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Close Diversified Income Portfolio Fund

Monthly fund manager update

May 2019

Performance

Close Diversified Income Portfolio Fund fell 0.64% in May. This compared to -0.96% for the IA 20-60% sector. This takes the year to date return for the Fund to 4.3%.

Whilst the fund outperformed in May, it did so despite a couple of significant headwinds. Further political rhetoric around nationalisation meant PFI Infrastructure funds came under pressure, while six of the Fund's investment trust holdings announced fund raisings, which are typically done at a discount to the current share price and tend to temporarily depress the share price down.

Market roundup

Equity markets were negative across the board over the month, although due to sterling's weakness (on Brexit/Tory party leadership battle) international equity markets did not do as badly as the headlines suggest for UK investors. In the month UK large caps were -3.5%, US -6.2% (but only -3.2% in GBP terms), Europe -6.7% (but only -4.2% in GBP terms) and Japan -7.5% (but only -2.2% in GBP terms).

Gilts rose in price in May as the 10 year Gilt yield fell from 1.18% to 0.89%. Corporate bonds underperformed Gilts in the month as BBB spreads rose from 1.80% to 2.01%. BBB spreads are almost back to the long-term average.

The main reason behind the risk-off markets was the fading hope of a quick end to the US-China trade dispute. Trump actually increased tariffs on China from 10% to 25%, followed this up with a 5% tariff on Mexico, and then ended India's exemption to tariffs too. Trump has threatened Mexico with an additional 5% every month until a total of 25% is reached in October. Trump also blacklisted Chinese technology company Huawei, and has instructed his team to start working on raising tariffs on the rest of China's imports to the US. On-going issues over trade seem to be impacting global growth, with China's Manufacturing PMI falling back into contraction territory at 49.4. China has raised tariffs on US products in retaliation and is said to be considering further restrictions.

Alternatives

Political rhetoric around the subject of nationalisation stepped up once more, driving down the PFI Infrastructure funds up to 6% in the month. The Labour Party published details on its proposals for publically owned energy networks in a document entitled "Bringing Energy Home", whilst the target of the document was the energy sector, International Public Partnerships Ltd has a shareholding in Cadent, which is one of the nationalisation targets mentioned, and HICL Infrastructure has a holding in Affinity Water - another sector in the sights of Corbyn. Law firm Clifford Chance re-iterated their stance that just as with PFI, nationalisation of any sector would have to be done at market value, not at a Labour Government's valuation. It has to be said though that a government can do lots of other things without legal recourse – such as raise taxes and introduce much tougher regulatory reviews etc., which could hurt the equity value of UK companies.

Fixed income

I took the opportunity to up-weight the Starwood European Fiance (6.15 yield) and the Real Estate Credit Investments (6.8% yield) positions as two of the investment trust placings noted above. As debt funds

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they stand to be more able to withstand any economic shocks to come, compared to REITs, but still offer attractive returns should the cycle continue. Other positions added to in the month included Helical 2019 (2% yield), Hiscox 2045 (callable in 2025) at 4.25% yield, and Primary Health Properties 2019 (2% yield). New holdings included TP ICAP 2026 (5.25%). We already hold the TP ICAP 2024 bond and their soon to be maturing 2019 bond.

Equities

In the equity space I added to two holdings. Arbitration and litigation finance provider, Burford Capital, was added to after a negative note was issued by Canaccord causing a notable fall in the share price. It is my belief that Canaccord's main points can be easily rebuffed and that their calculation of Return on Invested Capital was wide of the mark. Furthermore, Canaccord's suggestion Burford need to raise equity is odd given they did so at the end of 2018, and have launched two new $300m funds and agreed a $1bn joint venture with a sovereign wealth fund – meaning there is plenty of capital to invest before they decide whether or not to raise more capital. I added at prices below 1500p and by the month end the share price was back up at 1670p, buoyed by a positive decision on one of their large cases.

The other position I added to was Lancashire Holdings which fell after its Q1 trading statement. Again the shares bounced by the month end. Whilst I remain cautious on equities, these both have some similarly appealing characteristics in that they are mostly dollar earners and not correlated to economic conditions.

Yield and NAV

The fall in Net Asset Value combined with lower cash levels (2% from 3%) meant that the yield has gone back up to 4% from 3.8%. The yield on the Fund is the result of all the individually picked attractive risk:reward ideas. In this tough environment the hard work continues to find attractive risk:reward ideas across the whole spectrum of asset classes that the Fund is able to invest in. It is worth noting that over the next 2 months the Fund will see 7.5% of the Fund mature into cash. This will give the Fund plenty of firepower to reinvest should markets fall further, but actually will not impact the yield of the fund even if I do not re-invest immediately as the yields of the securities due to mature are now very small. This 7.5% rolling off into cash will only reduce the Portfolio yield from 4% to 3.95%.

Close Diversified Income Portfolio Fund discrete performance as at 31 May 2019

	YTD	2018	2017	2016	2015	2014
Close Diversified Income Portfolio Fund	**4.3%**	**-1.8%**	**5.4%**	**7.8%**	**2.4%**	**5.0%**
IA Mixed Investment 20-60% shares	5.8%	-5.1%	7.2%	10.3%	1.2%	4.9%

Source: FE Analytics 04.06.2019; all are X Acc share classes; performance is total returns, net of fees with dividends reinvested.

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