THE SCOTTISH Investment Trust

The CONTRARIAN SPRING 2019

ANALYSIS AND INSIGHT FROM **THE SCOTTISH INVESTMENT TRUST**

Live long and prosper!

Have you thought about the type of lifestyle you would like in retirement? For many of those currently in work, retirement feels a long way off – but to be comfortable in our golden years, it's important to start saving early.

A longer life

Long-term demographic trends are favourable. We are in general living longer and, as long as we remain healthy, later life can be enjoyed to the full. However, finances are a factor. Whether we spend our later years in comfort is largely dependent on us and our actions in advance.

We should all think about preparing for a longer retirement. Although we are inevitably working later in life, current UK 'pension freedoms' mean that some pensions can be accessed from the age of 55, whether one continues working or not. Pension income could supplement a wage or be a major source of income in retirement. Whichever, its importance in later life is likely to be considerable.

A longer income

The downside of living longer is that the money, which we save up from our working career, needs to last longer. Gone are the days of gold-plated, defined benefit schemes and annuity rates of over 10%. With interest rates so low, bond yields and, in turn, annuity rates are also low. In this environment, your pension fund in retirement needs to be bigger than ever.

The logical imperative is to save more. Most of us would like to maintain the standard of living that we have grown accustomed to. But still, some are sleepwalking into a lower standard of living by not putting enough aside. Those who come to realise this often do so too late to do much about it. The key is to start to save at a young age and to put sufficient sums away. Easier said than done, of course, when there are so many competing claims on our money.

Invest long-term and prosper slowly

The good news for the young is that the longer one is invested, the greater chance one has to build up a substantial sum of money to fund retirement. The upward bias of markets over the long-term, the benefit of reinvested dividends and the magic of compounding – are key factors required to drive returns.

Continued: Overleaf

ABOUT

The Scottish Investment Trust

At The Scottish, our experienced team actively manages a high conviction, global investment portfolio with the aim of generating above average investment returns over the longer term for our investors. Our contrarian approach is benchmark agnostic and aims to benefit from profitable opportunities in any market environment. Founded in 1887, the trust has a long tradition of providing shareholders with an accessible, low cost way to invest in companies from around the world, whilst further boosting returns through the provision of a growing dividend. The Scottish has grown its regular dividend every year for the last 35 years. Our independently managed, closed-ended fund structure allows us to be patient with our investments.

Please remember that past performance may not be repeated and is not a guide for future performance. The value of shares and the income from them can go down as well as up as a result of market and currency fluctuations. You may not get back the amount you invest. The Scottish Investment Trust PLC has a long-term policy of borrowing money to invest in equities in the expectation that this will improve returns for shareholders. However, should markets fall these borrowings would magnify any losses on these investments. Investment trusts are listed companies and are not authorised or regulated by the Financial Conduct Authority. Please note that SIT Savings Ltd is not authorised to provide advice to individual investors and nothing in this newsletter should be considered to be or relied upon as constituting investment advice. If you are unsure about the suitability of an investment, you should contact your financial advisor. Issued and approved by SIT Savings Limited. Authorised and regulated by the Financial Conduct Authority.

Live long and prosper!

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Historically, equities have been one of the best assets for maximising returns over the long run, although they can be more volatile than bonds. Investing over the long-term can smooth out the corrections in equity prices that will occur during the period you are building up funds for retirement.

The UK currently has tax efficient schemes to facilitate and encourage pension saving. There are a number of alternatives, but one way to take advantage of tax benefits on offer as well as the ability to select and allocate all assets, is through a Self-Invested Personal Pension (SIPP) plan. Investments in a SIPP can grow free of capital gains and income tax and, when paying into a SIPP, government tax relief is received. Though remember that, in most cases, access to SIPP savings is only available from the age of 55. Also, the value of any tax benefit depends on individual circumstances and tax rules may change in the future.

Contrariwise

A fund with a contrarian approach could be a useful component of a diversified pension portfolio. This style does not chase the investment fads of the moment or become swayed by current themes but aims to provide investors with above-average returns over the longer term. It demands patience, recognising that some stocks, while representing good value, can stay 'unloved' or shunned by the market for some time. Good companies can go out of fashion, but they often remain good companies with the potential for share prices to recover.

Being an independent, closed-ended fund allows the investment managers at The Scottish to select companies where they have a high conviction and a view to long-term payback – appropriate for long-term investors. The Scottish has one of the lowest ongoing charges figures within the AIC Global sector which is important as seemingly small differences can have a surprising impact on investors' returns over the long-term.

Similarly, dividends have historically accounted for a significant portion of total returns. According to the Association of Investment Companies (AIC) figures, The Scottish has one of the highest dividend yields in its peer group. The AIC have also named the trust a 'Dividend Hero' as it has grown the regular dividend for the past 35 years. However, it should be remembered that dividends are not guaranteed and can fall as well as rise.

By consistently investing from a young age – and taking a long-term approach – you are more likely to build your pension fund to a substantial level, helping to ensure a happy and fulfilling retirement.

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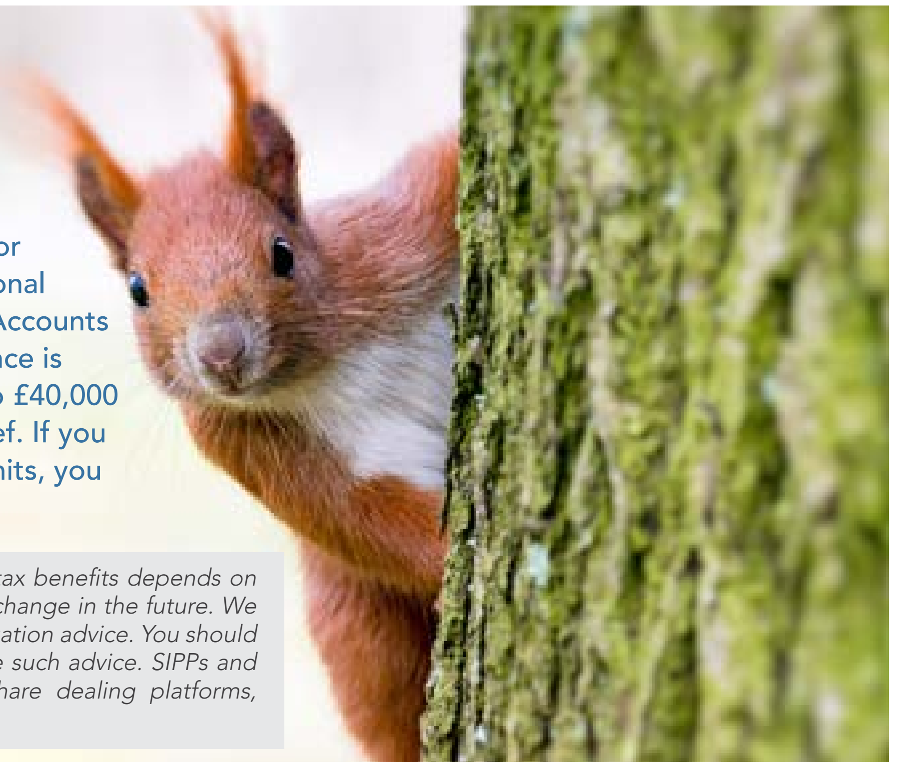
Are you a long-term investor in The Scottish?

We'd love to hear about how investing has helped you to achieve your financial goals. Get in touch and share your investment journey with us...

(Contact details: Back Page)

In a nutshell...

Squirreling something away for your golden years is important. There are a number of tax-efficient ways to invest for retirement including Self-Invested Personal Pensions (SIPP) and Individual Savings Accounts (ISAs). Currently, the ISA annual allowance is £20,000 and SIPP contributions of up to £40,000 per annum receive government tax relief. If you wish to take advantage of this year's limits, you can do so by the 5th of April.



It should be remembered that the value of any tax benefits depends on your individual circumstances and tax rules may change in the future. We are unable to provide individual investment or taxation advice. You should consult a professional adviser should you require such advice. SIPPs and ISAs are widely available including through share dealing platforms, stockbrokers and other financial intermediaries.

POSTCARD FROM CHINA

by Alasdair McKinnon, Manager

Greetings from Shanghai!

China is a land of contradictions. It's a communist country and yet, capitalism operates in raw state. It's poor and yet it's rich. Growth has slowed mind you. Nobody wants a trade war.

See you soon.

In January, I paid a visit to Shanghai. On the day I arrived, the headlines were dominated by economic gloom. Apple had just issued a profit warning, blaming China for its slowing sales, Chinese manufacturing data had been disappointing and the slowest growth figures for a decade were about to emerge. China already seemed to be suffering from the trade war with the US.

The trade war is only the most recent example of the increasingly tense relationship between East and West. Shanghai itself testifies to that relationship. The city's rise – from minor town to trading port to financial centre and sprawling metropolis – was accelerated by colonial interventions by Western powers.

That legacy is readily apparent. The city's best known feature is the Bund, its colonial era waterfront, where some of the grandest old buildings in Asia are today dwarfed by the towering modern skyscrapers. The Bund reminded me of the waterfront in Liverpool, another city that was also once of global importance. Its comparative decline underscores how everything is cyclical – one of the key concepts of our contrarian investment approach.

The Bund symbolises China's changing fortunes. The imposing HSBC building – designed by British architects in the 1920s – is now topped with the red star of the Chinese Communist Party. Next door, the Customs House clock, which used to play the same bongs as Big Ben, now plays the Mao era favourite The East is Red.

Across the Huangpu River from the Bund are the gleaming spires of the Lujiazui financial district. At night, these are lit up with spectacular neon advertising. Some of this promotes domestic companies, but a lot is for US products.

This surprised me somewhat, given the trade war and the anti-American sentiment we hear so much about. But US goods are still very prominent in Chinese life. Despite Apple's grumbles about the Chinese market, the iPhone was still ubiquitous and so were Nike trainers. Most Chinese people I spoke to seemed baffled by the trade war and by Trump's hostility to their nation.

Ironically, one outcome of the trade war may be to accelerate the Chinese disregard for intellectual property that so annoys the US. I met the representatives of an elevator company that specialises in reverse engineering of Western technologies. This sort of close-to-the-wind import substitution is being encouraged by Trump's tariffs. More generally, domestic producers are seeing an opportunity as imported goods become more expensive.

In the meantime, the trade war is certainly having a painful impact on the economy. The Chinese authorities appear keen to intervene and have already loosened their monetary policy by reducing the reserve requirements for the banks. From talking to the company management teams I met during my visit, I got a strong impression that there's still considerable faith in the government's ability to put everything right.

That faith may be sorely tested, especially if Trump's tariffs continue and other foreign governments become more suspicious of Chinese companies with close links to the state – such as telecom giant Huawei. As it becomes more apparent that China is not a perpetual growth machine, keeping the show on the road may prove to be difficult.

For some time, China has been meeting this challenge through debt, but that's hardly sustainable. Unstable amounts of local government debt are posing increasing problems. The instability of lenders is becoming more apparent too. My visit came just after the collapse of Xinhehui, only the latest of China's peer-to-peer lending institutions to flounder. Such collapses – in which ordinary people risk losing large amounts of their savings – are likely to foment popular discontent. That's what the Chinese authorities, wary of the fate of many imperial dynasties, fear most of all. Indeed, the additional impact of the trade war is most unwelcome.

As Apple's warning shows, the trade war is also having an economic impact on the US and it's affecting Japan and Europe as well. The economies of East and West are now so closely intertwined that the trade war may come to be seen as the last futile effort to assert the fading dominance of the American Empire.

> "Its comparative decline underscores how everything is cyclical…"

Again, everything is cyclical. That includes the balance of global power. The Chinese were well ahead of the West in all sorts of ways for millennia, but that eventually led to complacency, decadence and then shock when Europeans arrived with superior technologies.

Has the West now grown decadent? And if so, is China the hungry, rising power that Western countries were in the colonial era? After the trauma of its sixteenth and seventeenth century wars, Europe went on to the successes of the settlement of the Americas and the Industrial Revolution. The turmoil of China's 1949 revolution and its aftershocks profoundly reshaped its institutions. Those shifts may have left it primed to continue the economic successes of the past 30 years, even as the West diminishes.

As at 28 February 2019

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