



Wealth well managed

**IFDS BROWN SHIPLEY STERLING BOND FUND**  
**Institutional Investors Report**

**“A Risk Conscious Route to Income”**

**October 2011**

For Professional Investors Only

This document should not be circulated to Retail Investors

## Introduction

- The aim of the **IFDS Brown Shipley Sterling Bond Fund** is to offer investors a “Risk Conscious Route to Income”. The fund seeks to achieve this aim by generating a highly competitive level of income, whilst seeking to preserve capital over the medium term. In tandem, the fund aims to deliver a low volatile experience for share holders.
- Specifically, the fund is mandated to be amongst the top decile of income generators within the IMA £ Corporate Bond sector, whilst preserving capital over the course of a complete interest rate cycle.
- The Institutional Investors Report is designed to provide professional investors with a level of disclosure exceeding that displayed by the competition.

Should you have any questions or comments about the report or any other fund related matter, please do not hesitate to contact one of the team:



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## **Risk Warning**

- This report, which is issued by Brown Shipley Funds (BSCo), contains information gathered by fund managers and analysts at BSCo and is being provided to professional investors and advisors for information purposes only.
- This information has been provided by BSCo as discretionary fund managers who may have acted upon it for their own purposes. It does not constitute investment advice and should not be used as the basis of any investment decision, nor should it be treated as a recommendation for any investment.
- Neither BSCo nor any of its officers or employees give any representation or warranty, nor will accept any liability, in relation to the accuracy or completeness of any information contained within this report.
- The income and redemption yields on the fund may change over time, due to future changes in the average maturity date of the bonds held by the fund or changes in current or perceived future interest rates.
- If the redemption yield is lower than the income yield, the investor is buying income at the expense of capital. As with all bond funds, there is a risk of default on either the income payment or capital payment or both by the underlying investments of the fund.
- The value of investments and the income from them are not guaranteed and therefore investors may not get back the full amount invested. Past performance is no guarantee of future performance. The investment management charge on the fund is levied against the capital property, which may constrain capital growth.
- A simplified prospectus is available from our website and a company prospectus can be obtained by calling the IFDS Brown Shipley helpline on 0870 043 4830. For security purposes, telephone calls may be monitored or recorded.



## IFDS BROWN SHIPLEY STERLING BOND FUND

### Market Review

**“A Risk Conscious Route to Income”**

October 2011

# Gilt Curves

With the Bank of England engaging in an additional round of quantitative easing (QE), Government bond markets continued to be well bid, pushing yields down in the process.

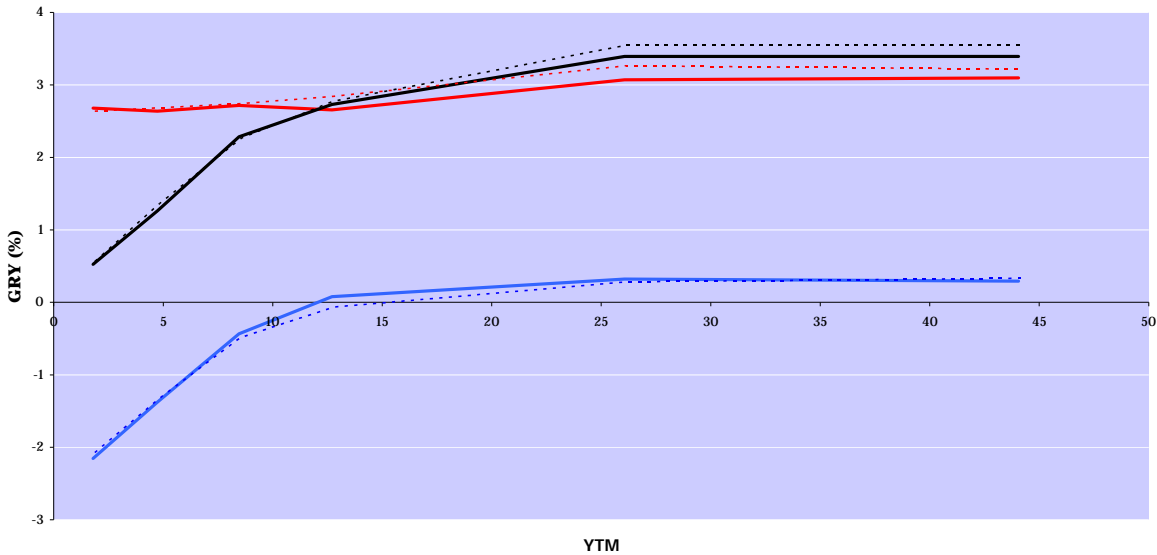
Despite UK inflation data showing a year-on-year increase not surpassed at any time since 1991 (when base rates stood at 10.5%), the source of the yield decline came via a lowering of inflation expectations.

For the first time in many months, real yields remained relatively constant. Displaying negative real returns for all maturities up to and including 10 years, the rationale for such an investment remains puzzling to say the least, irrespective of the ultimate inflation outcome.

Source: Bloomberg

## Real, Nominal and Implied Inflation Gilt Yield Curves

Source: Bloomberg



Recent: 31 October 2011      — Real Yield      — Implied Inflation      — Nominal Yield  
 Historic: 30 September 2011      - - - Real Yield (Historic)      - - - Implied Inflation (Historic)      - - - Nominal Yield (Historic)

## Credit Spreads

Despite the lack of real progress within the Euro region as to the design of a lasting solution to the debt crisis, the promise of one was sufficient for spreads to follow the lead from equity markets.

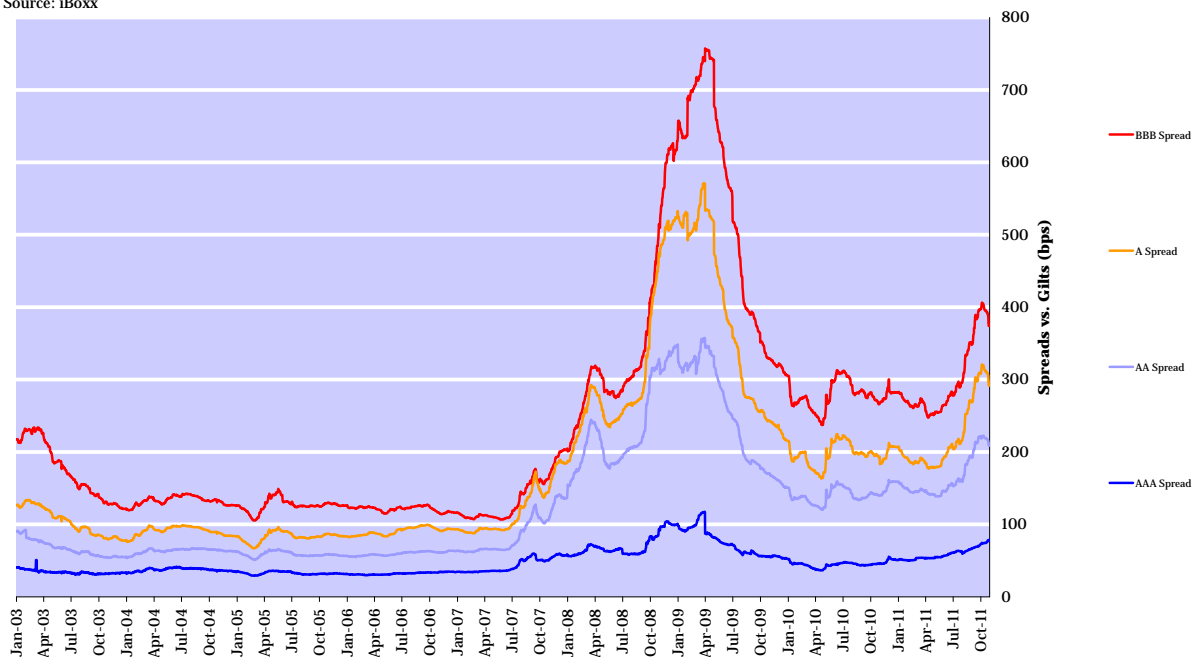
The initial response to the EU leaders “three-pronged” plan to lower Greece’s debts, recapitalise the banking system and leverage the powers of the European Financial Stability Fund was taken positively. As we discuss in our outlook section, the plan raises as many questions as it answers in our opinion, but was sufficient to encourage a risk-on appetite.

Whether such an appetite will remain in place is debatable. Post the market close on the evening of Halloween the Greek Prime Minister, George Papandreou, spooked investors with the announcement of a referendum on whether to accept the terms and conditions of the bail-out package. Acting as a further delay to the process, the vote if rejected, has the potential to open up a raft of implications for the Greek economy and the Euro project.

Source: iBoxx

## Credit Spreads

Source: iBoxx





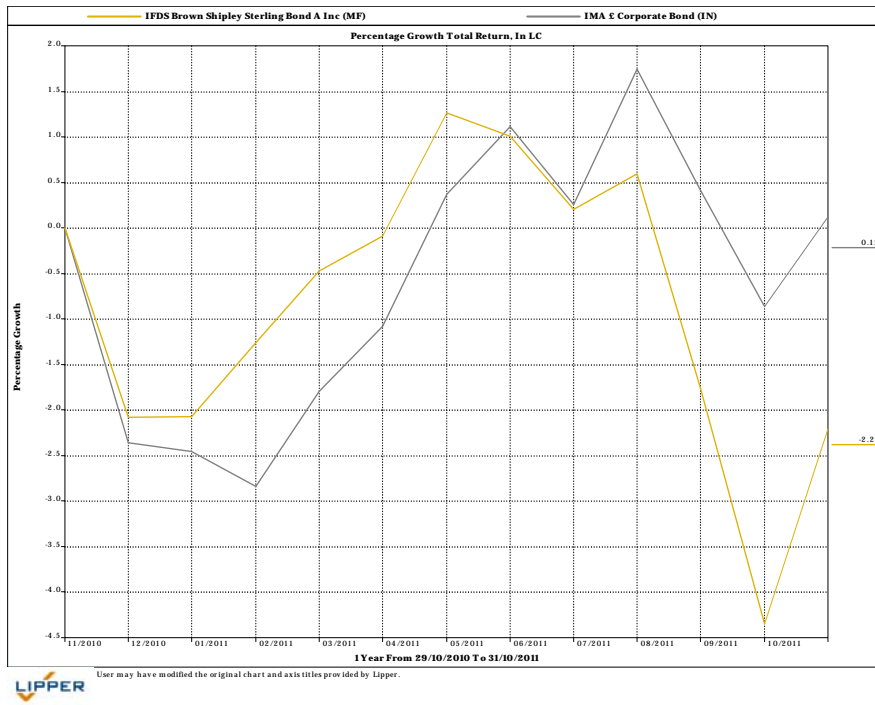
IFDS BROWN SHIPLEY STERLING BOND FUND  
Performance Review

**“A Risk Conscious Route to Income”**

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# Performance Charts

## 1 Year



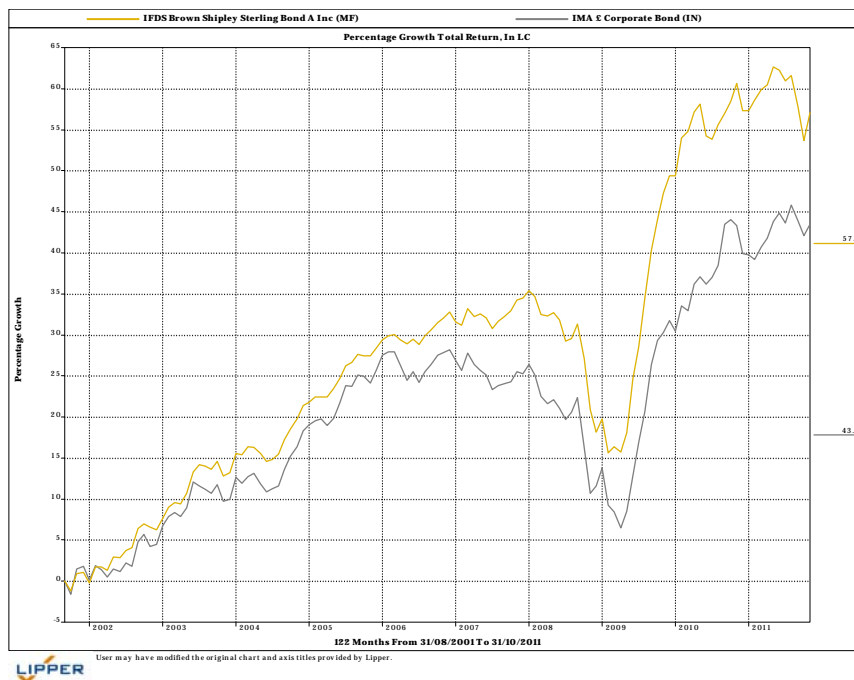
Mid to mid, gross income reinvested in UK Sterling.

## 5 Year



Mid to mid, gross income reinvested in UK Sterling.

## Since Manager



Mid to mid, gross income reinvested in UK Sterling.

## Mandate Objectives

### Top Decile Income Generation

Since changing manager (31 August 2001), the fund has generated £594.51 respectively per £1,000 invested. This places the fund within the top decile of income generators amongst the IMA £ Corporate Bond sector.

### Capital Preservation

The fund continues to hold the Lipper Leaders award for Capital Preservation.

### Low Volatile Experience

The fund is currently amongst the least volatile funds within the IMA £ Corporate Bond sector as measured by standard deviation of monthly price movements since August 2001.

**PERFORMANCE REPORT**

**IFDS Brown Shipley Sterling Bond Fund**

30/09/2011

SS

VAL

31/10/2011

SS

VAL

ID ISIN	Issuer	Cpn	Maturity	Holding	Price	Value	%	Holding	Price	Value	%	Performance	Performance Contribution
<b>Government Securities</b>													
<b>Supranationals</b>													
<b>Monoline Wraps</b>													
<b>Mining</b>													
XSO288783979	Glencore	6.5	27/02/2019	1,750,000	101.07	1,768,679.50	1.64%	1,750,000	105.19	1,840,758.50	1.72%	4.62%	0.08%
XSO366204393	Xstrata	7.375	27/05/2020	1,450,000	114.13	1,654,914.00	1.54%	1,450,000	113.58	1,646,943.35	1.53%	0.07%	0.00%
<b>Oil &amp; Gas Producers</b>													
XSO145515655	Talisman Energy	6.625	05/12/2017	1,550,000	116.27	1,802,192.75	1.67%	1,550,000	116.57	1,806,879.95	1.68%	0.74%	0.01%
<b>Chemicals</b>													
<b>Construction &amp; Materials</b>													
XSO430665108	Lafarge	10	30/05/2017	1,500,000	106.84	1,602,622.50	1.49%	1,500,000	109.24	1,638,630.00	1.53%	3.04%	0.05%
<b>Aerospace &amp; Defence</b>													
<b>Industrial Engineering</b>													
XSO18106243	General Electric	6.25	29/09/2020	1,350,000	108.17	1,460,346.30	1.36%	1,350,000	107.91	1,456,771.50	1.36%	0.25%	0.00%
XSO276102265	Hutchinson Whampoa Finance	5.625	24/11/2017	1,700,000	110.25	1,874,302.70	1.74%	1,700,000	110.73	1,882,420.20	1.75%	0.87%	0.02%
<b>Automobiles &amp; Parts</b>													
<b>Beverages</b>													
<b>Food Producers</b>													
<b>Health Care Equipment &amp; Services</b>													
<b>Personal Goods</b>													
<b>Pharmaceuticals &amp; Biotechnology</b>													
<b>Tobacco</b>													
XSO182188366	British American Tobacco	6.375	12/12/2019	1,400,000	116.32	1,628,545.80	1.51%	1,400,000	117.59	1,646,194.20	1.53%	1.55%	0.02%
XSO433179618	Imperial Tobacco	7.75	24/06/2019	1,500,000	121.39	1,820,827.50	1.69%	1,500,000	121.89	1,828,362.00	1.70%	0.96%	0.02%
<b>General Retailers</b>													
XSO471074582	Marks & Spencer	6.125	02/12/2019	1,750,000	106.24	1,859,270.00	1.73%	1,750,000	107.57	1,882,475.00	1.75%	1.74%	0.02%
XSO421003665	John Lewis	8.375	08/04/2019	1,500,000	121.64	1,824,607.50	1.70%	1,500,000	121.76	1,826,340.00	1.70%	0.68%	0.01%
XSO269903869	Next	5.875	12/10/2016	750,000	107.84	808,818.00	0.75%	750,000	108.41	813,048.00	0.76%	0.99%	0.01%
XSO630204351	Next	5.375	26/10/2021	750,000	100.21	751,543.50	0.70%	750,000	101.16	758,701.50	0.71%	1.41%	0.01%
<b>Travel &amp; Leisure</b>													
XSO181013607	FirstGroup	6.125	18/01/2019	1,800,000	106.56	1,918,071.00	1.78%	1,800,000	107.99	1,943,731.80	1.81%	1.83%	0.03%
XSO163019143	Enterprise Inns	6.5	06/12/2018	3,750,000	71.63	2,686,012.50	2.50%	3,750,000	72.50	2,718,750.00	2.53%	1.99%	0.05%
XSO206404724	Spirit Issuer	2.02313	28/12/2011	1,200,000	104.21	981,000.00	0.91%	1,200,000	106.84	939,000.00	0.88%	-1.07%	-0.04%
<b>Media</b>													
XSO294391684	WPP	6	04/04/2017	1,800,000	109.49	1,970,807.40	1.83%	1,800,000	109.74	1,975,393.80	1.84%	0.70%	0.01%
XSO232037233	ITV	5.375	19/10/2015	1,500,000	98.37	1,475,387.50	1.37%	1,500,000	99.45	1,491,787.50	1.39%	1.56%	0.02%
XSO498542336	UWM	6.5	23/11/2016	1,500,000	104.21	1,563,165.00	1.45%	1,500,000	106.84	1,602,556.50	1.49%	3.05%	0.04%
<b>Support Services</b>													
<b>Industrial Transport</b>													
XSO124609370	Birmingham Airport	6.25	22/02/2021	2,032,000	109.19	2,218,653.42	2.06%	2,032,000	108.88	2,212,526.94	2.06%	0.21%	0.00%
<b>Food &amp; Drug Retailers</b>													
<b>Mobile Telecommunications</b>													
<b>Fixed Line Telecommunications</b>													
XSO063233679	Cable & Wireless	8.75	06/08/2012	1,150,000	100.61	1,157,043.75	1.08%	1,150,000	101.91	1,172,011.00	1.09%	2.03%	0.02%
XSO195160329	Telecom Italia	6.375	24/06/2019	1,500,000	92.49	1,387,279.50	1.29%	1,500,000	97.13	1,456,972.50	1.36%	5.61%	0.07%
XSO241946044	Telefonica	5.375	02/02/2018	1,850,000	96.32	1,781,908.90	1.66%	1,850,000	102.09	1,888,659.45	1.76%	6.46%	0.11%
<b>Electricity</b>													
XSO132784715	EDP Finance	6.625	09/08/2017	1,910,000	86.52	1,652,463.24	1.54%	1,910,000	88.36	1,687,754.31	1.57%	2.79%	0.04%
XSO306647018	Enel SPA	6.25	20/06/2019	1,800,000	98.83	1,775,260.80	1.65%	1,800,000	104.00	1,872,064.80	1.74%	5.99%	0.10%
XSO062992028	First Hydro Finance	9	31/07/2021	1,500,000	118.81	1,782,120.00	1.66%	1,500,000	117.67	1,765,027.50	1.64%	-0.32%	-0.01%
XSO435791180	Iberdrola Finance	6	01/07/2022	1,800,000	101.57	1,828,170.00	1.70%	1,800,000	103.10	1,855,746.00	1.73%	2.01%	0.03%
<b>Gas, Water, &amp; Utilities</b>													
XSO492282844	ESB	6.5	05/03/2020	3,750,000	92.13	3,454,687.50	3.21%	3,750,000	92.21	3,457,698.75	3.22%	0.69%	0.02%
<b>Banks</b>													
XSO572600335	Bank of Ireland	6.75	30/01/2012	1,060,000	98.82	1,045,319.00	0.97%	1,060,000	99.00	1,049,378.80	0.98%	0.97%	0.01%
GB00B177CL57	Coventry Building Society	6.092	29/06/2016	4,243,000	79.65	3,379,379.78	3.14%	6,243,000	79.00	4,931,970.00	4.60%	-0.16%	-0.01%
XSO20428154	Anglo Irish Bank	0	29/06/2049	5,847,000	0.00	0.00	0.00%	5,847,000	0.00	0.00	0.00%	0.00%	0.00%
XSO041971275	Bank of Scotland	10.5	16/02/2018	1,100,000	103.43	1,137,705.80	1.06%	1,100,000	104.35	1,147,874.20	1.07%	0.00%	0.00%
XSO542823892	CO-OP Bank	5.125	20/09/2017	1,500,000	98.63	1,479,456.00	1.37%	1,500,000	101.18	1,517,686.50	1.41%	3.03%	0.04%
GB0008389008	Standard Chartered	1.125	31/12/2049	6,200,000	62.00	3,844,000.00	3.57%	6,200,000	62.00	3,844,000.00	3.58%	0.15%	0.01%
FR0010306787	BNP Paribas	5.945	19/04/2016	7,950,000	66.21	5,263,559.85	4.89%	7,950,000	70.47	5,602,404.75	5.22%	7.20%	0.35%
GB00B130C039	Nationwide	6	15/12/2016	2,450,000	80.48	1,971,674.25	1.83%	2,450,000	83.00	2,033,500.00	1.90%	3.77%	0.07%
XSO40361503	Sklipton Building Society	10	12/12/2018	1,850,000	91.50	1,692,750.00	1.57%	1,850,000	92.50	1,711,250.00	1.59%	2.02%	0.03%
XSO440403797	Santander	7.3	27/07/2019	2,000,000	91.67	1,833,424.00	1.70%	2,000,000	92.36	1,847,288.00	1.72%	1.43%	0.02%
<b>Nonlife Insurance</b>													
XSO251382361	Amalin	6.5	19/12/2016	6,816,000	78.49	5,349,812.48	4.97%	4,066,000	82.00	3,334,099.67	3.11%	5.17%	0.26%
XSO270707283	Beazley	7.25	17/10/2016	2,280,000	74.50	1,698,611.40	1.58%	2,280,000	77.03	1,756,217.88	1.64%	4.22%	0.07%
XSO615238473	QBE	7.5	24/05/2021	1,750,000	91.90	1,608,328.75	1.49%	1,750,000	90.73	1,587,754.00	1.48%	-0.59%	-0.01%
<b>Life Assurance</b>													
XSO100688430	AMP Financial	6.875	23/08/2022	2,000,000	86.45	1,729,060.00	1.61%	2,000,000	91.11	1,822,120.00	1.70%	6.06%	0.10%
<b>Equity Investment Trusts</b>													
GB0008961913	City Of London	8.5	31/01/2021	675,000	130.85	883,203.75	0.82%	675,000	130.14	878,445.00	0.82%	0.01%	0.00%
<b>Real Estate</b>													
XSO37803930	Goodman Australian	9.75	16/07/2018	1,650,000	122.09	2,014,540.05	1.87%	1,650,000	122.36	2,019,019.20	1.88%	0.90%	0.02%
XSO222107186	Westfield Finance	5.5	27/06/2017	1,850,000	107.82	1,990,896.00	1.85%	1,850,000	108.10	1,999,914.75	1.86%	0.89%	0.02%
XSO236149877	Sagro	5.625	07/12/2020	1,750,000	103.54	1,811,885.25	1.68%	0	103.81	0.00	0.00%	0.72%	0.01%
XSO084734127	Capital Shopping Centres	6.875	05/03/2013	1,837,000	106.21	1,951,118.11	1.81%	1,837,000	99.89	1,834,927.86	1.71%	-5.41%	-0.10%
GB0006441967	Home Group	0	11/05/2019	2,900,000	68.07	1,974,030.00	1.83%	2,900,000	67.57	1,959,530.00	1.83%	-0.73%	-0.01%
<b>General Financial</b>													
XSO609183842	Henderson Group	7.25	24/03/2016	1,950,000	101.70	1,983,179.25	1.84%	1,950,000	103.10	2,010,352.50	1.87%	1.98%	0.04%
XSO233803153	Kensington Group	7.285	21/12/2015	2,248,000	71.63	1,610,130.00	1.50%	2,248,000	70.63	1,587,650.00	1.48%	-0.53%	-0.01%
XSO220965759	Provident Financial	5.594	15/06/2015	2,086,000	93.00	1,939,980.00	1.80%	2,086,000	93.00	1,939,980.00	1.81%	0.51%	0.01%
XSO459028626	Provident Financial	8	23/10/2019	1,600,000	91.21	1,459,296.00	1.36%	1,600,000	93.52	1,496,334.40	1.39%	3.28%	0.04%
XSO434590237	LSE	9.125	18/10/2019	1,550,000	126.48	1,960,435.35	1.82%	1,550,000	125.08	1,938,705.90	1.81%	-0.50%	-0.01%
XSO437404824	Tullett Prebon	7.04	06/07/2016	3,802,000	97.00	3,687,882.97	3.43%	3,802,000	97.50	3,706,950.00	3.45%	1.13%	0.04%
<b>CASH</b>													
		52	0	5,820,938.72	100.00	5,820,938.72	5.41%	6,675,289.31	100.00	6,675,289.31	6.22%	0.00%	0.00%
<b>TOTAL</b>						<b>107,609,603.33</b>	<b>100.00%</b>			<b>107,299,847.78</b>	<b>100.00%</b>		<b>1.76%</b>

Source - Brown Shipley & Company Limited

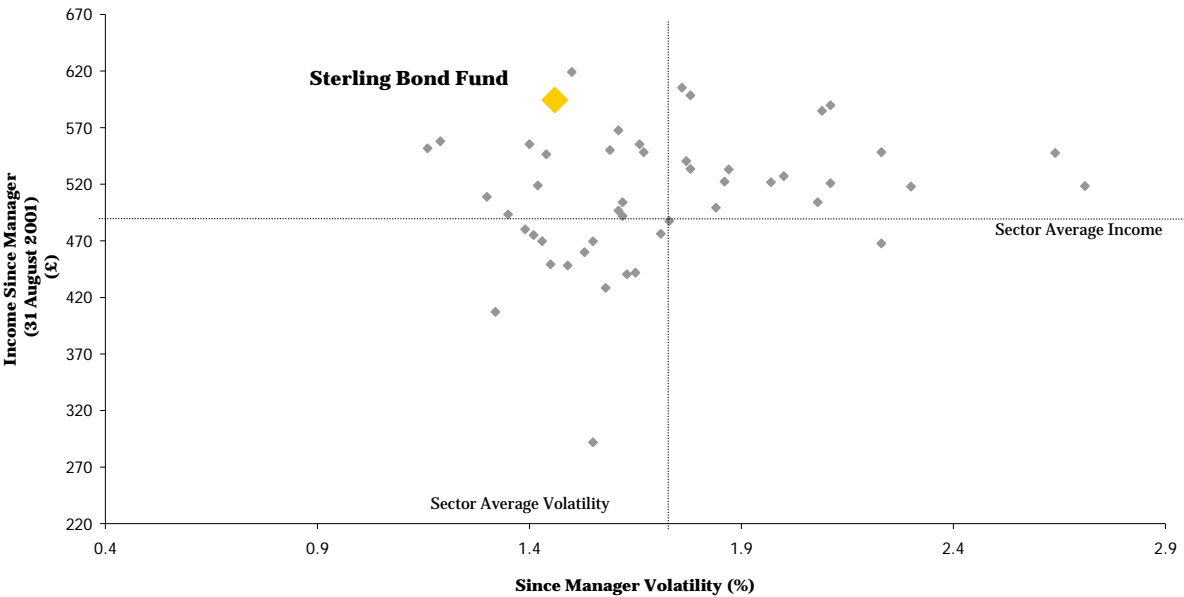
## Risk Conscious Route to Income

The aim of the **IFDS Brown Shipley Sterling Bond Fund** is to offer investors a “Risk Conscious Route to Income”. The fund achieves this by generating a highly competitive level of income, whilst seeking to preserve capital over the medium term. In tandem, the fund aims to deliver a low volatile experience for unit holders.

Given the fund’s objectives, we believe that our adherence to this mandate is best displayed using the scatter plot below.

### A Risk Conscious Route to Income

Source: Lipper Hindsight. Data to 31 October 2011. \*Income since manager (31 August 2001) based upon £1000 initial investment



The graph plots the volatility of funds within the IMA £ Corporate Bond sector against the income generated since manager (31 August 2001) by such funds. Those funds generating above average levels of income, whilst producing below average volatility appear in the north-west quadrant of the plot.



## IFDS BROWN SHIPLEY STERLING BOND FUND

### Activity Review

**“A Risk Conscious Route to Income”**

October 2011

## **Transactions for October 2011**

We strive to provide investors with a level of disclosure and transparency unrivalled within the sector. Our goal is to provide unparalleled access to fund managers and fund information.

To this end, we provide investors with access to details of all transactions undertaken by the fund together with the fund managers' journal entry which accompanies the trade.

Should you have any questions, our fund managers are always available to discuss any aspect of the portfolio. Please feel free to give us a call. Contact details can be found earlier in this publication.

# DEALING FILE NOTE

14 October 2011

<b>Funds Affected:</b>	Sterling Bond Fund
<b>Security:</b>	AMLIN 6.5% 2026 (Callable 2016) COVBS 6.092% Perpetual (Callable 2016)
<b>Action:</b>	Amlin to Coventry “Super 7” Switch

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Such has been the decline in the pricing of subordinated financial debts (particularly banking paper) that yields on certain issues have increased significantly.

Coventry Building Society Tier 1 debts have fallen to such a level that the yields available are now higher than those witnessed on our Amlin position.

Whilst we continue to have strong conviction about the merits of holding Amlin bonds within the portfolio, we feel that the risks associated with Coventry are lower than those faced with Amlin and therefore a yield pickup for the switch represents a mis-pricing.

In order to most efficiently allocate the fund’s capital, we have opted to switch some of the capital currently allocated to Amlin into an increased allocation to Coventry Building Society. The switch re-organises the “Super 7” element of the portfolio such that Coventry takes up a 5% slot, whilst Amlin is relegated to a 3% position.

From a short-term tactical perspective, reducing exposure to Amlin during the hurricane season reduces some of the fund’s episodic risk, particularly given the poor catastrophe climate endured during H1. We would anticipate a stronger environment for Tier 1 paper at financially strong organisations, such as Coventry, during the remainder of the year.

Longer term, the implications of Basle III and the recent Vickers report still leave Building Societies with the need to refinance PIBS, which will become ineligible as risk capital under

the proposed regulations. In our opinion, current market prices fail to take such regulatory changes into account. This represents an opportunity.

<b>SELL</b>	<b>2750/- AMLIN 6.5% 2026 (Callable 2016)</b>
<b>BUY</b>	<b>2000/- COVBS 6.092% Perpetual (Callable 2016)</b>

**Sources:**

**Bank for International Settlements**

# DEALING FILE NOTE

27 October 2011

**Funds Affected:** Sterling Bond Fund

**Security:** SGROLN 5.625% 2020

**Action:** Segro Disposal

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Following interim results in August, we expressed some concerns about developments at Segro. Whilst the balance sheet remained solid post the 2009 recapitalisation exercise, the interim numbers suggested an organisation having some difficulties in letting space into the industrial markets of UK and Europe at acceptable rates. With a high level of vacancies still in evidence, this raised a flag as to the operational prowess of the group.

It was against this backdrop therefore that, also contained within the results were indications that management intended to push ahead with some “speculative” development projects in Europe. Since 2008/09, though development projects had continued, they had been conducted on a pre-let basis and therefore carried less risk.

Given the letting backdrop, we commented at the time that such projects were questionable and the update was “uncomforting”.

At the time, spreads on the bonds were c.+240bps. Though they are wider today (+295bps), the deterioration in the European economy plus the increase in credit spreads has the impact of weakening the ability to let properties in the European industrial space, whilst potentially undermining the valuation of the properties on a yield basis.

Adding to the reasons for disposal, compared to similar such issuers, spreads have held in well. The fund also holds a position in Goodman Group – operating in the industrial sector in Australasia, the group arguably benefits from better demography and a less leveraged balance sheet, yet spreads have widened more dramatically than at Segro and stand at wider levels (+350bps).

At yields of just over 5%, the recent widening in spreads during the past few months provides more efficient means of deploying the capital currently allocated to Segro. There are other positions available to us, offering higher yields, for which we consider a lower amount of risk is undertaken. In keeping with our Fundamental Belief, we have therefore opted to dispose of this line, seeking to reinvest the proceeds elsewhere.

Yesterday's EU leaders summit statement has prompted a strong bid for credit in today's market. Having been quoted spreads of +310bps in recent days, our patience has been rewarded with being able to dispose at our target level today.

SELL                      1750/-                      SGROLN 5.625% 2020

Sources:

Segro Report & Accounts

Goodman Report & Accounts

Bloomberg



## IFDS BROWN SHIPLEY STERLING BOND FUND

### Outlook

**“A Risk Conscious Route to Income”**

October 2011

## Economic Outlook

Regardless of the area of investment these days, the immediate prospect for all asset classes appears to revolve around the developing situation in European sovereign bond markets. Whether it be the outlook for bonds, equity, commodities or property, all eyes are upon the major players in the Greek tragedy currently playing out on the continent. The same is true, not only for market developments but also for near-term economic prospects in most major economies.

In previous editions we have outlined the waves of contagion to be expected to propagate from the inevitable Greek default. Impacting upon the Greek banking system, stability and funding at the European Central Bank (ECB) and in turn the wider European banking network, the biggest risk comes from the possible dearth of demand for other European nation debts and the implications of a default at a larger Euro constituent such as Italy.

Under other systems, such a possibility would not be considered plausible since the central bank would act as the lender of last resort to the Government and hence be able to monetise the national debts via a Quantitative Easing (QE) programme.

The case in point comes via a host of real world examples. Over the past decade, central banks in Japan, the US and UK have all pulled on the QE lever in order to “assist” in the stabilisation of government debt markets against weak economic outruns and large fiscal deficits. The reward for doing so sees bond yields in these nations standing at 1.0%, 2.0% and 2.2% respectively in contrast to the 35% yields currently in evidence on Greek government debt.

It is this discrepancy in the design of the Euro project that threatens to bring down the house. As we have argued for some time now, the only sure fire means of extinguishing the current problems is for the ECB to engage in QE.

On the bright side, the past month brought some flickers of light to this subject. For some time now (since May 2010) the ECB have been intervening in the secondary bond markets via its Securities Market Program. Now operating to the tune of over €170bn the engagement from the ECB has been substantial.

Whilst the intervention from the ECB has certainly assisted the debt markets, the means by which they have funded these purchases via short term loans from the banking sector, has exacerbated the poor liquidity conditions in the inter-bank markets with Dexia being a victim of this phenomenon.

The good news, whence it came, was therefore the announcement from the ECB that they would be providing long term (1 year+) liquidity facilities in unlimited size for all banks. Provided they are able to offer sufficient collateral to secure the loan, this announcement ought to ensure that no European bank suffers a liquidity shortage anytime before 2013.

Coupled, with the liquidity announcement, the ECB also re-launched the Covered Bond Programme – a scheme which had previously lapsed in June 2010. Whilst the size of the scheme was increased only by €40bn, the important facet comes from the fact that such purchases are “non-sterilised”. Outside of the ECB, this term means that the money is created/printed in order to purchase the assets, re-opening the door to QE. If they could put these two pieces of the jigsaw together – printing of money + purchases of sovereign bonds, in our opinion, the crisis would evaporate overnight.

## Market Outlook

Based upon our Economic Outlook, it is our belief that the ECB have the ability to bring a swift and lasting resolution to the current crisis via QE. For the purposes of examining future market developments, however we are required to assess not only the likelihood of this happening, but also the probability of other eventualities.

As such, we propose three basic routes that the situation may develop along:

- Politicians create a credible and lasting solution (Option 1)
- ECB perform QE in order to support sovereign bond markets (Option 2)
- The problem is not solved, prompting a series of defaults and economic depression (Option 3)

Taking each in turn, presently we appear to be progressing along the lines of Option 1 – the political solution. So far, the leaders of the Euro nations have attempted no less than 5 “comprehensive” solutions to the crisis dating back to May 2010 with the initial Greek bail-out and creation of the Securities Market Programme (SMP).

In each instance, whenever the plan appears to have gained any traction, the myriad of players involved and opinions proffered have served to undermine the plan in some way, shape or form. And so it goes on. The latest comprehensive plan was put together during a marathon conference session with sketchy details being announced to the waiting world at 4am. A unanimous agreement it was not.

The reasons for these arduous machinations, whilst frustrating, are understandable. If investors are to look to politicians to create a solution, there has to be an acceptance that any such plan will be compromised by the need to play to both the electorate and the markets. Presently, the desires of these constituents are at times, diametrically opposed and so, until such time that the desires of these parties come together (something we have termed the “coalescing event”) any attempt at a political solution will be subject to attack and the law of unintended consequences.

For these two constituent groups to express a desire for a political solution, it seems likely that the situation will have to deteriorate further. At this point, the “man on the street” will come to realise that the “bankers” of this world do not own the assets which are plummeting in price, but are simply the custodians for the wider population. As prices decline, the impact on jobs, wages, investments, retirements and general asset prices will become increasingly more obvious, therefore helping to change the opinions of those currently clamouring for some sort of utopian collapse of the capitalist system - Option 3. In summary, Option 1 is best described as: “it gets much worse, in order to get better”.

Such pain can be avoided. As we have illustrated previously, via the ECB performing the traditional role of a central bank via the lender of last resort function, the current concerns about nations being able to finance their governmental expenditures would instantly evaporate. Despite what may be claimed, in our opinion, there is in fact an abundance of money present within the system to handle the current crisis. What is required is a re-establishment of confidence in money such that financial functions, which would happen naturally, are put back in place. Option 3 is a possibility. Yet the closer we get towards it, the more likely we are to change track and opt for Options 1 or 2.

## Fund Outlook

Perhaps there could be no greater opportunity than the proposed Greek referendum on the most recent bail out package for us to find the “coalescing event” that we have been expecting.

A “yes” vote would secure the next tranche of financing from the EU and IMF, whilst allowing as much as €100bn of debt to be written off via the agreed haircut process. Whilst the cost of agreeing to such a hand-out/let-off is the loss of economic sovereignty and further austerity measures, the consequences of rejecting this offer would lead to a less structured default situation and possible exit of Greece from the Euro project.

A “no” vote from the Greek public would unleash a number of known consequences (never mind the unknowns). As a Government, Greece’s expenditure outweighs its income, forming a budget deficit. Prior to 2010, these deficits were financed by lending operations in the capital markets.

Post early 2010, the Greek Government has been unable to borrow from the markets and so, was forced to turn to an alternative capital provider. In the absence of a central bank willing to fulfil this role, the Government has had to resort to successive loans funded by the EU nations and the IMF. Such loans have not been provided lightly – instead, each additional loan has been provided only after additional austerity measures have been agreed upon, much to the irk of the Greek population.

The Greek referendum seeks the authority from the people to accept the terms and conditions of the loan package, but without such loans the Government has no means to finance its budget deficit and so would be unable to honour a proportion of its payments – in effect, a “no” vote would therefore be a vote for yet further austerity.

This is of course unless the country subsequently left the Euro and re-established its own central bank from which it could borrow freely (presumably in Drachma).

The consequences of this action (again there are unknowns) would exact further punishment upon the Greek society. Whilst the Government would have the ability to fund its internal deficit, and hence pay wages to public sector workers etc, such payments would be made in a drastically devalued currency with little value on international markets, thereby obliterating the country’s terms of trade.

As a further consequence, aside from the costs of reverting back to a Drachma based economy and payment systems etc, the fact would remain that the debts of the nation and its inhabitants would remain in Euros. Set against the receipt of payments for goods and services in a devalued Drachma, any notion of being able to settle such debts would be eradicated prompting wholesale defaults, bankruptcies and repossessions of assets. Against the alternative of having to endure further austerity measures, a “no” vote equates to turkeys voting for Christmas.

For the fund, this development practically ensures that market conditions are likely to deteriorate until such time that either politicians or the ECB enact more powerful measures. As such, we must remain patient. In time, we would envisage opportunities arising on par, or better than those experienced during the latter part of 2008/early months of 2009. The fund remains liquid, short on duration and sufficiently well focussed that we will not spend the coming months tending to fire-fighting duties. Interesting times lie ahead.



IFDS BROWN SHIPLEY STERLING BOND FUND  
Portfolio Summary

**“A Risk Conscious Route to Income”**

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## IFDS Brown Shipley Sterling Bond Fund

	S	M	L	Totals	
AAA	0.00%	0.00%	0.00%	0.00%	<b>Run Yield (%)</b> 6.30
AA	0.00%	1.36%	0.00%	1.36%	<b>GRY (%)</b> 8.09
A	5.22%	10.23%	0.00%	15.45%	<b>Ave. Maturity</b> 6.96
BBB	9.79%	36.63%	0.00%	46.42%	<b>Duration</b> 4.37
<BBB	3.36%	3.12%	0.00%	6.48%	<b>Mod Duration</b> 4.05
N	8.51%	11.98%	3.58%	24.07%	<b>Adj Duration</b> 4.17
<b>Totals</b>	<b>26.87%</b>	<b>63.32%</b>	<b>3.58%</b>	<b>93.78%</b>	
			Futures P&L	0.00%	
			Cash	6.22%	
			<b>Total</b>	<b>100.00%</b>	

### Asset Allocation

Fixed Interest	87.77%
Convertible Securities	0.00%
PIBS	4.60%
Government Securities	0.00%
Preferred Equity	0.00%
Structured Note	1.41%
Futures P&L	0.00%
Cash	6.22%
<b>Total</b>	<b>100.00%</b>
Of which index linked	0.00%
Estimated addition to GRY	0.00%

### Credit Quality

AAA	0.00%
AA	1.36%
A	15.45%
BBB	46.42%
<BBB	6.48%
Unrated	24.07%
Futures P&L	0.00%
Cash	6.22%
<b>Total</b>	<b>100.00%</b>

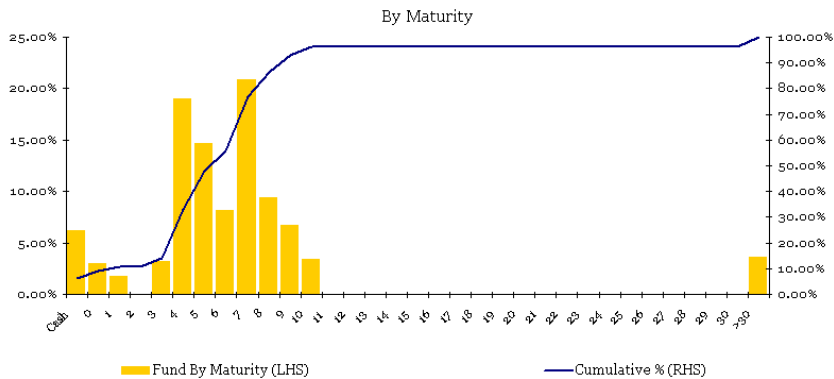
### Top 10 Sectors

1 Banks	22.07%
2 General Financial	11.82%
3 Real Estate	7.28%
4 Electricity	6.69%
5 Nonlife Insurance	6.22%
6 Travel & Leisure	5.22%
7 General Retailers	4.92%
8 Media	4.72%
9 Fixed Line Telecommunications	4.21%
10 Mining	3.25%
<b>Top 10 Sectors</b>	<b>76.42%</b>
8 Other Sectors	17.36%
Futures P&L	0.00%
Cash	6.22%
<b>Total</b>	<b>100.00%</b>

### Top 10 Issuers

1 BNP Paribas	5.22%
2 Coventry Building Society	4.60%
3 Standard Chartered	3.58%
4 Tullett Prebon	3.45%
5 ESB	3.22%
6 Provident Financial	3.20%
7 Amlin	3.11%
8 Enterprise Inns	2.53%
9 Birmingham Airport	2.06%
10 Nationwide	1.90%
<b>Top 10 Issuers</b>	<b>32.88%</b>
39 Other Issuers	60.90%
Futures P&L	0.00%
Cash	6.22%
<b>49 Total</b>	<b>100.00%</b>

## FUND DISTRIBUTION



Data as at 31/10/2011

Source: Brown Shipley

## “Non-Rated” Positions

Our Portfolio Summary details the proportion of the fund allocated to “non-rated” positions. This is an area of the portfolio we are regularly quizzed upon and so, in our time honoured tradition of complete transparency, the list below details each of our “non-rated” positions.

For the purposes of categorisation, the fund adopts the Bloomberg Composite method of ratings. The Bloomberg Composite is a blend of a security’s Moodys, S&P, Fitch and DBRS ratings. The rating agencies are evenly weighted when calculating the composite. The Composite is the average of the existing ratings, rounded down to the lower rating in the case the composite is between two ratings. **No composite is generated if the bond is rated by only one agency.**

In instances where no ratings exist from any agency, we “map” the ratings using a variety of techniques.

Issuer	Fund Exposure	S&P	Moody’s	Fitch	Mapped	Comments
Beazley	1.64%	BBB-				
Birmingham Airport	2.06%	BBB+				
Capital Shopping	1.71%				BBB+	Mapped to Westfield (A-). Adjusted for gearing and lower diversity.
City of London	0.82%				A-	Mapped to 3i (BBB+). Adjusted for gearing levels.
Enterprise Inns	2.53%	BB+				
First Hydro	1.81%				BBB-	Mapped to Wessex Water (BBB+). Adjusted for lower diversity.
Henderson Group	1.87%				BBB+	Mapped to Fidelity (BBB+).
Home Group	1.83%				BBB+	Mapped to similar housing organisations.
John Lewis	1.70%				BBB	Mapped to M&S (BBB-). Adjusted for gearing levels and margin comparison.
Kensington Group	1.48%			BBB-		Uses Investec’s rating.
Provident Financial	3.20%			BBB		
Standard Chartered	3.58%		Baa3			
<b>Total</b>	<b>24.07%</b>					
Of which Mapped:	7.87%					

Source: Bloomberg, Brown Shipley Calculations

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