FIRST & Foremost

LIONTRUST

A PERIODIC BULLETIN FOR PORTFOLIOS MANAGED BY JEREMY LANG IN ACCORDANCE WITH *THE LANG APPROACH*.

APRIL 2005

Liontrust First Growth Fund
(authorised unit trust): £185m

Liontrust First Equity Fund
(offshore fund): £8m

Liontrust First Exempt Fund
(pension fund pooling vehicle): £172m

INVESTMENT PHILOSOPHY – *THE LANG APPROACH*

- When a company announces higher than expected profits analysts revise their forecasts. This can drive share prices upwards as the market digests and catches up with events.
- Companies that have recently surprised the market with their profits have a tendency to do so again.
- By focusing on companies that have recently surprised, *The Lang Approach* aims to identify companies whose potential to surprise the market in the future is, we believe, underestimated by stock market analysts.

THE PORTFOLIO

- The portfolio will invest in a range of companies whose profit growth has recently been greater than the market's expectations.
- To reduce volatility and achieve greater consistency of performance the portfolio will be kept well diversified - 60-70 stocks - with no stock exceeding three times the average overweight position.
- Sector deviation from the benchmark index as defined by Liontrust is restricted to a maximum of 10% .

INVESTMENT COMMENTARY

Two pairs of jeans and a packet of crisps, please.

Tesco is selling jeans for £3. A pint of beer in many London pubs costs more. It takes me about 30 minutes to consume a pint of beer (I used to be quicker, but my trouser belt couldn't keep up). You can spend years consuming a pair of jeans. Or you could just chuck them when they are dirty: if you include valuable labour time in the cost of washing, it is probably cheaper to buy a new pair.

We have become used to falling prices. In the 1980s it became common to see the price of digital watches, ghetto blasters and computers fall. In 2005 an impressive array of products are being caught up in this whirlwind of deflation. A DVD player for twenty quid, a flight to Dubrovnik for a fiver, and a children's chair for a two pound coin. How is this possible?

The Americans go on about the productivity miracle. They think it has something to do with the computer. It's more complicated than that. This fantastic proliferation of value for money is driven by the basics of economics – better organisation of existing resources. Recently it has been all about better organisation of people in China.

In the 1980s, economic growth in the Far East motored along thanks to shipbuilding, steel making, t-shirts and shoes. More and more Western companies recognised they could make such things more cheaply in Taiwan, Korea, Malaysia and Indonesia, even if they had to ship them halfway across the world. Each of these countries followed a similar path. They started with labour intensive, low-skilled industries and gradually moved up the value-added curve as their economies prospered and their labour costs rose. As the more basic industries were sloughed the next cheap country took it over. Now the baton has passed to China. And, as we all know, China is enormous (and so is unlikely to pass the baton on for a very long time).

There are a number of key ingredients allowing the proliferation of remote manufacturing into so many products: better organisation of cheap labour, better quality control, more efficient delivery from maker to buyer, more efficient delivery from buyer to consumer. There are a number of UK-based companies which are part of this revolution.

China is industrialising fast. To do this it is investing in the basic infrastructure required for an industrial economy. This requires a lot of basic raw materials and energy. So demand for a range of basic commodities, where supply has been little changed for decades, is booming. We hold *BHP Billiton*, *BG* and a range of smaller oil companies in the portfolio to take advantage of this secular shift in demand. We also own some industrial companies which service the resource-based industries.

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Offshore manufacturing requires control and monitoring for quality and consistency. *Intertek* is one of a handful of companies which can provide these services. With the recent relaxation of trade restrictions in textiles, demand for its services is accelerating from already fairly rapid rates.

Once made, products need to be transported efficiently. Modern, efficient container transport is a key part of this. *P&O* operates a string of high volume container ports around the world. It also has a stake in one of the world's largest container shipping companies (Nedloyd). *P&O* is made up almost entirely of these trade-related businesses - the last legacy business (ferries) is in the final throes of rationalisation.

Finally, once the product gets to the UK, it needs to get to the consumer efficiently. Which brings us back to *Tesco*. In recent years *Tesco* has become one of the UK's largest clothing retailers, one of the largest CD and DVD retailers, one of the largest magazine retailers, and so on. It has achieved this by taking its existing stores and selling more through them – very efficient.

It may seem strange to write about the proliferation of deflation at a time of booming commodity prices. It is not. Commodity prices are booming for the right reasons – in the production of lots of cheaper products. Your heating bills may be going up, but you can always go and buy yourself a couple of pairs of jeans to keep warm.

Jeremy Lang
Joint Investment Director, Liontrust Investment Services Limited
April 2005

1. PERFORMANCE

Liontrust First Growth Fund

Cumulative years
Source: Lipper, bid to bid basis, net income reinvested at ex-dividend date. Figures to 31.3.05

	1 year	2 years	3 years	4 years	5 years	Since 1.4.96*
Liontrust First Growth Fund	+8.1%	+32.7%	-0.8%	-2.6%	-16.0%	+98.4%
FTSE All-Share Index	+15.6%	+51.4%	+6.3%	+2.9%	-8.2%	+73.5%
Average UK All Companies sector unit trust	+13.6%	+52.2%	+8.3%	+3.8%	-6.7%	+78.0%
Performance vs. benchmark	**-7.5%**	**-18.7%**	**-7.1%**	**-5.5%**	**-7.8%**	**+24.9%**
Sector quartile ranking	4th	4th	4th	3rd	3rd	1st

(Jeremy Lang assumed the management of the Fund on this date).*

Discrete years
Source: Lipper, bid to bid basis, net income reinvested at ex-dividend date.

	1 year to 31.3.01	1 year to 31.3.02	1 year to 31.3.03	1 year to 31.3.04	1 year to 31.3.05
Liontrust First Growth Fund	**-13.8%**	**-1.8%**	**-25.2%**	**+22.7%**	**+8.1%**
FTSE All-Share Index	-10.8%	-3.2%	-29.8%	+31.0%	+15.6%
Average UK All Companies sector unit trust	+10.1%	-4.1%	-28.8%	+33.9%	+13.6%
Performance vs. benchmark	**-3.0%**	**+1.4%**	**+4.6%**	**-8.3%**	**-7.5%**
Sector quartile ranking	4th	2nd	1st	4th	4th

Past performance is not a guide to the future. 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.

2. SECTOR ALLOCATION versus FTSE ALL-SHARE INDEX

Liontrust First Growth Fund

Sector	FTSE All-Share Index %	Liontrust First Growth Fund %
Resources	17.3	20.3
Basic Industries	3.6	3.8
General Industrials	2.6	6.6
Cyclical Consumer Goods	0.4	–
Non-Cyclical Consumer Goods	16.9	11.0
Cyclical Services	15.3	21.8
Non-Cyclical Services	11.0	9.7
Utilities	3.9	1.8
Information Technology	1.1	1.8
Financials	27.9	23.2
Cash	–	–

3. MARKET CAP. WEIGHTINGS

	FTSE 100 Index (%)	FTSE Mid 250 Index (%)	FTSE Small Cap. Index (%)	Cash (%)
FTSE All-Share Index	81.7	15.3	3.0	–
Liontrust First Growth Fund	73.8	22.6	6.6	–

4. TOP TWENTY HOLDINGS

Liontrust First Growth Fund

1.	BP	8.8%
2.	HSBC Holdings	5.9%
3.	Vodafone	5.7%
4.	GlaxoSmithKline	4.4%
5.	Royal Bank of Scotland	3.2%
6.	BHP Billiton	3.2%
7.	BG Group	2.9%
8.	HBOS	2.7%
9.	Shell Transport & Trading	2.7%
10.	Barclays	2.6%
11.	Tesco	2.5%
12.	Aviva	1.9%
13.	AstraZeneca	1.9%
14.	Standard Chartered	1.7%
15.	O2	1.5%
16.	BAe Systems	1.4%
17.	GUS	1.4%
18.	Imperial Tobacco	1.3%
19.	Reckitt Benckiser	1.3%
20.	Wolseley	1.3%

Total 58.3% (41.7% held in a further 62 stocks and cash)

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5. RISK ANALYSIS

Source : Lipper. 108 months to 31.3.05 bid to bid basis, net income reinvested at ex-dividend date.	FTSE All-Share Index	Liontrust First Growth Fund
Total return	74.47%	100.45%
Mean annual return	7.20%	8.64%
One month low	(11.76)%	(9.43)%
One month high	9.37%	13.00%
Maximum drawdown	42.9%	40.3%
Percentage of positive months	64.81%	62.04%
Alpha (annual basis)	0%	1.70%
Beta	1	0.88
Correlation Coefficient	1	0.91
R Squared	100	83
Relative Risk	1	0.96
Risk adjusted performance (annual)	0%	1.54%
Sharpe ratio (annual)	0.14	0.25

Bulletin Board News from Liontrust

Liontrust have launched a new unit trust, **LIONTRUST DISTRIBUTION FUND:**

- Invested 65% in UK gilts, 35% in UK equities.
- Gilt portion tracks the Citigroup UK Government Bond Index. Indexation provided by State Street Global Advisors.
- Equity portion managed by Jeremy Lang in accordance with *The Value Dynamic* (UK Equity Income) investment process (as used in the management of Liontrust First Income Fund).
- Interest distributions paid quarterly at the end of March, June, September and December.
- Income and Accumulation units available.
- Minimum investment £2,500.
- Annual management fee of 1.25% deducted from capital.
- Available within the Liontrust ISA for no additional cost.

LIONTRUST DISTRIBUTION FUND – a lower risk investment, combining the ability of a gilt portfolio to provide a consistent level of income and relative security in volatile markets with the potential for capital growth and rising income of a UK equity portfolio.

To find out more, contact our Broker Services team on **020-7412 1766** or **info@liontrust.co.uk**.

Glossary of Terms

MEAN ANNUAL RETURN : An arithmetic average (mean) of the monthly returns during the review period, multiplied by twelve.

MAXIMUM DRAWDOWN : The greatest loss that could have been experienced by an investor over the entire review period.

ALPHA : A measure of the portfolio's expected return when the benchmark produces no movement.

BETA : The amount the Fund is expected to gain or lose when the benchmark moves by one unit. It takes account of the relative risk of the Fund as well as the correlation of movements between the Fund and the benchmark.

CORRELATION : Measures the coincidence of movement that occurs between the Fund and the benchmark. Correlation coefficients can take values from +1 to -1. Correlation of +1 would indicate that the two portfolios move in perfect unison. A correlation of zero would indicate no relationship between the two. A negative correlation would indicate that they move in opposite directions.

R SQUARED : Measures the degree of explanation that can be made about movement in the Fund by a movement in the benchmark. A value of 100 equals 100% explanation. R Squared is also known as 'goodness of fit'.

RELATIVE RISK : The risk of the Fund measured in relation to the benchmark's risk which has a value of 1.00. Calculated by dividing the volatility of the Fund by that of the benchmark.

RISK ADJUSTED PERFORMANCE : The difference between the Fund and the benchmark return where the benchmark's return has been adjusted to the level of risk of the Fund. It is thought of as a measure of 'value-added' by a manager.

SHARPE RATIO : A measure of the annual excess return divided by the annualised standard deviation of returns of the benchmark. Excess returns are those in excess of the risk-free rate of return.