Discretionary Management Service

Manager update

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GENERAL MARKETS

We wanted to continue to share our thoughts on the market and provide updates on our thinking and portfolio positioning.

First, while it is clear that we face a significant economic hit from coronavirus, this downturn is different from the recession triggered by the financial crisis 12 years ago. While there will be a meaningful impact on both the supply and demand sides of the economy, most sectors will only face temporary damage and disruption. We are not exposed to those businesses which will be most badly hurt by the containment measures, namely the leisure and travel sectors.

There are many parallels that can be drawn from which we like to extrapolate underlying trends and opportunities. For example, during the nuclear disaster in Fukushima in 2011, supply chains were destroyed whereas today they have suffered massive disruption but activity will resume. The factories in the Pearl River delta, an important economic hub in China, are still standing but they just need workers to return to business. As we write, data suggests that the infection rate in China has slowed and that the country is getting back to work. This is evidenced by a rise in nitrogen dioxide emissions over China (which is primarily produced by traffic and factories and is a first-level indicator of industrial production) and near real-time data such as coal consumption and property sales are getting back to normal.

Panic and fear has exacerbated the decline, this will provide good investment opportunities

The evidence for this irrational mind-set was the performance of gold and Treasury bonds. When shares, precious metals and US government bonds are all being sold off on the same day, you know that investors are simply raising cash wherever they can, rather than looking at fundamentals and remaining diversified.

The growth in importance of algorithm-driven trading is another factor in the speed and violence of recent market movements. The rise of passive funds has also played its part. Personalised active management shows its value in such volatile markets.

PORTFOLIO PERFORMANCE VS INDICIES

DMS	
Portfolio mandate	**YTD performance %**
Defensive Income DMS	-15.62%
Conservative DMS	-15.85%
Balanced DMS	-16.62%
Growth DMS	-18.66%

SRI	
Portfolio mandate	**YTD performance %**
Income SRI	-13.15%
Conservative SRI	-12.98%
Balanced SRI	-13.95%
Growth SRI	-15.34%

Source: MSCI. All figures quoted in GBP. Past performance is not a guide to future performance. Performance is shown net of fees.

Indices	
Index	**YTD performance %**
UK Equity	-31.77%
US Equity	-15.58%
EU Equity	-23.96%
Japan Equity	-15.10%
Asia ex Japan	-15.64%
EM Equity	-19.31%
UK Gilts	0.27%
UK Index Linked	-8.44%
Infrastructure	-11.12%
Absolute return	-2.19%
Commodities	-15.63%

ACTIONS TAKEN ON PORTFOLIOS

We have made a number of trades over the last couple of weeks all of which have been with the intention of reducing overall risk by raising cash as we still think it is right to be cautious in our approach. We have not hit peak infection rates and the effect of the containment measures are still filtering through to global supply chains so it may yet be too early to put cash to work.

We have reduced broad based equity exposure to the major markets through the sales of trackers and funds in the UK, US (small caps), Asia and the Emerging markets. Our intention has been to reduce overall portfolio risk as markets try to price in the (as yet 'unknown') negative economic impact of the virus.

We are not complacent and will continue to actively manage the portfolios. Globally, governments and central banks are working hard to support markets and economies and the hope is that recent and future stimulus packages could bring about a v-shaped recovery at some point later in the year. A number of equities and corporate bonds are starting to exhibit attractive valuation entry points but we think it is still too early to put the money back into the market. However, we have a growing watch list of future potential investments and look forward to taking advantage of opportunities as they present themselves.

The measures we have taken have reduced overall portfolio risk, whilst still maintaining an appropriate level of diversification and conviction in holdings. As mentioned above, any bounce back could be sudden and investors, who are looking at the long term, should hold some comfort from the recoveries experienced in 2008 and 2016. Cash is around the 10% level for DMS and SRI clients and we are ready to put it to work when we estimate the time is right.

US

Federal Reserve Bank (Fed) actions

Measures include a sudden cut in interest rates, a multibillion-dollar bond-buying spree, a discount on short-term funding for banks, and a coordinated move with other central banks, to make it cheaper for banks around the world to borrow US dollars — a staple of global financial transactions. The Fed has also agreed to aid mutual funds by covering some of the heavy redemptions that have been experiencing.

1. Near-zero interest rates

The Fed cut its key interest rate, the federal funds rate, to 0-0.25%, down from a range of 1-1.25%. The federal funds rate is the interest rate banks charge one another for overnight loans, and it's the central bank's key tool for influencing the economy. It influences everything from mortgage rates and auto loans, to the interest rate on savings accounts and credit cards. Low interest rates can stimulate the economy by making it cheaper for people to borrow money to buy a home, purchase a car or to fund their business.

2. A bond-buying spree

The Fed also announced that "over the coming months," it plans to purchase hundreds of billions of dollars in bonds — specifically at least $500 billion in US Treasuries and at least $200 billion in mortgage-backed securities. Reminiscent of the Fed's so-called "quantitative easing" programs following the financial crisis, this bond-buying program is meant to keep financial markets functioning smoothly. The market for US Treasuries is one of the largest, most important financial markets in the world, but amid the coronavirus pandemic, trading securities has become more difficult. By purchasing billions of dollars in Treasuries, the Federal Reserve serves as a buyer of last resort in the market, creating more demand for bonds and getting cash into the hands of banks and other institutions that are trading these securities. All that cash sloshing around is meant to prevent a liquidity crunch. The same goes for mortgage-backed securities, which underpin US mortgage rates.

3. Cheap global access to US dollars

The Fed announced a coordinated effort with five other central banks — the Bank of Canada, the Bank of England, the Bank of Japan, the European Central Bank and the Swiss National Bank — to make it cheaper for banks around the world to borrow US dollars. This move is important because US dollars are considered a safe-haven asset and are a staple in international transactions. The Fed has agreed to lower the rate on dollar swaps to 0.25%, in an effort to "ease strains in global funding markets, thereby helping to mitigate the effects of such strains on the supply of credit to households and businesses, both domestically and abroad."

4. Back-up loans for banks

Banks sometimes need short-term, back-up funding to keep their operations running smoothly. When that happens, they can turn to the Fed's so-called "discount window" to borrow those funds directly from the central bank. In a strong economy, banks are often reluctant to do so, however, because they fear it can send a negative signal to the public.

The Fed has since acted to reduce the stigma associated with the discount window, making it cheaper for banks to borrow funds through that mechanism and extending the length of loans to up to 90 days.

Capitol Hill and fiscal spending

The Trump administration's $1 trillion proposed rescue plan, which forms the basis for fast-moving negotiations on Capitol Hill, includes sending two large checks to many Americans and devoting $300 billion toward helping small businesses avoid mass layoffs. Priorities laid out in a two-page Treasury Department document also include $50 billion to help rescue the airline industry and $150 billion to prop up other sectors, which could include hotels.

All told, between several legislative packages advanced on Capitol Hill and other actions the government has taken, the White House is pushing an economic plan that is "over $2 trillion and counting" to try and arrest the coronavirus's negative economic impact.

UK

Bank of England (BoE) actions

The monetary policy committee voted unanimously to slash the bank rate from 0.75% to 0.10% at its first unscheduled set of meetings since the depths of the 2008 financial crisis as part of a coordinated package of measures alongside the chancellor, Rishi Sunak's budget.

The central bank also announced a new term-funding scheme to support small and medium-sized companies, as well as new steps to help commercial banks lend more. They have also engaged in £645 billion pounds worth of asset purchases.

UK Government and fiscal spending

The U.K. pledged a £30 billion ($39 billion) emergency boost to spending as Boris Johnson's government battles to stop the coronavirus outbreak wrecking its economy.

The chancellor set out his multi-billion pound three-point plan, including £7 billion to support businesses and individuals:

- The National Health Service will get "whatever it needs, whatever it costs," with a £5 billion emergency response fund immediately for public services
- People will get financial support if they need it to cope with the virus, with statutory sick pay for everyone who's been told to self-isolate, and more generous welfare rules
- Supporting businesses: government to refund sick pay bills for 14 days in full, for 2 million companies with fewer than 250 employees.

In other measures announced in Sunak's Budget:

- The threshold for paying National Insurance will be increased from £8,632 to £9,500, "a tax cut for 31 million people," typically worth £104 per person
- Public spending will be £100 billion higher over the next five years
- £800 million to establish two or more new carbon capture and storage clusters, creating 6,000 jobs
- Entrepreneurs' tax relief will be reduced but not be fully abolished, despite speculation it would be axed
- Research and development investment will be raised to £22 billion a year
- Fuel duty will be frozen for another year and a planned rise in beer duty will be cancelled.
- More investment in transport infrastructure across the U.K., and extra spending on broadband

European Central Bank (ECB) actions

The ECB will buy up to 750 billion euros, or $820 billion, in government and corporate bonds and other assets, pumping cash into financial markets deeply rattled by the pandemic. The ECB said it would buy even more assets if need be, signalling that it is prepared to defend the Eurozone with all the weapons at its disposal.

Bank of Japan (BoJ) actions

The BOJ will bolster its asset-buying program, expanding purchases of stocks, corporate bonds and corporate commercial paper, while also boosting its loan support program to help businesses deal with any liquidity issues. The central bank will double its upper limit of annual purchases of exchange traded funds to 12 trillion yen ($112.46 billion) and of real-estate investment trusts to 180 billion yen per year.

It will also expand the upper limit of its corporate bond balance to 4.2 trillion yen and its commercial paper balance to 3.2 trillion yen, each up 1 trillion yen.

In addition, it will start a lending program for commercial banks, providing them with one-year loans in exchange for corporate collateral worth 8 trillion yen.
Other policy tools were kept unchanged, with short-term interest rates at minus 0.1% and long-term interest rates at around zero. It will continue to increase its holdings of Japanese government debt by 80 trillion yen a year.

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PORTFOLIO PERFORMANCE

Performance	1 yr	3 yrs	5 yrs	2019	2018	2017
DMS Defensive Income	4.34%	7.39%	-	6.84%	-3.41%	7.37%
DMS Conservative	3.19%	6.72%	16.99%	10.53%	-4.83%	8.22%
DMS Balanced	3.27%	9.02%	19.84%	13.28%	-5.85%	10.71%
DMS Growth	3.19%	10.07%	22.07%	15.71%	-7.18%	12.77%
SRI Income	7.67%	-	-	13.99%	-3.72%	-
SRI Conservative	8.93%	15.80%	-	15.61%	-3.76%	10.22%
SRI Balanced	10.06%	19.00%	-	17.87%	-3.79%	12.10%
SRI Growth	10.82%	-	-	20.75%	-3.86%	-

This data is shown as at 29/02/2020. Past performance is not a guide to future performance. Performance is shown net of fees.