

Hi

Happy New Year, and as I am writing this in Singapore, Gong Xi Fa Cai! I hope the year of the monkey is good to you.

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Having read numerous economic reviews at the turn of the year, the general consensus is very positive and for a change, most economists seem to agree.

## 1. Economic Outlook

### Growth

- The world economy has clearly passed a point of inflexion. While there may still be arguments about the strength of recovery in Europe and Japan, nobody seriously doubts that the global cycle has turned and something of a boom lies ahead. There is always a pessimist that argues this is a bear market rally, but the overwhelming majority of economists seem to think otherwise.
- There should be no great surprises on growth in America and Britain. Fuelled by the almost unprecedented stimulus from rock-bottom interest rates, exploding budget deficits and a 20 per cent devaluation of the dollar, the US economy is expected to expand by about 4-5% (and achieving this figure will make 2004 the strongest year for US growth since 1984). Unemployment is falling, albeit slowly, company profits are increasing and so is capital investment.
- The boom in consumer refinancing in the US and UK which has seen householders cash in on the rising value of their homes will end and so reduce consumer spending, which will put a brake on growth. The explosive growth in property prices will also end with very conservative or even no growth. They are expected to drift down next year.
- Britain should also achieve Gordon Brown's forecast of 3 per cent growth comfortably, making it the 13th year of consecutive economic growth. Japan is likely to grow by 2.5%, Korea by 5.5%, China by 7.5% and the rest of Asia by 7%.
- Europe is likely to disappoint, struggling to grow 1%. The huge revaluation of the euro this year, not only against the dollar but also against most Asian currencies and the pound, will act as a powerful brake on the continental economy — and the normal lag between the currency strengthening and exports falling off, suggest that its impact has hardly begun to be felt yet. Eastern Europe should continue its strong growth.
- Service industries will continue their migration to India and manufacturing to China, but having just come back from our office in Ho Chi Min City (Saigon), keep an eye on Vietnam.

- The one serious threat to this rosy picture is the US debt. Consumers have their highest ever debt levels, hedge funds are highly leveraged and the US balance of payments is the highest ever and will cause severe inflation.

### **Inflation**

- America, however, could have some nasty surprises. With interest rates some 5 per cent below nominal GDP growth, a devaluing dollar, exploding budget deficits and pre-election protectionist gimmicks, the US now has the most inflationary combination of economic policies seen in any major economy since the 1970s. Inflation is predicted at 3% this year followed by 4-5% next year.

### **Interest Rates**

- Rising inflation will mean higher interest rates. With a US election coming there will be pressure to delay this as long as possible but it is inevitable. They could go as high as 2.5% in the US and 4.5% in UK by the end of the year. However they will remain low in Europe (1.5%) & Japan (zero).

### **Currencies**

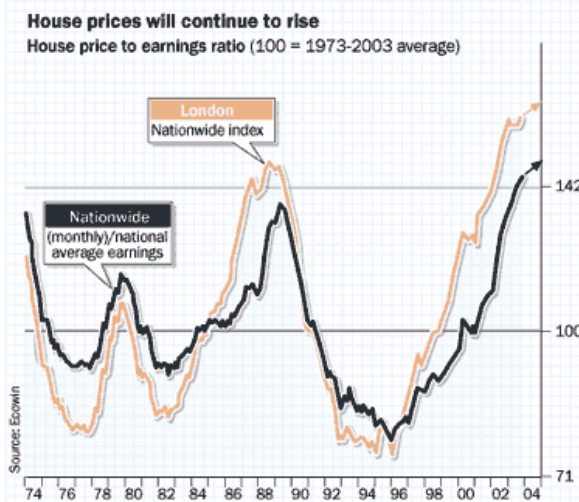
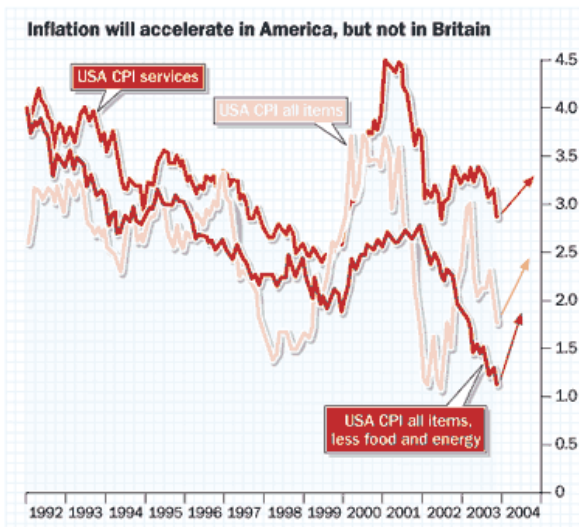
- The main concern is the weakness of the US dollar. A breakdown of confidence would have a dramatic effect. The US government are doing nothing to support the dollar, so recovery will come only by default. The dollar is likely to remain weak for most of the year but with the European economy slumping, the euro will look even worse. Most economists predict that the dollar will recover against the euro - and so will the pound - but will remain weak against the yen and other Asian currencies. Expectations are that it could weaken a little more and then settle around \$1.30 to euro and \$1.80 to sterling and then rise towards year-end.
- The White House has been pressing China to revalue its currency and if it gets its way, it may find that China's willingness to keep buying US Treasury Bills may diminish and this will push up interest rates and cause the dollar to fall dramatically as it could have a knock on effect around Asia. The US is very dependent on Asian countries to keep buying American debt instruments. If there is a change in this policy, then the implications could be very severe.

### **Markets**

- Given the excellent US growth outlook, valuations on Wall Street are only moderately expensive and thus there is scope for further gains in the short term. By the middle of the year, however, rising long-term interest rates and fears of inflation could give investors quite a shock and share prices will probably end the year around where they started. As usual, there is a large range of predictions from -10% to +10%. However I would add that a market correction of around 10% is not unlikely at these levels as the market has risen substantially in the last 12 -16 months and they may need a breather as they look for direction again.
- The British market should do somewhat better, with the FTSE 100 ending the year up to 12% higher. European equity markets, by contrast, are likely to see bigger losses, since the French and German markets assume economic recoveries that will not occur. Eastern Europe should continue to make very good gains.

- The one part of the world where stock market investors can expect to prosper this year is the Far East. Japanese shares remain extremely cheap relative to corporate cash flows and the shift in global growth leadership to Asia is bound to create some great investment opportunities, at least in the short to medium term. Thailand was the best performing market world-wide last year with India and China close behind.
- The bond market is likely to fall substantially as interest rates rise. Because of interest rate rises and inflation, bond yields are likely to rise about 2% above the present 10 year bond yield of 4.2% which will depress the price of bonds already in issue.
- Gold will continue to rise while the dollar falls but provided confidence holds up, the dollar may be close to its bottom.

To bang the old drum again, this scenario reinforces my belief that a fund of funds is the best way to invest in the stock markets as the fund managers will move assets towards Asia to take advantage of the growth there and then move it out again as the west recovers in subsequent years. From a currency point of view it is advisable not to convert out of USD at present unless you need it in the short term. The “comfortable” economic level for sterling is around \$1.55 and for the euro around \$1.05. If you want to speculate, the yen is probably a good currency to hold this year. I have included the following charts from The Times



## 2. Investment Strategy

As always, diversification between fund managers and between asset classes (particularly for lump sums) is the key to successful investing. In particular, as markets grow at different rates, an investment approach using “funds of funds” is the best way to ensure your money is being actively managed. The old days of staying with the same funds are no longer the best policy. The Lanson Financial & Collins Stewart funds of funds have out performed the markets over the past 2 years and show every sign of continuing to do so. Both groups select the best performing regions and then the best funds in each region. They review the performance of their selected funds and move money out if they drop. Lanson uses an automated methodology to select the funds and determine a “stop loss” whereas Collins Stewart use a macro economic methodology to determine when to enter and leave a fund. The main thing though is that both groups actively manage their assets. Lanson changed fund manager 2 years ago and improved their strategy and the changes have worked very well as you can see from the figures below.

The Momentum All Weather Fund is a fund of hedge funds designed to be of low volatility and give steady low risk growth and can be used to balance the predominantly equity investments of Lanson Financial & Collins Stewart.

One thing is proven, that the way to accumulate wealth is by saving regularly each month. Many people forget this when markets are down but those who have continued to save through the down periods will show the most gain as markets recover. Regular saving means that you “average in” over a long period and are not so subjected to market fluctuations. Long term monthly savers should still expect to see the best return in funds such as Lanson and Collins Stewart who are primarily equity based but also use hedge funds and bonds

For example saving \$500 per month for 25 years at a growth rate of 10% pa (the average S&P 500 growth since 1975) yields over \$660,000. Or at 8% (the average very long term S&P growth rate) yields \$475,000.

Those making savings now will see particularly good growth in the coming years as we recover from the worst market crash since 1974. Now is a good time to review your contribution level.

Lump sums savers should consider putting some of their portfolio into viaticals (traded life policies) as these are offering the safe returns (9-10% pa or more). We can offer equity funds of funds, funds of hedge funds, fund of property funds, funds of traded life policies and funds of endowment polices. Also gold and bond funds.

## 3. Fund Performance

To 31st<sup>th</sup> December 2003

	Price	1 month	1 year	since 1 Jan 2002	
<b>Lanson International Growth</b>	1.115	6.8	32.6%	25.1%	since launch in May02
<b>Lanson Optima Fund</b>	0.661	6.3%	28.5%	15.6%	
<b>Collins Stewart Aggressive USD</b>	1.225	7.0%	31.7%	37.6%	
<b>Collins Stewart Growth USD</b>	1.014	4.1%	25.0%	16.3%	
<b>Student Accommodation (GBP)</b>	1.217	0.3%	6.5%	17.2%	Closed to new investors
<b>Momentum All Weather (USD)</b>	1.076	0.7%	7.8%	8.4%	
<b>S&amp;P 500 Capital Return</b>	1,108	4.8%	22.0%	-5.5%	
<b>Dow Jones Indust Cap Return</b>	10,410	6.4%	21.0%	1.5%	
<b>NASDAQ</b>	2,007	2.4%	44.7%	-2.6%	
<b>FTSE 100 (in GBP)</b>	4,510	3.9%	12.6%	-15.3%	
<b>Quadriga GCT USD</b>	2354.70	16.28%	26.35%	113.8%	
<b>Premier Low Risk Fund (GBP)</b>	1.269	-1.4%	2.7%	8.3%	

It was a good year for equity markets and the Collins Stewart & Lanson Financial funds beat the broader indices and most managed funds handsomely, proving that this is the best strategy.

#### Lanson Financial current fund allocation:

	% Market Value	
	OptimaLIG	
Fidelity European	14.23	15.27
Parvest US Small Cap	13.09	13.96
Parvest US Quant Fund	12.38	13.78
Gartmore Emerging Mkts	13.30	0.00
MLIIF US Opportunities	12.33	9.30
Schroder UK Alpha Plus	10.54	0.00
Mellon Global Bond Portfolio	10.35	10.15
HSBC India	1.32	8.33
Clariden Biotechnology	0.83	5.25
JPMF US Technology	0.89	5.60
JF Pacific Technology	0.76	4.77
AHL Diversified Futures	0.67	4.21
Equities	0.33	2.06
Cash (\$ & £ Deposit)	8.98	7.32
Total	100%	100%

Hedge funds did well, although Quadriga had its worst year at only 26% growth! This was because for most of the year, markets lacked major direction.

#### 4. New Guaranteed Hedge Funds

We work with the MAN Investment Group and with Quadriga. MAN is a British company and the largest hedge fund management group in the world now with over \$30 billion under management.

Quadriga is an Austrian company and manages over \$500 million in managed futures.

Both companies offer hedge funds with a capital guarantee from time to time and both have a fund available very soon:

**MAN RMF Multi-Style** fund is a multi strategy hedge fund that guarantees your capital (using a major bank) and targets 13-15% annualised growth with 7-9% volatility. It has a profit lock in feature. Previous tranches over the last 6 years have achieved their targets. Minimum investment is \$50,000. There will be diminishing penalties for exit within 5 years. Open to receive funds from 9<sup>th</sup> Feb – 19<sup>th</sup> March 2004. Minimum investment \$50,000

**Quadriga Superfund Garant V** is a single manager managed futures hedge fund that provides 100% capital guarantee (from ABN Amro) and targets 10-12% annualised growth with maximum 10% volatility. It has a profit lock in feature. Previous tranches have all been successful. There are diminishing penalties for exit within 5 years. It is open now until February 29<sup>th</sup> 2004. Minimum investment \$15,000.

Americans can only invest in these through an offshore portfolio bond.

Hedge funds are very complex but have now come of age and proved very reliable over the past years showing no correlation to stock markets and making good gains. Certainly they should now form part of a balanced portfolio. If you would like to know more, please let your consultant know.

#### 5. Other services

If you would like a review of your investments – and I would earnestly suggest that you look at the level of your monthly contributions and consider restarting or increasing them so you do not miss out – then please let me know.

Please don't forget that we can organise your medical insurance, life insurance, critical illness insurance and if you are British, income protection insurance. Please contact your consultant for more information