. Activist investors Elliott Advisers bought a large slice and pressed for substantial changes which at first were resisted but in the event resulted in the departure of the Chief Executive and Chairman and a new board. A new policy is now being instigated whereby Willis Towers Watson take overall control, under the board, with a multi-manager approach, starting with eight managers all given a relatively free hand. A deal has been set up whereby the Elliott shareholding will be bought back thus removing that outside pressure. Great things are promised from the new approach and ongoing charges will be kept down to 0.65%. The market appears to believe in it since the discount has now dropped dramatically although some of this will be due to some fairly aggressive buying back of its shares.

Scottish Mortgage

This is now the largest of all the trusts with assets at almost £5 billion. Despite its size, it has consistently achieved an outstanding performance. North America makes up 49.6% of the portfolio with only 4.3% in the UK. At the top of the table of investments are a few companies where the individual holding is a significant part of the total. Thus Amazon represents 10.8% and Illumina 7.6% of the portfolio. It would seem to follow that the performance is vulnerable to something going wrong in just a few companies. Ongoing charges are also low at 0.45%. Not surprisingly in the light of its record it regularly trades at a premium. It's one we are very glad to have in our portfolios.

Witan

This is another large old-established global trust founded in 1909. After a period of poor performance it changed, exceptionally, to a multi-manager approach. A Chief Executive was employed to choose the managers and allocate money among them. The idea is that the managers are specialists in particular areas rather than having one manager handling everything. At the end of the last half year they had 10 managers plus about 10% of the portfolio held directly. Witan shares stood at a big discount for a long time and it has been the most active of all the trusts in buying back its shares. The number of shares in issue is now less than half of what it was when they started the process some 12 or 13 years ago. The discount has reduced although we suspect this is because the market came to believe in the multi-manager approach rather than because of the buying-back process. The multi-manager approach does not lend itself to low fees and the ongoing charges figure for 2015 was 0.99% including performance fees.

Law Debenture

This is an exception to the general pattern in having a professional trustee business running alongside the investment trust activity. The business makes a distinct contribution to income and it often seems that the share price does not fully reflect the value which it adds. Although it calls itself a global trust, 71.4% of its assets were in the UK at the last half-year end. This is another one priding itself on low cost with an ongoing charge of 0.46%. It has continuity of management in that James Henderson has managed the trust for many years. Long-term performance has been good but it has slipped a bit in more recent years.

B. SPECIALIST TRUSTS

Here we have a small selection to give just some idea of the range available. There are also, for example, single country trusts including China, Russia, Brazil and many more. Generally expenses tend to be higher than for general trusts, possibly to allow for higher research costs.

Caledonia Investments

This £1.7 billion self-managed trust is controlled by the Cayzer family and they directly or indirectly own just short of 50% of the shares. In contrast to mainstream trusts, they operate through five investment 'pools' where the largest is in the unquoted sector. They also have an exposure to hedge funds. They are quite prepared to take a large equity stake in a private company if they know the operators and be a supportive and long term investor. This has brought them some unusual investments. For instance at their year end on 31 March 2016 their biggest investment was in a privately held caravan park operator. Ongoing charges are relatively high at just over 1%. The shares usually stand at a substantial discount possibly because performance has not been outstanding.

European

This is a medium-sized trust investing entirely in continental Europe which could make it an interesting part of a portfolio in the light of Brexit. For a specialist trust it is economically run with an ongoing charge of only 0.6%. The years 2006 to 2011 produced poor performance with the NAV dropping considerably. Since the Brexit vote performance in sterling terms has been helped by the exchange rate movements. Apart from that, it has not been brilliant since the managers' value-based approach has not been favoured in the market. The shares trade at a considerable discount.

Herald

Another medium-sized trust concentrating on technology and media companies of which 56% are invested in the UK. Katie Potts, who is a graduate in Engineering Science, has been managing the fund since it was launched in 1994 and is Managing Director of Herald Investment Management Ltd which was established to manage the fund. The ongoing charge rate is 1.08% which is not unexpected for a specialist trust. As one might expect with such a specialist vehicle, performance has been a bit more erratic than with some of the general trusts but overall quite satisfactory. As we write the shares stand at a discount of 18.0%.

RIT Capital Partners

This is a large investment trust (£2.5 billion) run by the Rothschild family. Lord Rothschild and his family trusts own about 20% and it has had an excellent record over the years. It is run as an absolute return fund, that is it seeks to return a profit come what may. On the whole it has done that by investing in funds from around the world, each with very different characteristics, and often unquoted on the main stockmarkets. These would be difficult for the private investor to gain access to on his own and we assume the Rothschild name has helped. The usual generalist trust will normally stock pick from the main indices in the quoted sector.

Part of the appeal of this trust is low volatility as a result of its wide spread of investments. It generates very little income and in recent years has paid most of its modest dividend from realized capital profits, as investment trusts have been allowed to do for some time. Ongoing charges are 0.68% and the shares usually stand at a premium.

TR Property

Here we have a trust investing in shares and property companies with a small amount in direct property. While one might think one could just as well invest directly in property companies, the fact that they have 65% in Continental Europe means that it would be very hard to reproduce anything like the portfolio as a private individual. The latest ongoing charge is 1.06% including the performance fee although it was 1.64% in the previous year. The performance fee element gives a substantial payment to the managers if they do well which is held to be justified because there is a basic fee fixed in money terms and a very small ad valorem element. Performance has been erratic although with very good returns over the last three and five year periods. The shares trade at a material discount.

Roy Colbran and George Miller

Our January Issue Competition Results

In the January issue of PI I explained that I was hopeless at selecting AIM shares and invited members to do better in the form of a competition. It seems that I am not alone as there were only SIX entries.

So, the winner will collect £60, the 2nd will get £24 and the 3rd will get £12.

Out of the 25 companies shown, fifteen different companies were chosen:

Brainjuicer was selected four times.
Asos, Cohort and IQE was selected three times.
Dart Group, Finsbury Food, Hotel Chocolat, Playtech, Sprue Aegis and SQS Quality Systems was selected twice.

There were single selections for: Adv. Medical Solutions, Majestic Wine, Mulberry, Newmark Security and Victoria.

Malcolm Howard

Letter to the Editor

Reply to Malcolm Howard

Malcolm Howard has told us in the Monthly Magazine (Issue 186) why he avoids AIM shares. My experience is different and I would argue that there is scope here for careful stock pickers who are prepared to do their own homework.

I have always been more interested in smaller companies but it was only as the years mounted up that I started to take a specific interest in AIM because of the potential IHT benefits; a 40% saving offsets quite a bit of risk. Since 2010, I have been shifting a useful proportion of my portfolio – and, to a lesser extent, my wife's - into BPR/IHT qualifying AIM shares. In mid-2014, we decided to reduce the risk of relying entirely on my investment decisions and placed part of our AIM funds (in my wife's case, the majority) with a specialist investment manager whose policy includes the avoidance of oil, gas, commodities, blue sky outfits, high borrowings and overpaid management. On the plus side, the manager is looking for long term holds with steady businesses, good cash conversion and experienced directors whose interests are aligned with those of shareholders. The objectives are to preserve capital and to keep risk down and our portfolios contain up to 30 shares. We both have separate beneficiaries, so overlap between portfolios is not a problem.

We started the managed portfolios with lump sums and have topped up at intervals. Allowing for the timing and for all costs and dividends, the performance of my wife's managed fund has been +25% pa compound since inception, admittedly over only 2 ½ years. Of the 29 shares in her portfolio, six are in the red. My own (non-managed) performance is difficult to calculate, being spread over many years, with AIM shares being mixed into my general portfolio, and, until recently, being too much aligned towards speculation. So far as I can measure, the last five years show an increase of somewhat under 20% pa compound. Looking at Malcolm's list, we hold Cohort (+78%), IQE (+53%), Advanced Medical (+80%) and Abcam (+125%); Hotel Chocolat (+71%) has been sold recently and Majestic (+24%) was sold a year ago. An additional bonus can come from takeovers and the rewards can be substantial, as with Avesco (+124% in 6 weeks; not on Malcolm's list).

There are downsides. The prices of the larger, more marketable AIM shares seem to be inflated by the weight of money chasing them, which has the knock-on effect of lowering dividend yields. Our manager, seeking to avoid the crush at the top, is small enough to include smaller companies; that's fine when they are going well but it can difficult to get out if things go wrong. In the longer term, an investor looking to escape IHT via AIM has to take into account the possibility of a change in the tax rules which could have the added effect of depressing prices significantly.

I am not recommending that everyone dashes into AIM; there is little reliable analysis on any except the largest companies, so it is necessary to read company accounts and try to understand the business and management. I use the Stockopedia web site and find their Stock Rank system useful for assessing a company's strengths and weaknesses. The advfn Bulletin Board can contain some useful commentary amongst the dross. For example, the GW Pharma thread (until it went to NASDAQ) was consistently high quality and, a couple of years ago, I would have saved myself money if I had heeded 'WAN's' dissenting comments on the Carclo thread. Investors can also look at the objective commentary on AIM company accounts on the UKSA web site http://www.uksa.org.uk/campaigning/aim-100 ; this isn't meant to be investment advice but it does give a picture of how the company operates. Whilst writing this, could I please make a plea for volunteers to help writing these commentaries; if anyone can help, please contact me at hubertpbeaumont@gmail.com – you can also use this address to question me or to demolish my arguments above.

by Hubert Beaumont

That Green Paper

by Peter Parry

The following is the covering letter that was submitted to BEIS on 17th February 2017 with UKSA's response to the Green Paper on corporate governance.

Dear Sirs,

This response to the Green Paper has been developed jointly by The UK Shareholders' Association (UKSA) and the UK Individual Shareholders' Society (ShareSoc). Both organisations represent the interests of private shareholders who invest (directly or indirectly via nominee accounts) in public companies or in other forms of equity-based investment. Both are independently funded by concerned individuals who pay a membership fee.

Fundamental Issues

Engagement between shareholders and companies is not working. Shareholders are not exercising effective stewardship and control, and boards are failing to fulfil their fiduciary obligations to members. As a result, public trust in business is low. This is bad for business and for long term investors. It needs to be addressed.

The ownership structure of public corporations means that the views and interests of ultimate beneficial owners are not given sufficient weight. The bulk of public company shares are controlled by institutions whose interests are often not aligned with those of the beneficial owners. BEIS (when it was BIS), to its credit, addressed this in its recent report on share ownership (Research Paper 261).

Shareholder Committees: We strongly support the concept of Shareholder Committees, provided that they represent the interests of all shareholders, including private investors and investors in employee share plans. Our recent very disappointing experience with the Board of the Royal Bank of Scotland Group plc suggests that UK boards are unlikely to implement shareholder committees unless these are mandatory.

Problems of the voting chain: This is not highlighted in the Green Paper. The proliferation of shareholders who are not directly interested in the companies in which they own shares– for example, intermediaries, ETFs, tracker funds and other index-related funds - corrupts the governance and stewardship process and the associated governance checks and balances. This is exacerbated by stock-lending – a process which is actually a sale-and-repurchase in which ownership rights (including the right to vote) pass to the 'borrower' for a fee. This prejudices the concept of corporate governance based on shareholder oversight, and places too much influence over our companies in the hands of traders - the ultimate cause of short-termism.

Theresa May - a friend to the private shareholder?

Disenfranchisement of individual shareholders: The Green Paper recognises the problem that most private investors are now obliged to hold their shares in pooled nominee accounts wherein shares are legally owned by an intermediary. The ability and rights of informed individual investors to influence the affairs of companies in which they have invested is fundamental to good governance. With current digital technology it should be feasible to ensure that, at a minimum, the names of beneficial owners are placed on the share registers of the companies in which they invest so that they can receive normal shareholder communications and voting rights.

Peter Parry
Policy Director

Complexity of boardroom pay: Systems of remuneration for directors have become excessively complex as a result of the structural governance weaknesses identified in the Green Paper. The mechanisms for triggering bonus payments have become opaque, the quantum of the payouts is often impossible to predict, the true motivational impact has become questionable while the reporting to shareholders has become cumbersome and often obscure to the point of incomprehension.

Weaknesses of long-term incentives: Boards and their advisors have taken advantage of the lack of voting integrity to implement complex LTIPs as a major part of the overall remuneration package. It is widely accepted that the longer a reward is deferred the less motivational impact it has on the recipient. It is also accepted that for performance incentives to work, the achievement of outcomes must be within the control of the recipient. The current system of long-term incentives fails both these tests. The current system to a large degree reflects guidance from institutional investors (who via engagement and voting have insisted companies pay directors this way). We take a simple view: the use of complex financial incentives to do a responsible and challenging job properly is inappropriate. It can also encourage perverse behaviour which we do not want from those who run our companies.

Shareholder Committees are a core part of the solution to the problems of corporate governance. There are many other elements of governance and control that can be improved and we have commented in our response on those where we have specific knowledge. However, without Shareholder Committees, and concomitant reform to restore the rights of individual shareholders, other changes to corporate governance are unlikely to produce meaningful change.

Our responses to the specific questions set out in the Green Paper are given below*. ShareSoc and UKSA would be pleased to discuss these and the summary above in more detail with the Department.

Please note although we remain separate organisations, UKSA and ShareSoc are working increasingly closely together. In recognition of this we have decided that we should each submit a response to BEIS but that the response should be exactly the same in each case. We would however like to be listed separately on your list of those organisations who have responded to the Green Paper.

Yours sincerely,
Peter Parry, Policy Director

*Refer news item on our website.

Tim Harford, 'The Undercover Economist' writing in the FT, riffed on motivation and whether precise targets did the trick. Commenting on the idea of giving bonuses to teachers based on the test score results of their students he wrote: "We rely on teachers to do many things for the students in their class, not just boost their test scores. Rewarding teachers too tightly for test scores encourages them to neglect everything we value but cannot measure."

Perhaps those responsible for the current directors' remuneration regime should give this some thought?

UKSA Branches

Where no contact name or number is given contact the UKSA office

MEETING with RWS plc 6th April	
Location	RWS Group, Tavistock House, Tavistock Square, Bloomsbury, London, WC1H 9LG
Assembly	10:30 for 11:00
Duration	1 hour + Q&A
Access	Euston Square, Euston & Euston mainline
Telephone Website	020 7554 5400 http://www.rws.com
Presenter	Richard Thompson CEO
UKSA Organiser	Gerald Roberts

VISIT to HSBC Holdings plc 19th April	
Location	HSBC Offices, 8 Canada Square, Canary Wharf, London, E14 5HQ
Assembly	11:30 am
Meeting start	12:00, lunch, followed by presentations from Douglas Flint and Richard O' Connor, with Q&A.
Meeting numbers	50
HSBC Company contact	Karen Wainwright (0207 991 1684)
UKSA Organiser	Phil Clarke Tel: 01689 834479 e-mail: pjejclarke@outlook.com

Branch name	Leader	Administration	Main purpose	Description
London & South East Region	Harry Braund 020 8680 5872 harrycb@gmail.com	Tony Birks 01322 669 120 ahbirks@btinternet.com	To co-ordinate activities in London and the South-East	Meetings in Croydon three times a year
London company visits	Nick Steiner	Individual meeting organisers	To arrange private meetings with companies	20/30 meetings per year individually arranged
Specialist company visits	David Lowe Adrian Phillips	Under review	To arrange and/or participate in events in conjunction with investor service companies	Meetings with small-company management, for experienced investors only
Croydon & Purley	Harry Braund 020 8680 5872 harrycb@gmail.com	Tony Birks 01322 669 120 ahbirks@btinternet.com	Social meetings to discuss investment issues	Meetings in Croydon monthly
South West	Peter Wilson 01453 834 486 07712 591032	Peter Wilson 01453 834 486 07712 591032	To arrange and develop activities for members in the region	Company visits and social events as arranged
North East	Brian Peart 01388 488419	Julian Mole 07870 890973 julian.mole@btinternet.com	To arrange and develop activities for members in the region	Company visits and social events as Arranged
North West	Julian Mole 07870 890973 julian.mole@btinternet.com	Julian Mole 07870 890973 julian.mole@btinternet.com	To arrange and develop activities for members in the region	Company visits and social events as Arranged
SmartCo	Charles Breese	Charles Breese	Arranging access to 'Smart Companies' - those with the potential to make good investment returns from benefiting society at large	Programme awaiting start-up
Brighton	Dee O'Hare 075 6815 6725 dfohare@hotmail.com	Dee O'Hare 075 6815 6725 dfohare@hotmail.com	Education on basic investing, and discussion with local UKSA members	Monthly evening meeting - presentation, Q&A, then socialising