IMS Capital

IMS Capital Quarterly Summary

July 2019

In our last update we talked about the dramatic shift in sentiment between the previous two quarters; at the end of 2018 we saw fears about rising interest rates and increasing trade tensions cause markets to tumble, followed by a complete reversal in the first quarter of 2019.

At the time we indicated that despite welcoming the recovery, we were concerned that markets had lost a degree of rationality, ignoring some indicators which were showing less than positive signs. The latest quarter has seen a continuation of this fervour and many markets, especially those in the US, have continued to top all-time highs.

A primary driver of this was the softening of the Federal Reserve's (Fed) stance on interest rates. In 2018, the focus was on rising rates which concerned investors as this would have made it harder for companies to take on more debt and would therefore act as an impediment to growth. As the months have gone by, the Fed moved first to a neutral position and now appear to be considering a cut in rates. Australia, New Zealand, Chile, India and Russia have all cut rates already this year and the recent announcement from the European Central Bank indicates that they are considering a return to quantitative easing.

From a Fed perspective, there are many reasons for this change of attitude but one factor that they insist is not related is the pressure that Donald Trump has been trying to exert. Somewhat unsurprisingly given his background, Trump is very keen on lower interest rates and has been critical of the Fed chairman, Jerome Powell, and his refusal to bow to the Presidents wishes. Whatever the reasons for the current situation, it has been well received by markets and has allowed this record-breaking bull run to continue.

Trump was involved in the other big story of the quarter and in continuing his trade dispute with China he seemed determined to put a halt to the onward march of markets. In May, months of trade negotiations were due to come to an end and hopes had been relatively high that a positive resolution would be found but no agreement was reached. The resulting threat of an increase to tariffs on $200 billion of Chinese goods from 10% to 25% caused the worst week for many indices since the start of the year, with the FTSE 100 index falling to a six-week low.

Since then, however, markets have recovered and continued to do so ahead of a meeting between Trump and Chinese Premier Xi Jingping at the G20 summit in Japan. The two nations agreed at this meeting that talks would begin again and that the proposed tariffs would not be enforced. Of course, this moderation does not mean that the trade war is over; hundreds of billions of dollars of goods are still subject to earlier tariffs and the effects of these penalties are being felt far and wide.

With the situation between the US and China looking to have improved for now, Trump has again turned his attentions to the EU, which he also considers to be using unfair trade practises in its dealings with America. Following on from the $21bn of tariffs which were announced in April, the US government is said to be considering penalties on $4bn of additional products, including Italian cheese and Scottish whisky.

The combined effects of all of this talk of tariffs are impacting on global growth. The German government have cut their growth estimate for 2019 to 0.5%. This is down from the earlier estimate of 1% and is the second cut this year, with the government previously cutting predictions from 1.8% in January.

The International Monetary Fund has also downgraded its global economic growth forecast for 2019 and now expects expansion of 3.3% which is its lowest since 2009. This is down from 3.5% previously and reflects their concerns about the impact of global tensions over trade as well as Brexit.

Despite these downgrades, sentiment remains positive and corporate results, which should be further boosted by looser monetary policy, appear resilient. Employment data is also very strong with the UK unemployment rate falling to the lowest level since 1975. However, it is important to understand that the reason for the softened approach of central banks is that they have concerns about global growth and inflation.

It is this combination of factors which gives us pause for thought. As ever, we invest for the long term and need to see past the noise to see what lies beneath.

IMS Capital is a trading style of Compass Wealth Management Consultants Ltd, Active Financial Partners Ltd, and AE Financial Services Ltd which are authorised and regulated by the Financial Conduct Authority.

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Performance summary

The performance over the quarter was very strong, both for markets generally and also for the IMS portfolios. Returns were generated across multiple sectors, with bonds and equities both doing well. We have taken steps over recent quarters to add much greater diversification to the portfolios, with the intention being that this would hopefully provide some insulation should markets turn less positive. In light of this, it is especially pleasing to see that the portfolios have performed so well. More details on this process are explained below.

Portfolio	3 month performance	12 month performance	36 month performance	60 month performance	12 month historical yield %
Defensive Income	2.57	3.61	16.26	25.29	3.16
Benchmark	2.46	3.14	12.20	19.48	n/a
High Income	3.07	2.61	22.58	35.05	3.56
Benchmark	3.57	3.13	22.12	31.33	n/a
Cautious	3.89	3.71	22.92	35.32	2.54
Benchmark	2.96	2.78	17.42	24.91	n/a
Balanced	4.77	3.55	29.34	44.75	2.30
Benchmark	4.01	3.39	25.76	36.41	n/a
Growth	5.16	3.89	34.95	52.94	2.05
Benchmark	3.78	2.65	26.73	37.16	n/a
Ethical	6.43	6.74	34.96	45.80	1.77
Benchmark	4.01	3.39	25.76	36.41	n/a

All data are to 30/06/2019. Source: Financial Express Analytics

Portfolio changes

Over the last few quarters our strategy has been to reduce the risk across the range by raising cash and gilt levels, and by increasing diversification by introducing new asset classes, such as Infrastructure. We are aware that markets have been very strong for a long period of time and whilst runs like this do not die of old age, it is sensible to adjust the portfolios so that they are not fully exposed to the downside.

We have conducted a thorough review of all of the IMS portfolios, as we do each quarter, and this looked at both the asset allocation as well as the funds in which we invest. Having considered all of the options available to us we have made the unusual decision to make no changes on all of the portfolios bar the two income models for this quarter. Clearly this is preferable to making changes where none are needed and we have spent a great deal of time thinking about this decision.

It is important to remember the many levels of investment management that make up the IMS portfolios. We start with our asset allocations, then we select funds, and then we allow the fund managers to operate within their mandates and adjust their funds as they see fit. This means that although we may not be making any changes ourselves, there are always changes happening within the funds themselves.

By way of an example, we use M&G Global Macro Bond across the accumulation portfolios. It describes itself as “go-anywhere” and can invest in a wide range of markets and instruments. At the start of the quarter the fund held under 3% in money markets and at the last update this allocation had risen to over 20%. We have a preference for funds which take an active approach like this and are confident that with the changes we have made over the last 12 months, the portfolios remain well positioned.

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