



**LIONTRUST**

# **LIONTRUST EUROPEAN GROWTH FUND**

**MANAGER'S SHORT FINAL REPORT**  
FOR THE YEAR ENDED 30TH APRIL 2011



Managed by Gary West &  
James Inglis-Jones in accordance with  
**The Liontrust Cashflow Solution**

# THE LIONTRUST CASHFLOW SOLUTION

LIONTRUST EUROPEAN GROWTH FUND IS MANAGED BY **GARY WEST** AND **JAMES INGLIS-JONES** IN ACCORDANCE WITH THEIR INVESTMENT PROCESS FOR EUROPEAN EQUITY PORTFOLIOS, **THE LIONTRUST CASHFLOW SOLUTION.**



This Fund aims to provide long-term capital growth through investment in a concentrated portfolio of mainly European companies (excluding the UK), broadly equally weighted. It invests in companies with strong cash flows which we believe are likely to beat investors' low profit expectations. Cash flows provide an accurate guide to future profits growth. They reveal valuable information about a company's investment decisions and its managers' prudence in recognising reported profits. The concentration of the portfolio could mean that the Fund will be volatile when compared with its benchmark. There are no limits on geographical or industrial sector exposures, which will not closely mirror that of the benchmark.

# MARKET ENVIRONMENT

In the year under review the FTSE All-World Developed Europe ex UK Index rose 16.9% driven by strong returns from stocks in the Automobiles & Parts (+41.0%), Personal Goods (+38.9%) and REITS (+38.4%) sectors. Alternative Energy (-46.4%), Leisure Goods (-21.1%) and Utilities (-4.4%) stocks fared poorly. The Fund over the course of this period rose 24.2%, a significantly better return than the Index and the peer group average who returned 16.9% and 15.2% respectively. Investors who have held the Fund since inception in November 2006 have seen a return of +49.0%. An investment in the Index or a composite of the peer group would have yielded less than half the return over this period, +24.2% and +18.5% respectively.

Over the course of the last twelve months optimism regarding the momentum of global economic recovery increased as investors responded to better than expected economic data. In Europe manufacturing continued down a path of recovery as both investment and export demand remained strong. Germany, with its export oriented economy, benefited particularly from these developments. European companies with a high proportion of overseas exposure to emerging markets have benefited from robust growth in emerging markets such as China, India and Brazil. However, companies with domestic exposure, such as general retailers, have continued to struggle with sluggish end demand.

In the first quarter of 2011 the market remained remarkably robust in the face of increased turmoil in the Middle East, the Japanese earthquake, rising oil prices and further signs of stress in peripheral

Europe's sovereign debt. However, there remains a tension between the short-term tangible evidence of recovery contingent on continued emerging market growth and longer-term concerns regarding fears of a slowdown in emerging markets, particularly China; continued sovereign debt concerns in Europe (which will be only exacerbated by emerging public health and pension liabilities in forthcoming years); and, the impact of domestic government austerity measures. Furthermore, valuation measures, adjusted for the economic cycle, tell us that the market is expensive relative to its history, suggesting some caution is warranted.

## Analysis of Portfolio Return

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A powerful theme driving stock market returns in 2010 was investor preference for companies with significant exposure to emerging markets. In addition, having paid very little attention to whether or not companies were meeting their earnings expectations in 2009 and the first half of 2010, it became much more important for companies to meet their profit expectations in the second half of last year. The tendency for investors to focus more on profit delivery, as the stock market recovery matures, is usual and provided a constructive backdrop for our process over the course of the year.

The Fund responded well in such an environment as our process did a good job earlier in the year highlighting companies during our research period that went on to deliver strong third quarter results that exceeded analysts' expectations. However, in January 2011 this favourable environment

## MARKET ENVIRONMENT CONTINUED

dramatically reversed and there was a significant change of leadership, unusual for this stage of the stock market cycle. This was a negative development for the portfolio, causing the Fund to lag behind the Index and peer group at the start of this calendar year.

There appear to have been three elements of this marked change in European stock markets: a shift out of stocks with exposure to emerging markets in favour of stocks with exposure to developed Europe; a move from stocks in the core of Europe to peripheral regions that had been roiled by sovereign debt concerns in 2010; and, a violent change of leadership with stocks that had performed well in 2010 underperforming dramatically in January, whilst underperforming stocks in 2010 increased significantly in value. What was unusual about this rotation was that price reversals of such magnitude are normally associated with market troughs or peaks, or turning points in the economic cycle. These developments had an adverse impact on the portfolio in the short term. However, the impact was insufficient to offset the strong returns delivered earlier in the year, resulting in a good return overall for the Fund over the course of the financial year as a whole.

Over the course of the Fund's financial year there were some stocks that performed outstandingly well. Of note were *Lundin Petroleum* (+145.1%), *Tekla* (+125.8%) and *Andritz* (+67.5%). With the exception of *Tekla*, which received a bid from Trimble Navigation in early May 2011, *Lundin Petroleum* and *Andritz* both benefited from corporate earnings news that was significantly better than analysts or investors had expected. *Lundin Petroleum*, the

Swedish oil exploration company, enjoyed good news over the course of the year delivering production and earnings updates in their quarterly results that were much better than expected. However, the most significant development for the group was the discovery of a significant oil find in their Luno field in the North Sea. Subsequent to the publication of the Avalsnes oil discovery, *Lundin Petroleum* published a series of further updates elaborating on the size and potential of the Avalsnes prospect and the company's broader exploration portfolio. These were well received by the market causing the stock to move steadily higher over the course of the year. We originally purchased *Lundin Petroleum* for the portfolio as we were impressed by their cash flow generation as well as their cultural focus on capital return and cash generation.

*Andritz* has also been an extremely rewarding investment for the Fund. The group manufactures plant equipment principally for the paper and packaging, hydropower and metal industries. Despite a recovery in their business that was well beyond analyst's expectations, a further positive surprise has been the operational gearing effect of this recovery on the group's earnings. Even more impressive has been its ability over the course of the year to sustain strong cash flow despite the recovery in their turnover, a characteristic that often drains cash flow from a business owing to the need to invest in working capital to support higher sales. *Andritz's* cash flow development over the course of 2010 was sufficiently strong to cause the stock to continue to rank in the best 20% of the market on cash flow this year and as a result the stock will continue to be held in the Fund.

At the other end of the performance spectrum *Electrolux* (-1.3%), *AstraZeneca* (-0.3%) and *Ahold* (-0.25%) performed poorly. *Electrolux* performed poorly due to investor concerns about the impact of rising raw material prices and the ability of the group to recover these rising prices through price increases. *AstraZeneca* and *Ahold*, as companies in more defensive sectors, suffered owing to investor preference for cyclicality. However, in addition to this negative head wind both stocks also delivered somewhat disappointing corporate news over the course of the year. *AstraZeneca* suffered from two pipeline setbacks in December and concerns regarding the FDA's deliberations over *Brilinta*, *AstraZeneca's* experimental blood thinning pill. Furthermore, their first quarter 2011 results showed the continued negative impact of generic drug launches which was troubling to investors and analysts. *Ahold* reported a series of underwhelming corporate results that tended to slightly miss expectations, causing a series of earnings downgrades in the last year.

## Portfolio Activity and Construction

Portfolio turnover is highly seasonal due to our focus on company annual report and accounts as the basis of our research into cash flows. As a reminder, the *Cashflow Solution* investment process that we have developed is designed to identify companies from their annual reported accounts that are prudently run, generate strong cash flows from their operating assets, and are available at a bargain price. Companies that fit this description are most likely, in our experience, to deliver positive surprises to investors either from unexpectedly good earnings or

return on invested capital. Our minimum requirement for a stock to be considered as an investment is that their cash flow characteristics are sufficiently attractive to rank in the best 20% of the universe of European stocks we address. In our experience, measured over long time periods, buying strong cash flow companies cheaply produces consistently positive results.

Once companies begin to report full audited annual accounts, usually between March and April, we can begin our qualitative research into new ideas for the portfolio. By the middle of May we have usually completed this research, resulting in a significant rise in portfolio turnover as the portfolio is restructured to reflect the new ideas. In the first half of the financial year we executed a number of trades in order to reflect our research into the cycle of annual reporting in 2010. We commented on these developments in the fund's interim report. As a reminder, having sold eight companies over the course of the earnings season beginning in January 2010, we then sold a further seven companies in May 2010 that failed to generate sufficient cash flows: *Munich Re*, *Topdanmark*, *Kas Bank*, *Colruyt*, *Kuoni*, *Interroll* and *Alstom*. However, these sales were more than offset by the purchase of 20 new additions to the portfolio that passed our assessment of their final results: *Lundin Petroleum*, *Fred Olsen Energy*, *Omega Pharma*, *Nutreco*, *Societe BIC*, *Electrolux*, *Telenor*, *Metro*, *Ahold*, *Axfood*, *Mediq*, *Sodexo*, *Schindler*, *Andritz*, *Semperit*, *Kaba*, *Securitas*, *Umicore*, *Clariant* and *Tessenderlo*. Earlier in the year, we had also purchased *Alfa Laval*, *Metso*, *Kongsberg Gruppen*, *Cargotec* and *M-Real*. The holdings we retained in

# MARKET ENVIRONMENT CONTINUED

the portfolio from 2009 were *Bolsas y Mercados*, *Technip*, *Tekla*, *Wincor Nixdorf*, *AstraZeneca*, *Ekomes*, *Mobistar*, *Publicis*, *Vallourec*, *CFE*, *Wacker Chemie* and *Eramet*. These changes had an effect on the sector weights within the portfolio arising from our underlying stock selections. The notable difference was the reduction in the Fund's exposure to Financials which dropped from a sector weighting of 12.3% earlier in 2010 to only 2.5%, whilst the exposure to Basic Materials and Consumer Goods companies both increased to 10.5% and 16.7% respectively.

The scale of the changes to the portfolio in the first half of the fund's financial year reflected the impact of the financial crisis on company balance sheets and cash flows over the course of 2009. We found a number of cyclical companies had strong cash flows as a consequence of the working capital benefit brought about by falling sales in 2009. Some of these companies had the characteristics our process seeks to identify and were included in the portfolio.

In the second half of the financial year there was no change to the portfolio. However, over the course of March and April we were able to conclude our research into the reported annual results of stocks in the portfolio along with a number of new ideas for the portfolio. By the end of the year under review we were in a position to draw up a list of transactions to

reflect our research to be implemented in May and which we will report upon in the Fund's interim report later this year.

## Outlook

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Having concluded our research into new and existing ideas during the year under review it seems clear that the process has favoured higher quality companies this year - measured by their ability to generate consistently high cash returns from their operating assets. Many of the cyclical companies that were more in vogue last year have had to reinvest in working capital as their sales have recovered. This reinvestment into working capital has acted as a drain on cash flow, with the result that cyclical companies' cash flow characteristics are now less robust than they were at the bottom of the economic cycle. In 2011 we will run a more concentrated portfolio reflecting a greater depth of research this year. Our expectation is that the environment should continue to be constructive for our process as it is usual at this stage of the market cycle for investors to place a premium on companies that can exceed earnings expectations, whilst shunning companies that disappoint short-term profit targets.

### Gary West & James Inglis-Jones

Liontrust European Investment Services Limited  
June 2011

# FUND PROFILE

## Investment Objective and Policy

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The investment objective of the Fund is to provide long-term capital growth through a concentrated portfolio of investments primarily in European companies excluding the UK.

Although the Fund may invest in all economic sectors in all parts of the world, it is intended that it will currently invest primarily in equities in companies incorporated in any European Economic Area ("EEA") Member State, together with Switzerland, but other than the UK, which are listed on a recognised stock exchange of an EEA Member State or Switzerland. The Fund may also invest in transferable securities, money market instruments, warrants, cash and near cash and deposits. The Fund may also invest up to 10% of its property in units or shares in collective investment schemes. The Fund is permitted to use derivatives for the purposes of efficient portfolio management and for investment purposes.

## Investment Approach

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This Fund aims to provide long-term capital growth through investment in a concentrated portfolio of mainly European companies (excluding the UK), broadly equally weighted. It invests in companies with strong cash flows which we believe are likely to beat investors' low profit expectations. Cash flows provide an accurate guide to future profits growth. They reveal valuable information about a company's investment decisions and its managers' prudence in recognising reported profits. There are no limits on geographical or industrial sector exposures, which will not closely mirror that of the benchmark.

## Risk Profile

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The Fund is invested exclusively in European securities (excluding the UK). The principal risks identified by the manager are those associated with foreign currency risk and stock market investments. The concentration of the portfolio could mean that the Fund's returns are volatile when compared with its benchmark the FTSE All-World Developed Europe ex UK Index.

## Total Expense Ratio

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	30th April 2011	30th April 2010
Class R income units	1.69%	1.64%
Class I income units*	0.97%	—

\* launched 1st November 2010

# PERFORMANCE

<b>Net Asset Values <i>pence per unit</i></b>			
	<b>30th April 2011</b>	<b>30th April 2010</b>	<b>% Change</b>
Class R income units	132.26	107.70	+22.80
Class I income units*	132.47	–	–

The Fund distributes income once per annum, on 30th June. The ex-dividend date is 1st May each year. Income can be reinvested to purchase units at no initial charge.

<b>Distributions <i>pence per unit</i></b>		
	<b>30th April 2011</b>	<b>30th April 2010</b>
Class R income units	1.48	1.24
Class I income units*	1.75	–

<b>Total Return (%)</b>				
	<b>6 months</b>	<b>1 year</b>	<b>3 years</b>	<b>Since launch<sup>†</sup></b>
Liontrust European Growth Fund	15.3	24.2	24.1	49.0
FTSE All-World Developed Europe ex UK Index	12.0	16.9	10.3	24.2
Quartile Ranking	1	1	1	1

<b>Discrete Years' Performance (%)</b>					
<b>To previous quarter, 12 months ending:</b>	<b>Mar '07</b>	<b>Mar '08</b>	<b>Mar '09</b>	<b>Mar '10</b>	<b>Mar '11</b>
Liontrust European Growth Fund	–	3.2	-30.3	50.7	20.4
FTSE All-World Developed Europe ex UK Index	12.4	2.8	-30.8	48.2	7.5

Up-to-date past performance information may be obtained from the Fund's most recent fact sheet, available on our website ([www.liontrust.co.uk](http://www.liontrust.co.uk)) or by calling our Administration and Dealing team on 0844 892 1007.

Past performance is not a guide to future performance. The value of investments and the income from them can fall as well as rise and are not guaranteed. Investors may not get back the amount originally subscribed. The issue of units in the Fund may be subject to an initial charge, which is likely to have an impact on the realisable value of the investment, particularly in the short term. Equity investment should always be considered as long term.

Performance data source: Financial Express as at 30.04.11, total return, bid-to-bid.

\* Launched 01.11.10

<sup>†</sup> Launch date 15.11.06

# PORTFOLIO

Geographical Breakdown				
Country	FTSE All-World Developed Europe ex UK Index	Liontrust European Growth Fund		
	30th April 2011 %	30th April 2011 %	30th April 2010 %	
Austria	0.83	5.70	–	
Belgium	1.99	12.45	11.97	
Denmark	2.71	–	3.24	
Finland	2.24	10.08	15.68	
France	23.84	13.25	24.96	
Germany	19.03	7.73	10.86	
Greece	0.50	–	–	
Ireland	0.56	–	–	
Italy	7.11	–	–	
Luxembourg	0.04	–	–	
Netherlands	6.09	6.33	0.61	
Norway	2.15	9.42	10.15	
Portugal	0.73	–	–	
Spain	8.59	2.24	4.14	
Sweden	7.16	15.54	9.04	
Switzerland	16.43	7.90	6.26	
		<b>90.64</b>	<b>96.91</b>	
<b>Cash (including SSgA* cash deposits)</b>		<b>9.36</b>	<b>3.09</b>	
		<b>100.00</b>	<b>100.00</b>	

\*State Street Global Advisors

## PORTFOLIO CONTINUED

Top 10 Holdings			
As at 30th April 2011		As at 30th April 2010	
	%		%
Lundin Petroleum	5.16	Ekornes	6.75
Umicore	3.40	Technip	6.45
Kongsberg Gruppen	2.99	Vallourec	5.60
Wacker Chemie	2.96	Publicis Groupe	5.51
Cargotec	2.90	Colruyt	4.98
Semperit	2.87	AstraZeneca	4.92
CFE	2.87	Tekla	4.87
Andritz	2.83	Wacker Chemie	4.84
Schindler	2.80	Mobistar	4.38
Clariant	2.60	Bolsas y Mercados	4.14
<b>Total</b>	<b>31.38</b>	<b>Total</b>	<b>52.44</b>

## FURTHER INFORMATION

### Unitholder Notice:

#### Change of Name

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On 30th September 2010, the Fund underwent a change of name from Liontrust Continental Europe Fund to European Growth Fund. Any historical reports available on the Liontrust website can be found under the name in use at the date to which the reports pertain.

#### Investment & Borrowing Powers – Investment in other Collective Investment Schemes

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Paragraph 13 (e) of the Fund's Prospectus sets out the limitations for the Fund investing in other Collective Investment Schemes. We have amended the rule references in this clause of the Prospectus so that they reflect the COLL regulations of the FSA Handbook, which replaced the CIS regulations, as previously noted within this clause. Whilst this has the potential to widen the universe of available collective investment schemes available, it is not intended that this will affect the way the fund is currently invested. The investment limits have not changed.

#### Liontrust Asset Management Plc

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Liontrust provides portfolio management services in UK and European equities and in fixed income securities. These are managed on a long-only, long/short and absolute return basis through unit trusts, individual savings accounts (ISAs), offshore funds, pooled pension funds and segregated institutional accounts. The Group currently manages £1.3 billion (as at 31st March 2011).

We market our investment products to professional investors, predominantly in the UK and Continental Europe. These include pension funds and other institutional investors, family offices, private banks, private client managers, multi-managers, stockbrokers and financial advisers. Some private clients, to whom no advice has been given, have chosen independently to invest with us.

# FURTHER INFORMATION CONTINUED

## Further Information, Report & Financial Statements

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Further information on the Fund and its portfolio, the Manager's Long Final and Interim Reports & Financial Statements and the Prospectus and Simplified Prospectus are available free of charge from the Manager upon request, and from [www.liontrust.co.uk](http://www.liontrust.co.uk).

## The Manager

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Liontrust Fund Partners LLP, 2 Savoy Court, London WC2R 0EZ.

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Authorised and regulated by the Financial Services Authority.



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Authorised and regulated by the Financial Services Authority.