Polar Capital
Global Financials Trust plc Update
December 2014

Performance of the Polar Capital Global Financials Trust plc ("PCFT") has not been good enough and we are disappointed and frustrated particularly with what we have delivered over the last couple of months.

Why has it been poor? From a relative standpoint we are very underweight the US (which along with Canada represents ~50% of the MSCI World Financials Index) and has performed very well over the last year. As an example, we do not own any US REITs (our exposure has been to a number of Singaporean REITs) which are up 13.7% since the end of September.

We have much larger positions in emerging markets, which has helped over the last year, but our exposure to European banks has been a significant drag. European banks have lagged US banks for example by 8.7% since the end of September (European banks down 3.2% vs US banks up 5.5%) and by around 17.0% over the last year.

Geographic exposure

Europe	29.9%
North America	27.1%
Asia Pac (ex-Japan)	13.5%
UK	9.5%
Fixed Income	9.0%
Eastern Europe	5.7%
Latin America	2.1%
Japan	1.7%
Cash	1.5%

Source: Polar Capital, 31 October 2014.

Our exposure to asset managers such as Azimut and Blackstone has also dragged back our performance. We had taken some profits on our holdings but they have fallen more than we would have expected considering that equity markets have been fairly buoyant (and both seeing good inflows). We have since added to our holding in Azimut.

Our performance over 12 months, to 17 November 2014, is ~7.5%[1], not as good as we would have hoped but better than the majority of our peers including Jupiter, Henderson, Aptus, JP Morgan, Fidelity and Blackrock and Scottish Widows but not as good as Axa. Three month performance lags almost all and is poor.

What have we done most recently?
Last month, we reduced our exposure to US banks at the margin to add to our European bank exposure. We believe that there is significantly more upside in European banks both as they remain extremely cheap and trade on a large discount (to the order of 20-25%) to US banks and (close to 50%) to the wider market.

Where do we go from here?
Apologies for probably sounding like a broken record, but we believe that some of the catalysts that could help see the sector perform better, and European banks in particular over the next few years outside macro being better than expected are:

1. Past performance is not indicative or a guarantee of future results. In GBP terms and net of fees. It should not be assumed that recommendations made in future will be profitable or will equal performance of the securities in this document. A list of all recommendations made within the immediately preceding 12 months is available upon request.

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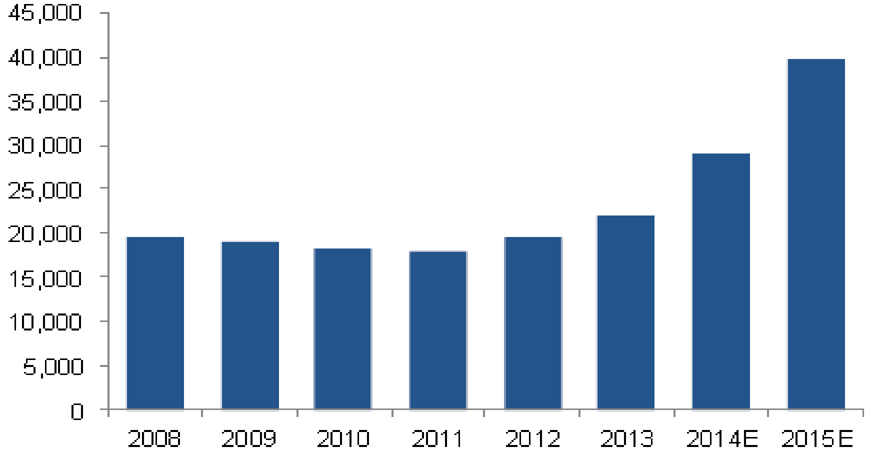
Significant increase in dividends - is key over the next couple of years especially as capital should not be seen as an issue for the majority of banks. Post the positive stress tests/AQR, the weakness in share prices of European banks could be argued as more to do with the weak European macro data/disappointment about QE in Europe than capital (two of our banks reiterated their intention to return capital post the results).

US Bank (Payout Ratio)[1]

	Dividends (%)				Repurchase (%)				Total Payout (%)			
	12A	13A	14E	15E	12A	13A	14E	15E	12A	13A	14E	15E
Large/Mid-Cap												
BAC	16%	4%	13%	20%	0%	31%	44%	47%	16%	36%	57%	67%
BBT	29%	42%	33%	31%	1%	0%	22%	38%	30%	42%	55%	69%
C	2%	1%	12%	18%	0%	7%	23%	43%	2%	8%	35%	61%
CMA	20%	22%	25%	25%	59%	51%	56%	70%	79%	73%	81%	95%
FITB	20%	22%	28%	28%	40%	45%	53%	52%	60%	67%	81%	80%
HBAN	23%	26%	31%	30%	25%	20%	37%	47%	47%	47%	68%	77%
JPM	23%	33%	27%	28%	8%	29%	22%	44%	31%	62%	49%	72%
KEY	20%	22%	22%	23%	30%	53%	62%	69%	5%	75%	84%	92%
MTB	37%	33%	38%	32%	0%	0%	0%	0%	37%	33%	38%	32%
PNC	29%	23%	27%	27%	8%	1%	28%	51%	37%	24%	55%	78%
RF	5%	13%	22%	28%	0%	32%	29%	45%	5%	45%	51%	73%
STI	6%	15%	23%	26%	0%	8%	31%	45%	6%	23%	54%	71%
USB	27%	29%	31%	29%	35%	44%	47%	53%	62%	73%	78%	83%
WFC	26%	30%	32%	32%	21%	23%	36%	36%	47%	53%	68%	68%
ZION	4%	8%	16%	19%	0%	0%	13%	43%	4%	8%	29%	62%
Average	19%	22%	25%	26%	15%	23%	34%	46%	34%	45%	59%	72%

Europe – Aggregate dividend distribution (€m)[2]



1. Source: Barclays (US large- cap & mid-cap banks report, 18 March 2014). **2. Source:** Bloomberg, SG Cross Asset Research/ Equity. It should not be assumed that recommendations made in the future will be profitable or will equal the performance of securities in this document. A list of all recommendations made within the immediately preceding 12 months is available upon request.

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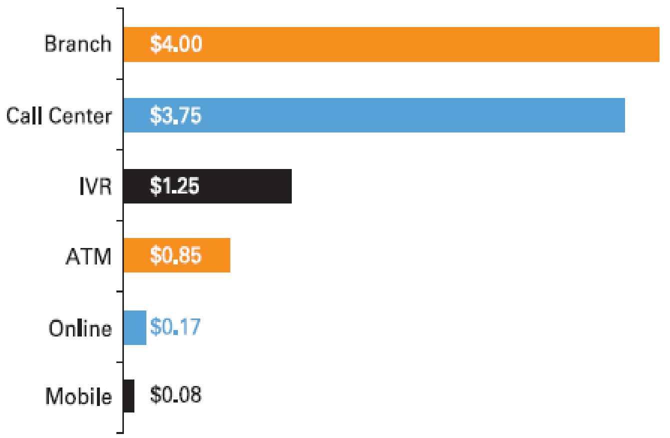
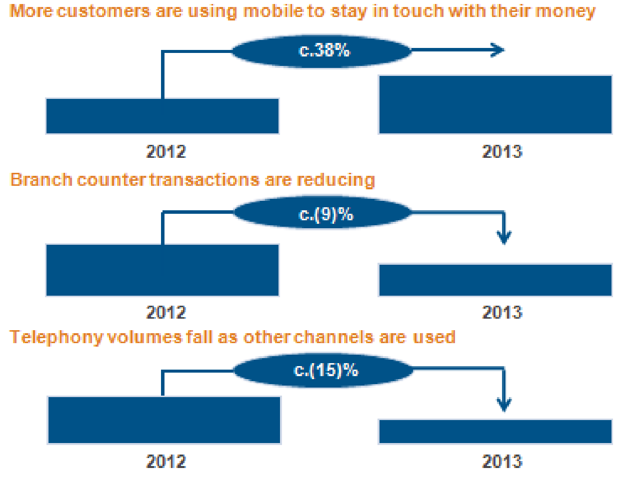
Potential for banks to cut costs - Swedbank announced in its latest results it would be cutting costs from 17.5bn krone to 16.0bn over the next 2 years. McKinsey have undertaken a study that banks could cut their costs by 7% points (driven by branch closures/smaller branches etc.) which would be a significant boost to profitability if pricing is unchanged.

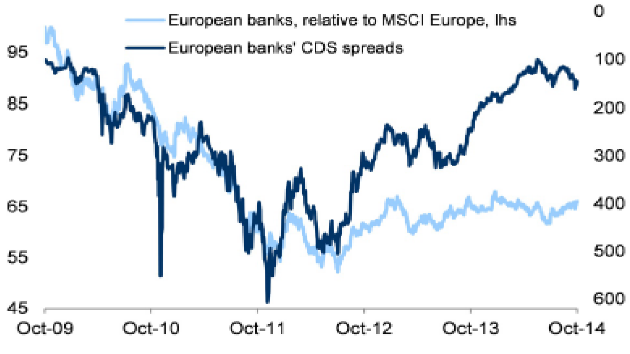
Per-transaction costs by banking channel[1]



Customer are using different channels[2]



Lower funding costs – European banks arguably have not priced in the improvement in funding markets and therefore, the lower cost of capital/funding. When European banks have traded previously at the current relative lows they do vs US banks they have then gone on to outperform in relative and absolute terms significantly.

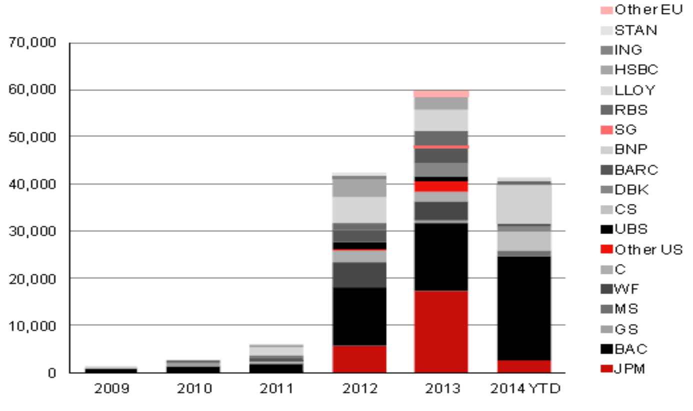


Source: Datastream, Morgan Stanley Research.

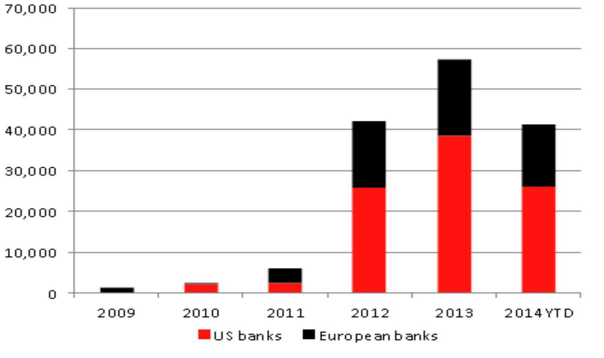
1. Source: TowerGroup, Fiserv/M-Com Data: Mobile transaction costs based on actual data from M-Com, the international mobile banking and payments solutions provider and Fiserv partner. **2. Source:** LBG analysis. It should not be assumed that recommendations made in the future will be profitable or will equal the performance of securities in this document. A list of all recommendations made within the immediately preceding 12 months is available upon request.

Fines to be largely resolved - over the next 18 months or so and as can be seen in the chart below just how outsized these have been (banks that we are own that are susceptible represent ~13% of PCFT). Not to say that certain banks will not suffer significantly higher fines (FX etc.) in the next 6 months.

Regulatory/legal settlements ($m)[1]



Settlements – Europe vs US ($m)[2]



PCFT is certainly not all about European banks but that is probably been the single biggest driver of recent poor performance and so hopefully if we are right a positive driver of performance going forward but in the short-term macro data will likely be a bigger driver of absolute and relative performance.

In this respect arguably the fall in oil prices should be seen as good news as well as the comments from Draghi about QE etc. TLTROs, ABS purchases will all be helpful but take time to have a positive effect. The Citigroup Economic Surprise Index for the Eurozone has turned sharply higher in the last few days (CESIEUR) is also a good sign.

Source: Bloomberg, 19 November 2014.

Source 1 & 2: Company data, Macquarie Research, June 2014. Both graphs include anticipated settlements in the BNP sanctions case ($8bn) and the BAC mortgage case ($12bn).

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