Heritage

Quarterly Newsletter & Investment Review

Issue 78 Quarterly news & investment review from Heritage Quarter 2 2017

In this issue

Heritage Capital Management Limited

Heritage Capital Management Ltd is an independent, specialist investment management company based in London and regulated by the Financial Conduct Authority, providing a wide range of investment services to individuals, trusts, companies and pension funds.

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A good quarter for the Heritage funds

We are pleased to report that despite the uncertainty created by the recent unexpected snap UK general election and a small decline this quarter by the FTSE index, the Heritage funds have continued their good run with our largest fund, the Managed Portfolio Fund gaining 3.12% in quarter two.

Further details of our Funds including the current asset allocation and a commentary on performance can be found as usual on page 3 and we now also include information on our new fund, the SVS Heritage Balanced Portfolio Fund on page 4.

Advantages of a fund based approach

Originally investment funds were set up to allow the not-so-wealthy to "pool" their resources in order to allow access to a professionally managed and well diversified spread of investments which would not otherwise be available cost effectively on an individual basis.

This logic still applies today, but other considerations such as simplicity of administration, costs and tax planning advantages now mean that even the wealthiest of private clients tend to choose a fund based approach in preference to direct investment. The main advantages of investing through a fund can be summarised as follows:

Diversification and security – A fund allows individual investors to obtain exposure to a wide range of investments through a single holding. Additionally, many asset classes such as private equity, property and other alternative investments are not easily accessible to an individual investor but can be accessed through a liquid pooled fund. Also, investors in the fund benefit from the assurance that their assets are securely held with separately appointed and regulated auditors, custodians, administrators and managers involved.

Management – Investment decisions can be taken purely on the basis of the investment merits, rather than being complicated by tax related concerns, as a fund is not liable to taxes such as capital gains tax that can apply to individuals. Also, the fund's portfolio will receive the full time attention of a professional manager, whereas an individual portfolio will quite often only be reviewed and managed on an occasional or ad-hoc basis. Furthermore, in the case of a fund where the managers have their own wealth invested in the fund, the investor can take further comfort from the fact that the manager is happy to "eat his own cooking".

Tax planning and efficiency – Holding a portfolio of investments within a single fund is also simpler and more flexible from a tax planning point of view. For example, a non-distributing ("roll-up") fund can be held for a number of years, or even indefinitely, without giving rise to any tax liability. This allows the investments to compound tax-free for many years as well as providing the investor with the ability to plan to only pay tax at a future time and date that suits him – for example, when he becomes a lower rate tax payer or becomes non-resident.

Administration and simplicity - A further benefit, which should not be underestimated, is the reduction in record keeping, administration and calculations required to keep track of many individual holdings, trades, dividends and interest etc., thereby eliminating the need to incur additional accountancy fees.

Costs – The economies of scale that are available to a pooled fund give rise to cost advantages that are not available to individual portfolios. For example dealing within the fund should be at institutional commission rates rather than the higher rates usually charged to individual investors.

At Heritage, we continue to offer both an individual portfolio management service and our own fund-based service for our investment clients. However, for the reasons outlined above we continue to believe that the funds approach offers the best solution for the majority of clients.

Heritage Capital Management Limited

Review for the quarter ended 30th June 2017

Market Commentary and Outlook

Following a positive start to the year, global stock market returns were more mixed in the second quarter with declines for the UK and Europe balanced by positive returns for the US and Japan.

There has recently been some eye catching news on valuations of relatively new companies that have drawn comparison with the technology boom and subsequent bust experienced at the turn of the century. For example the market is now valuing electric car maker, Tesla, at $45bn despite the fact that it had revenues of just $7bn in 2016 and is yet to make a profit. To put this into context, Ford Motors which has been around for over 100 years and last year made around $5bn profit on revenues of over $150bn has a significantly lower market cap of just $34bn.

Another potential warning sign is that even those companies that have proved that they can make a profit are incredibly highly valued on traditional metrics such as price earnings ratios. Taking a look at the so called "FANGs" shows PE ratios for Facebook of 43, Amazon of 197, Netflix of 347 and Google (now named Alphabet) on 33 times earnings.

Whilst these are all undoubtedly good companies that have fundamentally changed the markets in which they operate, their valuations have already priced in and taken for granted a huge amount of future profit growth which may or may not be ultimately realised in a fast changing and uncertain world. However, rather than speculating as to whether or not these stocks are in unsustainable bubble territory, we prefer to stick to analysing companies on more sensible valuations which may have less stellar potential but have a proven business model and decent prospects.

United Kingdom

Whilst the FTSE 100 index has at least finally managed to remain above the 7,000 mark that it passed earlier in the year it has failed to make further progress in the second quarter.

This may at least be partially due to the uncertainty created by the surprise general election. Theresa May's failure to secure an outright victory, let alone the increased majority that she had hoped for has left the UK without the "strong and stable" leadership required to negotiate a successful Brexit deal. However, in the mean-time the underlying corporate news has been reasonably encouraging and the hope is that most companies will ultimately be able to successfully navigate whatever issues are thrown up by the politicians.

United States

The US has continued its good start to the year with the S&P 500 appreciating by a further 2.6% this quarter.

As commented above, the valuation of the overall US market is currently being skewed upwards by a small number of very highly priced technology companies. However, the way that Apple has matured over the years, to the point where it has now overtaken ExxonMobil as the world's biggest dividend payer, shows that at least some highly valued tech companies can grow into their lofty valuations.

As expected the Federal Reserve Bank has continued to nudge US Dollar interest rates up and although 1.25% is still low by historic standards, the premium over European and Japanese rates is now becoming more significant.

Europe

After leading the way in the first quarter Europe was the weakest of the major markets in quarter two.

The unexpected and meteoric rise to power of Emmanuel Macron and his new En Marche! party has produced an optimism about France that has not been seen for some time and it will be interesting to see if this translates into any meaningful improvements. Following surprise election results in the US, France and UK within the last year all eyes will now turn to the German elections in September.

Japan

Japan was the best performing major market this quarter with the Nikkei index gaining over 5%, although as is often the case with Japan for foreign investors the underlying returns have been countered by an opposite move in the exchange rate.

Emerging Markets

Emerging markets have continued their good run in 2017 with an overall double digit return for the year-to-date outpacing the more lacklustre gains from the major markets. For investors the big news this quarter was MSCI's decision to start including China's previously excluded large A share market of Shanghai listed companies in its emerging market index.

Investment Statistics - 30/06/2017

Equity Markets	Q2 2017	2017 ytd	2016	PE Ratio	Dividend Yield	Central Bank Interest Rates	10 yr Gvnmt Bond Yields	Exchange Rates	
								vs GBP	vs USD
TR Global ($)	4.47%	11.83%	8.49%						
US (S&P 500)	2.57%	8.24%	9.54%	21	2.4%	1.25%	2.30%	1.3027	1.0000
UK (FTSE 100)	-0.14%	2.38%	14.43%	24	3.9%	0.25%	1.26%	1.0000	1.3027
Europe (STOXX 50)	-1.69%	4.60%	0.70%	16	3.4%	0.00%	0.47%	1.1392	1.1423
Japan (Nikkei 225)	5.95%	4.81%	0.42%	18	1.7%	-0.10%	0.08%	146.35	112.35

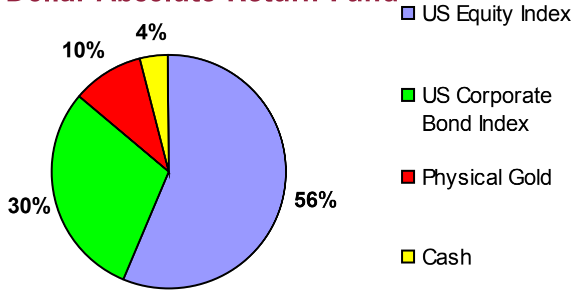
Total returns- including dividends

Source: Thomson Reuters and the Financial Times

Heritage Investment Fund Limited
Review for the quarter ended 30th June 2017

Performance	US Dollar Absolute Return Fund	Managed Portfolio Fund	Inflation (US)	TR Global World Index (£ total return)
Risk profile	Low	Medium		
Minimum investment horizon	3 years +	5 years +		
Target net annual return	4-5%	6-7%		
Price at 30 June 2017	US$150.37	£284.79		
Return for quarter (net)	2.09%	3.12%	0.54%	0.65%
Year 2017 return (net)	4.53%	6.75%	1.16%	5.92%
Year 2016 return (net)	2.08%	7.48%	1.16%	29.59%
Year 2015 return (net)	-0.47%	6.80%	0.08%	3.49%
Year 2014 return (net)	5.42%	7.74%	1.65%	10.99%
Year 2013 return (net)	3.98%	13.85%	1.49%	19.85%
Year 2012 return (net)	1.95%	13.27%	2.10%	7.93%
Compound annual return (from 1/01)	2.44%	6.59%	2.12%	6.43%
Annual volatility	4.10%	4.03%	0.18%	8.85%
Size of Fund (millions)	U$12.7	£172.2		

US Dollar Absolute Return Fund



The US Dollar Absolute Return Fund aims to protect investors capital and generate annual returns in excess of inflation by investing in a range of liquid, well-diversified exchange traded funds which track US equity, corporate bond and gold indices, and whose returns have a low or negative correlation in order to reduce losses and volatility.

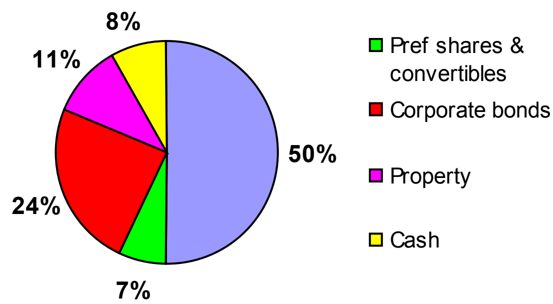
The Fund's core growth investment in the equity index ETF, which tracks the S&P 500 largest US companies, was 56% at the end of the period. The gain for the quarter was 1.56%, as the US equity market rose on lower interest rate and inflation expectations.

The Fund maintained its 30% investment in the US investment-grade corporate bond ETF, which yields 3.33% per annum, both for income and as a hedge against equity market weakness. The gain for the quarter was 0.70%, as bond yields and corporate bond spreads both fell on the expectation that there may only be one further interest rate increase this year.

The Fund maintained its investment in the physical gold ETF at 10% during the quarter, as a hedge against inflation and US Dollar weakness. This ETF lost 0.03% for the quarter, as inflation fell and the US Dollar weakened.

The Fund produced a positive return of 2.09% for the quarter and is up 4.53% for the year to date. It is well positioned to generate future returns in excess of inflation over the medium term.

Managed Portfolio Fund



The Managed Portfolio Fund seeks to generate long-term capital growth at a lower risk than that associated with pure equity market investment through active management of a well diversified multi-asset portfolio.

The Fund had another good quarter, appreciating by 3.12% despite a flattish performance by the overall market and for the year to date the Fund is now up by 6.75%.

Within our share portfolio the major contributors this quarter included Intermediate Capital, Beazley, Bellway, HSBC, Computacenter, Compass, System 1 and Charles Taylor, whilst on the negative side there was only one significant detractor with the insurer, Novae Group, suffering a setback after a profit warning. We also benefitted from two very large special dividends declared on our holding in Electra Private Equity – in fact the dividends of just over £2.5m are well in excess of the £1.3m original cost of our investment and our remaining holding is still worth £1.3m.

Both our bonds and property holdings also had another decent quarter and we have been selectively taking profits in holdings that are starting to look a bit expensive and rotating into alternative holdings on more attractive valuations.

Overall, we continue to believe that our portfolio of investments remains well positioned to generate attractive returns for long-term investors, whilst our relatively defensive positioning and diversification should continue to provide some protection against any major market setbacks.

Automatic exchange of information

Governments around the world have introduced or will be introducing legislation which requires financial institutions to gather client information and report on such information to tax authorities. This legislation has been developed with the aim of fighting against tax evasion and protecting the integrity of tax systems. It provides greater transparency through tax authorities agreeing to collect and exchange information on each other's tax residents to prevent financial assets being concealed.

On 1st July 2014, the US legislation known as FATCA came into force with the aim of detecting and deterring US tax evasion by US persons who hide financial assets offshore. This was shortly followed on 15th April 2015 by the Crown Dependencies and Overseas Territories (CDOT) legislation which includes those persons from the Crown Dependencies such as Guernsey, Jersey and the Isle of Man, as well as the Overseas Territories which includes those persons from Bermuda, the British Virgin Islands, the Cayman Islands, Turks and Caicos Islands and more.

On 1st January 2016, the UK signed up to further legislation called the Common Reporting Standard (CRS) which provides the standard for all automatic exchange of financial information. Fifty jurisdictions worldwide signed up to undertake the first CRS exchanges by 2017 and by 2018, 101 jurisdictions worldwide will have committed to the CRS automatic exchange of information between tax authorities. Under the above legislations, Heritage is classified as a UK Financial Institution and consequently we are required to identify and report to Her Majesty's Revenue and Customs (HMRC) regarding any of our accounts held by clients who are resident in any of the countries covered by FATCA, CDOT or CRS legislation.

In relation to trusts, HMRC are looking at the tax residencies of the settlor, beneficiaries of mandatory and discretionary distributions and any person that exercises ultimate effective control over the trust. For companies, HMRC are looking into the tax residencies of those who hold equity interests.

Under FATCA, CDOT and CRS, the following information in relation to each identified Reportable Client will be reported annually to HMRC: Name and Address; Taxpayer Identification Number (TIN); Heritage account balance or value as of the end of the calendar year; and Total gross amount paid or credited to the Specified Person during the calendar year.

In order for Heritage to be compliant we will be contacting some of our clients to reconfirm to us their personal tax residency and tax identification number (TIN) via our 'Heritage Self-Certification Form'. In particular, for our US clients, under FATCA we are required to have your TIN documented. If required, we may request further documentation from our clients to confirm their tax status. Co-operation from our clients would be greatly appreciated.

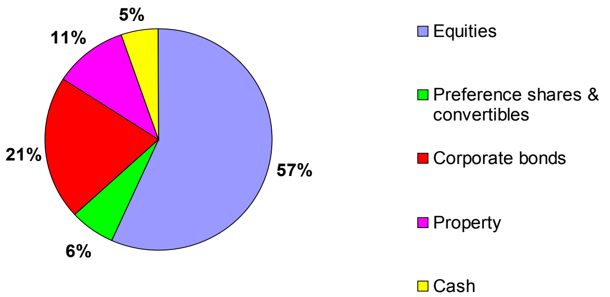
Under UK law, Heritage must report information to HMRC. If a client fails to kindly co-operate with Heritage regarding their tax residency and TIN, then we will still be obliged to disclose details to HMRC if we believe a client may be a Reportable Client based on the information we currently hold.

Please note that at Heritage we do not provide tax or legal advice. If you believe you are or will be affected by FATCA, CDOT or CRS, please contact your tax adviser.

SVS Heritage Balanced Portfolio Fund - summary of key features

Price at 30/06/17	110.2p (launched at 100p 1/12/16)
Fund size	£13.8m
Fund type	OEIC, UCITS (UK domiciled)
Eligible for	ISAs, SIPPs, Funds at Lloyd's
Sedol code	BDQPPL5
Pricing and dealing	Daily
Minimum Investment	£10,000
Management fee	1% per annum
Administrator/ACD	Smith & Williamson

Asset allocation



Commentary and performance

The Fund has continued its positive start with a gain of 3.5% this quarter.

The approach adopted is in line with the existing larger offshore version of the fund (the Guernsey regulated Heritage Managed Portfolio Fund) and the share price has increased by 10.2% from its starting level of 100p on 1/12/2016 to its current level of 110.2p.

Further details and the full fact sheet for the fund can be found on our web site at www.heritage-capital.co.uk.

The information set out above does not constitute an offer to subscribe to shares, which may only be purchased after reading the full Prospectus/Key Investor Information Document (KIID). The Prospectus and KIID can be found at www.heritage-capital.co.uk.

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