



TAM INVESTMENT PERFORMANCE REVIEW: Q1 2011

Trendwatch ASSET MANAGEMENT

KEY FEATURES OF TAM

- Gains are tax-free to UK investors.
- Gains (and losses) are geared.
- We use the gearing of spread betting to reduce portfolio risk by enabling you to have a wider spread of investments.
- We protect you from downside risk by using guaranteed stop-loss limits.
- We can go short as well as long — which also enables us to protect your trading portfolio through hedging.
- We use unique trend analysis techniques proven by simulations to deliver market-beating investment performance.
- Add or withdraw funds at any time (subject to a minimum investment of £5,000) — no maximum.
- Follow the progress of your investment in real time by logging in to your online account.
- We share the rewards through a 20% performance fee — if we don't perform, you don't pay us that fee.

HOW TO INVEST

If you are new to TAM, visit www.trendwatch.com, and read the information on TAM. When you're ready to go ahead, click on the "Apply to open an Account" button and complete the application forms online.

If you have any queries, please telephone TrendWatch Asset Management Ltd on +44 (0)208 242 6005
Or email: rob.cullum@trendwatch.com

IMPORTANT: While the historic performance figures quoted below are indicative of the skill of the investment managers, under no circumstances should you regard those figures as indicative of TAM's future performance. Future market conditions have no correlation with the past. Similarly, investments selected by the investment managers in the future, and the gains and losses on those investments, will bear no relationship to those selected in the past.

Introduction: The cataclysm in Japan

"Before we all float away on a cloud of euphoria, a short cautionary note is in order to help keep our feet planted firmly on the ground.... We can pretty much guarantee that there'll be rough seas sometime during the course of 2011...." [TAM Investment Performance Review: Q4 2010]

WHEN I wrote the above words, I was confident that they would prove to be prophetic - markets rarely get through 12 months without a temporary crisis of confidence. But of course it never remotely occurred to me that that the metaphorical reference to "rough seas" would so literally manifest itself on 11 March in the form of the cataclysmic tsunami, triggered by the biggest earthquake in Japan's recorded history. Earthquake triggering a tsunami, triggering a nuclear meltdown. More than 25,000 souls are now missing or confirmed dead, Around a quarter of a million are homeless. And yet there's little that any of us can do except offer utterly inadequate condolences, and marvel at the extraordinary dignity of the Japanese people in the face of so much terrible adversity. To go on from that and discuss in detail the resultant relatively minor collateral damage done to the TAM portfolio seems somehow crass and insensitive. Yet that's our job, and that's what I have to do now.

After a stunning third and fourth quarters last year, it was inevitable that there would be a reaction. The tsunami was the primary cause, but markets were further undermined by other factors, not least Libya, the 'Arab spring' turmoil and ongoing concerns about European sovereign debt, which cost TAM dear last year, and is still simmering.

As usual, we'll calculate the performance figures as at the nearest Friday to the end of the quarter; in this case between 31 December 2010 and 1 April this year. In that time, the FTSE 100 was up 1.86% [had we not included 1 April, it would have been almost unchanged on the quarter - to be exact, it rose by 0.15%]. In contrast, the net asset value of the TAM master account fell 14.9%, an underperformance of 16.76%.

Bearing in mind TAM's 5x gearing, this represents an underperformance of around 3.35%, which is hardly a disaster. Nevertheless, it was certainly disappointing. What went wrong? Have we lost our touch? No! There is a clear explanation, which I'll deal with in the next section. The good news is that, by mid-April, the portfolio had recovered pretty much all the fall caused by the tsunami, though there has been some slippage since. Compare and contrast the table below (which gives the position as at 1 April) with the table on the back page.

What happened in Q1 2011?

First, I should like to apologise for getting this Quarterly Review to you about three weeks later than I had planned. Among other things, this is partly due to the big changes that have recently taken place to TrendWatch.

"The harder I practice, the luckier I get", golfing champion Gary Player once said. That probably *doesn't* apply to most forms of gambling. If you're mad enough to stake large sums of money in a Las Vegas casino, whether you finish up

TAM Master a/c performance As at 1/4/2011 (£5,000 starting NAV)	£	%	£	%
Net unrealised and unrealised profit in 2009 (6 months):	£359.67	7.19%		
Net unrealised and unrealised profit in 2010:	£2,541.41	47.42%		
Net realised + unrealised profit in Q1 2011 (as at 1/4/11):	-£1,170.96	-14.82%		
Net realised + unrealised profit since launch:	£1,730.12	34.60%		

NOTES: 'Net' means that the figures include all WorldSpreads charges, and also dividend income. They exclude TAM's charges. The percentage figure for profits since inception represent the gain on the starting capital of £5,000. The percentage figure for profits in 2010 to date represents the gain on the starting capital of £5,358.35, as that was the NAV of the portfolio as at 31/12/2009. All open trades are valued on the basis of bid (i.e. closing) prices.

PLEASE NOTE: The performance of your own TAM account will bear only a loose relationship to the Master account unless you joined TAM shortly after its launch. Your profit may be higher or lower. If you joined relatively recently, you may still be showing a loss, as your first trades may not yet have clawed back the bid-offer spread and the guaranteed stop fees of the initial trades.
The purpose of analysing the performance of the Master account is that it gives an indication of how well TAM has performed over the medium term in varying market conditions. If the Master account is doing well, you can reasonably expect to do well in the medium term too, regardless of when you opened your account.



TAM INVESTMENT PERFORMANCE REVIEW: Q1 2011

How did we do in Q1 2011? (...continued from previous page)

rich or in the soup kitchen depends only a little upon your skill, but a great deal on "lady luck".

But almost everything else in life that you can think of has outcomes that also depend to a greater or lesser degree on luck; for example, on accidents of timing. Even if you hone your skills for hundreds of hours - as a golfer does, say, or a snooker player - whether you win or lose a championship can come down to whether your golf ball is fractionally diverted by concealed worm cast, or the cue ball has an almost microscopic grain of chalk dust clinging to it. These are accidents that cannot be anticipated.

It's the same with investment management. Bill and I can use all our analytical stock selection skills honed to a fine edge after years of practice... only to have a demented Lady Luck leap out from a dark alcove with teeth bared, ripping chunks out of your *glutimus maximus*.

We avoided that fate in Q4 2010. Almost everything that could have gone wrong didn't. Consequently, our performance in that quarter was stunning.

Not so the first quarter of this year. Not even the world's most eminent geologists were able to predict the Japanese tsunami, let alone the nuclear meltdown that followed. It was an unexpected misfortune of the most terrible kind.

As I mentioned earlier, it only needed our trades to put on an extra 3.4% (ungeared) and our performance would have been ahead of the market. So how come we failed to bridge that small gap?

We can't use the tsunami as an excuse in itself, since all equity markets were hit as well as TAM. However, it's worth noting that markets fell by almost exactly 5%. That happens to be an especially dangerous percentage fall for TAM. A 5% market fall is equivalent to a 25% fall in the value of TAM. The reason that's a dangerous figure is that our stop limits are set at around 20% below the peak price. A 25% fall results in many shares being stopped out. If the market then snaps back, as it did, then of course the shares that got stopped out can no longer contribute to the recovery in TAM's NAV.

Having a lot of shares stopped out in the event of a fall in the market of well over 5% would be a relatively good thing because it represents a dash to the safe haven of cash, enabling us to open new trades at a lower price. And a smaller fall means that the trades are not closed out anyway. But, as I say, a fall of around 5% is somewhat problematic to us. We have plans to combat that situation in the future by refining our stop limit settings. Instead of using a blanket 20% trigger, the stops will be set according to the beta (volatility) characteristics of individual shares.

However, in addition to stop factors, we were impacted by still being overweight in BP. As I've observed in previous *Investment Reviews*, this has been a great investment, as we were able to pick up the trades very close to the bottom following the Macondo disaster in the Gulf of Mexico. The price subsequently rose from 330p to around 520p, helped by an

ambitious deal struck in January for a \$16bn share swap with Rosneft, the Russian state-owned oil company, under which the two companies would collaborate on exploration of the Arctic. Unfortunately, this deal is now on hold and may not proceed at all because the Russian oligarchs who are shareholders in BP's other Russian alliance, TNK-BP, say that the Rosneft deal breaches the terms of the TNK-BP agreement.

BP's price fell back towards its stop level during the quarter, and is still looking weak.

We don't regret hanging on to BP, given that we picked it up at very close to its post-Macondo low. Now that the company has resumed dividend payments, the yield is attractive, and should be increasingly so if (as we expect) BP continues to raise its dividend. Furthermore, it's looking increasingly likely that BP will escape the worst-case litigation scenarios.

You may be a little curious to know the reason for the drop in the fire sale valuation since the end of 2010 (lower chart). Recall that the fire sale valuation is the value that would be realised if a catastrophe overtook the markets

and all of our shares were stopped out. Don't be alarmed about this. The main reason is that we set the stops increasingly tightly in the run-up to the end of 2010 so as to preserve our big gains in the event of a major market set-back - end-of-year figures are all-important to the investment management sector when it comes to reporting performance figures. The reduction in the valuation in Q1 2011 was mainly because we progressively reduced stop-levels back to 20%.

A secondary reason is that market sentiment in the first quarter has been so lacklustre that we've not been able to raise the stop levels at anything like the rate as in the previous quarter.

Even at this level, the fire-sale valuation is impressive. In our brochure, we told you that there was a theoretical possibility that you could lose all of your investment. But now, an investor who opened his or her account at around the same time that TAM was launched could lose only 25% at the most. A half-decent period on the market will enable us to get back to where we were at the end of Q4 2010.

One final comment, I want to remind you again that the performance figures quoted here relate to an investor who opened a TAM account close to its inception in 2009. I'm reminded of a TAM client who had opened his account early in 2010. He noted that we'd been singing the praises of TAM's performance. He asked why his account was barely in profit. The reason was that he had opened his account shortly before the eurozone crisis. When that was over, the market recovered strongly - but our investor would have got little benefit from that, as he would have been under-invested. So it's another one of those accidents of timing.

I have always said that you should regard TAM as a medium-term investment, just like a conventional equity portfolio. Allow a minimum of two years before you really see results.





TAM INVESTMENT PERFORMANCE REVIEW: Q1 2011

Pound cost averaging or catching falling knives?

WE'VE RECEIVED quite a lot of feedback from you regarding the changes to *TrendWatch* that we've implemented recently.

One of the changes was that we've said that we'll normally recommend six shares in each of the new jumbo-sized monthly issues.

In your feedback, several of you said that we should recommend fewer shares in adverse market conditions. The implication is that some of you may have felt that we were, on occasions, "scraping the barrel".

This is an interesting topic to discuss, because the number of shares we recommend in *TrendWatch* - and therefore the number of trades we open for TAM - is a key part of the TAM strategy.

The first point to make is that, following the changes to *TrendWatch*, we'll be making the same number of recommendations per month (six) as we were doing before. Nothing has changed. It's a strategy that has stood the test of time over more than a decade.

Second, we've never felt that we were "scraping the barrel". Even in the most adverse of market conditions, there are still shares bucking the market trend. Indeed, the very fact that such shares *are* bucking the trend is a *prima facie* indication that there's something special about that company.

I can think of only one occasion in the past 11 years when we simply couldn't recommend any share at all. That was in the immediate aftermath of 9/11. It wasn't surprising that we struggled, given the fact that the New York Stock Exchange was closed for a week because the attack knocked out tele-

communications in the area. On the day the market eventually reopened, the Dow Jones index lost 680 points, or 7%, the biggest one-day fall in its history. That week, it went on to lose 1,360 points or 14%, which also made it the worst one-week fall in the exchange's history.

Very occasionally, we struggle to find new uptrends that satisfy our high standards. In such cases, we may extend our search to slightly more mature uptrends; uptrends that are, say, up to a month old rather than just two weeks. Or we may go for a share that is right on the cusp of an unequivocal uptrend, but just fails to satisfy one criterion. As it happens, we did this with Centamin Egypt in the last issue. We see no reason why shouldn't exercise a little discretion, so long as we stick closely to the strategy we've set out for ourselves.

But now let's get away from *TrendWatch* and turn our attention to TAM. How many trades should we be opening a month. Or should it be a variable number? Should we only buy when the market is rising and stay away from the market when it's in a bear phase?

These are the questions I'll attempt to answer in the rest of this piece.

The answer to that last question is simple. It's generally ac-

cepted that it's best-practice in investment to continue buying even when the market is falling. Why? To get the benefit of *pound cost averaging*. If your normal investment unit is, say £1,000 per share, then other things being equal, if prices fall by, say, 5%, you'll get 5% more shares for your £1,000. When the market starts to recover, you'll get the benefit of "buying low".

Pound cost averaging actually refers to feeding your money into the market over a period of time, rather than all at once. If the market is buoyant, and prices are high, you'll get less shares for your £1,000, or whatever your unit cost is. If the market is weak and prices are falling, you'll get more shares for your money.

That's exactly what TAM does. When you made your investment in TAM, we don't rush to invest all your money in one go. If the market suddenly fell by 20% over a few days, you'd be stopped out of most of your shares, thus losing most of your money.

So instead, we feed your money into the market at a steady rate.

I know that some of you find this frustrating. It means that a large proportion of your money can remain in cash for an extended period of time, especially in poor market conditions. But don't be frustrated with us - be frustrated with the market. After all, if market conditions are poor, you should be grateful that a fair amount of your investment is safe.

Nevertheless, in adherence to the principles of pound cost averaging, even in bad market conditions, we're in there buy-

ing at a steady rate, taking advantage of lower prices. When the market clouds clear and the sun comes out again, you'll be glad that we did.

Here's another reason why pound cost averaging is such a good idea. Investment managers who try to guess what the market is going to do tomorrow, next week or next month will be for ever altering their investment strategy, buying furiously one day, selling furiously another. Excessive buying and selling of shares is known as 'churning'. Aside from a full-on bear market, nothing destroys performance like churning, because every trade involves transaction costs.

In contrast, *TrendWatch* is close to unique in that we actually tell you in advance the average number of new trades we aim for per month: six. So you know straight away that our performance

can never be eroded by churning.

Why six trades a month? Why not 3 or 5 or 8 or 10? Well, we've aimed for a figure that will result in your account becoming fully invested in a reasonable period of time - by that, I mean around a year. Now, you could reasonably argue that we're undershooting, and that we should push the number of new trades up to perhaps 8 per month. After all, the TAM master account has been open for two years now, and it's still only just over 80% fully invested.

WHAT IS THE DIFFERENCE BETWEEN POUND COST AVERAGING AND CATCHING FALLING KNIVES?

It's important that you understand the distinction between "pound cost averaging" and "catching falling knives".

Suppose you have a share in your portfolio (Connaught, say, or CPPGroup or Southern Cross Healthcare) and it falls 50%. Is it a good idea to do a bit of pound-cost averaging here and buy another £1,000-worth of shares? After all, you can now get 50% more shares than you had before.

Well, there's a group of specialist investors known colloquially as "bottom-fishers" that make a good living from doing just that. They may judge that the market has overreacted.

But in general, you should *never* average down on a share you already hold. A share that has fallen substantially should no longer be in your portfolio anyway - it should have been stopped out. By all means look at it again if and when it goes back into uptrend; but not before.

A share that has fallen substantially may look cheap, but that doesn't make it a bargain. Chances are it's cheap because no one else wants it. And cheap shares can keep on falling further and faster than you ever believed possible - hence the expression "catching falling knives".

If you doubt the wisdom of this advice, think back to when the technology bubble burst in 2001. Imagine how many holders of Marconi shares lost all their fingers catching falling knives. After all, Marconi was a blue chip share, was it not? It used to be known as GEC, once one of the proudest names in the UK corporate firmament. How could Lord Weinstock's great legacy fail? Yet fail it did, the share price falling from over £12 to 10p. Marconi became Telent (now a private company) with revenues of around £310m, a pin-prick compared to its glory days as GEC.

So let's be clear: When I talk about pound-cost averaging, I'm referring to continuing to buy share in uptrend, *not* buying another tranche of a failing company.



TAM INVESTMENT PERFORMANCE REVIEW: Q1 2011

Pound cost averaging (continued)

But then again, it has been a volatile two years, what with the eurozone crisis, the Japanese tsunami, and various other upsets. Every time, the market goes through a rough patch, an increased number of shares get stopped out. If the number of stop-outs exceeds six per month, the under-investment will increase. Given the market conditions, perhaps 80% is about right.

Pound cost averaging only works about 95% of the time. Occasionally, it might actually have been better to invest all your funds into the market if the market is at or near rock-bottom. But without a crystal ball, how would you know that the market was at rock bottom? The only way you could get your timing that right would be by pure luck.

For example, let me take you back to what happened in the immediate aftermath to 9/11. When the Dow Jones Industrial Average fell 7% on the day it re-opened, would you have felt confident enough to say to yourself "that's an over-reaction - there's only one way the market can go from here; and that's up"... and then placed a huge long bet on the market? If so, you would have been dead wrong. The market fell another 7%.

And then, having seen what had happened to the Dow at the end of that week in September 2001, would you have been confident enough to say "That's it. The market has bottomed out. I'm going in big-time". I doubt it. More likely, you would have been asking yourself: "Is this just the start of one of the worst bear markets in living memory?". It wasn't; but that only became apparent with the benefit of hindsight.

STOP PRESS

As we freeze the content of this Review just prior to publication, the following two tables give the latest information, correct as at the close of business on the May Day bank holiday, Monday 2 May 2011.

The top table gives the latest performance figures. You may want to compare them with the table on page 1. The bottom table shows what it says on the tin.

TAM Master a/c performance as at 2/5/11 (£5,000 starting NAV)	£	%	£	%
Net realised and unrealised profit in 2009 (6 months):			£359.67	+7.19%
Net realised and unrealised profit in 2010			£2,545.56	+47.49%
Net realised loss in 2011 to date:	-£1,435.74	-18.48%		
Net unrealised profit in 2011 to date:	£322.67	+6.28%		
Net realised + unrealised profit in 2011 to date:			-£1,113.07	-14.08%
Net realised + unrealised profit since launch:			£1,792.16	+45.90%

THE BEST TAM TRADES SINCE INCEPTION

Trade	Gain/ loss (ungeared)	Gain/ loss (geared)	Trade	Gain/ loss (ungeared)	Gain/ loss (geared)
Petronet	+131.8%	+659%	Virgin Media *	+66.0%	+330%
BowLeven	+129.0%	+645%	James Halstead *	+63.7%	+319%
Greenko *	+104.7%	+524%	Globo	+57.2%	+286%
Hallin Marine	+75.6%	+378%	Telecom Plus *	+54.4%	+272%

* Trades still open

About TAM

We are **Trendwatch Asset Management Ltd**, registered in England; company no. 470466. You can contact us in the following ways:

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You will find essential information about TAM on our website at: **www.trendwatch.com**

Your account is administered on behalf of TAM by our FSA-authorized partner spread betting firm **WorldSpreads Ltd**. If you

need to contact them, you can obtain their contact details by visiting their website at: **www.worldspreads.com/uk**

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We are registered with the Information Commissioner under the Data Protection Act. Our policy is to protect your privacy by never releasing your personal information to third parties (apart from WorldSpreads) without your express permission.

You can check our regulatory status on the Financial Services Authority's register at: **www.fsa.gov.uk/register** (FSA Firm no: 414207).



Risk warnings

Please note the warning at the top of page 1. TAM invests in futures markets. Like all financial markets, prices can go down as well as up. TAM's investment managers do everything possible to keep risk to a minimum, and TAM's stop-loss policy will ensure that you cannot lose more than your investment. However, substantial losses, or sharp falls in profit, are possible in extreme market conditions. TAM is a geared investment (you only have to put up approximately one-fifth of the money compared to a conventional investment with similar exposure). That means that the value of your investment can be extremely volatile. UK-resident clients should not be subject to income tax or capital gains tax under current legislation and HMRC rules. However, the tax treatment of spread bets may vary depending upon your personal circumstances, and tax legislation and rules can change over time.