Article from investment web-site: www.MichaelWalters.com
Posted on 8/10/2004

Junior Oils

When Jim Slater has an idea, it is generally worth paying attention. Now firmly a senior citizen, he has lost none of his interest in the stock market, and deserves his almost legendary status as a judge of share opportunities.

The rise and fall of Slater Walker, and Jim's own switch from golden boy to minus millionaire, then back to riches again has been well chronicled. Through it all, I have developed a deep respect for his abilities as a stock picker and investment guru.

Jim has a knack of making money in the market. That is why the instant I heard whispers that he was backing a new unit trust to invest in small oil stocks, I started making calls. And that is why I am writing an uncharacteristically enthusiastic note about the launch of the Junior Oils Trust which is about to hit the streets.

Slater had the idea for it six months ago, and it has taken that long to set it up. Like so many of the best ideas, it appears obvious in retrospect. The idea is to provide a vehicle to chase long term capital growth by investing in small and medium sized UK and overseas oil and gas quoted companies which own or are searching for oil deposits.

The oil price will rise and fall, but it seems clear that the era of what we know as cheap oil is over. Slater likes a quotation from Dick Cheney, the US vice-president when he was chairman of US oil giant Halliburton; "there will be an average of 2% annual growth in global oil demand over the years ahead, along with, conservatively, a 3% natural decline in production from existing reserves. That means by 2010 we will need in the order of an additional 50m barrels a day. This is equivalent to more than six Saudi Arabia's."

Exploration is not locating sufficient new sources. Alternatives are still costly and coming in slowly. As a trend, oil prices will move higher over the longer term.

Then we come to the universal stock market rules, and Slater's favourite remark "Elephants don't gallop". Shares in small companies rise further and faster than shares in big companies. Cairn Energy, a stock Slater bought himself, leapt four-fold on announcing extra reserves in India. Such news would barely move shares in BP.

The oil majors are likely to wish to add to their reserves. They will do it partly by buying smaller companies which have found new fields – and new fields are often much bigger than initial announcements indicate. Over the past five years, on average, junior oils have more than tripled, vastly outperforming the general market.

There are risks in backing the small boys, which is why it makes sense to have a spread of investments. The fund plans to steer clear of the Middle East, with the risk of armed conflict.

The new fund will be managed by Angelos Damaskos, an investment banker who has worked with the European Bank for Reconstruction and Development for over ten years, and who is Slater's son-in-law. In the past five years, he directed a portfolio of equity investments in unquoted private companies with an investment cost value of over $150m. Most of the companies were linked to the oil industry.

Damaskos will be the manager, but Slater will be in the background, putting up ideas and making introductions. The Slater family is putting £1m into the trust, which will be administered by part of Capita Group.

Minimum investment is £1,000, and the initial price is 100p. Prices will appear daily in the FT, and the fund will be eligible for inclusion in an ISA. The initial charge is 5.25%, with an annual charge of 1.75%.

Trading will begin to October 11. More details should be available on 0845 601 7637, by email on info@junioroils.com, or on the website www.junioroils.com

It is tempting to look at this, and chuckle sceptically. It is generally proved sensible to stay well clear whenever the investment industry launches a new fund linked to the hot stock market areas of the day. Remember the internet investment funds? Hard to trace any chunks of the wreckage these days.

Oil prices are at an all-time peak, small oil stocks are among the hottest movers, and speculative money is heavy into oil futures. Is this precisely the wrong point at which to be putting money into a junior oils trust?

There is obviously a danger. Yet the general market malaise has been such that there is no massive flood of money into such stocks. Many have risen sharply, but gains have often been supported by exploration success. Precisely because so many mistrust the oil price, the full impact of the gains has not yet been transmitted to share prices.

Analysts have been reluctant to factor in oil at much above $30 a barrel when looking at share values. Yet we are over $50 a barrel now. Some shares might be unduly inflated at the moment, and there is a widespread notion that the whole fashion will fade in the face of a lower oil price before too long.

It seems unlikely, though, that the price of oil is going to settle below $35 a barrel. Even that might be unduly conservative. The explosion in the Chinese economy looks certain to keep demand screwed up way beyond historic levels. And it would be a brave soul who could predict peace in the Middle East.

It is possible that this trust might be the first of a flurry.. Be clear, I do not know of any. But the idea has obvious attractions and can only help stimulate general interest in such stocks. Some will respond quite sharply to any surge in share buying.

Above all, Slater has his family money aboard. He hates losing money. And he knows who to value companies, and is familiar with the tricks of presentation and how prices can be manipulated by promoters. He is not managing the trust, but it is hard to imagine a more useful market operator to have sitting on your shoulder, watching the game.

Naturally there are no guarantees. But anyone who fancies the oil story and who wants a relatively low-risk vehicle to play the game ought to consider this trust. It is not one I intend to follow regularly, but I will keep half an eye on it. Good luck.

Ends