

## Manager's Comment

Following a maelstrom of falling prices in December, global stock markets recovered in January. BTEM participated to a large extent in the rally, with its NAV up +3.7% over the month despite the headwinds of a stronger sterling against most major currencies, and a slight widening of the portfolio discount by 40bps. Major contributors over the month included Cosan Ltd, EXOR, Pershing Square Holdings, Aker and Oakley Capital Investments, and the largest detractors were Fondul Proprietatea, Riverstone Energy, JPEL Private Equity and Kinnevik.

Pershing Square Holdings (PSH) substantially outperformed a strong US market (S&P 500 +8% in USD) with its NAV increasing by +18% over the month. Our long position in PSH added 68bps; our hedged position added a further 11bps. As a reminder, 45% of our total long exposure to PSH is hedged (i.e., 4.2% of BTEM NAV versus 5.3% for the outright long position) by shorting a *pro rata* amount of the underlying holdings, which provides us with the potential for equity-like returns from discount tightening from the currently very wide levels without taking additional equity market risk.

In a mixed US earnings reporting season, results released in January for PSH's portfolio companies exceeded expectations and confirmed their secular growth prospects, with positive share price reactions for all those reporting: ADP, Restaurant Brands International, United Technologies, and Starbucks. Chipotle reported shortly after month-end and provided more evidence of the turn-around spearheaded by its new CEO with same-store sales up +6% including a +2% boost from traffic.

An additional strong tailwind was provided by positions in Fannie Mae and Freddie Mac which, while only accounting for a relatively small part of the portfolio, more than doubled in price on the back of hopes for housing market reform in the US. As option-style positions with asymmetric return profiles and limited equity market correlation, we do not short these exposures in our hedged investment in PSH.

Despite the turn-around in PSH's performance, the discount remains unsustainably wide (c. 25%). It seems obvious to us that the company, having been fully invested up until the recent sale of their holding in Element Solutions (formerly Platform Specialty Products), should use the proceeds from the sale of this investment to fund a material buyback and/or tender offer.

*"In a mixed US earnings reporting season, results released in January for PSH's portfolio companies exceeded expectations and confirmed their secular growth prospects"*

Elsewhere in BTEM's portfolio, an excellent month for Cosan Ltd (CZZ) saw it add 86bps to BTEM's NAV despite a widening discount (a share price increase of +25% in USD terms lagged NAV growth, with the discount moving out from 25% to 33%). Cosan SA, the principal holding company beneath CZZ, announced that it would buy out the remaining 18% of Comgás, a Brazilian gas distributor, at an 18% premium to the pre-offer market price. While we applaud management buying more of what is already a successful investment, the acquisition – perhaps more importantly – indicates CZZ's seriousness in reducing the complexity of its holding structure which has led to an excessively wide look-through discount of 52%. We estimate the share price gain from simplifying the ownership chain into a single-holding structure should be in excess of +55% assuming a more normalised discount level.

EXOR contributed 81bps to the NAV in January, with its share price rising by +18%, driven by a combination of NAV growth (+15%) and discount tightening (from 34% to 32%). The share prices of EXOR's two largest listed holdings, Fiat Chrysler Automobiles (FCA) and Ferrari, increased by +18% and +25% respectively, providing a powerful boost to returns. FCA (34% of NAV) announced FY 2018 results just after the month end, posting EBIT of €7 billion (slightly below guidance) and a net cash position of €2 billion, which compares to €16 billion of industrial net debt when the late Sergio Marchionne took over as CEO in 2004. Despite the strong performance, and the value that management has consistently unveiled through spin-outs or asset divestitures, the shares continue to trade on a miserly 3.6x EV/EBIT. Given FCA's strong cash generation and the prudent capital allocation policies of FCA management and the Agnelli family, we think this too low.

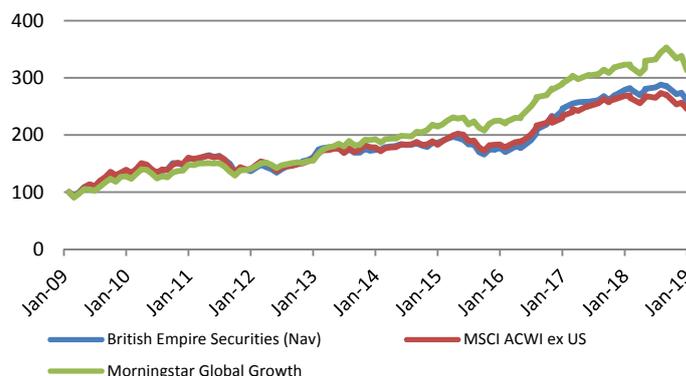
**Investment Objective:** To achieve capital growth through a focused portfolio of investments, particularly in companies whose share prices stand at a discount to estimated underlying net asset value.

## Performance Total Return

This investment management report relates to performance figures to 31 January 2019.

	Month	Financial Yr* to date	Calendar Yr to date
BTEM NAV <sup>1</sup>	3.7%	-7.2%	3.7%
MSCI ACWI Ex US <sup>3</sup>	4.2%	-5.5%	4.2%
MSCI ACWI Ex US Value <sup>1</sup>	4.1%	-4.7%	4.1%
MSCI ACWI <sup>1</sup>	4.5%	-6.5%	4.5%
Morningstar Global Growth <sup>1</sup>	4.6%	-8.3%	4.6%

Performance Total Return JAN 2009 - JAN 2019



## Top Ten Equity Holdings

Holding	%
Japan Special Situations***	14.7
Pershing Square Holdings #	9.5
EXOR	5.8
Jardine Strategic	5.4
Tetragon Financial	5.4
Pargesa	5.3
Fondul Proprietatea	5.1
Third Point Offshore	5.0
Riverstone Energy	4.9
Swire Pacific Ltd 'B'	4.9
<b>TOTAL</b>	<b>66.0</b>

\* 45% of this position (4.2% of NAV) is hedged, partially reducing BTEM's overall exposure to Pershing Square Holdings

Aker's share price rose strongly over the month (+28%), adding 44bps to returns. Even stronger NAV growth however, at +38%, saw the discount widen from 17% to 23%. Aker BP (71% of NAV) was the star performer in the portfolio, after making a series of positive announcements at its latest Capital Markets Day. To wit, Aker BP announced a 67% increase in the 2019 dividend – for a yield of 7% on the pre-announcement share price – and guided for a 45% reduction in operating expenditure per barrel by 2023. The prospects of higher dividends in the near future and a lower cost of production were received positively by investors, while a +15% recovery in the price of Brent crude oil – following sharp declines in the latter half of 2018 – provided an additional strong tailwind to performance.

Moving to look at the detractors from BTEM's portfolio, Fondul Proprietatea (FP) reduced returns by 56bps as investors further digested the implications of the Romanian government's Emergency Ordinance. The measures target banks, electricity and gas producers, and utilities in a bid to boost tax revenues and stabilise the State budget. The regulator's initial framework for putting the various measures into practice was more punitive than expected for Hidroelectrica (FP's largest holding at 41% of NAV), with the lowest-cost electricity producers being hit hardest in terms of both the proportion required to be sold on the regulated market and the regulated price at which it will be sold.

That said, the final outcome is still uncertain, and there are already signs of back-tracking with the proposals relating to electricity sales on the regulated market seemingly being pushed back by a year. Based purely on the proposals as they stand, FP's share price reaction seems over-done but we accept the market will assume the worst in the short-term in such an uncertain environment.

Riverstone Energy (RSE) was the second-largest detractor over the month, reducing NAV by 13bps as the share price fell -2%. RSE announced the sale of Meritage III (5% of NAV) at carrying value. We would be disappointed were the proceeds not used to buy back shares, which trade at a 26% discount at the time of writing.

Kinnevik was another detractor in January, reducing returns by 10bps. We (re)built a position in Kinnevik over the month following a widening of the discount out to 19-20%, having previously exited the stock in November 2017 on a discount of 12%. The negative impact from Kinnevik in January was a result of the -5% weakening of the SEK relative to GBP, as Kinnevik's share price actually rose +3%. The NAV performed even better, up +6% for the month, and driven to a large extent by a +21% gain in Zalando (28% of NAV), the German-listed online fashion retailer. Following a c. -50% fall in the share price of Zalando in 2018, we believe the company's valuation, at 1x EV/Sales, to be too low given the potential runway for growth. We are comfortable once again aligning our capital with that of the Stenbeck family, given their long-term mentality and track record of value creation through prudent investments and active stewardship.

Over the month, we reduced the positions in Investor AB and Pargesa following significant discount tightening. This highlights, we believe, the tactical approach we take to the portfolio alongside our long-term horizon: trimming positions to realise profits and recycle capital into attractive opportunities on wider discounts.

## Contributors / Detractors (in GBP)

Largest Contributors	1 month contribution bps	Percent of NAV
COSAN LTD-CLASS A SHARES	86	4.3
EXOR NV	81	5.8

Largest Detractors	1 month contribution bps	Percent of NAV
FONDUL PROPRIETATEA	-56	5.1
JPEL PRIVATE EQUITY LTD	-13	4.5

#AVI estimate. Previously, this breakdown was calculated by assigning one region to each portfolio company held by BTEM. From the 31-Dec-16 newsletter onwards, this is calculated using the estimated multi-regional exposure for each portfolio company. For listed underlying holdings, the country of listing is used; for unlisted underlying holdings, the exposure is typically assigned according to the country where a majority of sales are made.

## Statistics

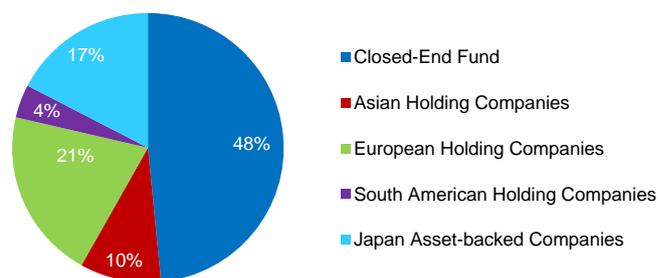
	Value	% 1 mo	% 1 yr	% 3 yr	% 5 yr
Price (£) TR <sup>2</sup>	701.0	5.3	-2.7	70.8	63.9
Net Asset Value TR <sup>1</sup>	763.3	3.7	-4.6	58.7	53.5
MSCI ACWI ex US TR <sup>3</sup>		4.2	-5.0	44.0	49.0
MSCI ACWI ex US Value <sup>1</sup>		4.1	-5.0	46.6	41.7
MSCI ACWI TR <sup>1</sup>		4.5	0.6	52.5	77.7
Morningstar Global Growth TR <sup>3</sup>		4.6	-0.7	58.8	82.1

Fiscal Yr Total Returns (%)	2018	2017	2016	2015	2014
Price <sup>1</sup>	12.0	18.7	34.3	-9.5	8.9
Net Asset Value <sup>1</sup>	10.0	18.8	31.0	-8.3	6.8
MSCI ACWI ex US (£)3	5.2	16.3	28.0	-5.6	5.1
MSCI ACWI ex US Value <sup>1</sup>	3.9	18.4	25.5	-9.8	5.7
MSCI ACWI <sup>1</sup>	13.5	15.5	31.3	0.4	11.8
Morningstar Global Growth <sup>3</sup>	16.7	21.3	26.9	3.7	8.7

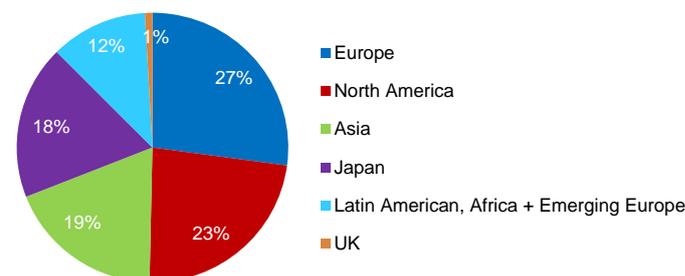
Capital Structure	
Ordinary Shares	129,526,165
Shares held in Treasury	18,621,612
8 1/8% Debenture stock 2023**	£15,000,000
4.184% Series A Sterling Unsecured Note 2036	£30,000,000
3.249% Series B Euro Unsecured Note 2036	€30,000,000
2.930% Unsecured Note 2037	€20,000,000
Gross Assets/Gearing	
Gross Assets	£946mil.
Debt par value	£88.3mil.
Actual Gearing (Debt less cash divided by net assets)	6.8%

- Source: Morningstar. All NAV figures are cum-fair values.
  - Source: Morningstar. Share price total return is on a mid-to-mid basis, with net income re-invested.
  - From 1<sup>st</sup> October 2013 the lead benchmark was changed to the MSCI ACWI ex US (£) Index. The investment management fee was changed to 0.7% of net assets and the performance related fee eliminated.
- \* British Empire Trust financial year commences on the 1<sup>st</sup> October. All figures published before the fiscal results announcement are AVI estimates and subject to change.
- \*\* Last audited figure updated annually
- \*\*\* A basket of 19 stocks: Fujitec Co, Kato Sangyo, Tachi-S, Nishimatsuya Chain, Pasona Group, Daiwa Industries, SK Kaken Co, Kanaden Corp, Toshiba Plant, Nissan Shatal, Teikoku Sen-I, Nakano, Mitsubishi Belting, Sekisui Jushi Corp, Nulfare, Toagosei, Konishi, Nippon Kanazai, Digital Garage.

## Sector Breakdown (% of invested assets)



## Risk Region Breakdown# (% of net assets)



## Further Information

Investment Manager – Joe Bauernfreund, AVI Ltd.  
+44 20 7659 4800 [info@assetvalueinvestors.com](mailto:info@assetvalueinvestors.com)

The share price can be found under 'INVESTMENT COMPANIES' in The Financial Times, The Times, The Daily Telegraph, The Scotsman and The Evening Standard.

Information may be found on the following websites.

[www.british-empire.co.uk](http://www.british-empire.co.uk) or  
[www.assetvalueinvestors.com](http://www.assetvalueinvestors.com)

## IMPORTANT INFORMATION

### Risk Factors you should consider before investing

Investment in the British Empire Trust plc (the "Trust") carries risks, which are more fully described in the Key Features Document. Listed below are some of the key risks:

Investors are reminded that past performance is not a guide to future performance and that their capital will be at risk and they may therefore lose some or all of the amounts that they choose to invest in the Trust.

The Trust utilises gearing techniques (leverage) which exaggerate market movements both down and up and which could mean sudden and large falls in market value. Movements in exchange rates can impact both the level of income received and the capital value of your investment. If the currency of your residence strengthens against the currency in which the underlying investments of the fund are made, the value of your investment will reduce and vice versa.

As with all stock exchange investments the value of investment trust shares will immediately fall by the difference between the buying and selling prices.

Where investments are made in emerging market, unquoted securities or smaller companies, their potential volatility may increase the risk to the value of, and the income from the investment.

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