ROSSIE HOUSE
INVESTMENT MANAGEMENT

March 2024

There have been a number of personnel changes which we want to share with you under "Office Matters". A great deal has been going on behind the scenes over the last few years in what have often been difficult circumstances. Whilst the way we work has probably changed forever because of the pandemic, we believe (perhaps old fashionedly) that we must preserve the client-centric culture, investment expertise and governance standards we have always had – we hope and believe they are top quality.

An awful lot of "stuff" has taken place since our last Periodical. There are so many issues affecting stock and bond markets at present. Our second article explains our views despite the very unclear backdrop.

Selecting what to invest in is difficult. It is made harder by taxes that continually change. These inevitably have to be taken into account. Various changes in recent budgets, including a much reduced capital gains tax allowance which will affect many of our clients, prompted us to review these changes. We include an article to remind our clients in the UK what has happened.

The next subject, we know, will be controversial. We have included a guest article on crypto assets by Sonya Kim of Progrmd Capital. We are aware that some clients will think we have taken leave of our senses. On the other hand, many of our younger clients may ask why we haven't held crypto before – after all, the returns from some crypto assets have outperformed conventional assets by some margin. We believe it is important to keep an open mind when investing. Although it is unlikely we will invest ourselves at the current time we continue to watch closely from the sidelines. Sonya is a highly intelligent fund manager who left a secure job to start a fund. She has explained some of her thoughts to Rossie House and we thought it interesting to share her views. For the curious we commend her website: https://www.progrmdcapital.com/

No investor presentation nowadays is complete without a page or two or three – sometimes seemingly added as an afterthought – on ESG (Environment Social Governance). However, some investors have been thinking about this area for a very long time and always used it as a sensible and basic screening process for durable companies. We delve a little deeper into the way Rossie House thinks about this important subject.

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We are sadly saying farewell to our compliance guru, Tim Myles. He has worked his way to a well-earned retirement, whilst gently handing over his responsibilities to Gill Wright. Tim has given truly excellent and decisive compliance advice during his tenure. His integrity and proportionality fitted snuggly with the Rossie House culture. This sort of person is rare. As a parting gift he graciously shared some of his perspectives on life in the office and how it has changed over a long career.

Not far from the original Rossie House office there is a hill outside Dollar which was owned by Sir Robert Stewart. Forty years ago, it was covered in ponticum, full of muddy hollows and felt like bleak hillside. How different it is today. His daughter, Sara Stewart, took on a project of renovating what had been a Japanese Garden. We asked her to write about this remarkable story and we hope a visit for Rossie House clients will be possible soon.

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OFFICE MATTERS

There is quite a lot to report under this section. As mentioned, Tim Myles' retirement was helped enormously by Tim giving us plenty of warning and offering to do a smooth handover. We owe him a great deal and we said a fond farewell to him, though we will see him occasionally in his new role as the firm's Consumer Duty Champion.

We have been very fortunate indeed, through an old contact who headed up the compliance department at Baillie Gifford, to have been put in touch with Gill Wright. Gill wished to retire from full time compliance work at Baillie Gifford where she had been for some 20 years and do something part time. The fit was perfect. She is hugely experienced and has already made a great impact working closely with our external compliance consultant and Scott Baikie (our compliance partner). We are thrilled to have such an able person taking on this crucial role.

We are aware that all flocks need renewing and time moves on! We have therefore been on the lookout for an able, but younger, potential investment manager to gain experience and then start taking on clients. Through a recruitment agent we came across Megan Kay who had been working at BlackRock as well as having been a highly accomplished Scottish Dancer (including performing at the Tattoo). Megan was doing her ACCA* exams whilst there and will be continuing these with us. She will then start the normal investment exams, all the time learning about our favoured funds and the Rossie House ethos.

After some five years at Rossie House we also said (what we hope may be a temporary) goodbye to Adam Mackie. Adam came as a school leaver who deliberately chose not to go on to university. He passed his investment exams and assisted the partners with the administration of portfolios. However, having gone on an extended holiday to Australia after passing his exams, he decided he wanted to travel more. We understand that – though of course we told him this was deeply selfish!

In a similar spirit we have recruited a new school leaver, Olivia Homan. Again, she also declined a university place and will be helping our administrative side and possibly the investment managers in due course. She joined just before Christmas on her eighteenth birthday. This was promptly followed by our office party where she was able to celebrate her first ever legal drink. She is proving immensely helpful and will hopefully greet you at the door if you are visiting our Edinburgh office.

In short, we continue to recruit to maintain a good balance between youth and experience (a euphemism for getting old). Our aim is only to recruit people of a high standard and to improve our ability to deliver an excellent service to our clients. We continue to look out for new additions as the firm grows steadily.

**(Association of Chartered Certified Accountants)*

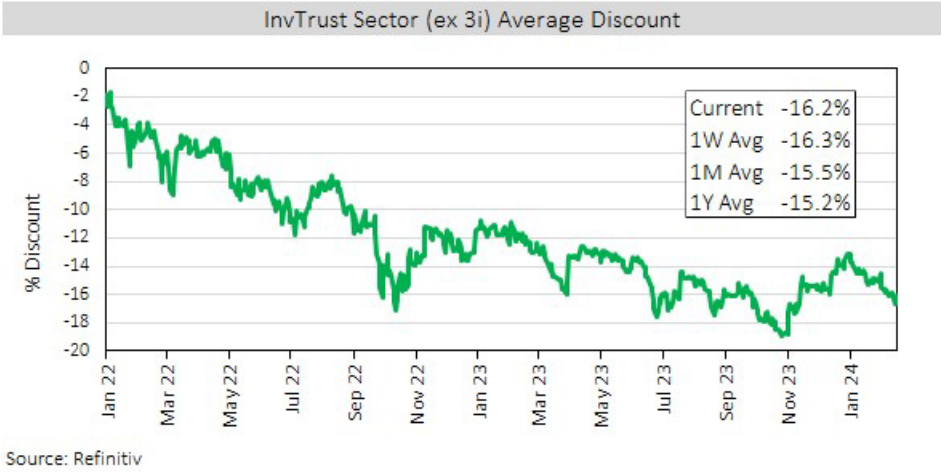
MARKET REVIEW

On Good Friday in 1930 BBC radio listeners tuned in at 8.45pm expecting to hear the news. Instead, the announcer said there was no news and piano music was played instead. Fund managers would give their right arm for such calm to return. Alas, we think that unlikely.

2023

Following a very difficult period for stock and bond markets in 2022, last year actually turned out to be reasonably satisfactory. That said, during the year there was significant volatility.

Interest rates were increased in response to clear inflationary pressures. The era of free money seemed over and investors were quickly reacquainted with a "cost of capital". For investment trusts exposed to "alternative assets" with leverage this proved devastating. Asset values came under pressure and, more painfully, share price discounts widened considerably. Mainstream trusts were similarly affected - an unhelpful but not permanent factor for Rossie House portfolios, which are heavily exposed to investment trusts.



In the spring of 2023, the solvency of US regional banks were questioned. This triggered the collapse of several banks including Silicon Valley Bank (SVB). The Federal Reserve reacted promptly arranging emergency loans and takeovers of failed institutions. Similarly in Europe, Credit Suisse had to be rescued by UBS. Stability was restored but not without worrying falls in equity markets.

Better news came in the form of Artificial Intelligence (AI) and the increasing prevalence of ChatGPT. This rekindled investors love affair with technology stocks, especially the US mega-cap companies. The top seven rose an average of 111% in 2023 and represented 28% of the S&P 500 index by the year end. These gains alone accounted for much of the rise in world stock market indices. Once again, the US has been the standout equity market performer. Other markets trailed, again not helpful to Rossie House portfolios which are underweight American shares.

As the year ended, lower inflation numbers brought forward market expectations of interest rate reductions. A strong Q4 rally followed in stock markets as well as gains in bond markets. The heart stopping start to the year proved to be just chest pains as the markets ended 2023 in good shape.

2024

Today, it is especially hard to decipher goings on. Some say it is always an uncertain world but, at the finance coalface, it seems to us that uncertainty has scaled new heights.

To start with, we continue to have a full-scale war on our doorstep in Europe. This is not something experienced for several generations. Inflation, although down from the double-digit rates of last year, remains high and many commentators think it will be hard to bring down to the 2% level because wages are increasing too much. War in Gaza has already caused skirmishes elsewhere in the Middle East and has the potential to escalate further. Then we have severe geo-political strains between China and the US. Climate change and net zero add further uncertainty. In the background, very high debt levels and poor demographics create more unknowns.

Market sentiment continues to be dominated by what will happen to inflation, interest rates and economic growth. The three are interlinked.

Inflation has started to fall in the US, less so in Europe and remains stubbornly high in the UK – especially core inflation. The consensus believes inflation will reduce, interest rates have peaked and that central banks in some countries will be able to start reducing rates in the first half of the year. This could be good for equity and bond markets.

The issue for us is whether, and how badly, economies are hit by recession. Evidence from the past suggests that "soft landings" after inflation of double-digit levels are very hard for Central Banks to engineer. It has been announced recently that the UK is just into a recession and extraordinary falls in nominal broad money supply suggest we may even flirt with deflation towards the end of the year without a change in policy.

Forecasts for growth in Europe and China look grim and the rest of Asia, including Japan, may struggle as a result. Only in the US is there some optimism of avoiding recession as huge fiscal stimulus continues. Even this may be too optimistic we think. As normal, most stock analysts' forecasts expect reasonable earnings growth in 2024. Should a recession cause earnings to be downgraded, equity markets are vulnerable, especially in America, where valuations are high.

A further concern we have is the very high levels of debt that have built up over the pandemic. This comes on top of those amassed after the financial crisis of 2008/09. There has been no proper recovery from that event, except perhaps in the US, and western governments have failed to reduce spending in line with tax revenues. Many countries, including the UK and US, are running significant budget deficits. So far, funding these deficits has proved possible.

We believe this may become more difficult in 2024. For nigh on fifteen years Quantitative Easing (QE) has largely funded government deficits, dampening the bond market's influence in setting the interest rate. As Central Banks tackle inflation, the support from QE has dried up and has been replaced by Quantitative Tightening (QT). Markets are now at the mercy of the so called "bond vigilantes".

Already the UK has debt to GDP approaching 100%. In Europe several countries have indebtedness at well over 100% and the US is at around 120% of GDP and increasing. Indeed, the equivalent of the Office for Budget Responsibility (OBR) in the US is forecasting debt to GDP to explode over the next half century. It is, of course, the level of debt servicing that matters and not the absolute level of debt. However, at interest rates of around 5% the mathematics of such high levels of debt become problematic. The status quo is not sustainable. If something is not financeable, markets will ultimately force a solution. Funding Government expenditure could easily become much more difficult, especially as there is a significant amount of short-term debt maturing this year in the US which will sap global demand for debt instruments. Bond investors may ask for higher yields to compensate – remember Liz Truss – even with disinflation.

Our long-held guess is that very high levels of debt are best cured by an extended period of modest inflation with short term interest rates held below the level of inflation. This is called 'financial repression'. Such an environment is hazardous for savers looking to maintain their real wealth. Investors should be aware that this could mean unexpected interventions by government. This would be a shock since almost all market practitioners have become accustomed to free markets, which have operated since the Thatcher reforms of the late 1970s. Recently, for example, the UK Chancellor has started to influence pension investment allocations towards private equity. Maybe, in the not-too-distant future, it will be UK government bonds.

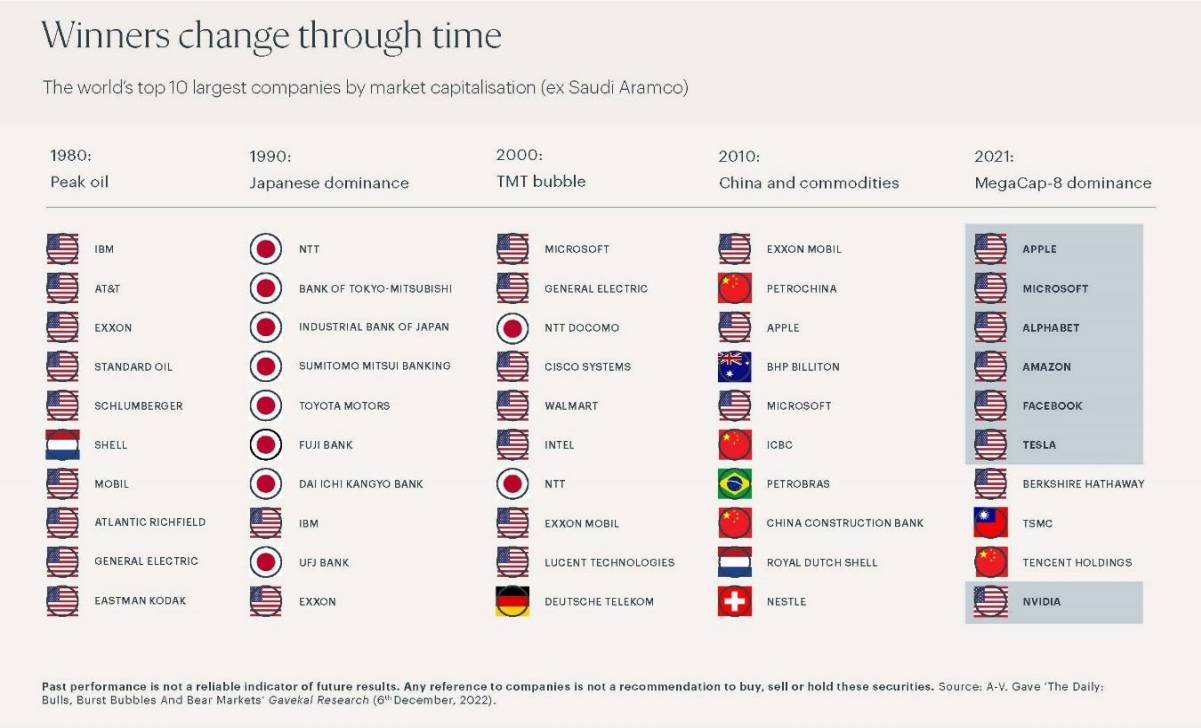
It is worth touching on liquidity. Everywhere it is low and has been declining as harsher regulatory capital requirements have reduced capital devoted to market making. In equities, and especially in the investment trust market, we have noticed a marked decline in liquidity. Additionally, wealth managers have bulked up and centralised their investment processes. Consequently, smaller investment trusts are ignored because the big firms can't invest sufficient capital into them. On the one hand this is a concern, but we view Rossie House's nimble size as an opportunity for us to deploy capital into these smaller trusts which can perform better.

Our Current Approach

One fund manager describes current markets as being "hyper financialised". We agree with this; fifteen years of free money resulting from QE has caused all sorts of distortions and below-the-surface risks. As Donald Rumsfield would have said, we feel there are many "known unknowns". Combine this with the sharp rise in interest rates in the past year and it is quite possible something will break.

We therefore feel it necessary to maintain our defensive exposure. Our capital preservation funds and index-linked bond exposure, especially following the rebasing of prices in the latter, should hopefully have an easier 2024.

With the muscle memory of investors heavily concentrated in a narrow list of stocks and hugely biased to the US market because returns have been so much better there than elsewhere, we feel this provides an opportunity to look further afield.



Markets such as the UK, Japan and Asia have been ignored and look to have attractive long term prospects. We prefer to emphasise these areas, especially through investment trusts, which now offer unusually wide discounts.

We also value the highly diversified nature of our portfolios. The world is an uncertain place - it feels never more so than now - and we remain humble in our ability to predict the future. We all know AI will change the world though we have no idea how. Our basic premise is that it is more of a threat than an opportunity. Fast innovation makes forecasting the future more difficult.

We would like to end on a more optimistic note. Whilst newspapers and the airwaves are full of despondent news, our meetings with fund managers and company management are often relatively upbeat. Cutting through the fog of big picture economic news – always wise given the forecasting difficulties – and concentrating on fund selection buoys our expectations for returns in the coming years.

BUDGET MUSINGS

We heard Chancellor Jeremy Hunt's second Spring budget on Wednesday 6th March. As is now common practice, many possible measures have been leaked and then tweaked. The headlines included 2p off National Insurance (a clever move fiscally as this is subject to an upper limit and – unfortunately – does not benefit pension income) and the new British ISA – an extra £5,000 of ISA allowance which will be introduced and which must go into UK listed companies. There were, as ever, quite a few other measures including reducing residential property Capital Gains Tax to 24% but restricting the tax advantages of holiday letting. The resident non-domicile tax regime is being got rid of, but with quite favourable transitional arrangements for those affected. All in all, it was a budget which offered some positives, but nothing very radical and almost certainly not enough to boost the government's electoral prospects. Inheritance Tax reform was very notable for its absence.

The real art of the conjuror Chancellor is in giving with one hand and taking away with the other. To understand how Jeremy Hunt has achieved this we need to look at his much more radical first Spring budget last year. The net effect of this week's budget was a modest giveaway of some £10 billion pounds, via the National Insurance reduction. This builds on the 2p lower rate National Insurance cut in the Autumn statement. However, this is offset by the fact that tax revenues from income taxes will have risen by nearly £100 billion over the course of this Parliament because of the freezing of personal allowances and thresholds. Inflation has effectively been harnessed by the government to drag up tax revenues. Stealthy.

One of the most significant issues for our clients, and a clear negative development, was the Spring 2023 budget's large reduction in the Capital Gains Tax allowance. The tax-free Capital Gains tax allowance was reduced from £12,300 to only £6,000 in the 2023 to 2024 tax year for individuals (and £3,000 for a trust). This is likely to affect many of our clients and bring them into the ambit of the 20% capital gains tax rate. Worse still, the number will reduce to £3,000 for an individual and £1,500 for a trust for 2024/25.

Many of our clients draw on a mixture of income and capital to fund regular monthly payments. Others may draw on capital to help children fund housing purchases or for myriad of other reasons. The £6,000 individual capital gains tax free allowance means many of you will end up paying capital gains tax on withdrawals, and this problem will compound when the allowance falls to £3,000 per individual in the 2024/25 tax year. There are few among us, however much we feel it our duty, who relish paying tax. The fact is that this measure is designed to raise more tax and it will, although it is arguably unfair in being a tax on inflation to a degree. The only consolation to be had for portfolio investors is that the Capital Gains Tax rate has remained 20%, so realising capital gains still remains much cheaper than receiving income for 40% and 45% taxpayers (or 41% and 47% in Scotland). The 2023 Spring budget did contain a plus for some clients. We all know that Chancellors like to reveal a 'rabbit' on Budget Day. This is usually a fairly uninspiring gimmick, the sort of rabbit you might see lurking on the roundabout at Edinburgh Airport. In March 2023 it was rather more exciting. There had been some speculation about the Pension Lifetime Allowance, the maximum pension value which you can accumulate without it being subject to punitive tax on amounts in excess

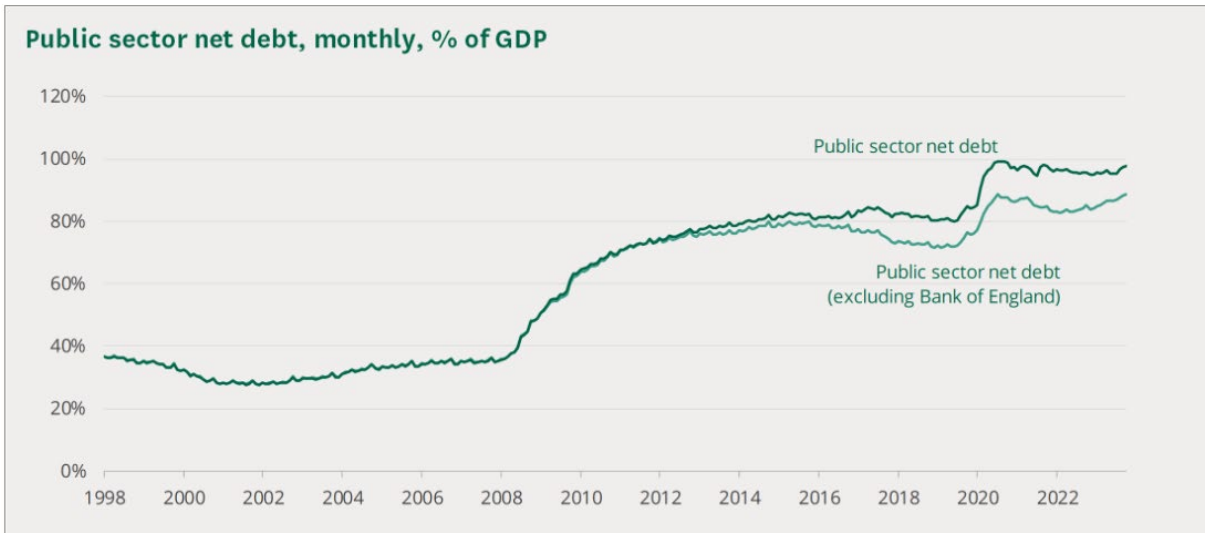
of this figure. This has long been the subject of much government fiddling and had most recently been reduced to £1m and then uprated to £1.07m in a nod to inflation. If you have a SIPP this figure is measured at the point you crystallise the benefits and is the value of the assets. In the case of Defined Benefit Schemes, the value is assessed as 20 times the income you will get on retirement.

Would the allowance go up and if so by how much? Might it even go down? Speculation had been rife, but nobody had predicted that …. the limit would be removed altogether. The amount you can contribute annually towards your pension has also increased to £60,000 from April 2023, although this remains subject to an earning cap, now £260,000 per annum, after which the contribution limit tapers down to a miserly minimum of £10,000. A SIPP retains its Inheritance Tax advantages in that you can pass it on to your children/ beneficiaries without an Inheritance Tax charge. They will be taxed on the money they withdraw as if it was income, when they remove it, but this is nonetheless a massive tax advantage. It is worth noting that those who are already accessing their pension can contribute £10,000 per year (increased from £4,000) to a pension although this must be from earned income. It is worth noting that the 'rabbit' was accompanied by another conjuring trick. The maximum 25% tax-free lump sum that can be taken from a SIPP on crystallisation is to be kept at £268,275 (25% of the 2022/23 Lifetime Allowance) and will be frozen going forward. Inflation is now going to erode its real value quite swiftly and hence increase the overall government tax take.

The area where we are most closely involved with clients in relation to pensions is with SIPPs. We are not financial advisors and cannot advise on specific tax matters as an accountant would, but we can make some observations which we hope have general relevance.

SIPPs remain an excellent and flexible way to invest for and fund a pension. Their inheritance planning advantages are very considerable, assuming you do not need all the contents of a SIPP to fund your retirement expenses. If you possess a well-funded SIPP, you are probably already aware of them. The difficulty for those of us currently in work and in a position to save is that, even making £60,000 contributions, it takes some time to build a SIPP large enough to generate a good retirement income. We would envisage those with SIPPs below the old Lifetime Allowance (£1.07m) will certainly wish to keep saving, with a view to retirement planning. What should you do once your SIPP reaches a value near the old Lifetime Allowance? In theory you should carry on investing for your own retirement and your children's future, all things being equal. There is after all no, limit on the size of SIPP you can own now, and the tax advantages are considerable. There is, however, the old truism that if things seem too good to be true then they probably are. A Labour victory at the next General Election looks likely. Labour have already said they will reverse the 'pension tax cut for the rich'. They have not been specific on how. Our expectation is that they will certainly do something and may reintroduce a Lifetime allowance, possibly at a level similar to the previous £1.07m plus a bit for inflation. One way of smothering the tracks of this not exceptionally aggressive measure, if adopted, would be to restrict the IHT advantages of SIPPs. This would provide 'soak the rich' headlines whilst not penalising, for example, middle ranking public sector workers with generous pensions excessively.

In conclusion, whilst politics is impossible to forecast, and makes fools of us so often it probably makes sense to consider the recent budget moves in light of the very strong possibility of a Labour government. A government of whichever hue and especially an avowedly socialist one would be unlikely to cut taxes given the state of our public finances, as shown by our Government Debt as % of GDP in the chart below. We would strongly suggest continuing to use the tax advantages of SIPPs, just not overly aggressively. We would also suggest, bearing in mind that the CGT rate could well become less favourable, factoring this into the timing of large withdrawals involving taxable gains. ISAs remain extremely attractive savings vehicles and should be used to the fullest extent possible. In all likelihood, the British ISA will be desirable to use, but we will need to see the fine detail behind the concept.



Source: Office for National Statistics

The comments and observations contained in this piece are of a general nature and limited in detail, as this is a complex subject. You should take advice from a qualified professional adviser on specific matters.

INTRODUCTION TO CRYPTO

Dear Rossie House Investors,

In 2022, I left my career as a value-focused equity portfolio manager to launch Progrmd Capital, Scotland's first actively managed fundamental crypto fund. Several friends and colleagues suggested that I might have, in fact, relinquished my sanity. However, I believe crypto remains a misunderstood asset class and will set out why here. I hope to explain why crypto assets have disruptive potential - meaning the poor popular reputation of crypto presents a contrarian opportunity for investors.

The 10,000 Feet View

Our societies and economies hinge on **communication** (the exchange of information) and **trade** (the exchange of value).

Communication has undergone a transformative evolution in the past century. Thanks to the Internet, we have transitioned from letters to real-time information transfer on our mobile devices. By contrast, progress in the exchange of value has badly lagged. Despite the ability to send instantaneous messages globally, transferring small payments worldwide frequently remains slow, expensive, and inefficient. This challenge persists due to the financial system's reliance on legacy infrastructure which is fragmented between both countries and corporations.

To illustrate, there are approximately 44,000 registered banks and credit unions in the world. Each maintains its own ledger and adheres to a specific technology standard. The largest network for cross-border transactions is SWIFT (Society for Worldwide Interbank Financial Telecommunication); but its network of 11,000 member institutions implies only 25% coverage. Additionally, SWIFT only represents a way for financial institutions to communicate - its member institutions must still make and settle cross-border payments. The great fragmentation in the existing system creates a huge hurdle to the dream of global value transfer as seamless as today's global communication.

The Solution: Blockchains, cryptocurrencies and tokens

Cryptocurrencies derive their nomenclature from "cryptography," the mathematical study of secure communication. Employing mathematical algorithms, cryptography encodes information, rendering it decipherable only through the possession of the correct key. This cryptographic foundation underpins blockchains, which are tamper-proof global records of value that securely record and update users' financial transactions.

The financial system today is a set of databases all owned and maintained by different companies, primarily banks. This means most transactions require at least two, sometimes meaningfully more, databases from different companies to communicate. This introduces friction. Blockchains do things differently, providing shared, global records of value. They emulate the open and public infrastructure of the Internet, and like the Internet, blockchains serve as a foundational platform upon which anyone can build applications. By being online,

one can send messages in real-time. By being "on-chain" (short for on the blockchain), one can send any value in real-time. In essence, blockchains constitute the "Internet of value."

Bitcoin was the first blockchain, but its limited functionality gave rise to newer chains with improved features, such as Ethereum and Solana. When engaging in on-chain transactions, users pay transaction fees to the blockchain network in the native currency of the chain – such as BTC, ETH and SOL. Hence, the value of these cryptocurrencies appreciates with more users and transactions within their respective blockchains.

What precisely can users achieve on-chain? Reflecting on the Internet's evolution provides a useful analogy for our understanding. In the early days of the web, users created email accounts and exchanged messages. Analogously, blockchain users can create digital wallet accounts and transfer cryptocurrencies. However, this merely scratches the surface. Just as the Internet saw the emergence of sophisticated applications and innovative business models, like car-sharing (Uber) or home-sharing (Airbnb), blockchains are poised to incubate novel applications that reshape the current landscape of finance and trade. The full implications of a truly global financial system that is accessible to anyone and can update in real-time are yet to be felt.

On-chain applications frequently incorporate bespoke tokens, which are digital assets that encapsulate distinct utility or economic value. Similar to creating a website, anyone can produce a token. While certain tokens possess the potential to generate substantial value for holders, others may lack intrinsic worth. We see the same in websites or dotcom stocks. Platforms like Amazon.com and Google.com generate substantial shareholder value, while countless other websites possess no value at all. Progrmd Capital pursues long-term investment in the cryptocurrencies of blockchains and the tokens of on-chain applications that display potential for exceptional growth and value-creation.

Examples of blockchain applications

The on-chain world is still nascent. It is witnessing an influx of adept and youthful developers transitioning from established tech companies to pioneer innovative applications. A common thread among these applications is the empowerment of users to conduct peer-to-peer value transfers. Mainstream success of such peer-to-peer solutions would eliminate the need for certain financial intermediaries, including banks and payment companies. Let us explore a couple of examples that have garnered significant traction.

- **Stablecoins:** These on-chain assets are pegged to fiat (government-backed) currencies, predominantly the USD. At the time of writing, there is $140 billion of Stablecoins in circulation. Tethered to the stability of the dollar, Stablecoins are particularly important for individuals in emerging economies with volatile local currencies. They offer a secure avenue for savings, as well as near-instantaneous transfers, often at a fraction of a cent. That may sound simple, but if you have ever used Western Union, you will appreciate how revolutionary that is. Stablecoins are well-positioned to disrupt the multi-trillion-dollar global payments and remittances market.

- **Decentralised Exchanges (DEX):** Crypto exchanges facilitate the trading of crypto assets. They exist in two types: Centralised Exchanges (CEXs) and Decentralised Exchanges (DEXs). CEXs, like Coinbase and the now defunct FTX, provide custodial services, meaning they hold customer funds. They may allow for the trading of crypto assets, but they function as traditional financial institutions. In contrast, DEXs, built atop blockchains, are fully automated software that operate non-custodially, allowing users to trade directly from their digital wallets.

  The largest DEX is Uniswap, built on Ethereum. Since its inception in 2018, Uniswap has facilitated $2.2 trillion in trading volumes. With its UNI token (currently valued at $4.7 billion), the token holders wield governance over the project's future direction and oversee its $2.3 billion community treasury on the Ethereum blockchain. Currently, Uniswap is not charging user fees, in favour of prioritising growth. However, the decision to monetise the software rests with the UNI token holders. Once the fees are implemented, the UNI token could capture the economic value generated by the Uniswap application.

- **Decentralised borrowing/lending:** Traditionally, banks serve as intermediaries in the borrowing and lending market, connecting capital providers (depositors) with capital seekers (borrowers). In a departure from this norm, decentralised lending applications such as Aave, facilitate fully automated, instantaneous peer-to-peer borrowing and lending. Users in pursuit of yield deposit their crypto into an asset pool on Aave. Borrowers can borrow from this pool, subject to pre-determined collateral requirements encoded in the Aave software.

  Since its launch in 2017, Aave has amassed over $10 billion in user deposits. The platform levies a percentage fee from the interest charged to borrowers. In 2023, Aave realised approximately $30 million in fees, which were distributed among AAVE token holders. With its present valuation of $1.3 billion, the AAVE token gives holders governance power over Aave's critical risk parameters.

- **Games:** Gaming is a vast $250 billion industry, consisting of over 3 billion gamers worldwide. Gamers spend on in-game items, but they never own them. The gaming companies can arbitrarily confiscate the items or restrict players' ability to resell them. In contrast, blockchain-based games unlock digital ownership. Through digital wallets, users acquiring in-game items can assert genuine ownership of these assets, also known as NFTs (Non-Fungible Tokens). NFTs offer the flexibility of transfer to other wallets or resale in a secondary market. With time, perhaps this will unlock virtual economic activity in the same way that secure property rights can do in the real world. For now, blockchain gaming is still very early. However, there are few promising providers of blockchain gaming infrastructure, of which Immutable X is one. The project has a pipeline of more than 150 high-quality games currently in development. The revenue model of Immutable X will be based on a 2% fee levied on all secondary trades of NFTs.

Conclusion

The crypto industry weathered high-profile setbacks in 2022, which intensified public scepticism toward the asset class. Contrary to expectations, however, the crypto market rebounded strongly in 2023. The Bloomberg Galaxy Crypto Index (BGCI) surged 140% over the year, led by Bitcoin's impressive 155% rally.

I believe the crypto advocates extolling the possibility of a faster, cheaper, and global financial system based on shared, global databases were directionally correct all along. We should remember that trillion-dollar Internet businesses rose from the ashes of the dotcom bust. The path will not be smooth. But continued experimentation in the space will yield wonderful and meaningful improvements to our daily lives – and along with that, lucrative investment opportunities.

A crucial part of this journey will be the evolving stance of governments and traditional financial institutions, once staunch adversaries of crypto. In January 2024, the U.S. SEC granted approval for Bitcoin ETF applications from major asset managers such as Blackrock, Fidelity and Franklin Templeton. Ethereum ETFs await the regulatory nod next. This milestone paves the way for broader access to crypto for the American public through regulated channels, which will inevitably lead more investors into the realm of cryptocurrencies.

Progrmd Capital envisions crypto market's potential to be in the order of $10 to $100 trillion valuation (the market is at $1.8 trillion at the time of writing). The rationale is straightforward: blockchains empower users to securely own and transfer value over the Internet, leapfrogging the inefficient and costly systems operated by centralised entities. This technological advancement holds the potential to redefine money, finance, and the very fabric of the web.

Source: 1. Fiatmarketcap.com; 2. Companiesmarketcap.com; 3. Companiesmarketcap.com

Sonya Kim
January 2024

ENVIRONMENTAL, SOCIAL & GOVERNANCE (ESG) REVISITED

Four years have slipped by since we last tackled this multifaceted topic. Before jumping back in, some background may help in understanding how we arrived with ESG.

The ESG concept is not a new one. Many pioneers of responsible investing had their roots in religion where they identified 'sin stocks' and excluded them from portfolios – so called 'negative screening'. During the sixties and seventies, the modern green movement took hold in America. Catalysed by Rachel Carson's *Silent Spring*[1], politicians such as JFK and Lyndon Johnson added environmental protection to their agendas. As the 1990s unfolded this evolved into Socially Responsible Investing (SRI) with the launch of "green" funds and their varying hues, dependent on how strictly the green/ethical criteria were applied. The new millennium and its affinity for acronyms heralded the mainstream birth of ESG through its liberal use of the term within the UN's 2004 report, *Who Cares Wins*[2]. Interestingly, this report was 'endorsed', and we suspect widely contributed to, by some of the West's largest banks including HSBC, Goldman Sachs and Credit Suisse (RIP) to name a few.

To tease out the complexities of the topic, an example is in order. Let's compare two of North America's top ten companies, Tesla and Exxon Mobil. Exxon is of course an oil and gas conglomerate and Tesla, the comparatively young electric car and battery business[3]. Intuitively, you might expect Exxon to fair worse under the scrutiny of the large ESG ratings companies, however, things are more nuanced –

[4]	***Exxon Mobil***	***Tesla***
S&P Global ESG Score (out of 100)	**36**	**28**
Environmental Score	44	60
Social Score	34	20
Governance Score	44	34
MSCI ESG Rating (scale from AAA as highest to CCC)	**'Average'**	**'Average'**
Environmental	BBB	A
Social	BBB	BB
Governance	BBB	BBB

You can see that according to S&P Global, Exxon overall screens more highly than Tesla due to better scores on its Social and Governance factors - Mr Musk's influence taking their toll. It is more finely balanced at MSCI where both companies are given the rather dull rating of "average"– so, no difference then! We are not sure we could select two more different businesses. You can always rely on the finance industry to take a tricky subject and make it incomprehensible.

This example is an extreme one. Nonetheless, it shines a light on the dangers of dogmatically following such ratings. Attempting to simplify what is a complex and multilayered subject is unlikely to end well.

There is also the question of whether the financial establishment has all the right answers. Recall a few paragraphs ago that banks (!) were heavily involved in endorsing the ESG movement. Might it be conceivable that to get world-changing environmental change, corporate governance misgivings are a necessity? Take Tesla again as an example. The company has repeatedly been criticised for its unconventional governance and autocratic leadership. But do we really think that a committee, however well diversified in ethnicity and gender, would have delivered the disruption that Elon Musk has achieved within the automobile industry?

Common sense and thoughtfulness are attributes high on our agenda for those seeking to navigate this thorny subject. Close to the top of the list, in our opinion, is David Gait and his colleagues at Stewart Investors. David manages the Pacific Assets Investment Trust, which our very own David (Nichol)[5] helped launch and manage in 1985. David Gait developed and has led Stewart Investors' sustainability philosophy for more than three decades; pre-dating the birth of the ESG acronym. His performance as lead manager of Pacific Assets since 2010 has been impressive, whether compared against ESG-focused investors or more conventional peers.

We also find traditional investors, or those who avoid preaching their ESG credentials, as the more interesting observers - perhaps because of their detachment from the subject matter. Simon Edelsten formerly of Mid Wynd International Investment Trust and James Anderson of Scottish Mortgage Trust have both written informatively on this subject[6].

To achieve success as an investor over long periods of time is devilishly hard. To layer additional complexity (i.e. ESG) onto an already hard task seems akin to self-sabotage. However, if you look closely at the very best investors and their investment processes – Rossie House's raison d'être – you begin to appreciate that many of these factors are (and have been) implicit in their analysis. Examples include: consideration of the integrity and track record of company management (Governance); analysing a business's accounting policies – it can be surprising how this seemingly innocuous variable can divine the culture of a firm with potential read-throughs to the treatment of employees (Social); interviewing customers, suppliers and past employees for clues as to the true durability of a company's results (environmental/ social/governance).

Many of the fund managers which we select on your behalf are interested in the long-term success of the companies they own. Not to gauge governance, social and environmental factors in their decision making would be considered by them as border-line negligent.

The fund managers we target may not historically have badged such factors explicitly under the ESG banner. Nevertheless, many are considered, and will continue to have a significant influence on their investment decisions. In trying to quantify soft factors, ESG ratings can lose or misinterpret critical information, or worse still, they can be gamed by the underlying companies themselves. For this reason, Rossie House will continue to seek, and back, thoughtful fund managers who we believe have the judgement and skill to successfully steward your savings for the long term.

[1] Silent Spring, published in 1962 was written by author and biologist, Rachel Carson. It provided a powerful argument against the use of pesticides that were wiping out populations of birds, insects and other animals.
[2] Later leading to the creation of the UN supported Principles for Responsible Investment (UN PRI).
[3] Tesla is also developing artificial intelligence which may lead to services/products including autonomous driving and humanoid robots (Optimus).
[4] ESG ratings data sourced from Google's Gemini.
[5] David Nichol was a founding partner of Rossie House Investment Management. He was also chairman of the Pacific Assets Investment Trust.
[6] See Simon's FT Money article – "So many grey areas in the green revolution" (Jan 2021) and James Anderson's "Purpose not Governance" (Sept 2021).

OFFICE CULTURE OVER HALF A CENTURY

Concluding a 46-year 'office' career, with the last five years as a compliance consultant to Rossie House, inevitably leads one to question how and why office life has changed over that time, and perhaps also question whether those changes have been for better or worse.

It is interesting to consider the different sorts of changes that have taken place. Some, of course, (and these are the most important) are down to personnel. I have been lucky. Invariably fellow staff have put their best foot forward, and whilst a few have been tricky, I can say I have met no one who I wouldn't be prepared to share a drink with at the end of the day (although not, of course, each working day!) Even when I started, liquid lunches were becoming a thing of the past).

Other changes are due to the astonishing rise in technology, of which more later. Also, the rise of 'Human Resource' (HR) - thankfully a phrase seldom if ever used at Rossie House - and any number of other changes due to social, regulatory and legislative changes, have all had an impact; some of it mind-numbing, but some rather charming.

For context, office life for me started in Glasgow with a legal apprenticeship after university. After 30 years I moved away from the law into a financial regulation consultancy. Most offices involved less than 25 people, and never more than 140 or so. I therefore can only speak to the office culture of a few small firms.

Starting in the 1970s

First thing up, it was essential to realise that everyone, other than office juniors, had to be addressed as 'Mr', 'Mrs' or 'Miss'. Christian or forenames were seldom used, and an individual changing from say 'Mr' to 'Miss' was not then a received concept. Male apprentices, only, were referred to by their surnames alone. 'Ms' only slowly crept in, I think in the 1990s. Occasionally there were discussions as to whether all, or only some, male clients should be addressed (in letters) as 'Esquire'.

Secondly, it was essential to learn which members of staff did, and did not, speak to each other. For instance, in my first office, the cashier and receptionist (who would both have been members of staff for over 30 years) wouldn't speak to each other and had to have messages passed between them by an apprentice. Occasionally the apprentice would be considered by say the cashier to be too partial, in which case the initial apprentice had to pass the message on to a second apprentice and so on.

Word processing typewriters were just beginning to come in, but with a surprising nod to modernity, were not permitted in my office due to a new concept; 'health and safety'. The thinking was that wires were there to be tripped over, and electricity was therefore confined to lighting. Interestingly, decrepit gas fires were permitted. They often threw both heat and fire (!) across rooms, singeing thighs. The only other obvious acknowledgement of client or staff welfare were the smelling salts kept in the boardroom.

Overwhelmingly, the office had a hierarchy. At the top stood the Senior Partner. In our case we had a former war hero, who had lost a leg in a Spitfire. He was genuinely admired and liked by us all. As an apprentice one of my first tasks was to try to establish his family claim to salmon fishings on the Clyde opposite Govan. He was extremely deaf, and occasionally threw books and accidentally even a telephone, at apprentices. All part of the fun, and never resented.

Partners generally stood apart from staff and in truth I never considered it could be any other way until perhaps the early 1990s. However, around that time I was told by a Canadian employee, from a very different working culture, that she found the partners' paternalistic attitudes almost feudal.

When I thought about it, I realised where she was coming from. The ownership of a business is always going to create a degree of difference between those who do and don't own it, but one of the great improvements which I do think has taken place in the last 25 years or so, is that there is now much more openness and discussion amongst all staff as to what is going on and how things can be improved.

By some sort of karma, whilst it was originally only the office juniors who were referred to by their first name, it was also the office juniors who (unwittingly) engineered the collapse of old honorifics. Juniors assumed that if they were called by their first name, they should respond to all, including senior partners, in like fashion. Although a shock at first, no one quite knew what was to be said or done, so that by the early 2010s only staff close to retirement continued with a 'Mr' or 'Mrs'.

To a large extent IT technology has overwhelmed old office cultures. An obvious example today is people working from home. Whilst an internal office phone could be used in the past, the constant use of internal emails now, with such emails often going out to several people within the office, has in my view led or assisted in the democratisation of office life. Language and ideas have to be found which work for the highest and the lowest in the organisation, and in general I think this has led to a simplification of thoughts and ideas within the office. On balance therefore, emails have in my view improved things.

I wish I could say the same for some of the HR social concepts which have crept in over the years. One knew, or ought to have known, that if one worked hard, always put the client first, and did right by one's colleagues and where possible (this being the legal profession) other legal firms, you shouldn't go too far wrong. Creating artificial concepts, regulations and jargon, which at best only affirm basic principles, and at worst cause resentment or positively get in the way, is in my view time wasted.

Fortunately, for the firms I have had the privilege to work for, and certainly at Rossie House, this is all a long way from the prevailing culture. Those basic principles have stuck, and what is more, they embed good humour, great fun and friendships; all a long way from some of the new social shibboleths, or indeed from my old cashier and receptionist, both of whom, nevertheless, I would like to salute for their kindness to a poor and green apprentice in 1977.

The Japanese Garden, Cowden, Clackmannanshire
'To create a garden is to believe in tomorrow'

The historic Japanese Garden at Cowden is located approximately 30 miles north west of Edinburgh. Established in 1908 by my ancestor, renowned adventurer Ella Christie, the garden has enjoyed a chequered past of design, growth and vandalism, culminating in a ten year restoration project. The final replacement structure was installed in late 2023 and the garden is now fully open to the public between Wednesday and Sunday in the winter and Tuesday to Sunday during BST.

Founder of the Garden: Isabella Christie

Isabella 'Ella' Christie of Cowden (1861-1949) was a formidable lady whose achievements include being the first European lady to meet the Dalai Lama and to travel from Samarkand to Khiva. Between 1904 and 1905 she travelled to India and then on to Kashmir, Tibet, Malaya and Borneo. Although at times travelling in hostile conditions, her trunks contained dresses for parties, (which included a banquet given by the Maharaja of Kashmir and dinner with Lord Kitchener then Commander in Chief, India). She camped in the snow at Chorbat Pass, sailed in a cargo ship full of pigs, travelled by pack horse and cart in the Kashmir wilderness and trekked by foot for sixty miles in the Desoi Mountains. Aged 50, while waiting for the train at Dollar station Ella was asked if she was travelling to Edinburgh, the short reply "No, Samarkand" perfectly encapsulates the fearless spinster who was fluent in four languages, including Finnish.

1908, Ella returned home from a trip to China, Korea and Japan inspired by her tours of gardens. As might be expected, Ella's approach to developing the garden was trailblazing. She chose a female designer – the gifted Taki Handa – to create the seven acre site in the grounds of Cowden. Of little significance to Western ideology, it is remarkably the only one of such size and scale to be officially accredited to a Japanese *woman*, and it remains a unique and utterly authentic bridge between Scottish and Japanese culture. In addition, the garden was maintained by Mr Shinsaburo Matsuo between 1925 and 1937. Poet, Andrew Lang and HM Queen Mary were just two of dozens of interesting friends of Ella's to enjoy Cowden.

1955

Restoration

The garden was sadly vandalised in the 1960's and continued to deteriorate over the next fifty years.

In 2014 my father, Bobby Stewart, and I commissioned a team of experts including the renowned Japanese landscape architect, Professor Masao Fukuhara to restore the garden. The Professor is perhaps best known for winning the Gold Medal at the Chelsea Flower Show as well as the restoration of the Japanese Gardens at Kew, London and Tatton Park, Cheshire.

As the restoration progressed, wider interest in the project grew and it became clear that the garden should be opened to the public regardless of the level of progress. In addition, the Professor's estimate was blown within a month…. (the project ended up costing 25 times the original quote). A charity (Japanese Garden at Cowden SCIO) was formed in

2014 to raise the additional funds necessary to upgrade over 2,000 metres of paths, access, car parks and re-create structures suitable for visitors with 21st century expectations. In 2020 the Secretary of State for Scotland recommended the garden be awarded significant funds via the City Region Deal, which enabled the trustees to complete the restoration.

The Japanese Garden

The perimeter path round the large pond offers a complete view of the garden. As you emerge from the conifer trees the dramatic 'Borrowed Landscape' of the Ochil Hills in the distance sets the scene. The path meanders through the Welcome Gate, (sited on the same spot as the original), to the Garden Pavilion. This beautiful new building, designed by Ella's great, great nephew, Hugh Shaw Stewart, architect at Foster + Partners, is loosely based on the Katsura Palace in Kyoto and has replaced Ella's original Boat House.

The Dry Garden (Karesansui), at the west end of the pond is a traditional feature in many Japanese gardens. The raked gravel, carefully maintained by our volunteers, symbolises ripples in water. Behind Karesansui, the stone path leads to the remains of the Inari Shrine. The trustees have been advised to leave the shrine unrestored as Taki Handa, the original landscape designer, was a Catholic and it is likely that it was a later addition.

Over the small bridge and up to the foothills of 'Mount Fuji' where white flowering Azaleas have been planted to represent snow in late May. Further east lies the thatched sunshade. Ella was clearly an optimist as this was installed to protect her face from the sun… On the lower path, the memorial to Ella's head gardener, Matsuo, overlooks the pond. Finally, the North Gate signifies the boundary between the Japanese Garden and the more native landscape beyond.

Footnote

Annual visitor numbers now average 40,000 possibly due to generous TV coverage and a very loyal fan base. A new attraction, The Houldsworth Walk, designed by Julian Romney and renowned landscape designer, Michael Innes, in memory of trustee David Houldsworth was planted in February 2024. Our next mission is to raise £3m to construct a Japanese designed visitor centre to replace the temporary facilities and offer a residential bursary and lecture room.

The trustees hope that Cowden will once again inspire generations of historians, poets, artists, gardeners, and students of all ages and abilities.

Sara Stewart
www.cowdengarden.com

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As the issuer, Rossie House Investment Management LLP has approved the contents of this publication.

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