Fund Management Monthly Commentary

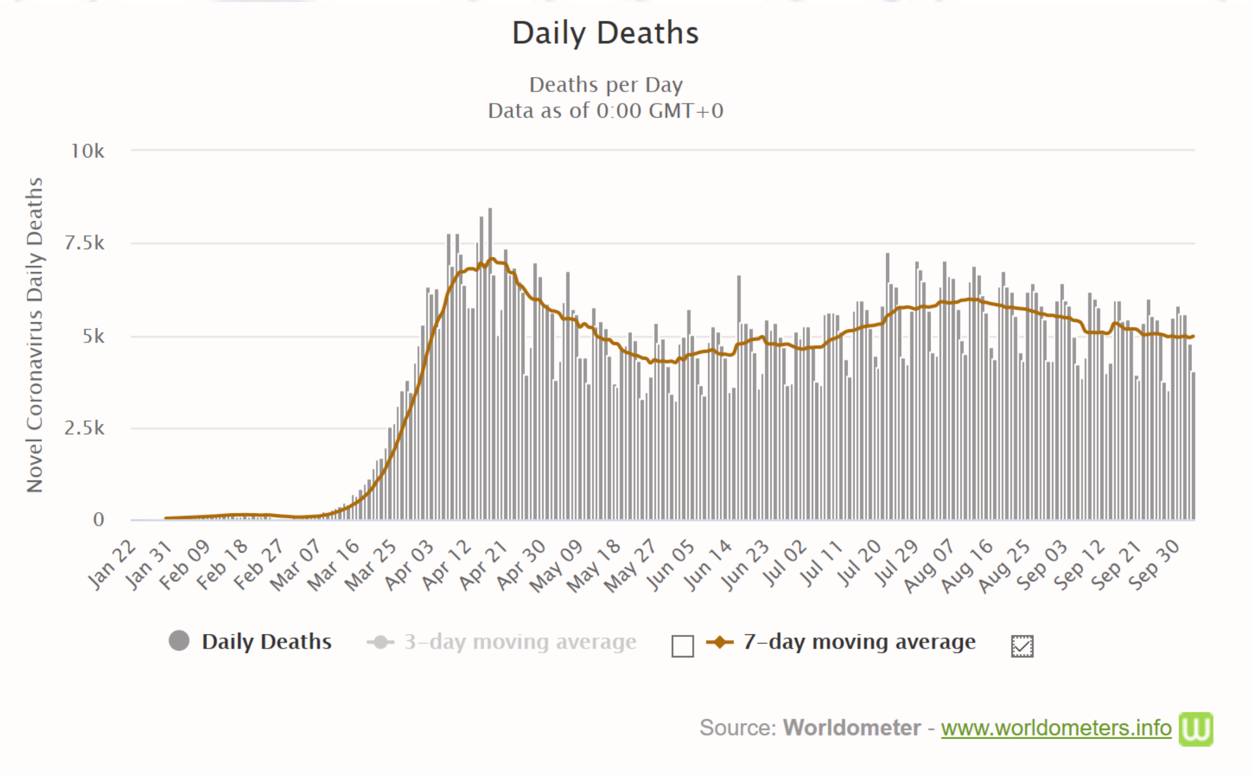
Covering the month of September 2020

September Market Update

Margetts' monthly diary discusses major economic and market developments that occur over the month. It is written by the Fund Management team.

Japan proved to be the strongest equity market during September, in part due to the election of a new Prime Minster. IA Japanese Smaller Companies was the best performing sector during the month (9.86%), followed by IA Japan (6.05%) and UK Index Linked Gilts (3.61%). In comparison the UK lagged, with IA UK Equity Income the worst performing sector (-2.32%), along with IA UK All Companies (-1.77%) and IA UK Smaller Companies (-1.15%).

The Covid-19 pandemic continued at pace in racking up daily confirmed cases. 34,203,088 was the cumulative total of declared cases by the end of September. USA and Emerging Markets countries remained the worst affected. Total worldwide deaths passed 1,000,000 at the end of September. One of the more positive aspects to focus on in the pandemic is the trend of daily deaths. As can be seen from the graph below, despite the continuing escalation of positive cases, deaths are not seeing a similar rising trend, and remain below the heights of the initial wave.



Progress on a vaccine remains promising, such that discussion in the media is turning to the challenge of manufacture and distribution, rather than the efficacy of the vaccines. The Oxford Vaccine, a joint venture between Oxford University and Astrazeneca, hit a typical late-stage testing hurdle when a UK volunteer saw a possible adverse side effect. Trials restarted in the UK and elsewhere but the US, which saw a similar effect in one of their volunteers, were not so quick to restart the trials, with the FDA refusing to grant the required permission.

The US election took an unusual twist at the turn of October, as Donald Trump tested positive for Covid-19, along with his wife and a significant number of his White House staff. The incident raises the uncomfortable spectre of Boris Johnson’s close shave with the virus earlier in the year, and the possibility that Donald Trump may not be in a fit state to act as President in the event of re-election. Equity markets and oil wobbled at the prospect. While there are historical occasions where the President has passed power to the Vice-President due to incapacity or death while in office, neither Republicans nor Democrats have ever had to change their nominations ahead of a presidential election. Joe Biden has continued his wide polling lead at national level and slight lead in the swing states, with no sign of the first presidential debate having significantly impacted the polls. Whether Trump’s illness will result in the sort of brief popularity bounce that occurred for Boris Johnson after his diagnosis remains to be seen. A Democratic win for Biden and in the Senate would result in significant fiscal stimulus above what has already been undertaken (and what has been proposed unsuccessfully by Trump), with the Fed already having signalled that interest rates will remain behind inflation. This would be a fillip for equity holders and would likely feed positively into global consumer and investor confidence.

The Brexit outcome remained murky over the possibility of achieving a trade deal before the transition period ends. The positive news to take from the matter is the agreement of both sides to continue discussions, despite the legal wrangle of the EU commencing legal action against the UK on the basis of the recent Internal Market Bill which passed through the House of Commons. Estimates of a no deal outcome are approximated at c.20-30%, with the likely outcome being a partial trade deal with challenging aspects to be ironed out later. The GDP impact of a no deal outcome is likely to be significantly lessened in the wake of the pandemic, with global trade volumes remaining considerably depressed. A successful deal ought to boost sterling and UK equities, as much for the long-awaited certainty of the outcome as the quality of the outcome.

In Japan, the Prime Minister, Shinzo Abe, resigned at the end of August due to lingering health complications, bringing to an end a period of unusual political stability. In September he was succeeded as the leader of the Liberal Democratic Party by Yoshihide Suga, who won the support of the vast majority of voting party members. Suga campaigned as a continuity candidate, which should broadly see the policy of “Abenomics” (monetary easing, fiscal stimulus and structural reform) maintained. The Bank of Japan ought to continue its extensive bond buying programme and close union with government policy on this basis. A general election is due by October next year and the possibility that Suga may trigger an earlier election to secure his own mandate should not be ruled out, with the LDP by far the most popular political party in the country, such that the ANN poll of 19-20 September after Suga’s election recorded a 53.9% preference for the LDP; a significant spike on Abe’s last polling figures in August. Investors can reasonably expect Japan to continue with business as usual.

Strategy

We maintain the belief that equities offer attractive yield, with significant capital upside. Three upcoming events could prove to be the catalyst for significant upward repricing; the US election, Brexit, and positive Covid-19 vaccine developments.

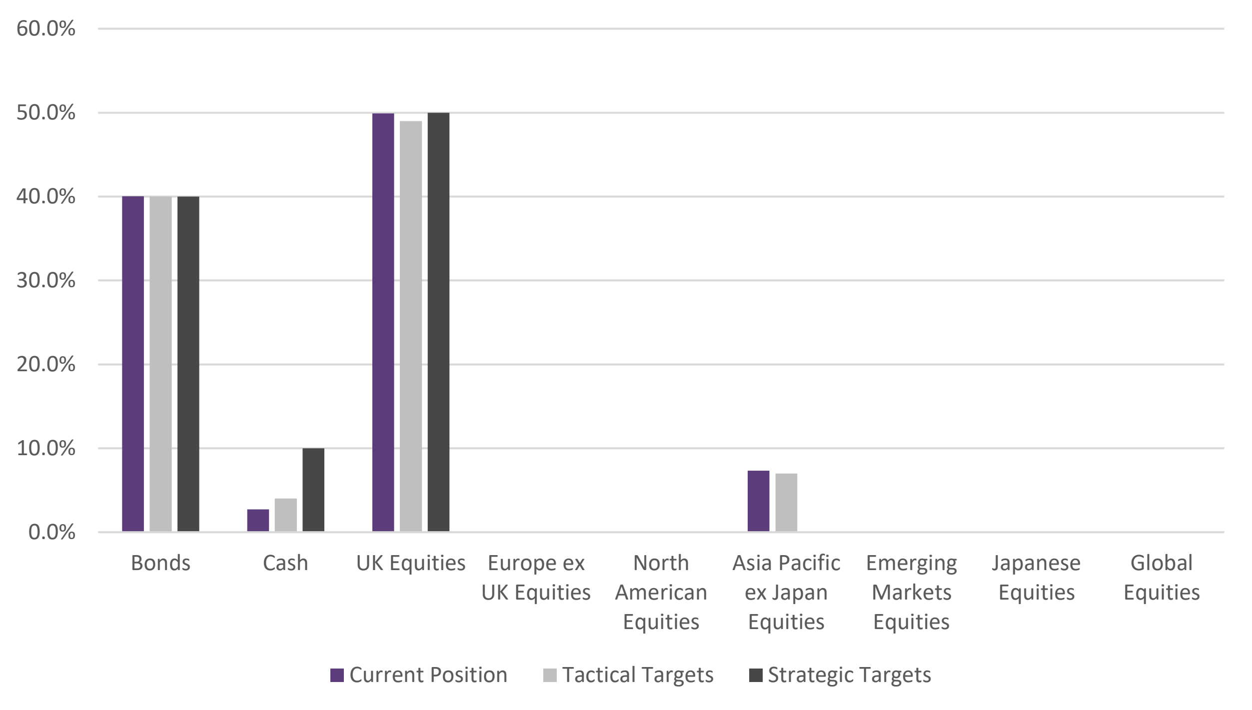
Bond valuations remain artificial, with central banks acting to suppress yields with no imminent end in sight for government borrowing to slow down. The longer that yields are suppressed, the easier paying for the pandemic will ultimately be. With decades-long government borrowing costing less than 1% in many developed markets, and bond investors scrapping for yield increasing, there is no sign that this equation will stop adding up. The risks of going long-dated in this market are not adequately priced in, and our bias is towards short-dated corporate bond funds, where above inflation yield is offered at an affordable price with lower credit and duration risk.

Our equity positioning is biased towards the UK on the basis of historically low valuations and as the most likely candidate for relative outperformance should value equities reverse their recent poor performance against growth stocks. We also maintain our overweight position in Asia pacific and emerging markets equities, on the basis that economic indicators and sentiment point to a v-shaped recovery from the virus, with the likelihood of wide-scale lockdowns reduced by effective contact tracing regimes. Our emerging markets holdings have little exposure to the worst affected countries, being mostly focused on developing Asian economies.

Margetts Risk Rated Funds

The below charts show the current positions of the funds, the tactical (short term) targets, and the strategic (long term) allocations. We aim to keep the current positions in line with the tactical targets from week to week. The differences between the tactical and strategic targets reflect the views and convictions of the Margetts Investment Committee.

Providence



There were no changes made to asset allocation and/or fund selection in September.

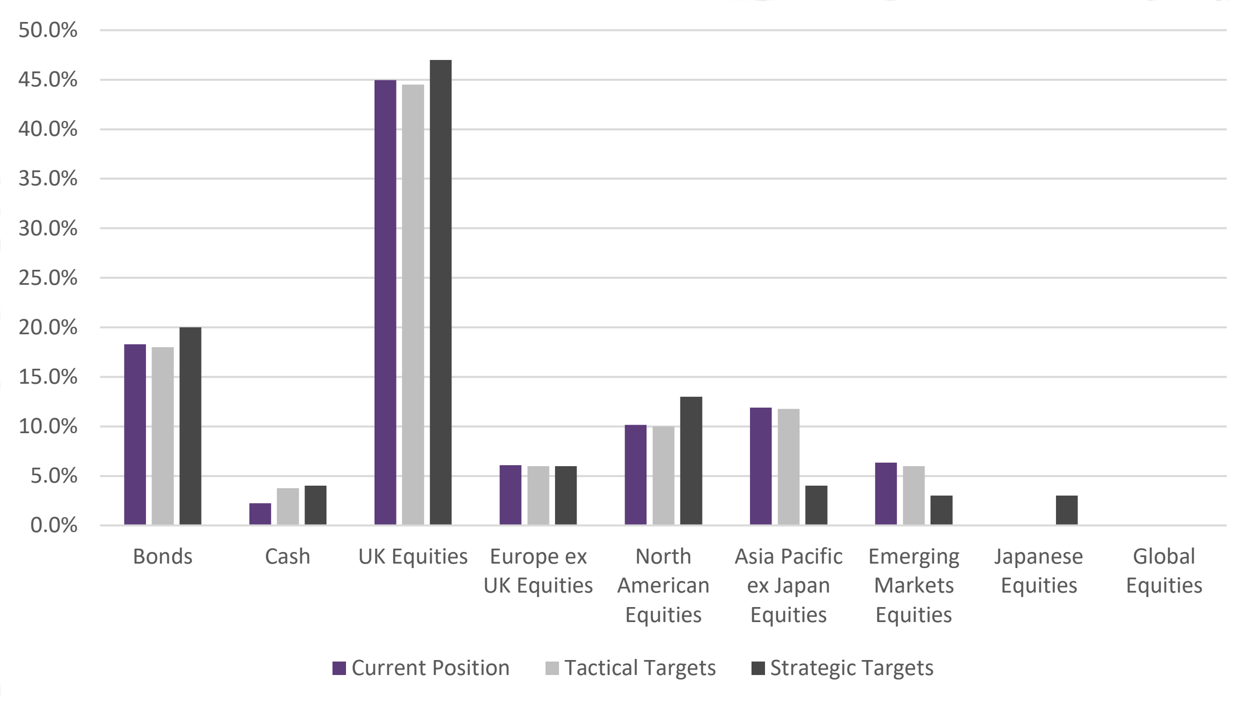
Providence was c.1 percentage point behind the IA Mixed Investments 20-60% Share sector during September.

Longer-dated bond funds within the Providence portfolio outperformed short-dated bond funds during the month, with the Royal London Global Index Linked and Royal London Sterling Credit funds the best performers in absolute terms.

The Legal and General Asian Income fund slightly lagged the IA Asia Pacific ex Japan sector during the month, with falling commodity prices having a negative impact via the fund's overweight exposure to Australia.

In the UK, the Threadneedle UK Equity Income fund was the best relative performer, with a c.1.1 percentage point outperformance of the IA UK Equity Income sector.

Select



There were no changes made to asset allocation in September. The Fidelity Asia fund was chosen to replace the BlackRock Asia fund due to an extended period of underperformance.

Select returned c.0.9 percentage points behind the IA Mixed Investment 40-85% Shares sector during September.

Longer-dated bond funds outperformed short-dated funds within the Select portfolio during the month.

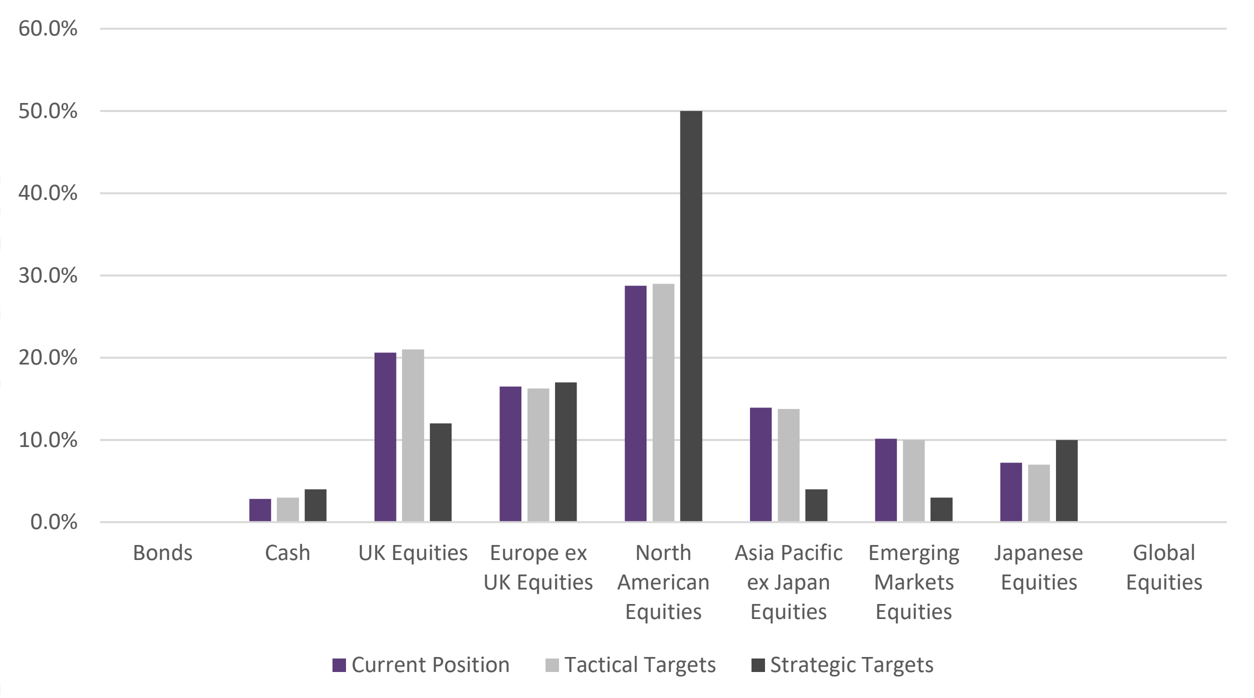
The Schroder Asian Income fund offset the weaker performance of the BlackRock Asia fund before the latter was sold.

The UBS Global Emerging Markets fund lagged the IA Global Emerging Markets sector during September.

The Fidelity European fund outperformed the IA Europe ex UK sector across the month, while both North American funds lagged the IA North America sector.

Most UK funds within the portfolio outperformed their respective sectors through the month.

International



There were no changes made to asset allocation in September. The JPM Europe Dynamic fund was sold and replaced with the Fidelity European fund due to poor mid-term performance.

International returned behind the IA Global sector by c.1.3 percentage points over one month.

The Baillie Gifford Pacific fund offset the weaker performance of the L&G Asian Income fund in September.

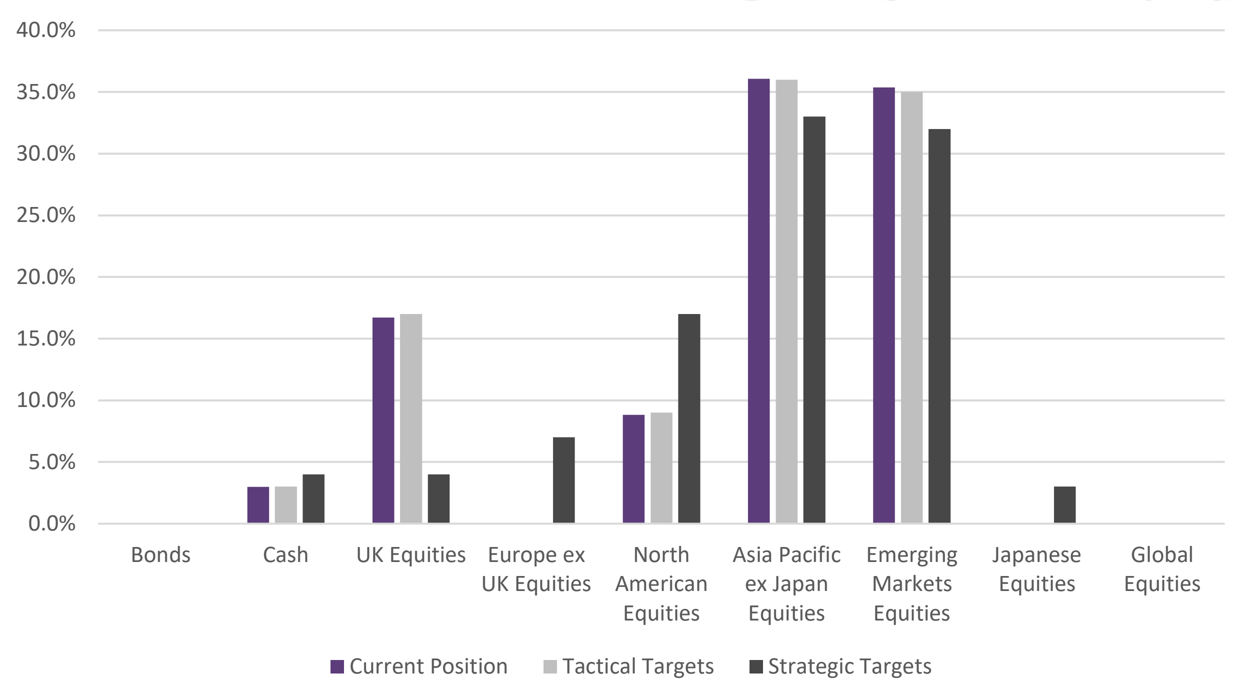
Within Japan, the strong performance of the Baillie Gifford Japanese fund, balanced out the relatively weaker performance of the Schroder Tokyo fund over one month. Both made positive absolute returns.

Both Emerging Markets funds returned close to the IA Global Emerging Markets sector during September.

The BlackRock Continental European fund offset the weaker performance of the JPM Europe Dynamic fund.

Two of the three UK funds in the International portfolio returned in line with the IA UK All Companies sector.

Venture



There were no changes made to asset allocation in September. The Fidelity Institutional South East Asia fund has been replaced with Fidelity Asia.

Venture returned c.0.6 percentage points behind the IA Flexible Investment sector during September.

3 out of 5 Asia Pacific funds were ahead of the IA Asia Pacific ex Japan sector over one month.

The performance of the underlying Emerging Markets funds was mixed, with 2 of the 5 funds returning ahead of the IA Global Emerging Markets sector.

The only US holding lagged the IA North America sector in September.

Large-cap UK funds outperformed the mid-cap holding in the portfolio over the month.

Important Information

Please note that the contents are based on the author's opinion and are not intended as investment advice. This information is aimed at professional advisers and should not be relied upon by any other persons.

Any research is for information only, does not constitute financial advice or necessarily reflect the views of the author and is subject to change. It remains the responsibility of the financial adviser to verify the accuracy of the information and assess whether the fund is suitable and appropriate for their customer.

Past performance is not a reliable indicator of future performance. The value of investments and the income derived from them can fall as well as rise and investors may get back less than they invested especially in the early years.

Important information about the funds can be found in the Supplementary Information Document and NURS-KII Document which are available on our website or on request.

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