

Querns Income First Fund - August 2010

The Fund Managers



Stephen Whittaker (Equities)

Stephen has 29 years' experience of managing a wide variety of UK portfolios, including small companies, special situations, income and growth funds

Phil Roantree (Bonds)

Phil has 23 years' experience in the financial services industry. He has managed a broad spectrum of bond portfolios for 18 years, including segregated, unit linked, sterling, global, government and credit portfolios

Fund Objective

The objective of the Fund is to achieve a high level of income, together with some long term capital growth

Fund Managers

Stephen Whittaker (Equities)
Phil Roantree (Bonds)

Launch Date

14 June 2010

Sector

UK Equity and Bond Income

Currency

UK Sterling

Type of Shares

Income and Accumulation

Yield

5.8% for gross shares*
5.3% for net shares*

Income Paid

Monthly

Minimum investment

Lump sum £1,000
subsequently £500
Monthly Savings £100

Management Charges

Initial Charge 0%

Annual Charge 0.75%
charged to capital

SEDOL And ISIN Numbers

Share Type	SEDOL	ISIN
Net Acc	B61JRG2	GB00B61JRG28
Net Inc	B625QM8	GB00B625QM82
Gross Acc	B613JG8	GB00B613JG83
Gross Inc	B602290	GB00B6022909

Investment Commentary

The fund launch in mid-June came at a time of much uncertainty: peripheral European sovereign debt was weak following the bailout for Greece. This had a knock-on effect for banks - large holders of the debt and also brought into doubt their ability to fund themselves in a risk-averse market. There was also speculation as to the outcome of the stress tests for European banks. The upcoming budget by the new coalition government in the UK was expected to be particularly tough in an attempt to reduce the massive fiscal deficit, but at what cost to growth? The UK stockmarket's largest dividend payer, BP, was under increasing pressure, following the oil spill in the Gulf of Mexico.

Most of the issues for the markets, however, were resolved, if only in the near term: Spain was able to issue billions in new bonds, enabling the relative cost of funding for it and other peripheral European countries to fall. This alleviated pressure on the banks, which were also boosted by a relaxation in the proposed new regulatory regime - Basel 3 - and a successful outcome for most banks when the stress test results were revealed. Bank results were also generally good, although much of the improvement came from lower loan loss provisions. The UK budget included a couple of better than expected elements for markets: Capital gains tax was only raised to 28% instead of the widely anticipated 40%, and the levy on banks was smaller than expected. Finally, BP was forced to come up with a \$20bn fund to cover costs from the oil spill, and decided to give in to political pressure in the US by halting its dividend payments for the rest of 2010. This was costly, but removed much of the uncertainty around what would happen - markets do not like uncertainty.

Having fallen by 6.7% from launch of the fund to its low at the beginning of July, the FTSE All Share index rebounded 9.2% by the end of July. Corporate bonds were less volatile, and remain underpinned by strong demand. The yield premium (spread) on the iBoxx Sterling Non-Gilt Index, fell 11bp to 165bp from launch to the end of July, which given little net change in gilt yields resulted in a 1.1% capital gain. The yield on the index is 5.15%.

Against this backdrop, the fund began investing favouring a 60% weighting in equities, with recent weakness suggesting better long term value. Despite a very strong run from corporate bonds since their lows of 2009, the allocation of 40% of the fund to bonds helped the overall yield, as the bond portfolio has a yield comfortably above the index level.

Asset Allocation

60% Equity
40% Bonds

Equity Portfolio

The equity investments benefitted from missing the fall in the stock market in June but capturing the strong rise in July. The strength in the market has indeed afforded profit taking opportunities in both Land Securities and Reed Elsevier while the remainder of the equity holdings were buoyed by other investors searching for income to replace the loss of BP dividends. The average equity yield was 5.27% at 31 July 2010.

Prices

Price at launch 14/06/10	100.00p
Price as at 31/07/10	104.82p**

** net accumulation price

Bond Portfolio

The bond portfolio has been invested across the capital structure in banks (senior, lower tier 2, upper tier 2 and tier 1) as well as insurance companies, although these account for less than 40% of bonds. Going forward, financials exposure is likely to increase, given the higher yields available. The overall fund yield has been enhanced by some sub investment grade bonds such as Enterprise Inns debenture and Ladbroke's, as well as the non rated Thomas Cook. The portfolio at purchase yielded 7.68%, 450bp more than gilts, but by the end of July had moved on to 7.16%, 423bp more than gilts.

Statistics as at 31 July 2010. Source: Querns Asset Managers. Past performance is not a guide to future returns. The value of the fund and the income from it may go down as well as up, so you may not get back the amount you invested. The tax treatment of the Fund may change and such changes cannot be foreseen. Please refer to the latest Full Prospectus and Simplified Prospectuses for more information. Querns only gives information about its own products and services and does not provide investment advice based on individual circumstances.

* Gross shares are shares where, in accordance with relevant tax law, distribution or allocation of income is made without any tax being deducted or accounted for by the fund. Gross Shares are available only to those investors in respect of whom distribution or allocation of income may be made without any tax being deducted or accounted for by the fund, for example UK pension funds and ISAs. All other investors will hold net shares.

The yield reflects the income declared in the previous 12 months based on the portfolio at 31 July 2010. In the case of net shares the yield is net of taxation deducted from the distributions, the yield will vary and investors may be subject to tax on their distributions. The fund charges and expenses, estimated to be 1.1% per year, are charged to capital. This has the effect of increasing the distribution(s) for the year by the amount of the charges and expenses and constraining the funds capital performance to an equivalent extent.