Close Brothers
Asset Management

For professional adviser use only.
Not for distribution to retail clients.

Close Diversified Income Portfolio Fund

Monthly fund manager update

DECEMBER 2019

STEPHEN HAYDE
Managing Director

PERFORMANCE

The Close Diversified Income Portfolio Fund rose 1.52% in December, finishing at a new all-time high Net Asset Value (NAV). This compared favourably with a 1.23% rise for the IA 20-60% sector. This took the 2019 return for the fund to +9.8% – its best year ever in terms of total return. It was ultimately behind the IA sector, but the fund remains conservatively positioned on a relative basis (beta 0.59, low duration, overweight alternatives, and underweight equities). If we look at the performance over the past two years, the fund only experienced 35% of the downside in 2018, but 82% of the upside in 2019.

The fund remains 1st out of 176 funds in the sector for risk-adjusted performance over its 8 years and 11 months track record, and has delivered 5.5% per annum over this period, compared to 5.0% for the IA sector.

MARKET ROUNDUP

UK General Election: With a resounding Conservative win, fears of an imminent implementation of some of Labour's radical agenda – nationalisation / insourcing / forced equity issuance to staff – evaporated. It was no surprise, therefore, to see a 'risk-on' environment in the UK.

The Private Finance Initiative (PFI) funds did well, particularly HICL Infrastructure (+5.8%) and International Public Partnerships (+5.4%), which have the most UK PFI equity exposure.

UK Real Estate Investment Trusts bounced, with Primary Health Properties (+8.7% – we own the convertible bond), AEW UK REIT (+6.9%), GCP Student Living (+5.8%) and Warehouse REIT (+5.2%) all strongly positive over the month.

Surprisingly, the Renewable Infrastructure funds bounced, too. Both political parties were pro-renewables so there was no obvious election result read-across, but it seems they were pulled up by the general mid-cap rally.

UK mid-cap equity holdings also rebounded strongly – Mears Group (+20%), Diploma (+9.9%), Babcock (+6.6%), IWG (+6.6%), Clinigen (+6.1%), and CVS Group (+5.6%) – but UK large-caps fared less well, held back by sterling strength.

Overseas: Further afield, US President Donald Trump pencilled in 15th January for signing the 'Phase 1' trade deal. The US Federal Reserve (Fed) continued to expand its balance sheet via QE4 (although they deny it is quantitative easing). This expansion is faster than their previous three programmes and is contributing to the recent equity rally. In fact, the US equity market has only been down during one week since QE restarting (the one week the Fed's balance sheet shrank).

China has started 2020 with additional easing measures, too, cutting its banks' Required Reserve Ratio by 0.5%. This comes after a rise in defaults in the domestic bond market, which has seen 20 new defaults since November.

EQUITIES

Equity markets around the world enjoyed a positive December (though slightly reduced in sterling terms, due to the pound strengthening after the election). UK large-cap equities rose + 2.7%, UK mid-cap equities rose +5.2%, US equities rose +2.6% (+0.6% in GBP) and European equities rose 1.1% (1% in GBP).

FIXED INCOME

In bond markets, the 10 year gilt yield rose to 0.81% from 0.7% (due to the 'risk-on' environment) whilst BBB corporate spreads fell to 1.61% from 1.74%. Corporate bonds outperformed sovereign bonds in December and BBB corporate bond spreads remain below the historic average of 2.14%.

Three bonds successfully matured over the course of the month: Unite Group 2020 (called early by the company), M&S 2019 and Tesco Personal Finance 2019.

ALTERNATIVES

In the alternatives space, we added to HICL at 160p in their pre-election placing. The election result took the shares up to 170.8p.

After cutting Greencoat Renewables in November, they announced a discounted placing at 113cents in December. We took part and quickly started to sell our position for a short-term +6% gain (equivalent to one year's expected return in a week or so).

With the price of investment trusts running up after the election, we took the opportunity to reduce a number of them in the last week of the year – given higher prices equate to a lower future expected returns. They included BBGI (4.1% expected return), Bluefield Solar (3.9% expected return), GCP Student Living (5.4% expected return), Foresight Solar (3.9% expected return) and Greencoat UK Wind (3.9% expected return).

One new holding, Octopus Renewables Infrastructure Trust (7.7% expected return), was added at IPO, and was the month's best performer, rising 7.5%. Two holdings were added to: Starwood European Real Estate Finance (6.9% expected return) and Real Estate Credit Investments (7.4% expected return), as they had failed to participate in the early post-election rally (so still offered attractive future expected returns).

YIELD AND NAV

The fund's yield fell -0.2% to +3.4%, reflecting the strong NAV growth over the month, the increase in the cash balance (three bonds matured and some of the alternatives were trimmed), and the purchase of Octopus Renewables Infrastructure Trust (0% yield for 2019). 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.

CLOSE DIVERSIFIED INCOME PORTFOLIO FUND PERFORMANCE AS AT 31 DECEMBER 2019

	2019	2018	2017	2016	2015	2014
Close Diversified Income Portfolio Fund	**9.8%**	**-1.8%**	**5.4%**	**7.8%**	**2.4%**	**5.0%**
IA Mixed Investment 20-60% shares	11.8%	-5.1%	7.2%	10.3%	1.2%	4.9%

SOURCE:

FE Analytics, 06.01.2020; 2019 (YTD) data as at 31.12.2019. Performance is total return, net income reinvested after fees, X Acc share class.