QUARTERLY REPORT
Q2 2018

HAWKSMOOR
FUND MANAGERS

THE MI HAWKSMOOR DISTRIBUTION FUND

The one-stop investment solution for income and growth.

INVESTMENT WEEK
SPECIALIST INVESTMENT AWARDS 2017
WINNER
Boutique Management Group of the Year (Multiple Strategies)

INVESTMENT WEEK
2018
FUND MANAGER OF THE YEAR AWARDS
WINNER
MANAGED BALANCED

Professional Adviser 2017 awards
WINNER
Best Multi-Asset Fund
Rising Income

Rating
ScoPiC A

SYNAPTIC RISK RATING 3.3

defaqto 2018
Multi-Manager Return Focused

defaqto 2018
Multi-Asset Income

5 defaqto
RISK RATING
LOW TO MEDIUM RISK

INVESTMENT OUTCOME

The Distribution Fund's primary aim is to deliver an attractive level of income. In doing this the managers will aim to ensure the Fund's yield will always be at a premium to a composite index of financial asset classes (equities, bonds, property and cash). The intention is to increase the distribution alongside an increase in capital growth in order to maintain an attractive distribution yield for new and existing investors. Therefore investors should expect to receive a total return on their investment that will be somewhat correlated to financial markets given the Fund's fully invested, albeit diversified, portfolio.

1 The Defaqto 5 Diamond Multi-Manager Return Focused Rating reflects the C Share Class. Defaqto Multi-Asset Income and Risk Ratings apply to all available share classes.

INTRODUCTION

"Price is what you pay. Value is what you get." - Warren Buffett

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Our Team

Daniel Lockyer *Senior Fund Manager*
Financial Express aggregated track record of 13+ years running retail funds – outperformed peer group by 44%, returning 125% versus 81% (13/01/2005 to 30/06/2018)

Richard Scott *Senior Fund Manager*
Financial Express aggregated track record of 18+ years running retail funds – outperformed peer group by 210%, returning 480% versus 270% (31/12/1999 to 30/06/2018)

Ben Conway *Senior Fund Manager*
Financial Express aggregated track record of 4+ years running retail funds – outperformed peer group by 8%, returning 38% versus 30% (01/01/2014 to 30/06/2018)

Hannah Isaac *Head of Fund Operations*

Dan Cartridge *Fund Management Assistant*

Left to right: Richard Scott, Hannah Isaac, Daniel Lockyer, Dan Cartridge, Ben Conway

 Source: Financial Express Analytics GBP total return

MARKET PERFORMANCE

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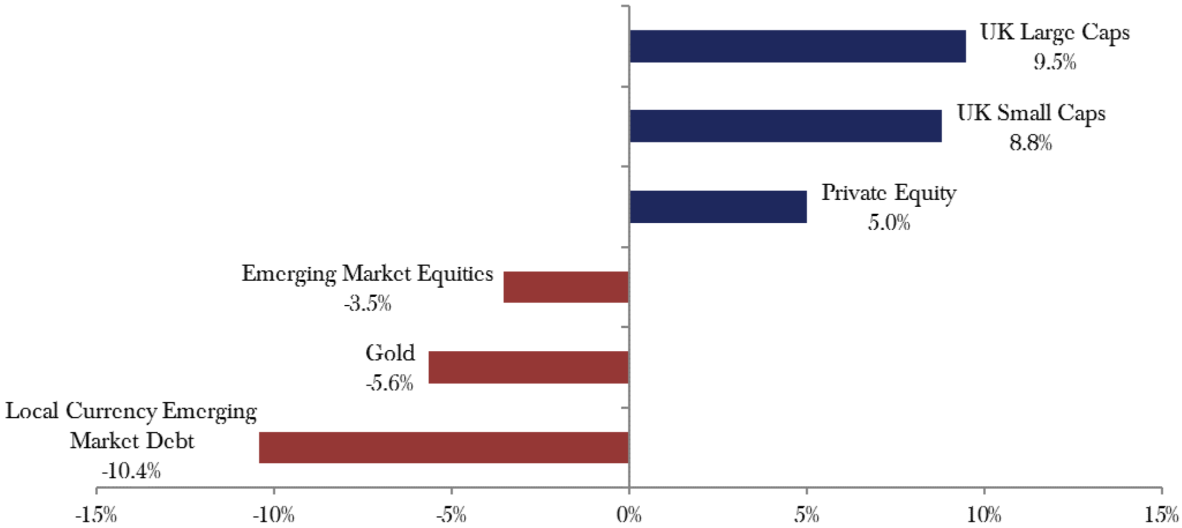
Top and bottom three performing asset classes



Commentary

The second quarter of the year saw the continuation of more volatile financial markets that began in earnest during the first quarter of 2018. In April, markets rebounded from the losses experienced in the first quarter of the year. Though, this strength was short lived. As the quarter progressed, politics again took centre stage as Italy struggled to form a stable government and noise around tit-for-tat trade war strategies reared their ugly head. Sentiment and subsequently flows towards emerging markets turned sharply negative, as strength in the US dollar increased the cost of servicing debt for those companies with dollar denominated debt operating in emerging markets. Sentiment to the asset class was further hampered by poor news out of Argentina and Turkey, which both battled high inflation. This led to significant falls in the value of both emerging market debt and emerging market equities during the quarter.

Weakness in sterling relative to other major currencies, notably the US dollar, benefitted UK blue chip stocks that generate much of their revenues overseas, culminating in UK large capitalisation stocks being the best performing asset class over the quarter. Towards the end of the period, the Federal Reserve raised short term interest rates for the seventh time since the Great Financial Crisis. This coincided with a weaker period for the gold price which tends to move inversely to the US dollar.

Elsewhere, private equity had a strong month. Positive news flow from investment trusts such as HGCapital, regarding disposals of companies at large uplifts to their carrying value saw share prices of private equity companies trusts react positively to the rising net asset values.

Indices: UK Large Caps - MSCI United Kingdom Large Cap, UK Small Caps - MSCI United Kingdom Small Cap, Private Equity - IT Private Equity, Emerging Market Equities - MSCI Emerging Markets, Gold - ETFS Physical Gold, Local Currency Emerging Market Debt - JPM GBI-EM Div Composite

 Source: Financial Express Analytics local currency total return 31/03/2018 - 30/06/2018

DISTRIBUTION FUND PERFORMANCE

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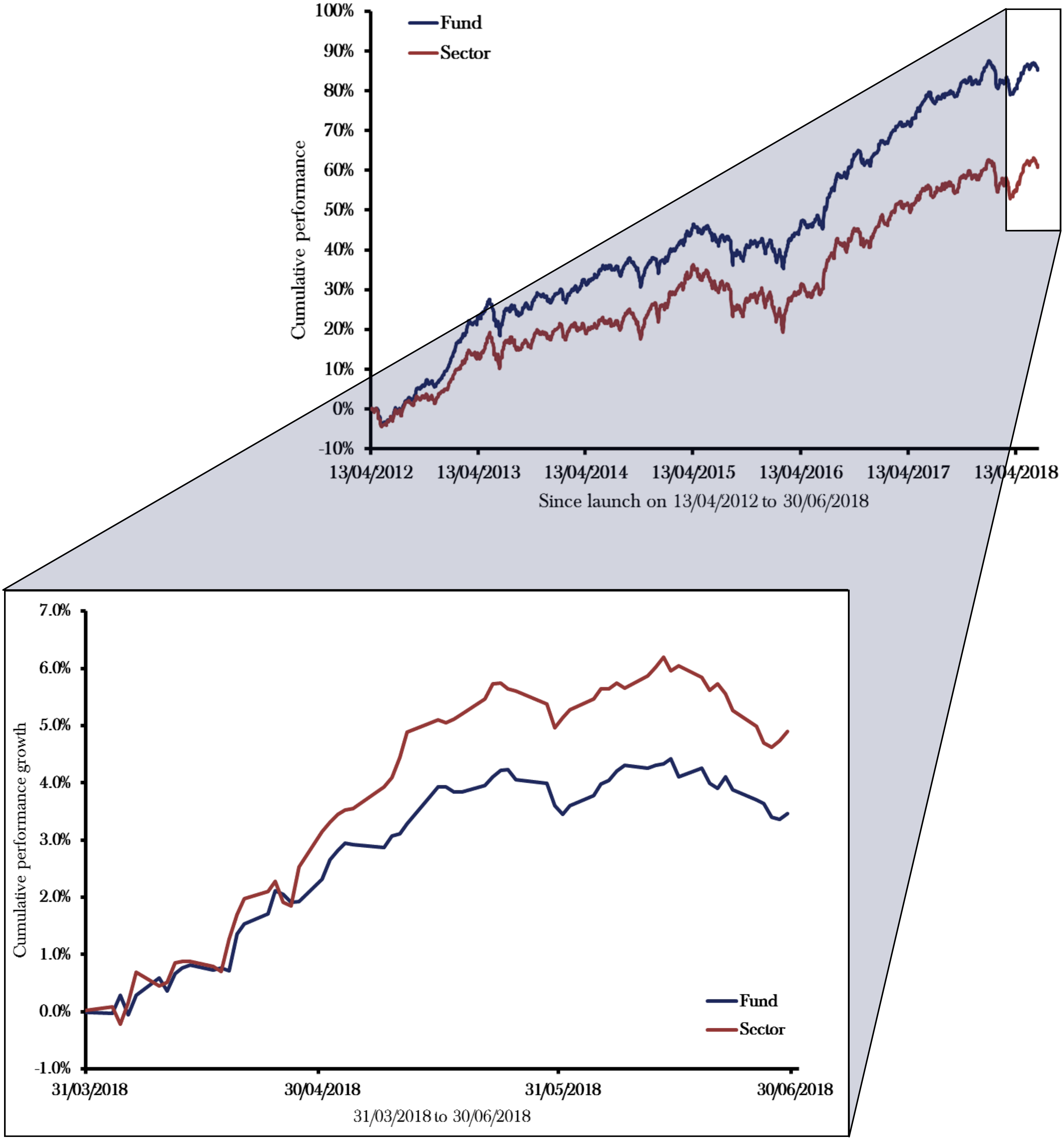
Since launch and last quarter



 Source: Financial Express Analytics GBP total return 30/06/2018. C Acc units. Sector: IA Mixed Investment 40-85% Shares.

DISTRIBUTION FUND PERFORMANCE

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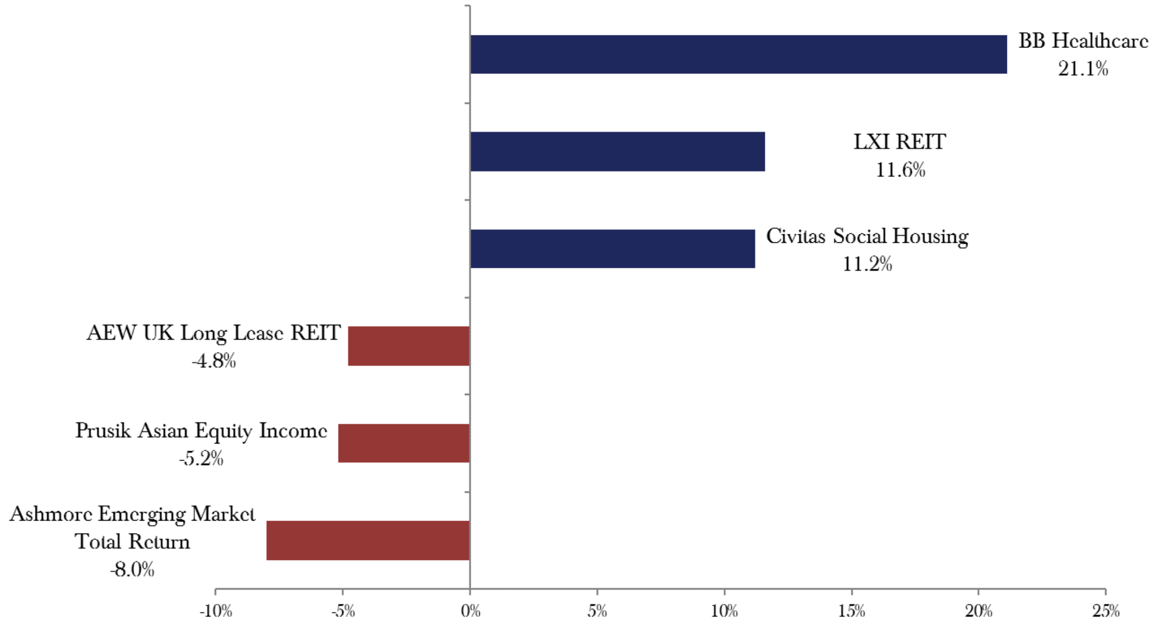
Performance by holding (top three and bottom three)



Best performers:

- **BB Healthcare** (thematic equity) - the trust benefitted from an improvement in investor sentiment following an anticipated speech from Trump on drug pricing, in addition high dollar exposure benefited sterling based investors as the currency appreciated relative to sterling.

- **LXI REIT** (commercial property) - the release of a strong set of full year results, combined with some profitable disposals of property saw the share price appreciate with the trust moving from a discount to a premium

- **Civitas Social Housing** (commercial property) - the trust had sold off sharply in the previous quarter on poor investor sentiment, which turned in this quarter leading to a marked appreciation in the share price moving the trust from a significant discount to a small premium

Worst performers:

- **AEW UK Long Lease REIT** (commercial property) - sentiment towards the trust weakened due to high property acquisition costs, resulting in the premium to NAV contracting from c.6% to c.0%

- **Prusik Asian Equity Income** (Asian equity) - returns for the fund suffered in line with broader Asian equity markets which sold off in the wake of poorer investor sentiment around emerging markets

- **Ashmore Emerging Market Total Return** (emerging market debt) - sentiment towards emerging markets was hampered by a strengthening US dollar and poor news out of Argentina and Turkey, resulting in large falls across both EM equities and debt

 Source: Financial Express Analytics GBP total return 31/03/2018 - 30/06/2018

DISTRIBUTION FUND PORTFOLIO ACTIVITY

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By holding

Purchases/Increases:

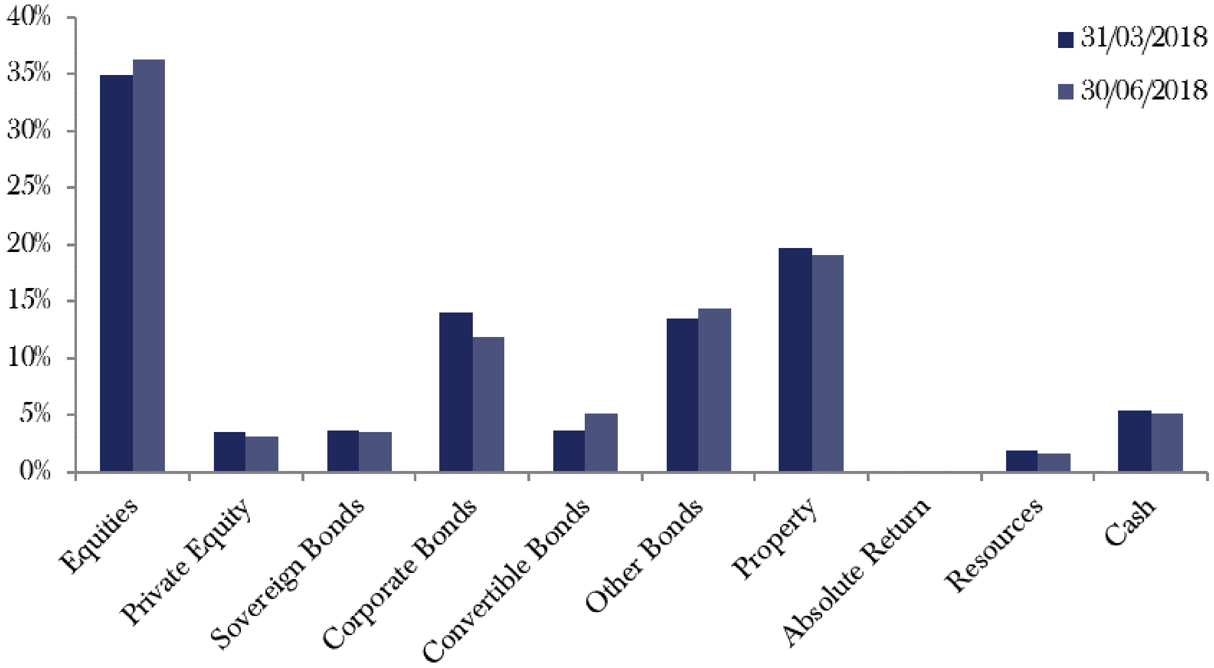
- Civitas Social Housing
- Close Select Fixed Income
- Real Estate Credit Investments
- Schroder Income Maximiser
- Semper Total Return

Disposals/Reductions:

- Baring European High Yield Bond
- BlackRock Frontiers Investment Trust
- Schroder Strategic Credit
- TwentyFour Income

Most of the activity during the quarter focused on our fixed income exposure. Early in the quarter we sold out of our position in Barings European High Yield Bond fund following a strong run that had seen the spread offered over investment grade bonds narrow significantly, diminishing the margin of safety on offer. We introduced a position in Close Select Fixed Income fund, a nimble credit fund, in its place. We sold our position in TwentyFour Income, bringing in Real Estate Credit Investments, a property debt fund with an attractive 7% yield that was trading on a discount. Schroder Strategic Credit was disposed of towards the end of the period with the yield on fund having come down a long way. We introduced Semper Total Return, which invests in US mortgage backed securities, offering a compelling risk-reward opportunity. Other dealing involved selling our holding in BlackRock Frontiers Investment Trust. Negative news out of Argentina prompted the sale as the share price failed to reactdespite the portfolio having significant exposure to Argentinian equities. We increased our exposure to Civitas Social Housing, adding the C shares to the Fund. We introduced Schroder Income Maximiser, a UK equity income fund offering a high income, partly manufactured from the use of call-overwriting, a strategy that should benefit from a rising volatility environment.

By asset class



This chart calculates the asset breakdown on a look through basis of the underlying holdings, therefore there may be differences in the breakdown shown here and on the pie chart on page 7.

Source: Internal

DISTRIBUTION FUND PORTFOLIO HOLDINGS

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Each fund has been allocated to an asset class for this pie chart, therefore there may be differences in the breakdown shown here and on the asset allocation chart on page 6.

 Source: Internal as at 30/06/2018

CLARIFYING THE EFFECT OF SYNTHETIC OCFS ON OUR FUNDS

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Investors may be aware of the new Packaged Retail and Insurance-based Investment Products PRIIPs legislation, which came into effect at the beginning of the year, which required all listed Investment Companies (ICs), including investment trusts and closed-ended funds, to produce a Key Information Document (KID) to provide information to retail clients about the risks, costs and potential gains and losses of the investment product.

Our note in January, "Are you KIDding me?", referred to industry concerns about the flaws in the new legislation and the potential for it to mislead the people it is designed to help.

In this article, we try to help investors understand these changes in the disclosure of funds' charges, and explain how they have affected the Hawksmoor Funds. **It is vital that investors understand the details behind all open-ended funds' charges when making comparisons**, as the headline Ongoing Charge Figures (OCFs) can be misleading when looking at them in isolation.

Our Fees Remain the Same

Until this year, the industry guidelines regarded ICs as listed equities with no requirement to disclose an OCF; therefore when our Funds' underlying (or synthetic) OCFs were calculated these ICs carried a nil cost. Now, because ICs need to produce KIDs and disclose their OCFs, the Hawksmoor Funds' synthetic OCFs will rise. It is important to state that just because the OCF of our Funds will rise, **they don't suddenly cost more**, and Hawksmoor is not earning or charging more.

These tables show the breakdown of the Funds' OCFs to highlight that it is **only the synthetic OCF that has increased**.

Vanbrugh Fund	30/10/2017	30/04/2018
Hawksmoor AMC	0.75%	0.75%
Synthetic OCF	**0.56%**	**0.93%**
Administration, ACD, Custody etc	0.25%	0.24%
Total	1.56%	1.92%

Distribution Fund	30/10/2017	30/04/2018
Hawksmoor AMC	0.75%	0.75%
Synthetic OCF	**0.43%**	**0.88%**
Administration, ACD, Custody etc	0.25%	0.24%
Total	1.43%	1.87%

Different Rules for Different Investment Vehicles

As active managers, we absolutely agree with the need to be transparent with investors as we need to demonstrate the added value we can provide above that offered by a passive solution. However, in our opinion, there are inconsistencies in these OCF calculations that are actually misleading and confusing to most retail investors.

For example, we have a significant allocation in our Funds to private equity and physical property via investment trusts, which we believe are the best vehicles for accessing such illiquid asset classes due to their closed-ended structure. These asset classes provide excellent diversification benefits relative to mainstream equity and bond markets and help make our Funds truly multi-asset. However, the newly declared OCFs of these investment trusts are much higher than those of listed equity funds or open-ended property funds that **do not face this new legislation until 2020**. This means that our peers that only invest in these types of vehicles will not be impacted by this for another couple of years and will optically look cheaper than our own funds as a result.

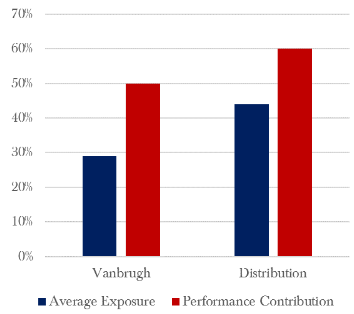
Our Funds Will Not Suddenly Cost More

It is worth expanding on the previously made point that just because the disclosed OCF of investment companies will rise, and in turn so too will our Funds' look-through OCF, neither suddenly cost more. Past performance reflects these costs that have always been in place – private equity businesses and property funds have always had to buy and sell assets and manage those to the best of their abilities to generate returns for investors and, as with all businesses, management are entitled to earn fair management fees, and sometimes performance fees if benchmarks and targets are exceeded. Therefore, just because these companies now have to report the costs involved, this doesn't alter how we view their historic performance or dissuade us from investing in them in the future.

Investment Trusts Have Added Considerable Value

We have shown through active management and accessing different asset classes that can only be accessed appropriately via investment trusts (sectors like private equity, property and specialist bond funds) that we can enhance the prospects of attractive risk adjusted returns compared to only investing in open-ended funds.

Internal analysis demonstrates that investment trusts have added considerable value over the years; in 2017, investment trusts represented on average 29% of Vanbrugh's portfolio yet contributed more than 50% of the return, whilst the average exposure to ICs for the Distribution Fund in 2017 was 44%, which contributed nearly 60% of the performance.



OCFs Calculated on NAV Not Share Price

Importantly, the OCF of an investment trust does not directly affect the return investors may receive, as that is dictated by the performance of its share price, which is driven by the difference between demand and supply. This can result in shares trading at a premium or a discount to its net asset value (NAV). As the costs are incurred at the NAV level, how does one calculate the true OCF of a trust that is trading at a discount?

Real Estate Investment Trusts Are Not Covered by PRIIPs

Most of the Funds' property exposure is held via Real Estate Investment Trusts (REITs), and this makes up a significant part of their portfolios (8% for Vanbrugh and 13% for Distribution). Peculiarly, the PRIIPs regulation does not apply to REITs and therefore they have no requirement to produce a KID, even though the majority do, and there is no requirement for the disclosed OCF to be included in the Funds' synthetic OCF calculation. If this legislation was to change in the future, we would see a further hike in our presented OCF, but of course, the charges are already reflected in the portfolios, via the performance of the trusts, and **it would not make our Funds more expensive**.

Further, different investment companies are interpreting the legislation differently, and some are uncertain on which costs should be included in the 'composition of costs' table on the KID, and in which category. For example, one of our investment trust holdings began the year with an OCF of 9% but, further to the annual review held in consultation with legal experts, have now changed the costs that are included in each category and therefore now show an OCF of 0%. There is every chance that other investment companies will change the methodology used for calculating these costs presented in the KIDs so it may be a couple of years before a consistent application of the regulation is adopted. This highlights that there is widespread confusion and perhaps the rules have been brought in too hastily.

Our Raison d'être

Despite the illusion of higher costs on our own Funds compared to passive solutions or funds that only invest in open-ended funds, we will continue to strive to demonstrate the added value investment trusts offer in terms of investment opportunities and diversification benefits, and endeavour to produce superior risk adjusted returns for our investors.

We hope that the regulators' obsession with costs will not hinder the true objective of any investors; to maximise real returns *after* charges and taxes.

Daniel Lockyer
Senior Fund Manager

9 Source: Internal. Funds performance data taken from FE Analytics.

CONTACT INFORMATION

For further information on any of our Funds or Services, or to arrange a meeting with a Fund Manager, please contact us on the details below:

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Please note, all telephone calls will be recorded.

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RISK WARNINGS AND OTHER INFORMATION

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