Why *Motley Fool Pro UK?*

Confidential Service Memorandum

Summer 2018

The Motley Fool
Pro

"Your quest for high-probability returns begins here – join us as we take stock-tipping to the next level..."

Nathan Parmelee, Pro UK Portfolio Manager

Why Go *Pro*? *Part 1*

Even when markets are up, extreme winners and losers are normal

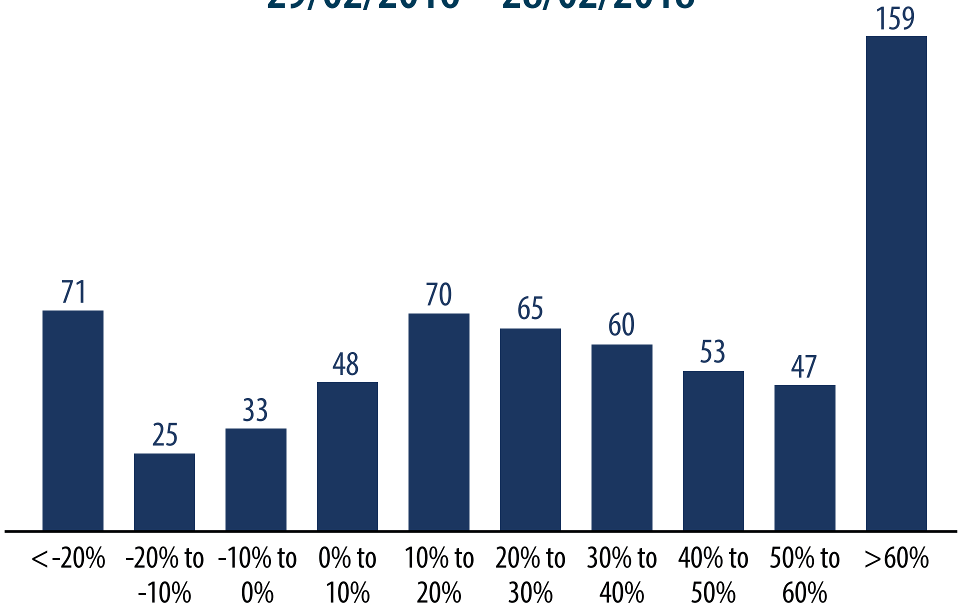
Conventional wisdom is that when the market is up, stocks go up.

However, that's not exactly the case as returns aren't normally distributed and there tends to be a big difference between successful shares and failed shares. These returns show up as "fat tails" when plotted on a chart as we've done below.

In the past two years the FTSE All-Share index is up 29%, and not surprisingly nearly half (58%) of the shares underperformed the market. But more than 3 in 10 (37%) shares trailed the index by more than 20%, while another 2 in 10 (26%) beat the index by 20% or more![1]

This is not uncommon. A study in the USA from 1983-2006 showed that 19% of shares significantly underperformed the market, while 25% of shares beat the market by an abnormally wide margin.[2]

Returns of Individual Shares vs. FTSE All-Share Total Return Index 29/02/2016 – 28/02/2018



1. Source: S&P Global Market Intelligence. Based on the performance of the FTSE All-Share Index from 29/02/2016 to 28/02/2018.
2. Source: http://longboard-am.com/assets/Capitalism-Distribution-1.15.14.pdf

Why Go *Pro*? *Part 2*

We begin by trying to eliminate potential losers

» Companies can be losing investments because of poor management, too much competition, secular changes in their industry, or simply because they're overvalued and already fully appreciated by investors. We look to avoid companies that possess any of these warning signs.

Greed and fear cost investors billions each year

» Investors are hit with a barrage of headlines sending them on an emotional roller coaster that can lead to buying high and selling low. We look to use swings in market sentiment to our advantage and have the experience to know when it can make sense to ride out a period of bad news and also when to sell companies entering long-term, secular declines.

Expect more of the same

» Economic dislocation, tax uncertainty, and unexpected political events make for a fragile market prone to extreme swings — one we think is ideally suited to a value-oriented, business-focused strategy like the one at *Pro*.

The *'Pro'* Difference *Part 1*

- When you join us as a ***Pro*** member, not only can you expect to receive a stream of our highest-conviction stock recommendations, but we'll also show you how each fits into **one of our four strategies** and how to put them to work together as part of a live, real-money portfolio.
- That's just one of the unique aspects of the ***"Pro approach"*** — portfolio manager Nathan Parmelee and his team are tasked with investing (and growing) **£100,000 of The Motley Fool's own money**[1] to showcase how to actively manage a portfolio of shares.
- Every stock recommendation that Nathan and his team make is purchased in cold, hard cash and then tracked on the *Pro* portfolio scorecard — not only does this demonstrate our conviction in the companies we're recommending to you, but it can also **help you determine how big a position** to take yourself.
- And whether you decide to mirror all of our trades exactly, or to just cherry-pick from our recommendations à la carte — *Pro*'s real-money portfolio provides a constant reference point that's there to help you make smart investment choices.

Pro's 4 Investing Strategies

Special Situations: < 20%

Covert Value: 15-20%

Income: 25-35%

Growth: 35-45%

1. The Pro real-money portfolio started with a £50,000 cash deposit on 27 October 2009. Additional monthly sums of £4,200 were added to the portfolio from 1 April 2014 to 1 February 2015, followed by £3,800 on 1 March 2015, which increased the total cash injected into the portfolio since inception to £100,000.

The *'Pro'* Difference *Part 2*

- What also sets *Pro* apart from traditional newsletter services, is that ***our analysts' buy, hold and sell alerts are issued to members in 'real-time'***. That means there's no fixed monthly schedule. Put simply, when the best new investment opportunities present themselves, or if the investment thesis of a company we've recommended has started to unravel, you'll hear from us right away about the action you need to take.

- It all adds up to a service with an investment approach that's not constrained by conventions such as company size, market capitalisation, geographical borders, or business style.

- Instead, *Pro*'s analysts strive to apply a ***'business-focused' investing philosophy*** — with the goal of buying shares in great companies at prices that they believe do not reflect their greatness. Our analysts must always be able to explain the reasons for the pricing discrepancy they're seeing when recommending a company to members as a BUY.

- *Motley Fool Pro UK* aims to beat the FTSE All-Share index by at least 3% on a rolling three year basis and will on occasion reduce positions to lock in gains and to defend against risk.

Meet Your *Pro* Team *Part 1*

Nathan Parmelee – Portfolio Manager

- You might already know Nathan from our *Motley Fool Share Advisor* newsletter service, where he's been a co-advisor since February 2012.
- Nathan has written for The Motley Fool since 2004, working on a number of our paid subscription services in both the US and the UK.
- Before joining the Fool, Nathan worked for a well-regarded industrial and financial services company (including a 3 year posting to Japan), where he learned the intricacies of corporate acquisitions.
- Nathan's investing interests include consumer goods, agriculture, industrial manufacturing and special situations.

Nathan Parmelee.

Meet Your *Pro* Team *Part 2*

Ian Pierce, Co-Advisor

» Ian is a long-time Fool from the States relocated to London, and has been writing articles for The Motley Fool.

» He's focused on AIM-listed small caps and growth shares of all stripes. His favourite companies are those that are looking to shake up stodgy industries with fresh ideas.

» After living and working in China for several years, he also seeks companies looking to take advantage of the long-term potential to be found selling to a 100-million strong Chinese middle class.

Ian Pierce.

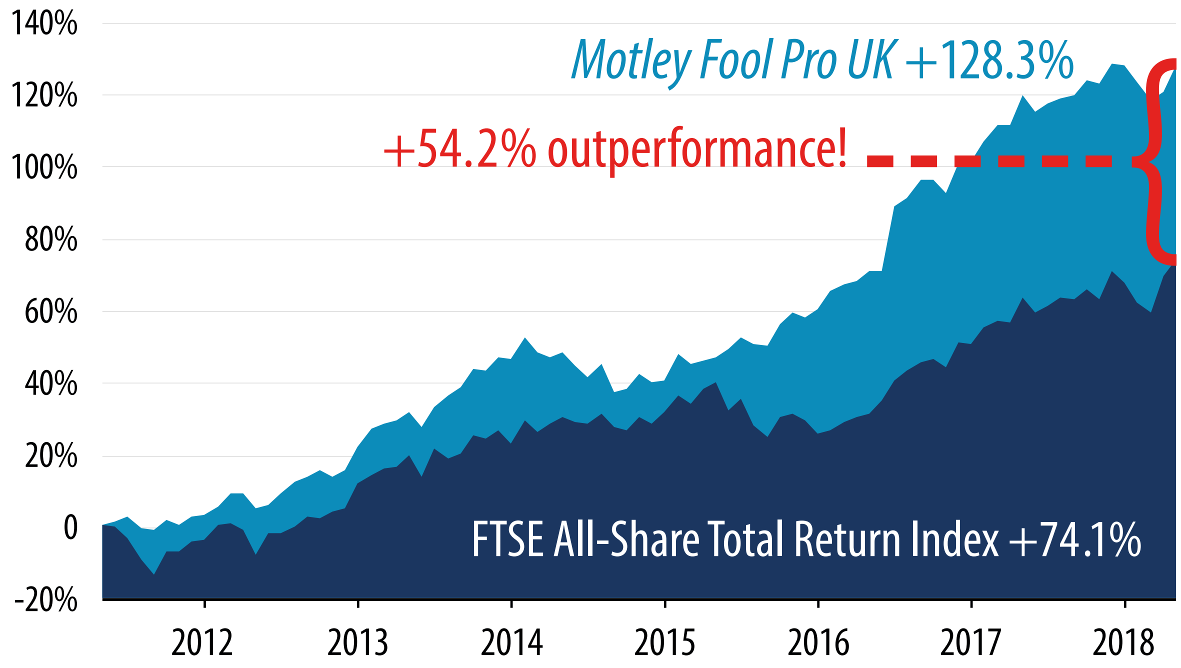
Pro's Performance

Our returns since Nathan became *Pro's* portfolio manager in June 2011

» Thanks to an expanded investment team and the benefit of volatile markets since June 2011, *Pro* has been able to unearth plenty of opportunities for members over the past several years.

» This has resulted in a solid market outperformance of **54.2%**[1] under Nathan's stewardship.

» Since inception *Motley Fool Pro UK* portfolio has delivered an overall return of **134.9%**.[2]



1. Since Nathan Parmelee and team took over the Motley Fool Pro UK portfolio at market close on 31/05/2011, the service has delivered an overall return of 128.3%. The FTSE All-Share Total Return index has delivered an overall return of 74.1%. Returns are calculated using a time-weighted rate of return (TTWR) methodology that includes dividends reinvested and trading costs. Returns are measured from 31/05/2011 to 31/05/2018. Transaction costs from Interactive Investor. 2. Since inception, the Motley Fool Pro UK portfolio has delivered an overall return of 134.9%. The FTSE All-Share Total Return index has delivered an overall return of 115.1%. Returns are calculated using a time-weighted rate of return (TTWR) methodology that includes dividends reinvested and trading costs. Returns are measured from 26/10/2009 to 31/05/2018. Transaction costs from Interactive Investor.

The Real-Money Portfolio

As of 31 May 2018, the *Pro UK* real-money portfolio consisted of £192,398 of The Motley Fool's own equity capital

» We currently have plenty of cash to invest in new opportunities, and the portfolio holdings paid out £2,407 in dividends last year, adding to our purchasing firepower.

» We're partners in this – if you make money, we make money.

You maintain complete control of your own investment…

» Either replicate the *Motley Fool Pro UK* portfolio, trade for trade, in your own share dealing account…

» Or cherry-pick from our recommendations à la carte to suit your needs — it's your call.

No gimmicks, you retain complete control of your money.

» All trades are communicated via real-time trade alerts, complete with full rationale and detailed portfolio guidance, at least 24 HOURS in advance of the *Pro* portfolio trade.

» All critical elements of the trade, including assessment of risk versus reward… exactly when to get in and when to get out… and precisely how to size your positions.

Pro's Investment Process

Initial Research and Estimate of Intrinsic Value

Team Idea Review and Approval

Assess Risks & Opportunities

Fundamental Research

Identify Potential Catalysts

Refine Estimate of Intrinsic Value

Determine Initial Position Size

Articulate Thesis and Sell Strategy

Add to Portfolio

Monitor & Update

Sell or Add based on Valuation and Risk/Reward

Research

Analysis

Portfolio Management

How We Invest *Part 1*

Identifying High-Quality Businesses

Our goal is simple: capture high-probability returns. We aim to achieve this goal by investing in great businesses at good prices, uncovering exciting turnaround stories and zooming in on temporary "mispricings."

We favour companies with…

» Recurring revenues and consistent cash flows protected by durable competitive advantages over competitors.

» Strong balance sheets (we avoid companies with excessive debt loads).

» Shareholder-friendly management. We like to see management incentives aligned with shareholders and a track record of returning value to shareholders.

We focus on valuation

» We target investments with a potential annual return of at least 15%.

» Larger positions will typically feature potential gains of 25% or more.

» We continually assess the intrinsic value of our shares and are committed to reducing or eliminating positions when they exceed our valuation estimates.

We're rigorous about trying to protect our capital — and yours — from permanent loss

» We reduce our exposure when markets are euphoric and add positions when pessimistic.

» We resize positions when our outlook on risk/reward changes.

How We Invest *Part 2*

To meet our goal of capturing high probability returns we use our valuation criteria and qualitative factors to allocate capital to four strategies we believe have the best chance of providing market-beating returns.

Strategy	Target Allocation	Description
Growth	35% – 45%	Fast-growing businesses we believe can continue growing for many more years, because of secular shifts in their industry and/or strong competitive advantages.
Income	25% – 35%	We seek to balance our investment in growth share strategy with high-quality companies that have proven management, predictable cash flow and pay a significant level of dividends.
Covert Value	15% – 25%	High quality businesses with under-appreciated competitive advantages or unique assets. Often our thesis is that these qualities can lead to higher margins and greater profitability.
Special Situations	< 20%	We focus on spin-offs, rights offerings, and turnarounds with a change in management and/or a significant change in strategy. We look for companies where a new, focused strategy can lead to a step change in profitability.

How We Invest *Part 3*

Making the initial purchase and risk management

BBA Aviation (LSE:BBA) is a leading provider of refuelling, cargo handling, and other airport services.

Please note: This example is shown as an illustration of our investment process and is not representative of gains and losses made across the whole *Pro* portfolio. Not all the shares *Motley Fool Pro UK* owns have made gains like this, and of course some have even fallen in value. Pricing data from *Interactive Investor* and *Yahoo! Finance*. The returns given on this page for BBA Aviation and the FTSE All-Share index include trading costs but no dividends.

Initial Purchase

BBA Aviation was originally purchased at 269p on **6 October 2015** as a special situation.

Our participation in BBA's rights offering to acquire a competitor (Landmark Aviation) allowed us to purchase additional shares for 133p on **27 October 2015** for an initial target allocation of 1.5% of the *Pro* portfolio. After participating in the rights issue, our initial average cost per share was 195p.

The combination of a market-leading position, highly cash generative business model, and an attractive-looking valuation convinced us that it was time to take a modest investment in the company, with an eye to adding more if we should get the opportunity.

Topping Up

Shares of BBA declined in the first few months we owned them, because of concerns over the Landmark Aviation acquisition and market volatility ahead of the Brexit vote.

20 January 2016 — With the share price 15% lower than our initial purchase price, we issued a second Buy Alert to bring our allocation up to 2.5% of the *Pro* portfolio.

16 September 2016 — We issued a third Buy Alert, following what looked to us to be a strong set of results, which showed BBA's acquisition of Landmark was proceeding as expected. This took our position up to 4.0% of the *Pro* portfolio. While the shares were above our initial purchase price, we believed the market still wasn't recognising the full value of the enlarged business.

Current Strategy

We still hold BBA shares in the *Pro* portfolio. In the past year, the company has sold some of its non-core business units, which has helped to reduce its debt levels and brought greater focus to its high-margin private jet services business.

While in our view the shares are still reasonably priced, they no longer offer the compelling value we saw in late 2015 and 2016.

We see the potential for continued improvement in the business and a higher share price, but with a relatively large position (4.6% of the portfolio) we're content with our position size right now.

Our unrealised gain on our entire BBA position was 70.1% as at 31 May 2018, compared to a gain of 21.7% in the FTSE All-Share index since 6 Oct 2015.

How We Invest *Part 4*

Exiting our position and locking in gains

Smith & Nephew (LSE: SN) is a leading global manufacturer of medical devices.

Please note: This example is shown as an illustration of our investment process and is not representative of gains and losses made across the whole *Pro* portfolio. Not all the shares *Motley Fool Pro UK* owns have made gains like this, and of course some have even fallen in value. Pricing data from *Interactive Investor* and *Yahoo! Finance*. The returns given on this page for Smith & Nephew and the FTSE All-Share index include trading costs but no dividends.

Due Diligence

In **February 2011**, Smith & Nephew's CEO of four years retired to be replaced by Olivier Bohuon.

While Bohuon had a strong career in the pharmaceutical industry before coming to Smith & Nephew, there is some uncertainty about his transition to the role, and his stated plan for acquisitions.

We've been looking at Smith & Nephew as a way to play the global trends of a rapidly ageing population, rising wealth, and the pursuit of a higher quality of life in old age, so are interested to see how Bohuon steps into his new role.

20 September 2011 — We publish a short report adding Smith & Nephew to our Watch List with the shares at 594p.

Decision To Buy

22 November 2011 — We publish our buy report, and recommend buying shares of Smith & Nephew at prices below 575p.

24 November 2011 — *Pro* purchases shares at 556p. Smith & Nephew's third-quarter results had disappointed the market earlier that month, due to weakening operating margins.

While maintaining profitability is important to Smith & Nephew's success — and our investment thesis — management had reasonable explanations for the short-term weakness in margins.

We were happy to take advantage of the market negativity to start a position in Smith & Nephew, while keeping an eye on margins and management's acquisition strategy.

Decision To Sell

15 April 2013 — *Pro* sells part of its stake at 747p. With the shares up 33.3%, a full 10% above our valuation estimate, and representing 5% of the portfolio, we decided to sell two-fifths of our position to manage risk within the portfolio. As a well-positioned medical device firm, we were comfortable with an ongoing 3% position.

25 September 2014 — We announce that *Pro* is to sell its remaining stake. We estimate the shares are pricing in optimistic growth assumptions and a bid premium. We're sceptical an offer will come, and exit our remaining position for an 83.2% gain. The overall gain of 62.5% on the initial purchase compares to a 31.2% gain from the FTSE All-Share over the same period.

How We Aim To Make You Money At *Pro*

Make asymmetric bets

» We believe in allocating more capital to our best ideas.

Think like owners (even if we end up being renters)

» We take a long-term outlook, even if our actions turn out to be short-term.

Appraise value skillfully, not just quantitatively

» We approach each position in a manner that fits the unique circumstances of its particular business.

Take risk seriously

» We will strive to avoid losses. It's the first step to successful long-term, portfolio growth.

Maintain portfolio boundaries & manage risk

» We maintain sizing limits for individual positions and sectors, and manage our overall exposure to different countries.

Be rationally opportunistic

» We aim to be wholly rational in how we size up the market's opportunities and risks, then act decisively.

Embrace intelligent speculation

» We won't shy away from rare, fleeting opportunities that don't allow for comprehensive research. However, in these instances, our initial position will always be conservatively sized.

Playing Attack & Defence

***Motley Fool Pro UK* is…**

» The Motley Fool UK's most exclusive and advanced membership service.

» Professional management, focusing on investments we believe offer high probabilities of favourable outcomes while avoiding lower-quality investments that offer a poor probability of market-beating returns.

» Targeted market-beating returns while defending against significant business and valuation risk — giving you the peace of mind to stay the course even in troubled markets.

And Most Importantly...

» *Motley Fool Pro UK* might be right for you if you share our long-term perspective on trying to compound capital in a risk-averse manner.

» Our goal is neither to maximise profit on every trade, nor to be excessively conservative.

» We're aiming to capture high-probability returns that allow us to beat the FTSE All-Share index on an annual basis while defending against risk.

How our Motley Fool services compare – by feature:	*Share Advisor*	*Hidden Winners*	*Pro UK*
Carefully researched share recommendations	**2 per month**	**1 per month**	**Any time** (no fixed schedule)
Ongoing coverage for all recommendations with clear 'buy-hold-and-sell' advice	●	●	●
Guidance on how much of each recommendation to buy	-	-	●
All recommendations backed by a real-money portfolio of the Motley Fool's own cash	-	-	●
Lively comment section with access to Motley Fool analysts	●	●	●
Regular international investment opportunities	-	-	●
Turnarounds, special situation and small-cap investments	-	Only small-cap investments	●
Highlights investment ideas from other Motley Fool global services	-	-	●

Doors open on Tuesday!

If you think you have what it takes to invest like a Pro and you're ready to commit to a long-term investment strategy...

Watch your inbox on **Tuesday, 12 June** *for your priority invitation to join us!*

Risk Warning

- The prices of all shares, and the income from them, can fall as well as rise.
- You run an extra risk of losing money when you buy shares in certain smaller companies including "penny shares".
- There is a big difference between the buying price and the selling price of these shares. If you have to sell them immediately, you may get back much less than you paid for them. The price may change quickly, it may go down as well as up and you may not get back the full amount invested. It may be difficult to sell or realize the investment.
- You should not speculate using money you cannot afford to lose, or rely on dividend income for non-discretionary living expenses.
- Some securities may be traded in currencies other than sterling, and may also pay dividends in other currencies. Changes in rates of exchange may have an adverse effect on the value of these investments in sterling terms. You should also consult your stockbroker about any additional dealing or administrative charges.
- We have taken all reasonable care to ensure that all statements of fact and opinion contained in this publication are fair and accurate in all material aspects.
- Investors should seek appropriate professional advice from their stockbroker or other adviser if any points are unclear.
- This newsletter gives general advice only, and the investments mentioned may not necessarily be suitable for any individual.

Motley Fool Pro UK is a Motley Fool product:

For all queries please email *Pro*@Fool.co.uk. Alternatively you can call us on **0207 462 4300** between 9am-5pm, Mon-Fri (except for public holidays).

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