Amati
Global Investors

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CITYWIRE AAA

FE CROWN FUND RATING

QUARTERLY NEWSLETTER

Investment in smaller companies can be higher risk than investment in well-established blue chip companies. Funds investing significantly in smaller companies can be subject to more volatility due to the limited marketability of the underlying asset. Please refer to the risk warning on page 6.

"AIM provides a wealth of under-researched opportunities, but the work required to uncover them is significant. Dr Paul Jourdan and the Amati team have the experience and level-headed approach needed to succeed in this market."

Richard Troue, Head of Investment Analysis
Hargreaves Lansdown

Past performance is not a reliable indicator to future performance

AMATI AWARDS

We were delighted to receive Money Observer's Best UK Smaller/Mid Cap fund of the year 2017 for the second year running. The award is in recognition of consistently superior risk-adjusted performance over a 3 year period to 31st March 2017. This is the second year in a row that TB Amati has won this award but this year, rather than differentiate between larger and smaller funds, Money Observer pitted all Smaller Companies funds, large and small, against each other – and the TB Amati fund has taken the crown.

Money Observer FUND AWARDS 2017
Best UK Smaller Mid Cap Equity Fund
TB Amati UK Smaller Companies

In July of this year David Stevenson attended the prestigious Investment Week Fund Manager of the Year Award ceremony at the Royal Albert Hall in London. Paul Jourdan, Douglas Lawson &

David Stevenson picked up the award in the UK Smaller Companies category for TB Amati UK Smaller Companies Fund.

The aim of the Investment Week Fund Manager of the Year Awards is to highlight funds that produce consistent performance and where there is, in the judges' opinion, a high chance that the manager will not disappoint in the future.

A look at the previous winners section shows many of the managers who won in the past are still considered to be at the top of their peer groups today. While the last few years have seen a high level of manager turnover, the awards are only for funds where the manager has been in place for three years or more. Just as the judges are looking for consistency of return, they believe one of the best ways for a fund to achieve this is via the consistency of a fund manager's tenure. The top managers tend to be those who stick with their portfolios for the long-term.

Douglas Lawson commented "The team at Amati is thrilled to have been awarded Investment Week's UK Smaller Company Fund Manager of the Year award for its TB Amati UK Smaller Companies Fund. Investment Week is a well-respected industry commentator and judged the finalists on a rigorous set of quantitative and qualitative factors. We are delighted with this vote of confidence in our investment philosophy and process."

INVESTMENT WEEK
FUND MANAGER OF THE YEAR 2017
WINNER
UK Smaller Companies

Why We Buy Expensive Stocks

Douglas Lawson

Fevertree Drinks PLC listed on AIM in November 2014 at 134p per share. This represented a price to earnings (P/E) ratio of 20.6x based on the broker's estimate of full year profits for 2015. Looking ahead to 2016, the broker's forecast put Fevertree on 17.6x. Come the day of the IPO, the shares were soon trading at 166p, pushing these P/E multiples up to 25.5x and 21.8x, respectively. Was Fevertree expensively priced at IPO? Did it become expensive on the day the shares began trading? We didn't think so. We subscribed for shares in the IPO itself, then added to our position shortly afterwards. At the time of writing the share price is 1779p and, whilst we have been taking profits into this appreciation, we continue to hold a position in Fevertree, even though the stock is valued at 64x current consensus 2017 earnings (and 75x historic 2016 earnings).

The success of Fevertree (1,227% gain since IPO) serves as a warning against being fixated with P/E multiples in isolation. When assessing the valuation of a growth company we look ahead several years in order to determine whether the price we are paying today is a fair one. This is because high growth companies on a high multiple of near term earnings can be trading on a comparatively low multiple of expected earnings in several years time. This is usually not factored into market forecasts, which will nearly always factor in a 'fade rate' for growth, meaning current, run-rate levels of growth will decline year on year. These forecasts may therefore underestimate the potential of companies that are capable of delivering extraordinary levels of growth for multiple years. Coming back to Fevertree, at the time of the IPO, forecast earnings per share for the year to December 2016 was 9.6p. The actual result was 23.7p, an incredible 147% above expectations at the time of the floatation. This is an example of the disconnect between what the broker must publish to avoid accusations of conjuring up figures that look unrealistic on paper and the real earnings potential of great growth companies.

When the market latches on to businesses that have repeatedly upgraded their earnings forecasts, the stock tends to 're-rate' meaning that, as well as the earnings forecast climbing up, the P/E ratio also rises. As a share price is a function of the earnings forecast multiplied by the P/E multiple, this delivers a double whammy to investor returns. In today's market, such stocks can re-rate to multiples akin to those of Fevertree. At this stage, investors are right to revisit the valuation question.

So, is Fevertree's current rating of 64x justifiable? It depends. Having delivered earnings growth of 106% in 2016, the market is forecasting 17% earnings growth in 2017 and 12% in 2018. Given the company's history of upgrades, and the slowdown in growth this would represent, it would be little surprise to see these numbers moving up. Let's for a moment take a scenario where a company, like Fevertree (Stock A), is trading on 75x historic earnings. Suppose that company's growth rate slows from 106% in the prior year to 50% for the next 3 years. Looking out 3 years, the P/E ratio falls from 64x to 22x. If you extend this to 5 years, the P/E falls to under 10x.

An investment in a VCT carries higher risk than other forms of investment. An investment in the Amati VCTs is suitable only for investors who are capable of evaluating the risk and merits of such investment and who have sufficient resources to bear any loss which might result from such investment. Investors should check their eligibility for income tax relief with a professional adviser.

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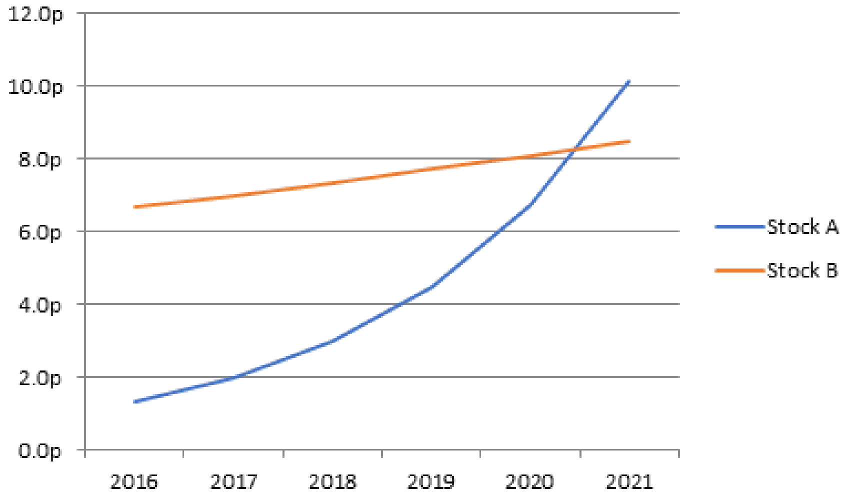
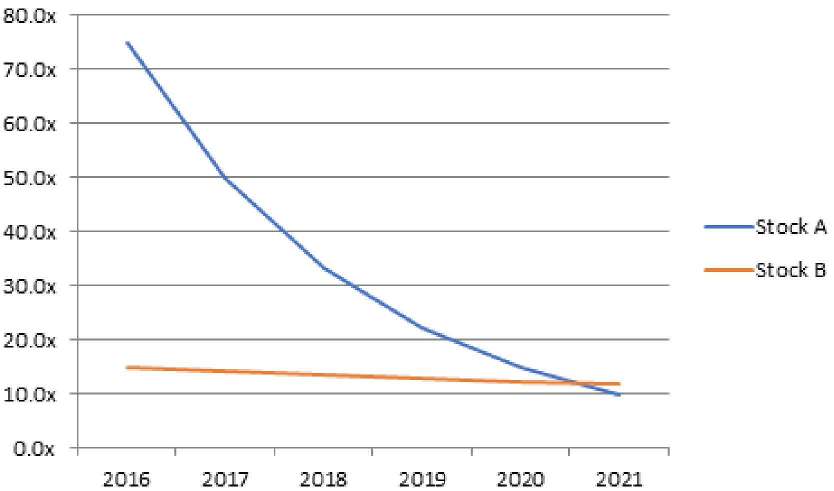
Let's compare this to a company (Stock B) on 15x historic earnings that has an earnings growth rate of 5%. If you look at historic or near term P/E ratios in isolation you would conclude that Stock B is significantly cheaper than Stock A. If you model compound annual earnings growth of 5% over 3 years, Stock B is trading on a P/E of 13x – it is still cheaper but the discount to Stock A is narrowing. Over 5 years, Stock B is trading on 11.8x versus stock A on 9.9x. In other words, looking out 5 years, Stock A is cheaper than Stock B and I would be inclined to argue that the growth prospects of Stock A remain better than Stock B.

This approach comes with a number of caveats, not least that a company (like Stock A) that experiences a material slowdown in growth relative to market expectations will not only see its earnings forecasts revised down, but is also likely to be 'de-rated', meaning its P/E rating will fall – a reverse double whammy to the share price. Fundamental analysis and vigilance can reduce an investor's prospects of being caught in this situation, but not eradicate them.

Example Earnings per Share (EPS) Movement: Stock A versus Stock B



Example Price to Earnings (P/E) Ratio: Stock A versus Stock B



Sources: Amati Global Investors, Factset

Amati Global Investors

Amati Global Investors are managers for:

- Amati VCT
- Amati VCT 2
- TB Amati UK Smaller Companies Fund
- Amati AIM IHT Portfolio Service

Investment markets and conditions can change rapidly and as such the views expressed should not be taken as statements of fact nor should reliance be placed on these views when making investment decisions. Past performance is not a reliable indicator to future performance.

Portfolio Companies Spotlight

Frontier Developments - Frontier Developments is a video games publisher. Its founder, David Braben, co-authored Elite, a popular 1980s video game, which was originally published by Acornsoft for the BBC Mirco and Acorn Electron computers. He went on to set-up Frontier to create and develop games for the world's largest gaming companies, such as Microsoft (Xbox) and Sony (Playstation), before deciding to transition Frontier back into higher margin self-publishing. The first step towards this movement was the re-launch of Elite in 2014 under the title 'Elite:Dangerous'. This turned the original game into a multi-player, virtual reality enabled space epic encompassing 400 billion star systems. The re-launch of Elite was followed by the release of Planet Coaster, the group's second franchise, in 2016. Frontier is planning to release its third self-published game franchise, based on a currently unnamed Hollywood movie, in 2018. The Amati VCTs invested in Frontier in 2013, shortly before its AIM IPO. The investment was made using a convertible loan, which converted into equity at a discount to the listing price at the time of the IPO. The current market capitalisation is £188 million.

Ideagen - Ideagen provides governance, risk and compliance (GRC) software into regulated industries such as healthcare, banking, aerospace and energy. The GRC market has attractive growth characteristics as industries move towards increased regulation, and organisations must be able to demonstrate effective risk management processes are in place and that staff are adhering to those processes. Ideagen now has a customer base of over 3,000 organisations using its suite of products, including names such as BAE Systems, Emirates, Shell and the European Central Bank. The 'must have' nature of Ideagen's software means that customer churn is very low and, therefore, visibility of income is high with recurring revenue running at 75% of the total. As well as organic growth, Ideagen has pursued a 'buy and build' strategy through the acquisition of a series of related software businesses. The Amati VCTs invested in Ideagen in 2012 as part of a placing to acquire Plumtree, a management information software company that provided the group with access to the healthcare market. Since then Ideagen has completed a further eight acquisitions for a total maximum consideration of £52m. The current market capitalisation is £170 million.

Bioventix - Bioventix manufactures and supplies antibodies for use in medical diagnostic applications such as blood testing. Bioventix uses sheep monoclonal antibodies (SMAs), which have proven advantages over antibodies from other animal cells such as the ability to bind to targets for longer which produces results of greater sensitivity and precision, especially where the target is present in low concentration. Bioventix offers a portfolio of antibodies to customers for both commercial use and R&D purposes for the diagnosis and monitoring of a broad range of conditions, including heart disease, cancer, fertility, thyroid function and drug abuse. As an example, the company recently announced the launch of a new test by Siemens for troponin, a key biomarker used in heart attack diagnostics, which incorporates antibodies created by Bioventix. Under the terms of the supply agreement, Bioventix will receive royalties on sales of Siemens' units. The stock is held in the TB Amati UK Smaller Companies Fund and the Amati AIM IHT Portfolio Service and has a market capitalisation of £99 million.

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Amati VCTs' AGMs & Investor Event

Amati again held its annual investor afternoon at the wonderful Guildhall School of Music & Drama on 28 June 2017 and hosted both Amati VCTs' AGMs to an increased number of investors and advisers. We were delighted to be joined by Ideagen and SRT Marine Systems, two portfolio companies held within the VCTs. If you weren't able to join us on the day, you might like to take a look at the presentation videos on our website here.

Feedback from our investors was on the whole very positive and below are some of the comments received:

"I found the event to be quite refreshing, it was nice to see the two companies present and I did find the information regarding the deal flow very informative."

"I thought it all worked very well and created a strong 'investor family' feel, which I like."

"Excellent event. Comprehensive information on the VCT strategy and answered questions fully."

Amati Guildhall Creative Entrepreneurs' Award

Following on from our Amati VCTs' AGMs and company presentations, we saw the fourth Amati Guildhall Creative Entrepreneurs' Award with presentations from Salon Musical, Vox Integra and Gestalt Arts. Our judging panel keenly listened to all three pitches, but after much consideration this was awarded to Gestalt Arts. You can view all three pitches and the award presentation on our website here.

Gestalt is a contemporary opera company which uses opera and music theatre as a tool to explore, unite and celebrate unique places and peoples. They work with different geographic communities, interest communities and sectors of society. They use participants experience, expertise and humanity to create fascinating and unusual, operatic works which helps create a dialogue with a larger audience and foster an attitude of interest, openness and understanding.

Ruth Mariner, writer and director for Gestalt Arts was presented with the award at the prestigious London Guildhall School of Music & Drama - "I'm absolutely honoured to receive the award, and the money will pay for that initial set of workshops with the teenagers from Huddersfield and make it so much easier for us to get funding for the next stage. The money will also go towards a collaboration with opera company Opera Schmopera, devising an opera with teenagers about identity."

We would welcome your feedback/comments on any of the areas covered in this issue. Please either email the team on **info@amatiglobal.com** or call on 0131 503 9100. If you would like to receive our monthly fact sheets by email please send a request to **info@amatiglobal.com**.

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Amati Fund Performance

as at 30 June 2017*

For further information please refer to the most recent fund factsheets: **TB Amati UK Smaller Companies Fund**, **Amati VCT**, **Amati VCT 2** and **Amati AIM IHT Portfolio Service**

	1 mth	3 mths	6 mths	1 yr	2 yrs	3 yrs	5 yrs	Since launch**/take-on#
Amati VCT	**-3.66**	**8.47**	**18.57**	**37.59**	**34.03**	**23.88**	**62.01**	**71.79****
Amati VCT 2	**-4.44**	**8.00**	**18.52**	**36.50**	**43.16**	**32.40**	**73.70**	**95.45#**
Amati AIM IHT Portfolio Service	**-2.38**	**7.42**	**14.11**	**40.93**	**52.68**	--	--	**75.11****
TB Amati UK Smaller Companies Fund	**-4.52**	**5.16**	**13.88**	**40.51**	**51.30**	**65.33**	**132.61**	**510.28#**

Sources: Capita Asset Services, T. Bailey Fund Services, FE Analytics, Amati Global Investors

*NAV Total Return (%)
**Amati VCT: 24/03/2005, Amati VCT 2: 29/01/2001, IHT: 29/08/2014, TB Amati UK Sm Cos: 18/12/1998
#Amati VCT 2: 25/03/2010, TB Amati UK Sm Cos: 31/08/2000

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Risk Warnings

This newsletter does not constitute investment, tax, or legal advice, and nor does it constitute an offer, invitation or solicitation to invest in the products described. Amati will not provide any investment, tax, or legal advice, or make any personal recommendations as to the suitability or otherwise of these products. Before investing in our products we recommend that you contact your financial adviser.

These investment products place your capital at risk and you may not get back the full amount invested, even allowing for any tax breaks. The value of your investment may go down as well as up. Past performance is not a reliable indicator of future performance. Investors should be aware that any investment in equities is subject to risk, and that investment in smaller companies, in particular unquoted companies and those quoted on the Alternative Investment Market (AIM), carries an even higher risk than that of larger companies listed on the main market of the London Stock Exchange. This is due to the higher volatility and lack of liquidity often found in smaller company shares, as well as typically higher levels of business specific risks. Illiquidity means that buying and selling portfolio holdings may take some time, and in a worst case scenario portfolio companies could be delisted from AIM, making them very difficult to buy or sell, which in turn could affect the value of your investment. Current tax rules and the available tax reliefs offered on investments into AIM-quoted stocks may change at any time, and there is a considerable risk that if the legislation changed in respect of these tax reliefs, then those portfolio companies that no longer qualified for such reliefs would be subject to heavy selling pressure, potentially leading to significant investment losses.

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Calls are recorded and monitored.

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