MARTEN & CO

Initiation | Investment companies

30 April 2019

Polar Capital Global Financials Trust

Don't fear a slowing economy

It is 10 years since the worst of the financial crisis, and almost six years since Polar Capital Global Financials Trust (PCFT) was launched to take advantage of low valuations in the financial sector and to offer investors a lower risk way of accessing the sector.

Yet financial stocks (banks in particular) have lagged broader markets since then. This is despite banks rebuilding their balance sheets, margin recovery, bad debts at multi-year lows and, crucially for PCFT, which is designed to offer an attractive and growing yield, restrictions on dividend pay-outs being eased.

PCFT's managers acknowledge the signs that the global economy is slowing, but think investors' fears of a return to 2008 for the banking sector are misplaced. Regulatory actions and management's burnt fingers have restricted bank lending over the past decade. We have still been borrowing enormous sums, but the money has been coming from non-bank lenders. It is they who will have to deal with any surge in defaults and, if this reduces competitive pressures in the lending sector going forward, that will be good news for banks.

Growing income from financials stocks

PCFT aims to generate a growing dividend income, together with capital appreciation. It invests primarily in a global portfolio, consisting of listed or quoted securities issued by companies in the financial sector. This includes banks, life and non-life insurance companies, asset managers, stock exchanges, speciality lenders and fintech companies, as well as property and other related sub-sectors.

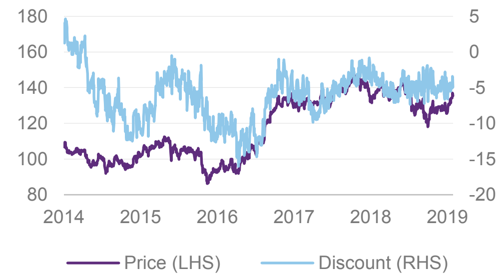
Year ended	Share price total return (%)	NAV total return (%)	Benchmark total return[1] (%)	MSCI AC World total return (%)
31/03/15	(3.0)	12.8	16.0	18.4
31/03/16	(5.6)	(4.6)	(7.2)	(1.2)
31/03/17	46.3	36.0	40.0	32.2
31/03/18	5.7	2.7	0.7	2.4
31/03/19	(3.7)	(0.6)	2.7	10.5

Source: Morningstar, Polar Capital, Marten & Co. Note 1) PCFT's benchmark is the MSCI World Index Financials plus Real Estate Index (see note on page 3)

Sector	Specialist - financials
Ticker	PCFT LN
Base currency	GBP
Price	135.5p
NAV	142.5p
Premium/(discount)	(4.9%)
Yield	3.1%

Share price and discount

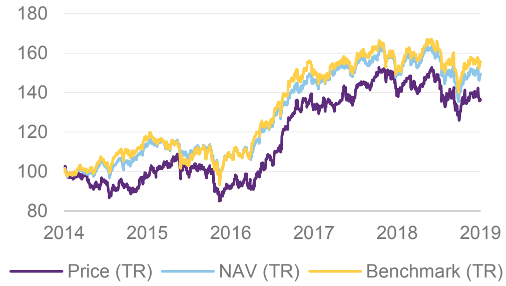
Time period 31/03/2014 to 26/04/2019



Source: Morningstar, Marten & Co

Performance over five years

Time period 31/03/2014 to 31/03/2019



Source: Source: Morningstar, Polar Capital, Marten & Co. Note: PCFT's benchmark is the MSCI World Index Financials plus Real Estate Index (see note on page 3)

Domicile	England & Wales
Inception date	1 July 2013
Manager	Nick Brind and John Yakas
Market cap	274.8m
Shares outstanding	202.775m
Daily vol. (1-yr. avg.)	330,000 shares
Net gearing	2.2%

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Fund profile

PCFT looks to grow investors income and their capital

More information on the trust is available on its website www.polarcapitalglobalfinancialstrust.com

Polar Capital Global Financials Trust (PCFT) launched on 1 July 2013 and has a fixed life that expires in May 2020. Its twin objectives focus on growing investors' income and their capital. Its global mandate makes it a useful alternative for UK-based investors looking to diversify their financials exposure.

Predominantly, the portfolio is invested in listed/quoted securities. The trust may have some exposure to unlisted/unquoted securities, but this is not expected to exceed 10% of total assets at the time of investment.

Reconstituted benchmark

The trust was benchmarked against the MSCI World Financials Index from launch until 31 August 2016. Then, when MSCI spun the Real Estate sector out of the Financials index, the benchmark became the MSCI World Financials plus Real Estate Net Total Return Index (in Sterling) – effectively a continuation of the pre-September 2016 benchmark. Marten & Co thanks the managers for providing us with data on the reconstituted benchmark.

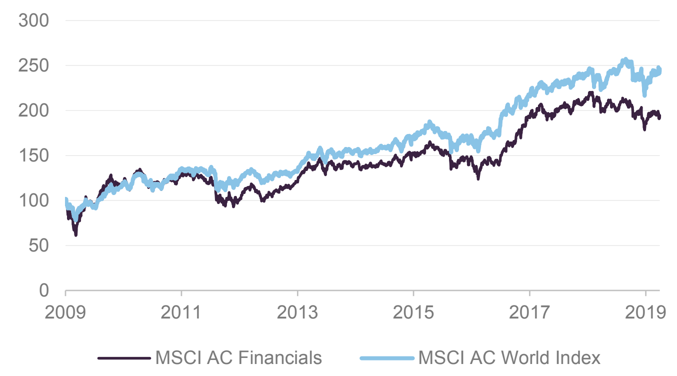
PCFT's AIFM is Polar Capital LLP and the lead managers are Nick Brind and John Yakas. More information on the management team is given on page 15.

Market outlook

The financial sector has underperformed both since the financial crisis and since the launch of PCFT

Financials are the largest of the industries that make up global stock markets (16.6% of the MSCI AC World Index at the end of March 2019) but, as Figure 2 shows, they have acted as a significant drag on the global index's performance since the nadir of the global financial crisis in 2009. There are several factors at work here, including a slowing global economy, political uncertainty in Europe (Brexit/Italy) and the shift from quantitative easing to tightening, but PCFT's managers believe that the sector is now undervalued. They say that the discount of the financials sector relative to the wider market is as wide as it has been in 2012 and 2016. Notably, the sector has also underperformed since PCFT's launch.

Figure 1: MSCI AC World Index and MSCI AC Financials Index since 1 January 2009 (rebased to 100)



Source: Morningstar, Marten & Co

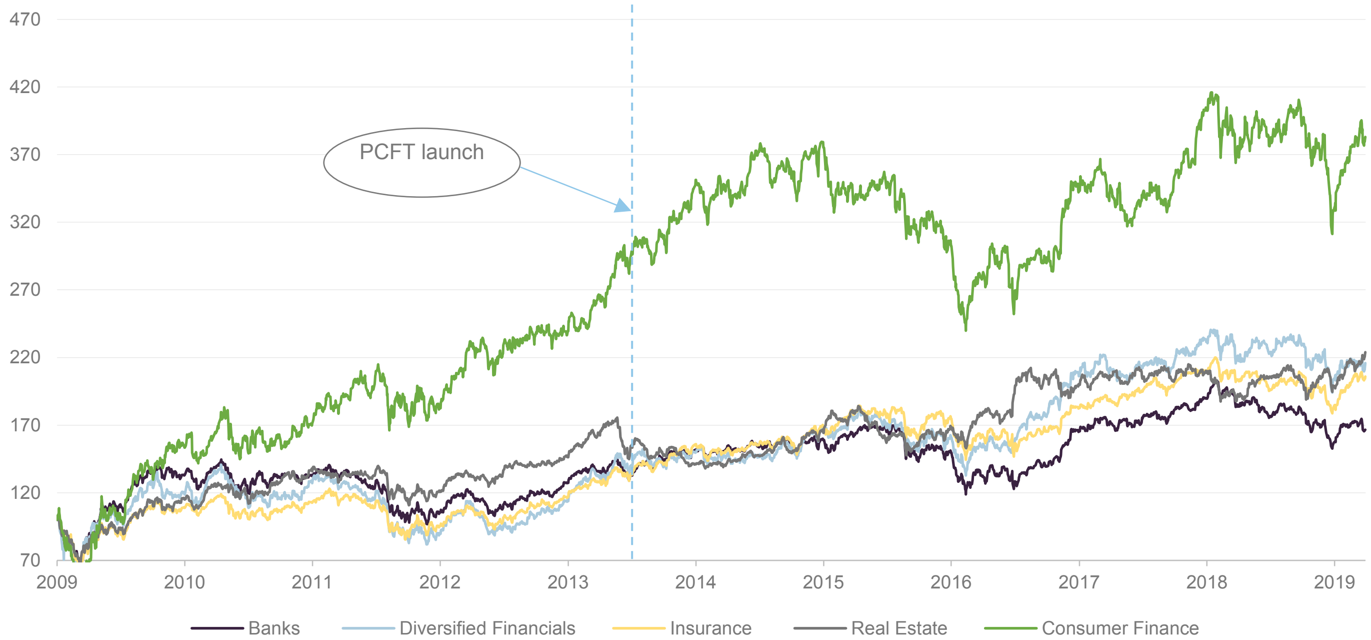
Figure 2: MSCI AC Financials Index relative to MSCI AC World Index since 1 January 2009 (rebased to 100)

Source: Morningstar, Marten & Co

Banks have been underperforming for some time

Within the financials index, the largest subsector is banks (diversified banks were 48.5% of the MSCI AC World Financials Index at the end of March and regional banks accounted for a further 4.5%). As Figure 3 shows, banks have lagged other parts of the financials sector since 2009, and have also underperformed since PCFT launched in July 2013, (note consumer finance is a subset of diversified financials).

Figure 3: Long-term performance of financial subsectors (MSCI All Country World Index sectors)



Source: Bloomberg, Marten & Co

One reason why banks may have lagged is that for all of the period since PCFT's launch, banks' net interest margins have been below their long-term averages. As Figure 4 demonstrates, they have at least been on an improving trend. The managers point out that margins are a reflection of balance sheet risk/mix and so, as the banking system writes lower risk lending going forward, its margins are unlikely to ever recover to levels seen pre-2008. Nevertheless, risk adjusted returns should be on a better basis as most of the riskiest lending has shifted to non-bank lenders.

Figure 4: US Bank net interest margin (quarterly)

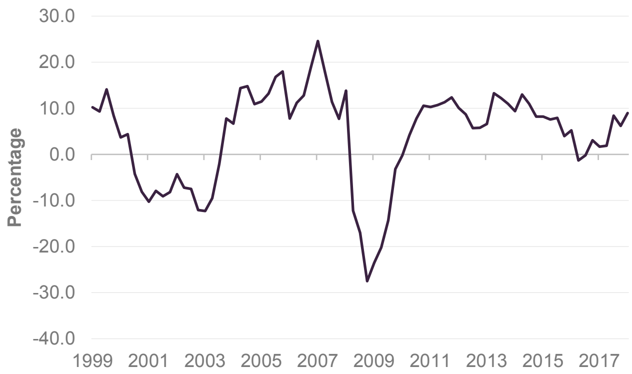
Source: Federal Reserve Bank of St. Louis, April 10, 2019

The Fed recently reversed its policy and said that there would be no rate rises in the US in 2019. The managers acknowledge that this may affect sentiment towards the sector but say the sector was not riding high on the prospect of rate rises in any case, and the market reaction to the news has not been too bad.

Absence of loan growth?

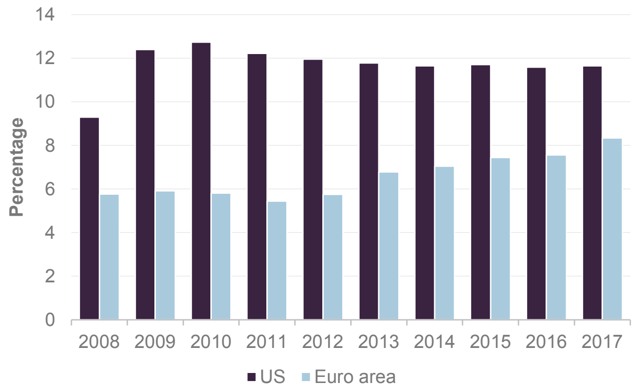
Bank loan growth has recovered since the financial crisis, but remains well below the highs of 2005/2008 and has been lagging nominal GDP growth. Part of the reason for this may have been the regulator's insistence on banks rebuilding their balance sheets, but the banks will also have been mindful of their experience in 2008.

Figure 5: Commercial and industrial loan growth, US commercial banks



Source: Federal Reserve Bank of St. Louis, April 10, 2019

Figure 6: US and European (Euro area) banks equity/assets ratio



Source: World Bank

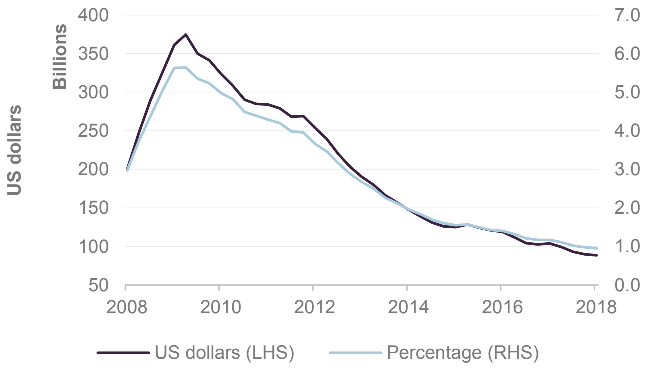
The good news is that US banks are reasonably well capitalised, more so than European ones (although the equity/assets ratio for European banks has been improving). Where banks have stood aside, non-bank lenders have stepped into the breach and private loan markets have boomed, aided by a resurgence in securitisation in the form of CLOs. The influx of non-bank lenders may have helped to depress banks' margins.

Alternative lenders seem to be experiencing problems with credit quality

Balance sheet lending from firms such as Lending Club is, in the managers' opinion, just a form of regulatory arbitrage. China is clamping down heavily on the subsector and the managers expect that this will happen elsewhere. Furthermore, there is a suspicion that many of the customers attracted by these lenders are of lower quality. That view might be reinforced by the recent news that Funding Circle SME Income Fund was throwing in the towel after predicting higher-than-forecast losses on business written in 2016/17. The managers note a similarity between some of the alternative finance companies and those of small banks pricing aggressively and funding wholesale.

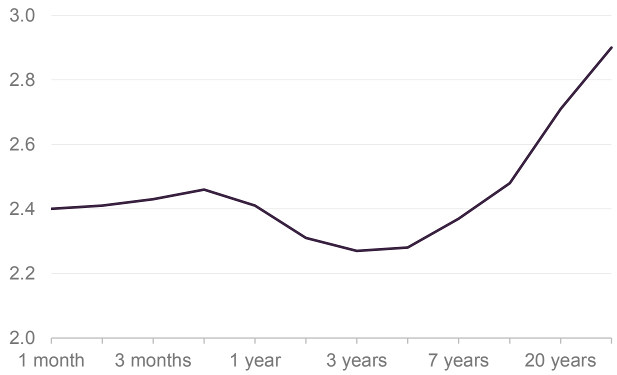
The managers conclude that banks have not been taking excessive risk and that this should stand them in good stead if the cycle turns.

Figure 7: US banks non-performing loans



Source: Federal Reserve Bank of St. Louis, April 10, 2019

Figure 8: US yield curve (10 April 2019)



Source: US Department of the Treasury, Marten & Co

As the global economy slows, investors may have shifted from worrying about margin growth to concern about defaults

Non-performing loans are not a problem currently, as Figure 7 shows. However, the US yield curve is fairly flat and inverted out to seven years. This is one of a number of indicators that suggest that we are approaching the end of the current economic cycle. Investors may now be worrying about an uptick in defaults. The consequence is that in the developed world, the banking sector underperformed quite markedly in 2018.

The managers agree that the economy is slowing, but they do not think that banks are going to be hit hard when the cycle turns down. They say that the warning signs that signalled past problems for the sector are not there today and, therefore, whilst margins may not rise from current levels, peak provisioning may not be as high as in previous cycles. Their reasoning is that the bulk of loan growth that has occurred in recent times has been the responsibility of non-bank lenders rather than the banks themselves. If the non-bank lenders are hit disproportionately, as the managers suspect, their capacity to lend will be constrained and that could translate into improved margins for the banking sector.

Managers believe the sector's income is sustainable

Strong balance sheets, low payout ratios and improved ROAs suggest that, at least for US banks, distributions are sustainable

Crucially, given PCFT's mandate, the managers think that the banks can sustain and even increase distributions to shareholders. The banks have strong balance sheets, and payout ratios in the US are fairly low but the profitability of US banks is quite high. Returns on assets (ROAs) have recovered from their post-crisis lows. The managers say that ROAs between 1% and 2% are good for banks operating in mature markets. It is true that ROEs are not as high as they were before the crisis, but this reflects the strength of banks' balance sheets.

Technological innovation

Financial services disruption is in its early stages but the banks are reacting

One factor that has unnerved some investors in the sector is the rise of fintech, which accounts for about 7% of PCFT (including Mastercard). There is a common belief that disruptive new entrants are going to drive down margins and capture significant market shares in a range of financial services. The managers say that it is too early to provide an assessment of who the ultimate winners will be. We are in the early stages of financial services disruption and it is important to remember that banks are reacting. Nevertheless, the managers will look to exploit opportunities where they can.

For PCFT's managers, accessing fintech creates a structural challenge; most of it is held by private equity (PCFT does have one unquoted holding, Atom Bank – see page 11). The managers note that in assessing fintech companies, there is a balancing act between high valuations and correspondingly low dividend yields versus PCFT's income requirement to be taken into consideration.

Payments companies, for example, sit on very high valuations. The managers do not think that this is necessarily justified – they cite a comparison between Mastercard and Square, for instance. In Q4 2018, the former processed $1.5trn of payments and made substantial profits, while the latter processed $23bn of payments and made a loss. Mastercard's business is 65x larger than Square's, but its market cap is less than 8x larger. The managers point out that the payments industry is always likely to be a heavily commoditised/regulated industry. Given this, they would prefer to hold a, hard-to-dislodge, incumbent.

Financial services companies know that they need to invest in systems but, fortunately, they have the budgets to do so

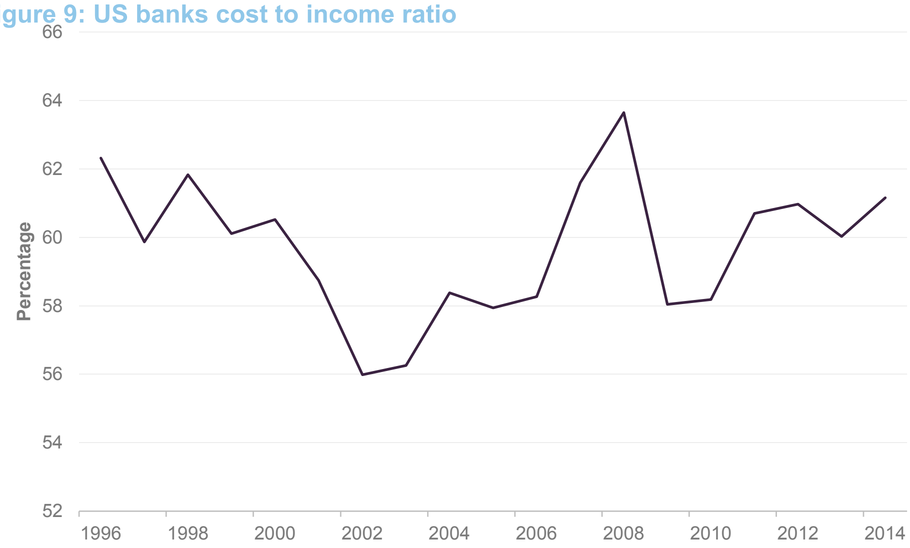
In general, many of the 'revolutionary' advances in financial services that fintech offers can be and are being adopted by incumbent businesses. It is true that legacy software systems need to be replaced/upgraded. Some companies responded by creating new standalone businesses – HSBC's First Direct is a good example of this. However, most are investing in existing operations and many have R&D budgets that far exceed those of the leading fintech companies (the managers point to data from Autonomus Research, which suggests Bank of America and JPMorgan are both investing more than twice as much as Ant Financial and three times as much as PayPal, for example).

The real challenge for new entrants is in acquiring profitable customers

Where the new businesses struggle most is in customer acquisition. Financial services customers are notoriously 'sticky' and will often only move to access services that are given away for free – not a recipe for making money. The managers do see the potential for some dynamic, customer-focused businesses to expand into financial services. Amazon might be a good example of this.

Many millions of words have been written about blockchain. The managers can see some advantages for some firms from the use of the technology (notably, the prospect of lower transaction costs), but they point out that many so-called blockchain companies have very tenuous links to the technology.

Figure 9: US banks cost to income ratio



Source: World Bank

Blockchain may lower overheads but past experience suggests savings will be passed onto customers

Figure 9 shows the cost to income ratio of US banks from 1996 to 2014, a period of considerable innovation. What is remarkable is how stable the ratio is. The managers say that cost-cutting is just given away in lower pricing. It seems likely that whatever advantages that blockchain brings will go the same way.

Regulation being eased

Consolidation back on the agenda

There is a strong argument that bigger is better in the banking world. Big banks have strong franchise values and find it easier to attract and retain customers. In May 2018, US lawmakers amended the 2010 Dodd-Frank Wall Street Reform Act to raise the $50bn threshold at which a bank is considered systemically important to $250bn. Effectively, this opens the door to a new wave of consolidation within the US banking industry. Only the three biggest banks remain blocked from making acquisitions. There has been an uptick in deals since the reforms – the recent tie-up between BB&T and SunTrust, for example – but the managers think there could be more to go for.

Could investment banking become more profitable?

At the other end of the scale, in a further sign that the post-crisis regulatory environment is being relaxed, sub-$10bn banks are no longer covered by the Volcker rules. This means that they can use their own capital for proprietary trading. This relaxation may not affect these small banks much, but it could presage rule changes that make investment banking more profitable.

End of curbs on dividend pay-out ratios

One change that is particularly good news for PCFT is that the Federal Reserve has lifted a soft cap on dividend pay-out ratios (as bank balance sheets are stronger than they were). This could lead to a boost in PCFT's revenue account.

Structural attractions in emerging markets

Emerging markets looking attractive once again

There was a significant bias towards emerging markets within the portfolio at launch (about 22% of the portfolio), predicated on superior economic growth, a growing middle class and a relatively low penetration of financial services products. However, a combination of factors, including a strengthening US dollar, encouraged more of an emphasis on US stocks and today emerging markets represent about 7% of the portfolio. With US rate rises on hold, the outlook for emerging markets could be brighter.

PCFT's Asian exposure is to stocks that the managers perceive as being high-quality. These are not cheap, but the managers think their ratings are justified by their growth potential. The portfolio has no exposure to the State-controlled banks in China and India, but does hold HDFC Bank. The managers see potential for significant growth in Indian lending products, including the mortgage market, where penetration rates are less than half of those in Thailand and China, let alone developed markets.

The theme of increasing penetration of financial services in Asia is exploited through positions in stocks such as AIA, Tisco Financial and Bank Central Asia.

Investment process

Emphasis on proprietary research

PCFT's managers are actively involved in the research process and, given their stock-picking approach, this is core to what they do. Their experience is that external research, produced by brokers and investment banks, tends to be quite short-term in focus. This may be because it is aimed at the hedge fund community. For that reason, aided by good access to companies' management, much more emphasis is placed on in-house research. The extent to which the team uses external research varies by degrees.

For balance sheet businesses, strong top-line growth may not be good news

Analysis of financial stocks differs from other sectors in that there is a focus on balance sheets. Strong top-line growth is not necessarily good news, because this may come at the expense of quality. Risk-adjusted analysis is therefore more useful.

Most financials stocks are very highly geared, and as a result there is a real need to focus on limiting the downside. Using the same lens as a growth investor when choosing financials could catch an investor out badly when the growth cycle turns down. The managers note that, in their experience, it is rare for the best short-term performers to do well over the long-term.

Global including emerging markets remit results in universe of about 500 stocks

The remit is global and includes emerging markets. The universe is about 500 stocks (the smallest stock that the managers would consider for PCFT's portfolio would have a market cap of around $500m). The managers say that this is a manageable number of stocks for the team to cover. The likes of Goldman Sachs and JPMorgan are complex beasts, but most banks have relatively simple business models. In many areas, pricing is commoditised and so the sector is quite generic, but research is essential to sort the good from the bad.

The managers use a scoring system to look at a range of variables around risk, growth and value. These include balance sheet strength; how the company is funded; the composition of the loan book; historical quality of the loan book; and trends in margins. This model is a framework for analysis rather than an engine to produce a buy list.

Meet about 400 companies a year

The team meets about 400 companies each year but a lot of this is double-checking their research findings. They talk to customers and competitors, for example.

For banks and similar companies, any assessment of value is based on a variation of CAPM – using returns on equity and price to book. The managers find that, for the reasons outlined above, p/e ratios and measures of growth do not work as well.

The sector is not just about balance sheet businesses, however, and it is evolving. The managers use a more earnings-driven, traditional approach to valuing other companies.

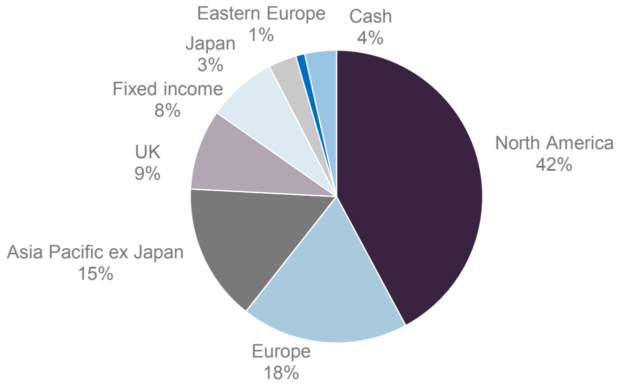
Asset allocation

The US dominates the benchmark. PCFT's focus on growth of income influences stock selection decisions and, relative to the benchmark, results in a small structural underweight exposure to the US. The fragmentation of the US banking market (there are over 5,000 US banks) allows the managers to make allocations to particular regions within the US.

The UK tends to be about 10% of the portfolio or lower. The managers say that UK banks are just not as attractive as others in the portfolio. Smaller UK banks tend to be biased towards the buy-to-let sector.

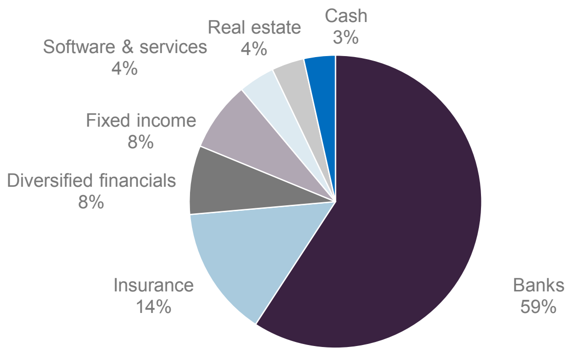
At the end of March 2019, there were 71 positions in PCFT's portfolio. Around 80% of the trust was invested in stocks with a market capitalisation in excess of $5bn, and 3.5% invested in small cap stocks with a market capitalisation less than $500m.

Figure 10: Asset allocation by country as at 31 March 2019



Source: Polar Capital Global Financials Trust

Figure 11: Asset allocation by sector as at 31 March 2019



Source: Polar Capital Global Financials Trust

The portfolio includes an element of fixed income, as a way of boosting the yield. Here the emphasis is on an assessment of credit quality (there is a credit analyst within the team). Changes to the regulatory environment, such as Basel III and BRRD, have created new opportunities as banks restructure their balance sheets.

Real estate investments offer income but are exposed to interest rate risk. John Yakas, through insight gained in managing Polar's Asian Opportunities Fund, tends to favour Asian REITs. Currently, these are cheaper than European and US stocks and are operating in an environment of higher economic growth. Relative to the benchmark, PCFT has a significant underweight exposure to real estate (4% versus 16.6% at the end of March 2019).

The trust has some asset management exposure (through Blackstone, the private equity company, and City of London Investment Group, a largely emerging markets and closed-end fund-focused investor). However, for the most part the managers are not attracted to the industry at the moment, given the competition from passive investments (which is putting pressure on fees) and ever-increasing regulation. There is no exposure to exchanges, which the managers consider to be momentum-driven stocks unsuited to their investment approach. Within the insurance market, the managers are encouraged by signs of firmer pricing in the property and casualty markets.

Top 10 holdings

Figure 12: Top 10 holdings as at 31 March 2019

	Country/Region	Subsector	% of gross assets 31/03/19	% of gross assets 30/09/18	% change
JPMorgan	United States	Banks	5.1	5.4	(0.3)
Bank of America	United States	Banks	3.7	4.1	(0.4)
Mastercard	United States	Speciality finance	3.1	3.2	(0.1)
Chubb	United States	Insurance	3.1	2.8	0.3
Arch Capital	Bermuda	Insurance	2.4	2.1	0.3
Sumitomo Mitsui Financial	Japan	Banks	2.3	2.5	(0.2)
Citigroup	United States	Banks	2.3	2.8	(0.5)
Marsh & McLennan	United States	Insurance	2.2	2.2	-
Toronto-Dominion	Canada	Banks	2.1	2.2	(0.1)
KBC Groep	Belgium	Banks/insurance	2.1	2.1	-
Total of top 10			**28.4**	**30.4**	

Source: Polar Capital Global Financials Trust, Bloomberg, Marten & Co

It is noticeable that the composition of the top 10 holdings has not changed much over the past six months, reflecting the managers' conviction in the portfolio. While four of PCFT's top 10 also feature prominently in the benchmark, the portfolio is clearly differentiated with notable underweight exposures to Berkshire Hathaway, HSBC and Royal Bank of Canada.

Atom Bank

Atom Bank is PCFT's only unquoted investment. The holding was valued at £3.2m at the end of September 2018. Atom Bank describes itself as the UK's first app-only bank. It offers fixed-term savings accounts, mortgages and business loans. It has raised £400m from investors, led by BBVA (which now owns almost 40%). At the end of March 2018, it had £1.4bn in retail deposits and had loaned £1.2bn. For the year to the end of March 2018, it lost £53m "in-line with its plans at the start of the year".

Performance

From launch until 31 March 2019, PCFT delivered an NAV total return of 65.1% or around 9.0% a year. In addition, the dividend has grown by an average of 7.0% a year.

Figure 13: PCFT NAV total return performance relative to benchmark[1]

Source: Morningstar, Polar Capital, Marten & Co. Note 1) PCFT's benchmark is the MSCI World Index Financials plus Real Estate Index (see note on page 3)

The scale on the graph in Figure 13 amplifies the volatility of PCFT's relative performance. In fact, PCFT's performance has matched the benchmark fairly closely since launch. Recent underperformance may reflect the portfolio's underweight exposure to REITs and exposure to US banks (both on the back of a halt to US rate increases); the exposure to India, which was affected by fears of a liquidity squeeze (hitting the non-bank financial subsector) and nervousness ahead of elections (although that has eased somewhat in recent weeks); and accusations levelled at Swedbank that it had facilitated money laundering (the managers topped up the holding subsequently).

Figure 14: Cumulative total return performance over periods ending 31 March 2019

Heading	1 month (%)	3 months (%)	6 months (%)	1 year (%)	3 years (%)	5 years (%)
PCFT price	(0.8)	4.4	(6.8)	(3.7)	48.9	36.4
PCFT NAV	(0.1)	6.6	(5.4)	(0.6)	38.8	49.5
MSCI World Financials plus Real Estate	0.6	7.2	(3.9)	2.7	44.7	55.7
MSCI AC World Index	3.4	9.6	(2.1)	10.5	49.5	74.9

Source: Morningstar, Polar Capital, Marten & Co

Figure 14 illustrates the extent of the financial sector's underperformance of the MSCI AC World Index. If the managers' theory that banks are oversold proves correct, PCFT's relative performance should improve.

Up-to-date information on PCFT is available on the QuotedData website

Note: no peer group information is included within this report. PCFT's listed peer group is eclectic and provides a poor comparison. PCFT's reports tend to compare the trust with the average of the Lipper Financial sector. For the year ended 30 November 2018, PCFT's NAV total return was 2.4% ahead, in absolute terms, of the average of the 56 open-ended funds in the Lipper sector, and 20.1% ahead since PCFT was launched.

Dividend

PCFT pays dividends twice a year

PCFT pays dividends semi-annually on its ordinary shares in February and August. All dividends are paid as interim dividends. The payments are not necessarily of equal amounts. The company does not pay a final dividend.

PCFT paid an interim dividend of 2.25p in August 2018. A second payment of 1.90p was declared for the 2018 financial year, to be paid in February 2019, giving a total of 4.15p for the year, representing a 6.4% year-on-year increase. PCFT has grown its annual dividend by an average of 7.6% over the four full financial years since its incorporation in 2013, handsomely achieving its core objective.

2018 revenue generation up nearly 20 percent

Being underweight in its exposure to US financials (particularly REITs) and overweight in European banks (relative to its benchmark in 2018) meant PCFT missed out on some extra revenue generation. That said, its managers believe that the investment case for European banks is now more compelling as they have moved back to financial crisis level valuations.

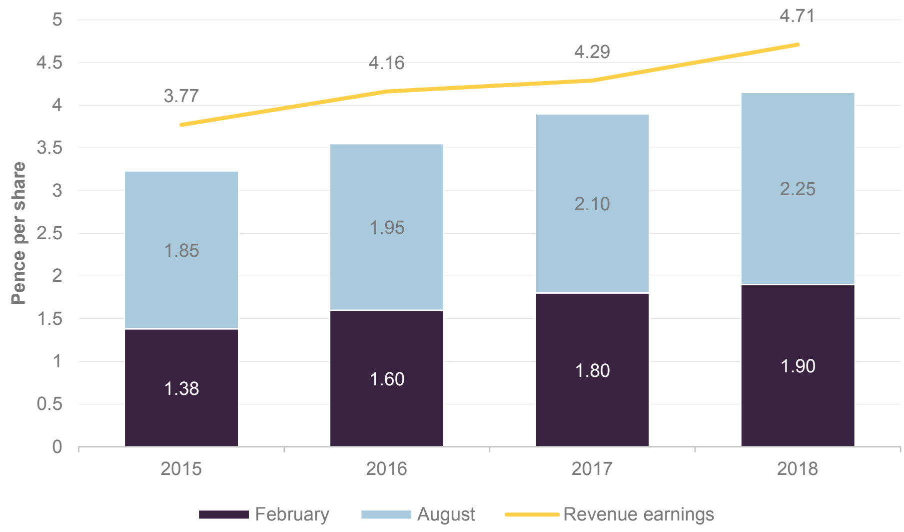
Uptrend of bank capital distributions remained intact

PCFT delivered a solid year of income generation with its revenue return increasing by 19.6% to 4.7p per share, as the underlying trend of banks continuing to return capital through dividends and share buybacks remained intact.

PCFT retains the capacity to smooth dividends.

As at November 30, 2018, PCFT had revenue reserves of 2.1p per share (after deducting the 1.90p interim dividend to be paid in February 2019). This is equivalent to half the total dividend for the 2018 year, suggesting that PCFT has some capacity to make up any revenue shortfall going forward (2017 equivalent figure was 38.5%).

Figure 15: PCFT four-year dividend and revenue earnings history



Source: Polar Capital Global Financials Trust

Discount

Figure 16: PCFT's discount over the five years to 31 March 2019

Source: Morningstar, Marten & Co

Over the year to the end of March 2019, PCFT's discount has moved within a range of 7.4% to 1.8% and has traded at an average of 4.7%. At 26 April 2019, the discount was 4.9%.

At times in its life, PCFT has bought back shares (4.25m in total) as a way of limiting the size and volatility of its discount. The managers observe that the discount has often reflected general sentiment towards the financial sector.

Fees and costs

Management fee is 0.85% of the lower of net assets and market capitalisation, and a performance fee is potentially payable upon PCFT's liquidation

PCFT pays a base management fee of 0.85% per annum on the lower of its market capitalisation and net asset value. Structuring the fee this way incentivises Polar Capital LLP to keep the discount narrow or eliminate it entirely. The base management fee is charged 80% to revenue and 20% to income.

Performance fee payable on PCFT's liquidation

Polar Capital LLP may also be entitled to a performance fee paid in cash. The fee is calculated and accrues daily but is only payable on the liquidation of PCFT. To date no performance fee has been accrued.

Any performance fee paid will be an amount equal to 10% of the excess return per share (on an NAV basis) over a performance fee hurdle.

The performance fee hurdle is 100p, increased or decreased by reference to the return on the benchmark index plus 1.25p a year (reduced proportionately for periods of less than one full year) over the period from the day following admission to the date on which it is decided to liquidate PCFT.

For the purposes of calculating the performance fee, with regard to the NAV:

- dividends will be reinvested on their pay date (i.e. the NAV total return will be used);
- the dilutive effect of the subscription share issue will be reversed out;
- any enhancement to the NAV from issuing shares at a premium will be reversed out; and
- any enhancement to the NAV from buying back shares at a discount will be reversed out.

The net effect should be that the adjusted NAV return reflects the actual performance generated by the managers after base management fees have been deducted.

Finally, any performance fee payable will be adjusted so that the payment of the performance fee does not leave shareholders with less than 100p per share.

Capital structure and life

Simple capital structure – 202,775,000 ordinary shares

PCFT has a simple capital structure with a single class of ordinary shares in issue (subscription shares that were issued at launch were all exercised on 31 July 2017) and trades on the Main Market of the London Stock Exchange. At 26 April 2019, there were 202,775,000 ordinary shares in issue.

Gearing

PCFT's mandate allows it to employ borrowing from time to time to enhance returns, subject to a maximum of 15% of net assets at the time of drawdown. PCFT has a £30m unsecured facility with ING Bank NV (a £15m one-year revolving facility and a £15m one-year term loan). The term loan has been drawn down in full and is due for repayment on 12 July 2019. The interest rate on this £15m loan is 1.775%.

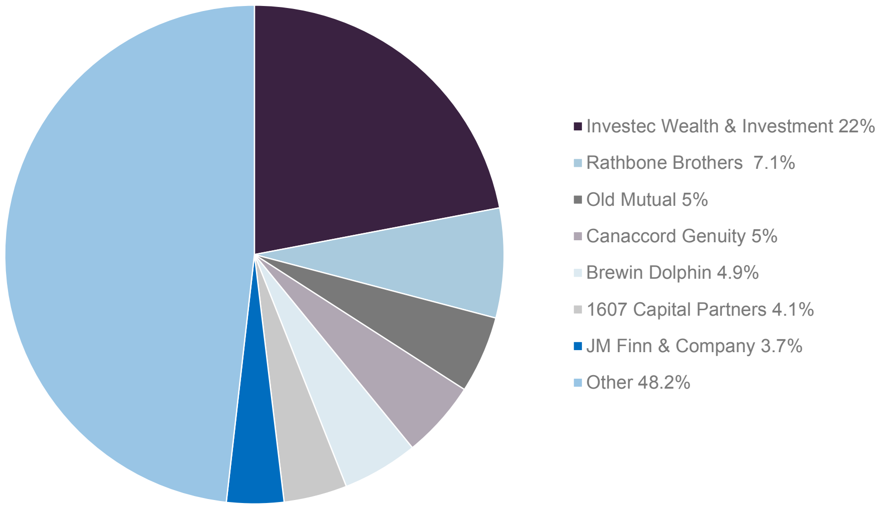
Liquidation resolution to be voted on in 2020

PCFT refers to itself as a fixed life company. Its articles of association require that, at the seventh AGM in 2020, the directors must put forward a resolution to place the company into liquidation. The voting on that resolution will be enhanced such that, provided any single vote is cast in favour, the resolution will be passed. The seventh AGM is expected to be held in April 2020, but in any event, no later than 31 May 2020.

This does not preclude the possibility that shareholders may decide to extend the life of the trust or take some other action that supersedes the liquidation resolution, which would likely include a follow-on vehicle as well as a cash offer at NAV less expenses.

Major shareholders

Figure 17: PCFT's shareholder base as at 30 November 2018



Source: Polar Capital Financials Trust

Management

The seven-strong financials team at Polar Capital LLC (four fund managers and three analysts) was managing approximately $2.3bn at the end of 2018. PCFT is one of five funds for which the team has direct responsibility. At 31 December 2018, each of those funds had outperformed its respective benchmark index since launch. The managers say that the trust sits at the conservative end of what the team does.

Two of the team focus on insurance companies. Nick Brind looks after the fixed-income element of portfolios. John Yakas specialises in emerging markets and Asian stocks. George Barrow covers Europe. There is considerable experience within the team, but they have quite diverse backgrounds.

Nick Brind

Nick joined Polar Capital following the acquisition of HIM Capital in September 2010, and is manager of the Polar Capital Income Opportunities Fund and co-manager of PCFT. He has 25 years' investment experience across a wide range of asset classes including UK equities, closed-end funds, fixed-income securities, global financials, private equity and derivatives. Prior to joining HIM Capital, Nick worked at New Star Asset Management. While there, he managed the New Star Financial Opportunities Fund, a high-income financials fund investing in the equity and fixed-income securities of European financials companies, which outperformed its benchmark index in all six years that Nick managed it. Previous to that, he worked at Exeter Asset Management and Capel-Cure Myers. At Exeter Asset Management, Nick managed the Exeter Capital Growth Fund from 1997 to 2003, which over this period was in the top decile of the IMA UK All Companies Sector. Nick has a Masters in Finance from London Business School.

John Yakas

John Yakas joined Polar Capital in September 2010 and is the manager of the Polar Capital Asian Opportunities Fund, Polar Capital Financial Opportunities Fund and co-manager of PCFT. John has 30 years' experience in the financial services industry. Previously, he worked for HSBC as a banker, based in Hong Kong, and was the head of Asian research at Fox-Pitt, Kelton. In 2003 he joined Hiscox Investment Management, which later became HIM Capital. John has won Lipper awards in the Equity Sector Banks and Other Financials Sector in 2010, 2011, 2012 and 2013 for the performance of the Asian Opportunities Fund. He has an MBA from London Business School and studied at the London School of Economics (BSc Econ).

George Barrow

George Barrow joined Polar Capital in September 2010 and works closely with John Yakas on the Polar Capital Financial Opportunities Fund and the Polar Capital Asian Opportunities Fund. With over 11 years' experience as an analyst, George has built up an in-depth knowledge of the banking sector, expanding his initial European focus to also cover Asia and emerging markets. Prior to joining Polar Capital, from 2008 he was an analyst at HIM Capital, where he completed his IMC. George has a Masters degree in International Studies from SOAS, where he graduated with merit.

Nabeel Siddiqui

Nabeel Siddiqui joined the Polar Capital Financials team as an analyst in August 2013 and works closely with John Yakas and Nick Brind, focusing on the global banking sector. Prior to this, he worked as an operations executive at Polar Capital. Nabeel began his career in August 2008 with Habib Bank, where he worked within a variety of functions. He has a Masters Degree in Money and Banking and has passed all three levels of the CFA.

Jack Deegan

Jack Deegan joined Polar Capital in October 2017 and works closely with Nick Brind on the Income Opportunities Fund. Prior to this, he worked at DBRS Ratings, covering the Swiss market as a lead analyst, as well as UK, Dutch, Japanese and Australian banks. Before DBRS, Jack worked in the Risk Management Division of the Bank of England for four years, assessing financial institutions with a view to determining access to the Bank's Sterling Monetary Framework (SMF) facilities, and internal counterparty trading limits.

Nick Martin

Nick joined Hiscox plc in 2001. He participated in the management buyout of Hiscox Investment Management in 2007 when the business was renamed HIM Capital Ltd, and moved to Polar following its acquisition. He has developed a broad knowledge of the insurance sector during this time and from working for chartered accountants, Mazars Neville Russell, where he specialised in audit and consultancy work for insurance companies and brokers. He is a qualified chartered accountant and obtained a first-class honours degree in Econometrics and Mathematical Economics at the London School of Economics.

Dominic Evans

Dominic Evans joined Polar Capital in October 2012 and is an investment analyst working with Alec Foster and Nick Martin on the Polar Capital Global Insurance Fund. He has 10 years insurance experience, having previously worked as part of KPMG's insurance segment, which he joined as a graduate trainee. At KPMG Dominic obtained broad experience working on a range of global insurance companies through roles within transaction services, audit and markets. Prior to KPMG he worked for a year in corporate finance, focusing on natural resource companies. Dominic is a chartered accountant and member of the ICAEW. He graduated with distinction in History with a first-class honours degree from the University of Newcastle upon Tyne.

Board

PCFT has a compact board of three non-executive directors

Robert Kyprianou, Joanne Elliott and Katrina Hart were all appointed to PCFT's board in June 2013, following its incorporation. There have been no changes to the board's composition since then.

All directors stand for re-election at three-yearly intervals. All three of PCFT's directors were re-elected by shareholders at the AGM in 2017. The directors meet at least four times a year, and the Audit committee meets at least twice a year.

Figure 18: Board member - length of service and shareholdings

Director	Position	Date of appointment	Length of service (years)	Annual director's fee (GBP)	Share-holding*	Years of fee invested*
Robert Kyprianou	Chairman	7 June 2013	5.9	37,000	67,456	2.5
Joanne Elliott	Director	7 June 2013	5.9	31,500	30,000	1.3
Katrina Hart	Director	7 June 2013	5.9	26,500	51,700	2.7
Average (service length, fee, shareholding, fees invested)			5.9	31,667	49,424	2.2

Source: Polar Capital Global Financials Trust, Marten & Co. Years of fee invested based on PCFT ordinary share price of 136.5p as at 25 April 2019.

Robert Kyprianou (non-executive chairman)

Robert was appointed to the board in June 2013 (as were Joanne and Katrina), bringing with him over 30 years of experience in asset management. He was previously CEO of Framlington until his retirement in September 2009. Robert has also served as global head of fixed income, and later deputy CEO and global head of securities at AXA Investment Managers SA; business head and global head of fixed income at ABN AMRO Asset Management Ltd and head of portfolio management at Salomon Brothers Asset Management Ltd. Robert also serves as the chairman of Eurobank Cyprus Ltd and is an independent director at Pimco Europe. He also chairs PCFT's nomination and remuneration committees.

Joanne Elliott ACA (non-executive director)

Joanne has a wealth of experience working with property-related businesses in particular. She is currently the CFO of the property team at Thames River Capital and is the long-standing finance manager of the TR Property Investment Trust (since 1995). She has also served as the director of property, finance and operations for the Europe region at Henderson Global Investors. Joanne, through her association with Thames River Capital, holds directorships at several private companies and is the chair of PCFT's audit committee.

Katrina Hart (non-executive director)

Katrina spent most of her career in investment banking, initially in corporate finance roles with ING Barings and Hawkpoint Partners. She then made the move to equity research at HSBC, where she covered financials. More recently, Katrina managed the financials research teams at Bridgewell Group and Canaccord Genuity, where she focused on fund and asset managers. Katrina chairs PCFT's management engagement committee and holds three additional non-executive directorships at Miton Group, Keystone Investment Trust and AEW UK REIT.

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