




LIONTRUST

LIONTRUST UK GROWTH FUND

FINAL REPORT

FOR THE YEAR ENDED 31ST DECEMBER 2010



Managed by Anthony Cross &
Julian Fosh in accordance with

The Liontrust Economic Advantage

THE LIONTRUST ECONOMIC ADVANTAGE

LIONTRUST UK GROWTH FUND
IS MANAGED BY **ANTHONY CROSS** AND
JULIAN FOSH IN ACCORDANCE
WITH THEIR INVESTMENT PROCESS
FOR UK EQUITY PORTFOLIOS,
THE LIONTRUST ECONOMIC ADVANTAGE.



This unit trust is managed to produce long-term capital growth using a disciplined investment approach which aims to identify UK companies whose competitive strengths (“Economic Advantage”) allow them to sustain a higher than average level of profitability for longer than expected. Economic Advantage is the collection of distinctive characteristics of a company that competitors struggle to reproduce. These assets deliver pricing power, protect margins, and thus drive sustained profitability. The market rewards excess profitability, particularly when it is higher than consensus expectations. The Fund invests in a portfolio of competitive UK companies which we believe will surprise the market with the profits growth.

MARKET REVIEW

Market Review

Whilst economic news from the UK and US remained volatile, the overall picture was one of gradual improvement. It was impossible to gauge whether the improvement was due to the sheer scale of the economic stimulus or a genuine and sustainable pick-up in economic activity. What was notable was the continued robustness of emerging market demand and this buoyed the results of the international engineering and service companies in particular. Sovereign debt issues, particularly within Europe, continued to be a feature with successive crises in Greece, Spain and Ireland prompting significant bail-outs and rescues. However, despite resultant market jitters, this did not overwhelm the sense of increased economic optimism and in the main, corporate results were encouraging. In the UK, the advent of a coalition government with a firm commitment to addressing the country's budget deficit was welcomed by markets.

The FTSE All-Share Index rose by almost 15% over the year, with the final quarter of the year generating almost half of this. This can be ascribed to economic optimism gathering momentum, but also the rise was no doubt helped by money from the economic stimulus finding its way into asset markets as well as the attractive yield valuation on equities when compared with bonds. International equities (as measured by the FTSE All-World (Ex-UK) Index) performed similarly well, rising by 11.1%, whilst, despite rising yields in the final quarter as the inflationary impact of recovery began to

weigh, UK government bonds (as measured by the FTSE British Government All-Stocks Index) returned +7.2% over the year.

Fund Review

The Fund performed well, comfortably outperforming its benchmark FTSE All-Share Index, and this outperformance was well spread throughout Fund constituents.

Fund outperformers outnumbered underperformers by two to one, with 29 constituents beating the 14.5% total return recorded by the Index and 15 falling short. The biggest individual return came from *Renishaw*, which rose over 130% as it successively upgraded sales and earnings expectations throughout the year. In total, two companies returned more than 100% (the other being *Hargreaves Lansdown*), 10 returned between 50% and 100% and eight returned between 29% (double the Index return) and 50%. These 'winners' were drawn from a diverse range of industries, including electronic and electrical equipment, financial services, travel and leisure, media, support services, oil equipment, services and distribution, industrial engineering, technology hardware and equipment and oil and gas producers. They also included companies (notably *Domino's Pizza* and *Rightmove*) whose earnings derive almost entirely from the UK, reminding us that specific attributes and positioning within a market at a micro-level matter far more than the 'macro-picture'. What united the 'winners' was that in the main they

MARKET REVIEW CONTINUED

exceeded market expectations or 'surprised' the market positively in terms of earnings or revenue growth, or both.

These 'winners' are in our portfolio because we believe they possess a distinct competitive advantage (which we call 'Economic Advantage') which arises by virtue of their intangible assets. All constituent companies possess at least one of the following intangible assets: intellectual property (IP); a strong distribution network; or high recurring income. These assets are particularly difficult for competitors to replicate and therefore help sustain pricing power. Other intangible assets are also important but are given less prominence. These include customer relationships, licenses and franchises, procedures and formats, culture and brand.

We expect our companies to deliver strong financial returns as a validation of their barriers to competition, and look at ten years of historic return on capital employed and two years of forecast returns to assess whether in fact they have done, and will continue to do so.

Although we expect such companies to deliver superior returns, sometimes they are not given the chance. Unsurprisingly, companies with these characteristics are attractive to competitors and during the course of the year *Chloride* was taken over following a protracted bid battle, its attraction being its extensive European network of service centres. Similarly, *Rightmove's* strong position within the UK

market enabled it to see off the threat of incursion from Google (as well as delivering a strong trading and share price performance).

Controlling risk is an important part of portfolio management and it is as important to avoid losers as to pick winners, if not more so. Only four of our fourteen underperformers fell by more than 10% (in absolute terms). Our biggest individual loser was smaller company *System C Healthcare*, which fell by 28% as it was caught out by the government scrapping centralised IT procurement for the NHS. The company has, however, switched strategy and in January 2011 the share price rose by 28.6%. *BP* fell 18%. We added to our position at lower levels as we judged that the fall in price more than discounted the financial impact of the Gulf of Mexico spill. *Carpetright* fell by 13% as the recovery in its markets weakened, and *Paypoint* fell by 12% on concerns over competition from Camelot. Our other laggards largely reflected concerns over UK government spending cutbacks (*Capita*, *BAe Systems*) and western consumer markets (*Diageo*, *Reckitt Benckiser*, *Unilever*) which, in the main, have yet to be reflected in reported earnings shortfalls.

Outlook

Inflation, rather than deflation, and the implication for interest rates is now the preoccupation of markets as commodities boom, the US GDP recovery continues (and US banks start to lend) and the Chinese rate-tightening cycle is already under way. Even

MARKET REVIEW CONTINUED

Europe is joining the party with France and particularly Germany leading the way. The UK may be a relative wallflower (on the evidence of the preliminary Q4 GDP number) but given the importance of Europe to UK demand this is unlikely to continue. Conventionally, rising rates are not necessarily an impediment to equity outperformance at this stage of the cycle as recovery delivers earnings growth, and on some measures (the proportion of GDP recovered since peak, for example) this is simply a 'normal' recovery, despite the extraordinary severity of the financial crash. And yet we are by no means out of the woods.

Consumer 'animal spirits' may remain subdued as austerity measures start to bite and the housing market continues to adjust. For companies this portends a potentially difficult year with the 'known-known' of rising input costs (evidenced by *Unilever* in its recent trading update) and the 'known-unknown' of

demand recovery. At this stage, unsurprisingly, guidance is erring on the cautious side. For equity markets, there is the added dimension that valuations have to some degree already reacted to reflect the 'west is bad, east is good' mentality and that should recovery falter financial strength will remain an important factor. Ireland, for example, owes the UK \$149bn, 6.6% of UK GDP, and Spain owes \$111bn.

Against this background, we continue to invest in a diversified portfolio of companies which have the competitive advantage and pricing power that enables them to survive and prosper, with the emphasis on quality (rather than value), financial strength and stability of returns.

Anthony Cross and Julian Fosh
Partners

Liontrust Investment Partners LLP
February 2011

FUND PROFILE

Investment Objective and Policy

The investment objective of Liontrust UK Growth Fund is to provide long-term capital growth through a portfolio of mainly United Kingdom ("UK") equities but with the option of investing part of the portfolio overseas.

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 securities in companies listed on the International Stock Exchange of the UK and Ireland. The Fund may also invest in shares issued by companies incorporated in any European Economic Area ("EEA") Member State other than the UK which are listed on a recognised stock exchange of an EEA Member State. 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

This unit trust is managed to produce long-term capital growth using a disciplined investment approach which aims to identify UK companies whose competitive strengths ("Economic Advantage") allow them to sustain a higher than average level of profitability for longer than expected. Economic Advantage is the collection of distinctive characteristics of a company that competitors struggle to reproduce. These assets deliver pricing power, protect margins, and thus drive sustained profitability. The market rewards excess profitability, particularly when it is higher than consensus expectations. The Fund invests in a portfolio of competitive UK companies which we believe will surprise the market with the profits growth.

Risk Profile

The Fund is invested exclusively in UK equities. It is invested in stocks throughout the FTSE All-Share Index, with no sector bias. The principal risks are those associated with stock market investments.

Total Expense Ratio (%)

31st December 2010 31st December 2009

Class R income units	1.62%	1.59%
Class I income units*	0.87%	–

* Launched 1st November 2010

Fund Calendar

Ex-dividend date	1st January
Income payment date	End of February
Accounting period ends	31st December

PERFORMANCE

Net Asset Values pence per unit			
	31st December 2010	31st December 2009	% Change
Class R income units	224.76	179.61	+25.13
Class I income units*	224.77	–	

Distributions pence per unit		
	31st December 2010	31st December 2009
Class R income units	2.64	3.18
Class I income units*	2.86	–

The Fund distributes income once per annum, at the end of February. The ex-dividend date is 1st January each year. Income can be reinvested to purchase units at no initial charge.

Total Return (%)		
	1 year to 31.12.10	Since manager inception to 31.12.10**
Liontrust UK Growth Fund	26.6	70.4
FTSE All-Share Index	14.5	64.9
Quartile Ranking	1st	2nd

Discrete Years' Performance (%)					
	2006	2007	2008	2009	2010
Liontrust UK Growth Fund	23.2	9.2	-32.9	26.9	26.6
FTSE All-Share Index	16.8	5.3	-29.9	30.1	14.5

* Launched 1st November 2010

** Anthony Cross and Julian Fosh took over management of the Fund on 25.3.09. 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) or by calling our Administration and Dealing team on **0844 892 1007**.

Performance data source: Financial Express, total return, bid-to-bid basis. 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.

PORTFOLIO

Top 10 Holdings			
As at 31st December 2010	%	As at 31st December 2009	%
Royal Dutch Shell 'B' Shares	6.57	Royal Dutch Shell 'B' Shares	7.57
GlaxoSmithKline	5.07	GlaxoSmithKline	6.33
BP	4.15	AstraZeneca	5.03
AstraZeneca	4.02	Unilever	4.00
BG	3.84	BG	3.57
British American Tobacco	3.66	British American Tobacco	3.43
Unilever	3.20	Compass	3.33
Diageo	2.89	Diageo	3.27
Reckitt Benckiser	2.86	Reckitt Benckiser	3.20
Petrofac	2.78	Petrofac	3.17
Total	39.04	Total	42.90

Sector Weightings			
	FTSE All-Share Index	Liontrust UK Growth Fund	
	31st December 2010 %	31st December 2010 %	31st December 2009 %
Basic Materials	14.08	–	–
Consumer Goods	11.30	12.61	13.90
Consumer Services	9.66	13.86	15.71
Financials	22.64	6.71	5.19
Health Care	6.91	11.07	13.28
Industrials	7.29	24.38	24.50
Oil & Gas	16.85	20.09	19.68
Technology	1.57	6.61	6.73
Telecommunications	6.02	–	–
Utilities	3.68	–	–
		95.33	98.99
Cash (including SSgA* cash deposits)		4.67	1.01
		100.00	100.00

* State Street Global Advisors

FURTHER INFORMATION

UNITHOLDER NOTICES

Introduction of the Institutional Unit Class

On the 1st November 2010 the Fund launched the institutional unit class, Class I, available to professional investors.

Change to Fund name

On the 30th September 2010 the Fund changed its name from Liontrust First Growth to Liontrust UK Growth.

Liontrust Asset Management Plc

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 December 2010).

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, Report & Financial Statements

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.

The Manager

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

Administration & Dealing Enquiries **0844 892 1007**
Administration & Dealing Facsimile **0844 892 0560**
Administration & Dealing Email **admin@liontrust.co.uk**
www.liontrust.co.uk

Authorised and regulated by the Financial Services Authority.

NOTES



LIONTRUST FUND PARTNERS LLP

2 Savoy Court, London WC2R 0EZ

Liontrust and Fund Enquiries **+44 (0)20 7412 1700**

Email **info@liontrust.co.uk**

Administration and Dealing Enquiries **0844 892 1007**

Administration and Dealing Facsimile **0844 892 0560**

Administration and Dealing Email **admin@liontrust.co.uk**

www.liontrust.co.uk

Authorised and regulated by the Financial Services Authority.