Harwood
Wealth Management Group Ltd

Quarterly Update

Q3 2020

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INTRODUCTION

Three months ago, the commentary started with "The first quarter of 2020 will be remembered in history." Put succinctly Coronavirus was sweeping the world, global economies rapidly went into freefall and recessions hit most economies – almost immediately - as commerce basically stopped. In response stock markets experienced huge falls, the oil price (albeit only for a short time) went negative and both governments and Central Banks of many nations went into overdrive with stimulus packages worth trillions of dollars to stop economies stopping.

With this backdrop, who knew which way the economies of the world and the capital markets would react? A policy mistake could/would lead to a great depression. In April alone the UK economy registered a fall of over 20%. A number so large and unusual that in reality it just does not register properly when taking history as a guide. It was estimated that 40 million lost their jobs in less than 10 weeks in America. To put that into some degree of framing, the population of the country is a little over 320m and the unemployment rate went from less than 5% to about 15% (although this number could actually be much higher) as the economy ground to a halt. Closer to home, the furlough scheme put in place by the UK Government to help individuals and businesses now covers over 8.5 million people and although certain parts of the economy are opening up again, it will be a long, slow process until the economy is recovered. Thoughts relating to how all of this will be paid back are not front of mind, but taxes are likely to rise. As the now famous "R" numbers ebbs and flows and regional spikes cause concerns (and further lockdowns) we are not out of the woods yet.

There is still a great deal of uncertainty out there. Will the transportation and hotel / hospitality industries recover for instance? During the pandemic, Warren Buffett – widely regarded as the world's best investor (and one of the wealthiest men on the planet) threw in the towel and sold his entire exposure to airlines. Considering he owned 11% of Delta Airlines, 10% of American Airlines, 10% of Southwest Airlines and 9% of United Airlines that certainly tells you something. Will Social distancing remain and what will be the impacts on the pubs and restaurant industry? How will events that have mass gatherings fare? Will the High Street survive? Will I be able to get my hair cut?

Companies still do not have much transparency in their earnings or profits. Businesses will suffer and a number have already gone under including well-known names. At the moment, analysts cannot forecast properly and there will be bumps along the road and big bouts of volatility. The “new normal” will change habits. Corporations will have to adjust. The coronavirus is far from beaten – there still is no vaccine, although over 100 companies are investing heavily on finding one. Don’t be surprised if governments come back with further stimulus packages.

In response to the stimulus packages already announced, equity markets experienced a massive revival of spirits. They have “looked through the valley of despair” and don’t think things are all bad. Within the first quarter of the year, the US stock market witnessed its largest ever fall; during the second the US stock market saw its sharpest ever rise / recovery. Who ever said investing was boring?! There will be winners and losers as we look forward, and this is being witnessed in our daily lives. For instance, the CEO of Microsoft said in May over 2 years of digital transformation occurred in the last 2 months and the share of online commerce in the UK rose by over 11% in the last quarter from 16% as more undertake their shopping via the internet, and companies such as Zoom become household names. On the other hand, the High Street suffered massively and many well-known names entered administration. The shape of the economy is changing.

As this commentary started, so it will end: The second quarter of 2020 will also be remembered in history..

Sector Analysis

Top Performing **31/03/2020 - 30/06/2020**		**Top Performing** **YTD 2019 (30/06/2020)**	
Tech & Telecom	28.78%	Tech & Telecom	18.56%
North American Smaller Companies	26.89%	UK Index Linked Gilts	13.21%
European Smaller Companies	26.82%	China/Greater China	11.42%
Japanese Smaller Companies	26.03%	UK Gilts	9.93%
Asia Pacific Including Japan	22.03%	Asia Pacific Including Japan	4.84%
Worst Performing **31/03/2020 - 30/06/2020**		**Worst Performing** **YTD (30/06/2020)**	
UK Direct Property	-1.85%	UK Equity Income	-20.18%
Short Term Money Market	0.03%	UK All Companies	-17.60%
Standard Money Market	0.14%	UK Smaller Companies	-16.63%
UK Gilts	2.77%	Property Other	-11.31%
Targeted Absolute Return	4.28%	UK Equity & Bond Income	-7.72%

Data from FE fundinfo 2020, dates as above.

FIXED INCOME

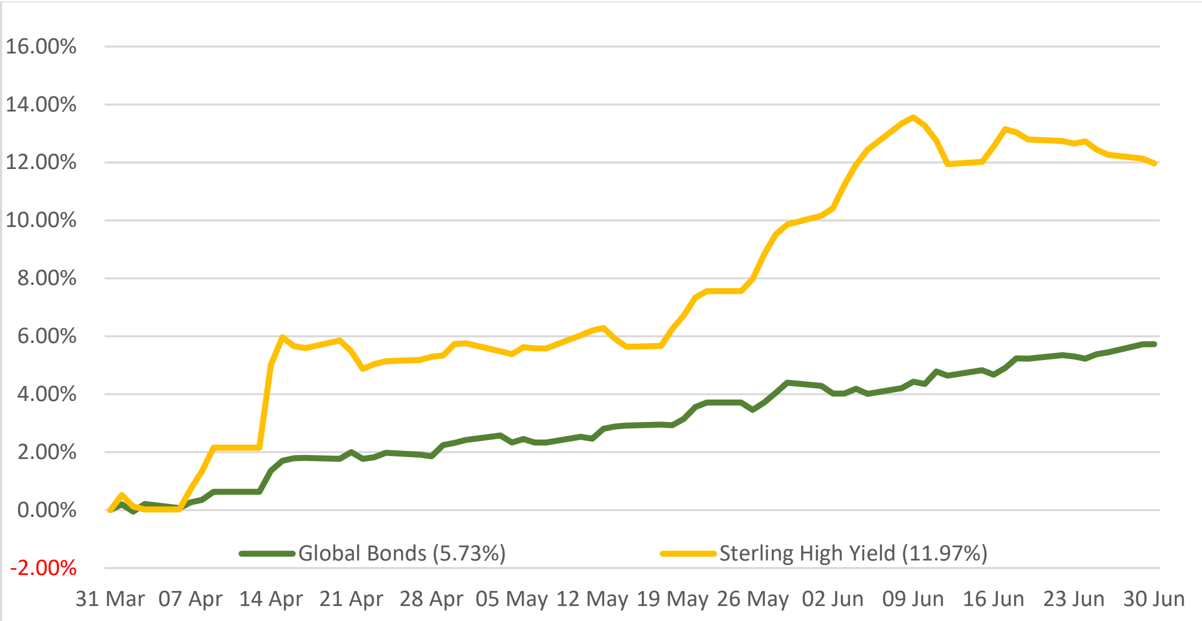
Sterling Bonds

Covid-19 shocked markets in the first quarter, but the second quarter has brought a swift reversal in fortunes as central banks and governments rode to the rescue, with coordinated action to cut interest rates and introduce other measures to support markets. In the UK, the Bank of England reduced interest rates to 0.1% and announced new plans for QE. The scope of the BoE's buying has been quite limited to date, with purchases limited to a narrow range of investment grade issues, but there is room for this to expand from the current level of ~3% to ~5-6%, which should provide a strong underpin to the market.

At the start of the quarter there was a considerable boost for fixed income when the US announced its own asset purchasing plans and indicated a willingness to include bonds of companies that have de-rated from investment grade to high yield, so-called 'fallen angels'. This proved to be instrumental in restoring investor confidence, allowing markets to re-open after the extreme illiquidity of March.
New bond issues began to come to market again in April, initially led by high quality businesses looking to shore up their balance sheets, but quickly followed by more economically sensitive businesses, including Carnival, the cruise operator, whose business has been very badly hit by the coronavirus crisis.

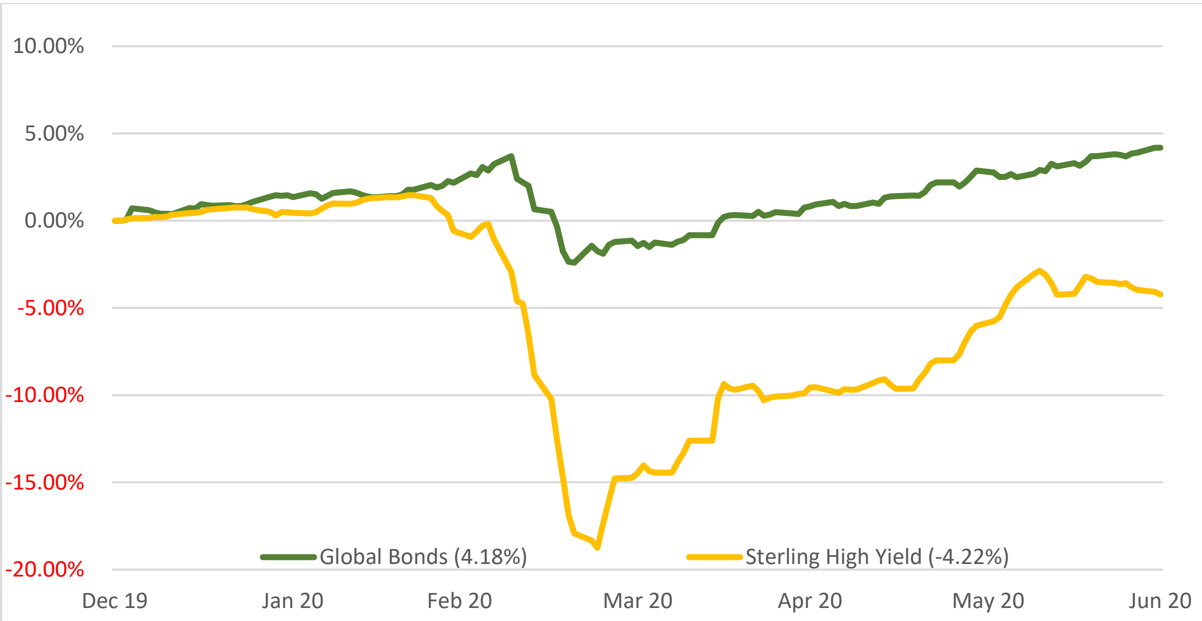
As risk appetite began to slowly return to the market, government bonds lagged and corporate bonds have fared better. The highest rated (AAA) part of the corporate bond market led, although the recovery in the BBB names, favoured by managers looking to deliver income, is also underway. Defaults have only just begun to come through and we expect to see these rise into the end of the year. Within high yield, the CCC rated names are likely to be most impacted, but the outlook looks particularly favourable for investment grade.

Sector comparison: Global Bonds and Sterling High Yield – 3 month performance



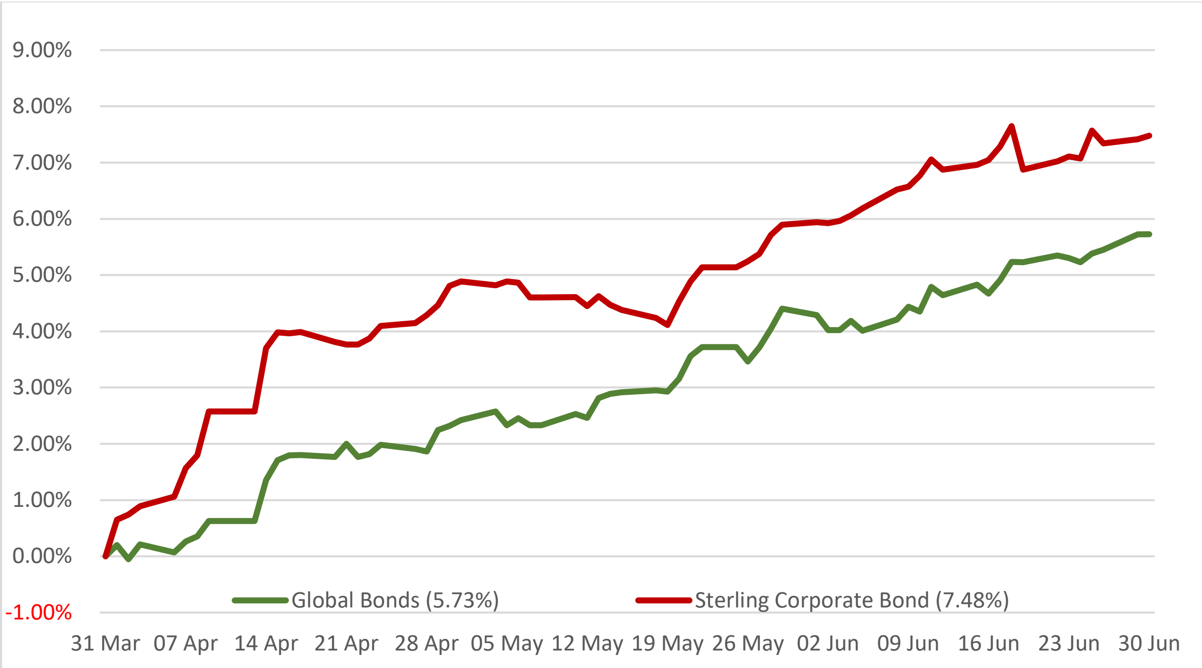
31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global Bonds and Sterling High Yield – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global Bonds and Sterling Corporate Bond – 3 month performance

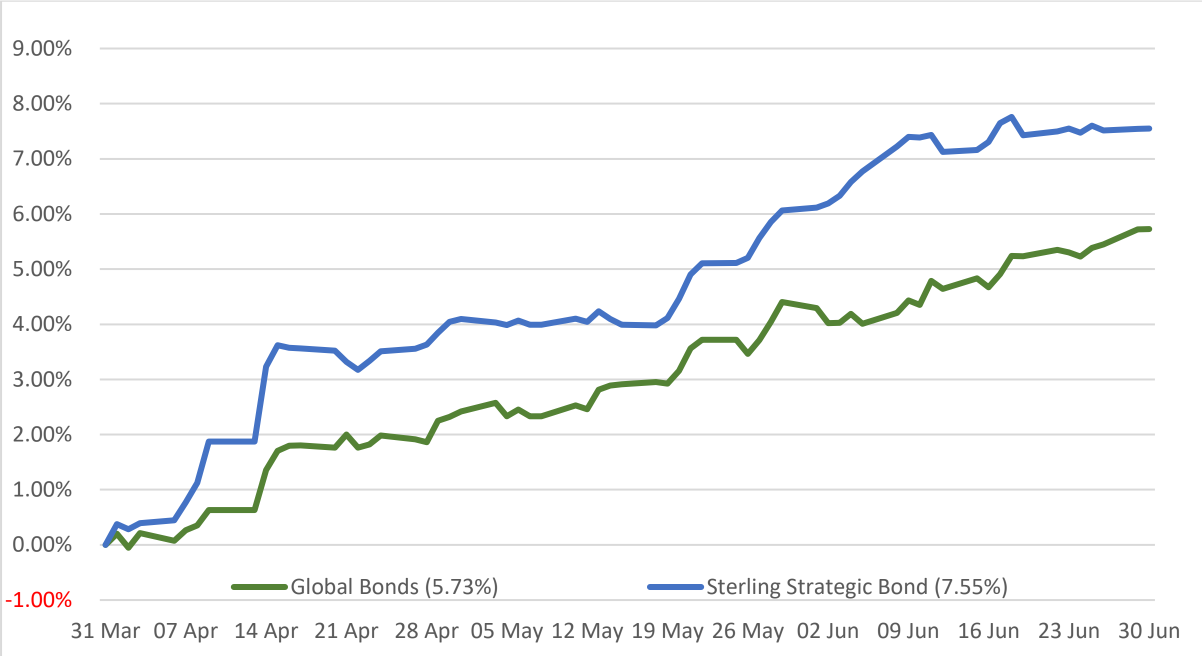


31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global Bonds and Sterling Corporate Bond – YTD performance

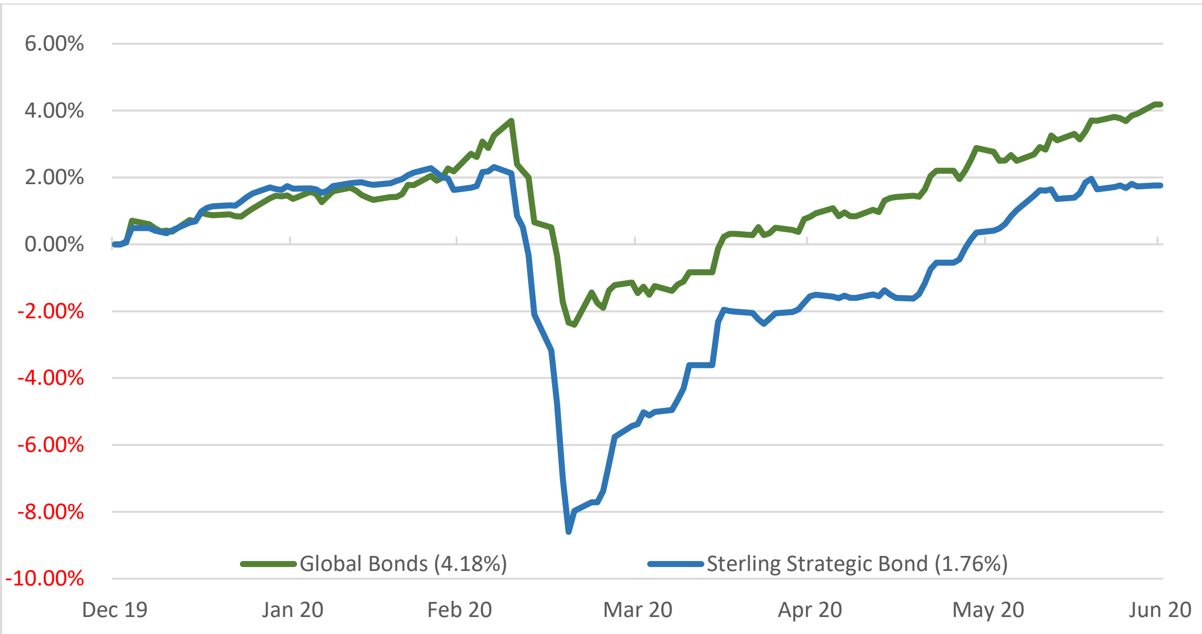
31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global Bonds and Sterling Strategic Bond – 3 month performance



31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global Bonds and Sterling Strategic Bond – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

Global Bonds

The economic impact of closing the world economy became increasingly apparent in April as some of the data released covering the previous month was the worst ever recorded. And yet, against this backdrop, financial markets bounced back from their March lows with many parts of the fixed income market delivering their best return in decades.

Helping to drive these returns were signs of the virus easing and central bank policy, whose extraordinary policies were able to be implemented rapidly. The US Federal Reserve's (Fed's) announcement of unlimited and open-ended Quantitative Easing (QE) in late March had helped to turn market sentiment. It then looked to push the bar further with an announcement in April that asset purchases would include high yield bonds helping to give further strength to the rally. In Europe, the European Central Bank continued its own QE programme, but stopped short of following the Fed to include high yield bonds in its asset purchases.

The rally in risk assets that began in late March continued during May and June. As the market became more optimistic, performance was skewed towards high yield and emerging market debt, which had until now lagged the recovery seen in investment grade markets. Two factors contributed to the ongoing rally: strong central bank support, and a continued slowing of Covid-19, which has led many countries to start exiting lockdown.

Despite this, default rates in the US, which has a high concentration of energy companies, have continued to rise with several energy companies filing for Chapter 11 bankruptcy, with rating agency Fitch stating that the US default rate was on course to hit a 10-year high.

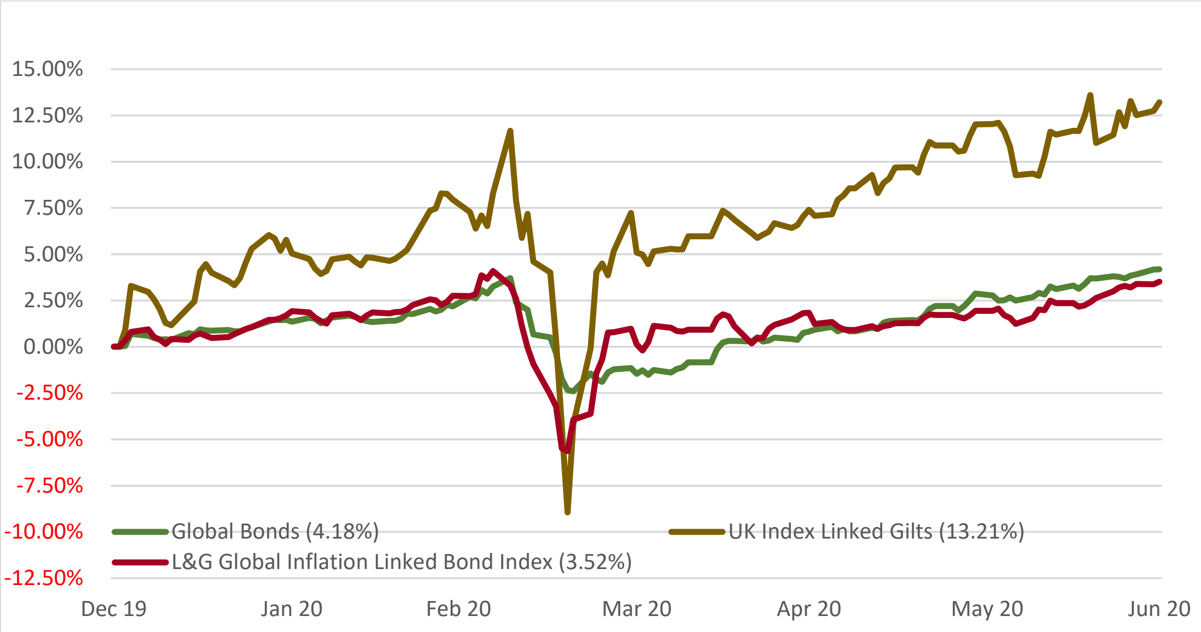
Sector comparison: Global Bonds and Short Term Money Market – 3 month performance

31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global Bonds and L&G Global Inflation Linked Bond Index – YTD performance

31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global Bonds, UK Index Linked Gilts and L&G Global Inflation Linked Bond Index – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

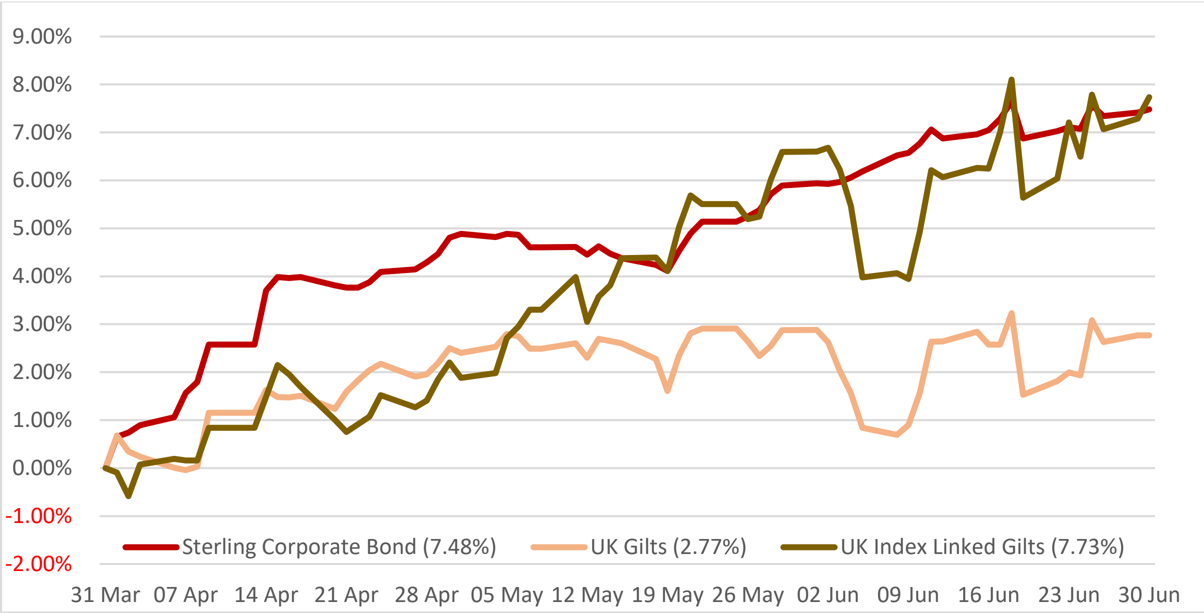
UK Gilts

The economic theory of supply and demand creating an equilibrium price doesn't seem to be working in these unusual times. Typically, if supply rises (i.e. the Bank of England issue more debt) and there isn't the demand, then the price falls and the corresponding income rises until there is a level at which it becomes attractive again. The twist in the tail this time (although in reality it has been going on for a decade – since QE was introduced after the Global Financial Crisis) is the government has the ability to "print" money and therefore has the ability to soak up all the supply and it has been doing so to keep the economy's head above water. The printed money is being used to help provide funds to furloughed staff, to cover revenues councils have lost due to business rates not being paid, to help banks out who are helping customers out with mortgage deferments and so on.

Gilts, as an asset class are a relatively secure form of investing. Governments of reputable countries are unlikely to go bust, and being as gilts generally have a finite life span, the biggest risk to capital and spending power tends to be the future path of interest rates and inflation. It's probably a safe assumption that neither interest rates, nor inflation are heading significantly higher for quite some time, and therefore, the yield offered on sovereign bonds at the moment is commensurately low, but investing in sovereign bonds is not risk-free.

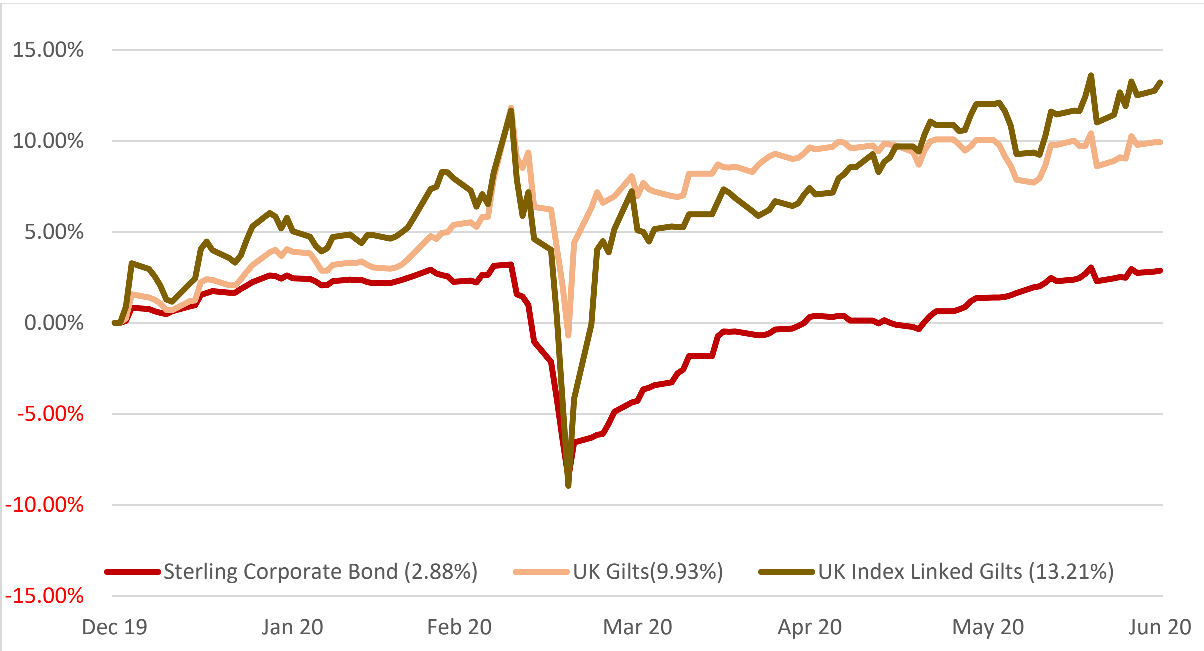
Due to their finite life, it is possible to invest across a range of gilts (known as the curve) and in essence, the longer you lend money to the government, the more income you should demand from them in interest payments. Positive returns have been made from investing across the curve, in the second quarter of the year, although this hasn't been achieved without high degrees of price volatility. Gilts are regularly used as an economic safe harbour when storms arrive and therefore it is no surprise that returns have been positive. It is widely accepted that the gilt market is very sensitive to economic activity.

Sector comparison: Sterling Corporate Bond, UK Index Linked Gilts and UK Gilts – 3 month performance



31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Sterling Corporate Bond, UK Index Linked Gilts and UK Gilts – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

DEVELOPED MARKET EQUITIES

UK

With Covid-19 having a greater impact in the UK than in most other similar sized economies, the main indices have unperformed world markets. Smaller, more nimble companies have done better but on the whole, UK equities have not enjoyed the same recovery which has remarkably seen many global indices make back all of their losses from earlier in the year.

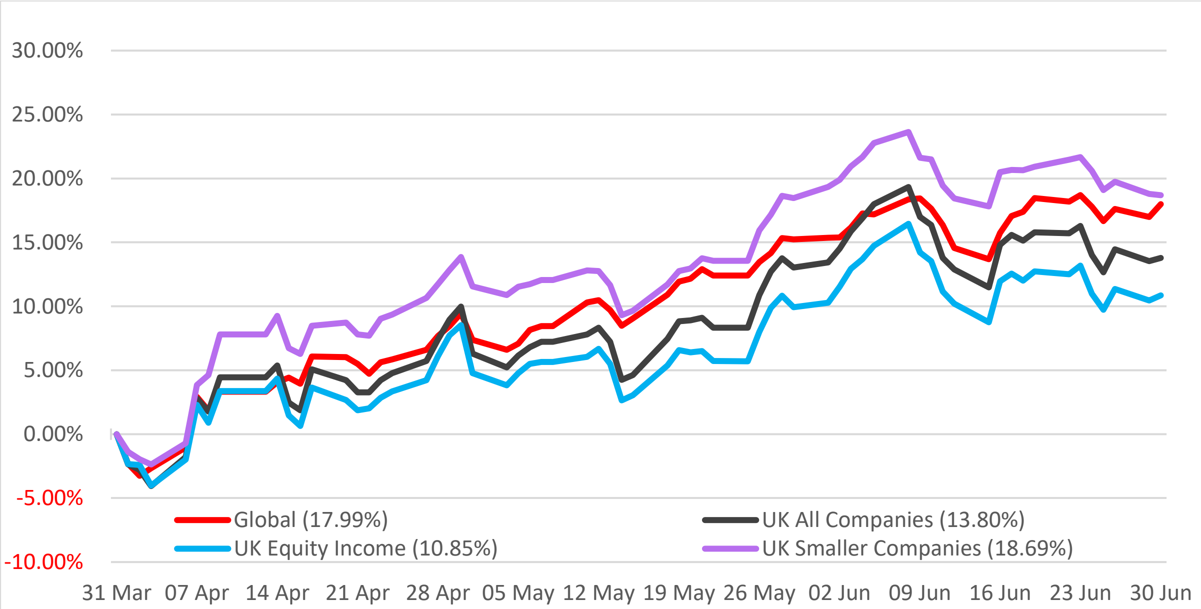
The response of the UK government and the Bank of England (BoE) has been robust and over the last quarter they have added to existing measures, widening the job retention scheme and announcing more support for struggling UK firms. The government's fiscal watchdog has forecast that the increased public spending and tax cuts already announced will cost over £130bn in the current financial year. As the country continues its efforts to reopen the economy, both the chancellor and the BoE are waiting to see how this impacts on the recovery before taking any further action.

The UK's ability to recover as quickly as its peers has not been helped by the weakness in sterling which has struggled to regain ground following the referendum on leaving the EU. In a report issued in June, Bank of America suggested the pound had taken on the characteristics of a liquid emerging market currency, rather than one from a leading economy. In their view this is not a temporary situation but an evolution into "a currency that resembles the underlying reality of the British economy: small and shrinking with a growing dual deficit problem." This is based on the volatility in the value which they say has more closely resembled the Mexican Peso than the US dollar, and that whilst other countries have seen their currencies settle since the start of the crisis, sterling has continued to struggle due to concerns about Brexit-related uncertainty and a rapidly rising deficit.

From an income perspective, one impact of the pandemic has been felt most strongly in the dividends paid by UK companies. Many have removed payouts entirely while some have reduced them, often dramatically. This included Shell which cut its dividend for the first time since the 1940's but even before this, the cancellation of payments from UK banks (as requested by their regulator) lead to estimates of a total reduction ranging from a 30%-50% in the annual payout from the FTSE100. On their own, the banks represented almost 10% of payments, with Shell and BP accounting for another 30%.

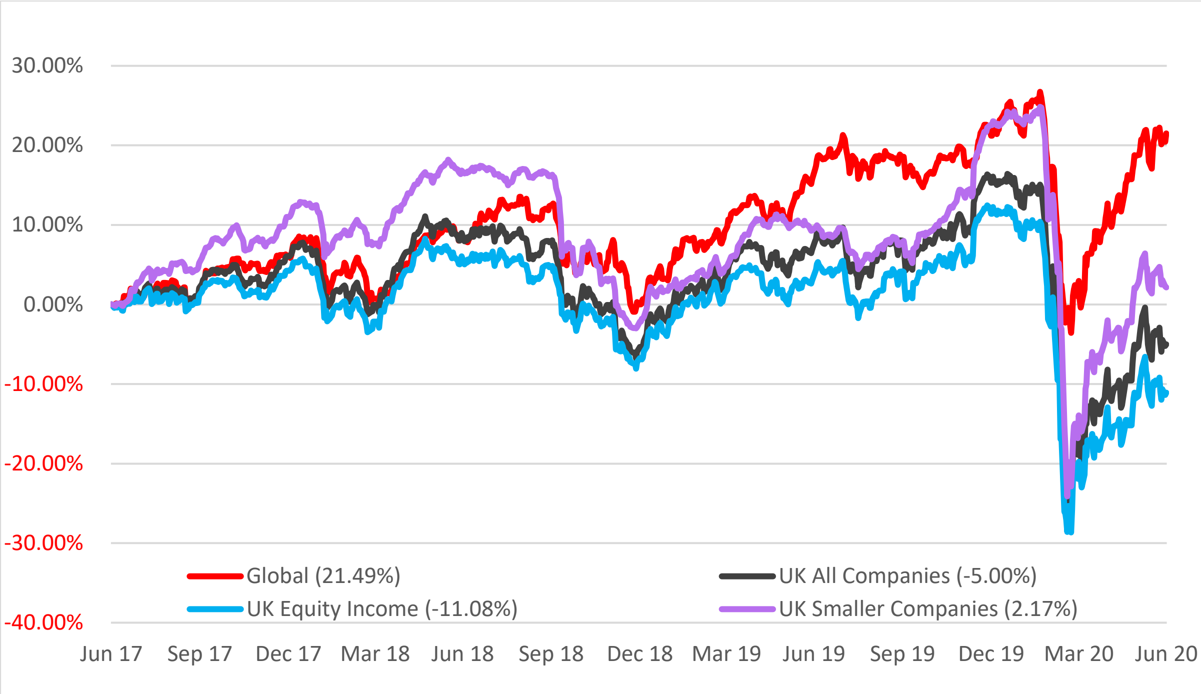
However, despite these cuts, with Gilt yields crumbling in the face of near-zero interest rates, UK equities have recently enjoyed the greatest spread in yields compared to 10-year Gilts since the First World War. At times like this it is critical that we select fund managers who are proactive in their investment decisions as there are many companies which continue to pay healthy dividends.

Sector comparison: Global, UK Equity Income, UK All Companies and UK Smaller Companies – 3 month performance



31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global, UK Equity Income, UK All Companies and UK Smaller Companies – 3 year performance



30/06/2017 – 30/06/2020 Data from FE fundinfo 2020

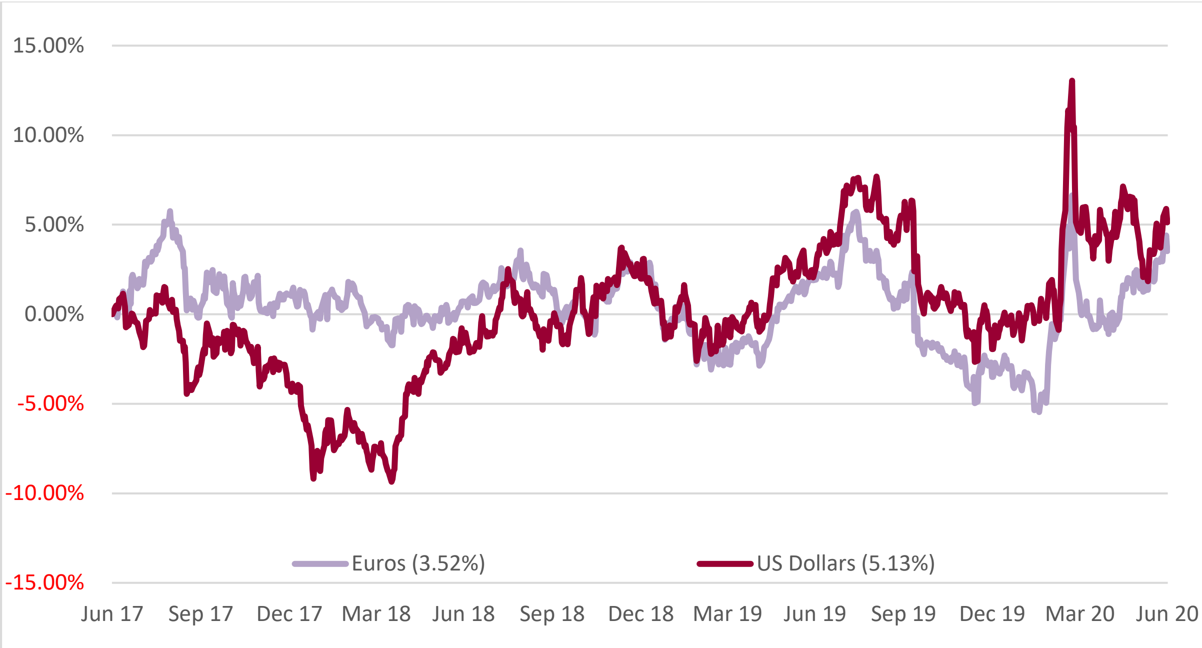
Europe

Equities rebounded strongly in the second quarter, and the European market was no exception with gains made in each of the three calendar months. Underpinning these gains, is a vast amount of monetary stimulus with the region's QE programme expanded to €1.35trn and due to run for another year. Further support has come from individual governments in the shape of fiscal stimulus. The German response, which is equivalent to 12% of GDP, is notable in terms of its scale and Germany's economic importance in the region, but also because in the wake of the GFC Germany was particularly wary when it came to loosening the purse strings. The same will not be said after the current crisis.

In terms of sectors, the initial recovery was strongest in healthcare (traditionally a more defensive sector) and consumer discretionary but as we moved through the quarter more economically sensitive parts of the market began to perform with financials and industrials strong in June. IT was strong throughout. Clearly investors have been reassured by the strength of the stimulus response and the improvements in economic data as the easing of lockdown conditions began, making them willing to look beyond through the crisis and focus on what lies beyond.

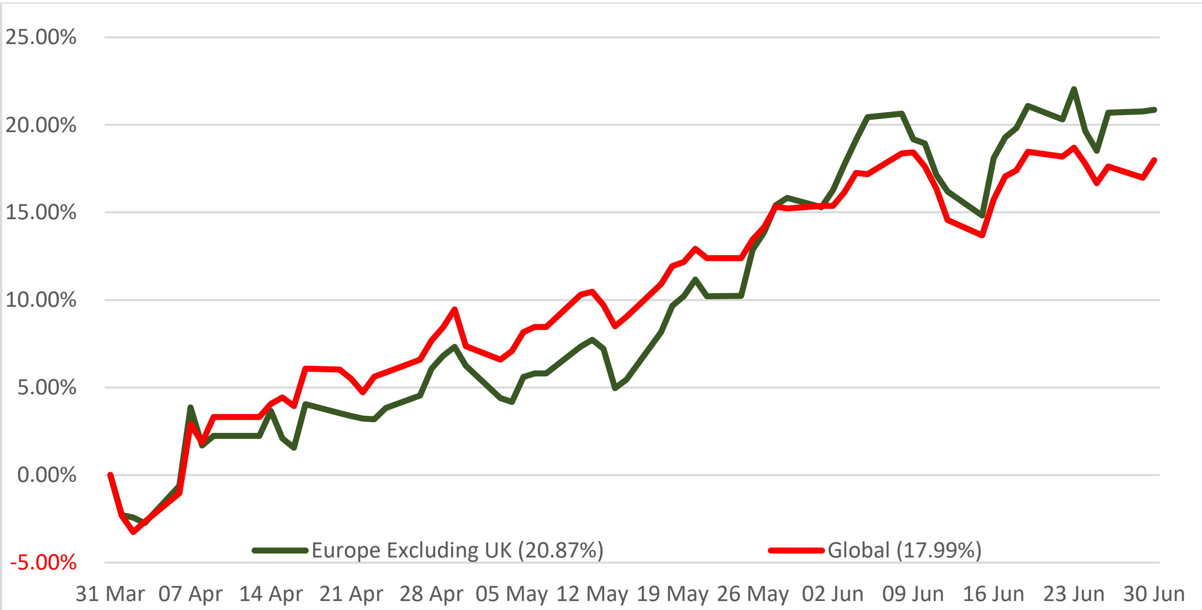
One significant issue during the quarter was the news emerging around Wirecard, a payment processing company. Auditors were unable to verify €1.9bn in cash, which appears to be 'missing' and as allegations of fraud and money laundering began to surface the company's share price collapsed. The case has been embarrassing for the German authorities, which had backed Wirecard by preventing short selling in the stock and launched legal proceedings against the FT, which first exposed the scandal back in January. Wirecard was held by a number of European growth funds popular with UK investors including high profile fund managers such as Alexander Darwall (Devon), Richard Pease (Crux) and Carlos Moreno (Miton).

Sector comparison: US Dollar and Euros – 3 year performance



30/06/2017 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global and Europe Excluding UK – 3 month performance



31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

US

The last three months has seen a remarkable different story in the US when comparing the economy to the stock market. While economic data has been grim with millions of Americans filing for unemployment, equity markets have shown resilience and in April recorded their best monthly gain since January 1987, with the S&P 500 ending the quarter back at levels seen at the start of the year. The rally was supported once more by technology stocks, with Apple and Amazon reporting higher sales as consumers increasingly turned to home delivery and streaming entertainment as most of the country remained on lockdown, while Microsoft became ever increasingly used while we work from home.

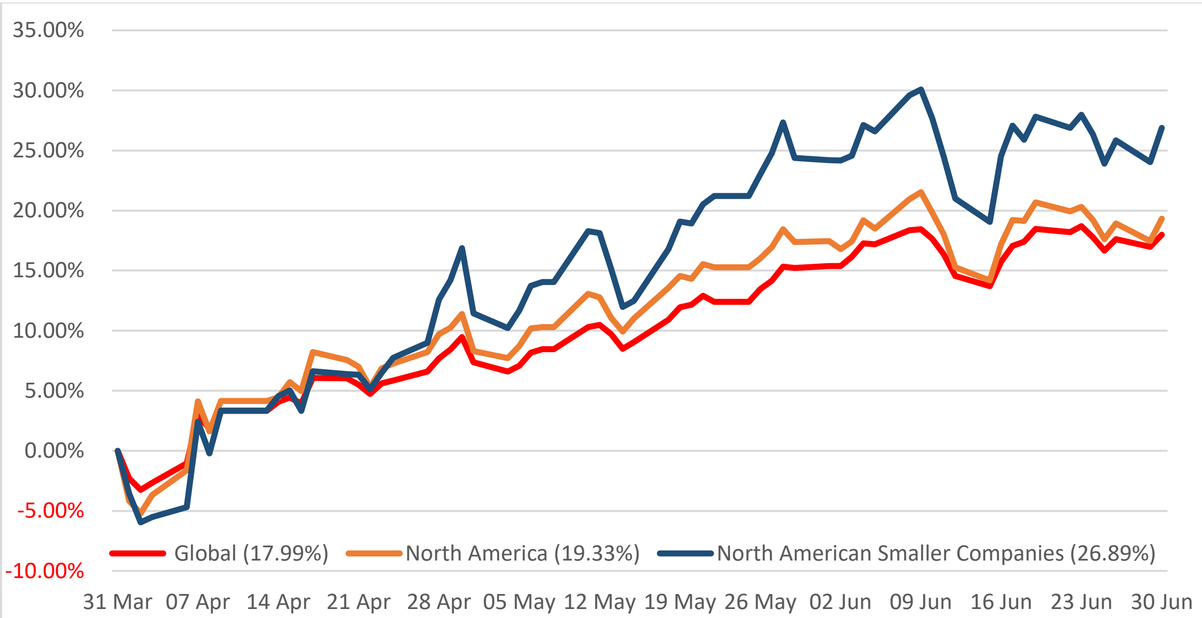
The effect of trillions of dollars being pumped into the economy and financial markets by the Federal government and central bank, along with signs that the lockdown measures may be having some success in reducing the rates of infection added to the optimism in equity markets. However, the US economy is facing a massive contraction, leading to significant corporate earnings downgrades for many companies. For the first three months of this year the US economy shrank by an annualised rate of 4.8%, its steepest decline since the last recession and ending a decade of near constant economic growth.

Over the last three months an unprecedented 40 million Americans have lost their jobs – the rate of losses means US unemployment is on track to reach levels not seen since the Great Depression of the 1930s. With so many workers losing their jobs, consumer spending, the main engine of the US economy, nosedived to record its steepest monthly decline since records began in 1959. By contrast, the US personal savings rate jumped to its highest level since 1981. Households cut back on purchases of big-ticket items, such as cars, as well as on services, for example, restaurant, hotels and sporting events.

However, as US equity markets have advanced higher and with company earnings under pressure due to the lockdown, US stock valuations - as measured by the S&P500 index 12-month forward price earnings ratio - are currently at their highest level in two decades.

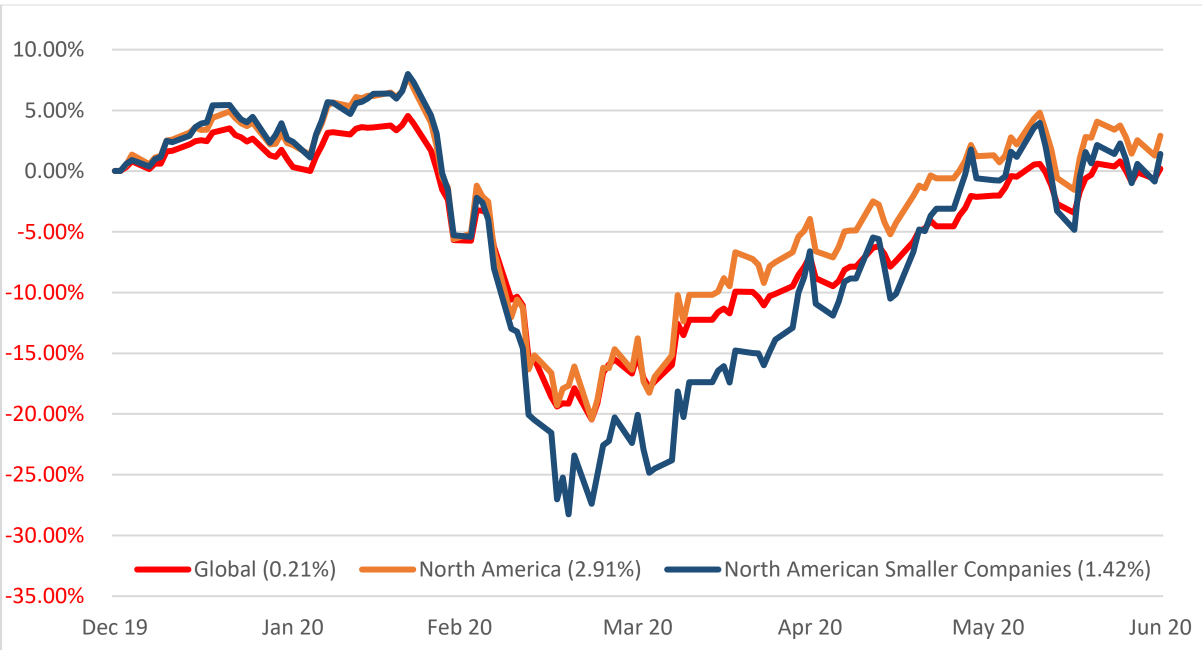
In other developments tension between the US and China rose in light of Beijing's intent to insert new legal provisions into Hong Kong's constitution, including measures aimed at curbing secession, foreign interference and sedition. Closer to home, civil unrest broke out across major US cities towards the end of May.

Sector comparison: Global, North America, North American Smaller Companies – 3 month performance



31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global, North America and North American Smaller Companies – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

Japan

In the second quarter, Japan was one of the weaker markets in the Asia Pacific region, partly due to a number of factors that worked against it. For instance, Japan isn't blessed with many natural resources, and with both commodity prices and the oil market rising from the extremes witnessed in the first quarter, this would have had a detrimental effect on the country and would have acted as an anchor on profitability. Second, although the cases related to Covid-19 were not as high as feared, the measured enforced by the government closed down many businesses and forced individuals to stay home. Enhanced measures (including a national state of emergency) were brought to the country in April which extended until the end of May.

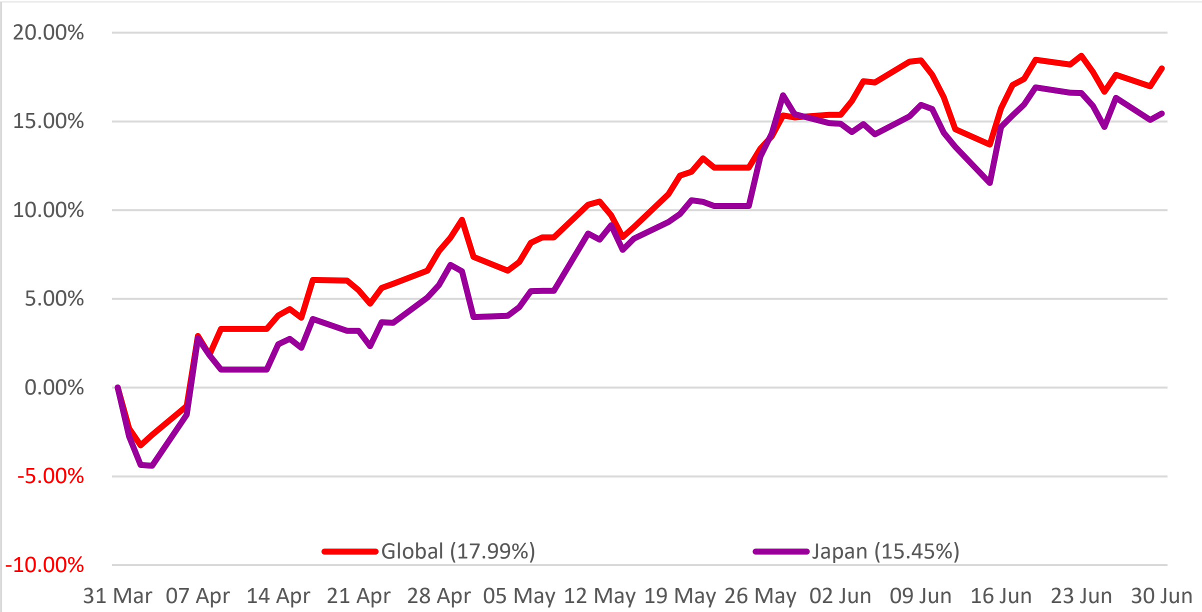
Japanese businesses typically run much more conservative balance sheets compared to the West and this should reduce the number of corporate casualties and in the same vein, Japanese individuals – also very conservative when it comes to their personal balance sheets – increased their savings. Arguably, when things get better, Japan could well be in a position to benefit….

The Bank of Japan and the Abe led government initiated a number of support packages to prop up the economy; another round is also slated for later this year, although forecasts for GDP this year have been revised down again to c-3% (although compared to a number of other major global economies, this doesn't seem too bad).

The country really doesn't have any interest rate cuts left should there be a second wave – it already operates with negative interest rates which are unlikely to fall further, so economic policy changes would have to come from the fiscal (ie taxation) side. Prime Minister Abe believes they have plenty of opportunities in this space though should they be needed.

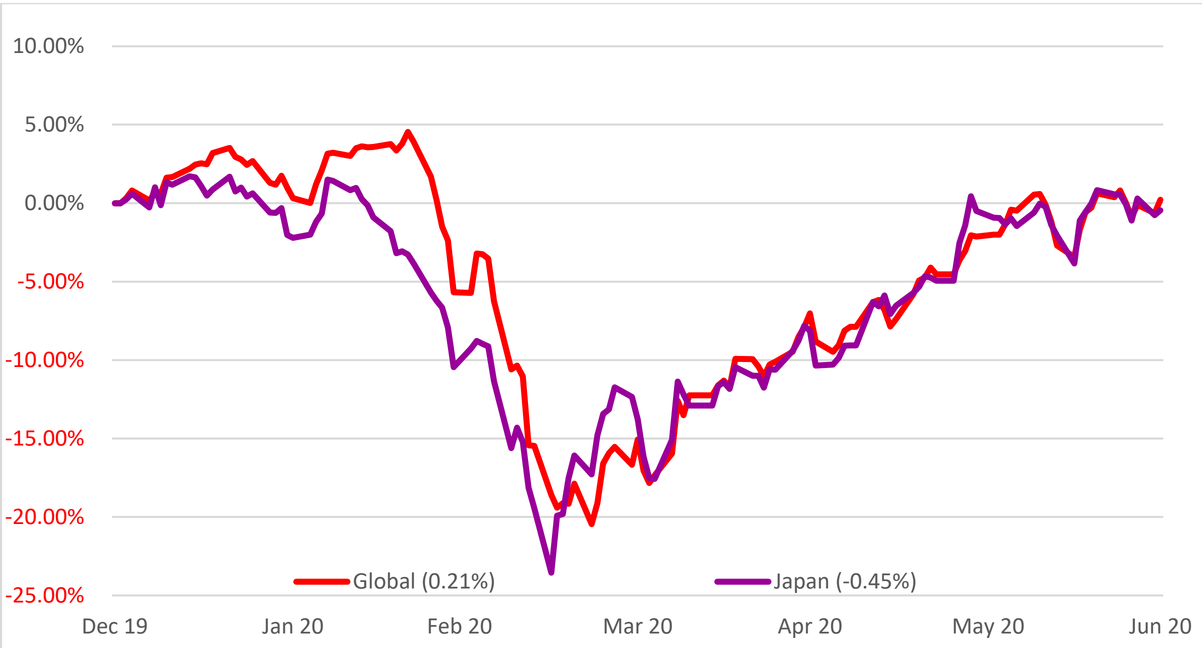
Many forecasters are suggesting the Japanese economy will transform post the fallout from the corona-crisis. The population in the country is falling and It is also one of the oldest in the world. Future corporate investment is likely to be significant in robotics and automation for instance and Japan possesses some of the leading businesses globally in this space. Assuming Japan isn't alone in wanting to spend on robotics and automation, this could be a boon for the country.

Sector comparison: Global and Japan – 3 month performance



31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global and Japan – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

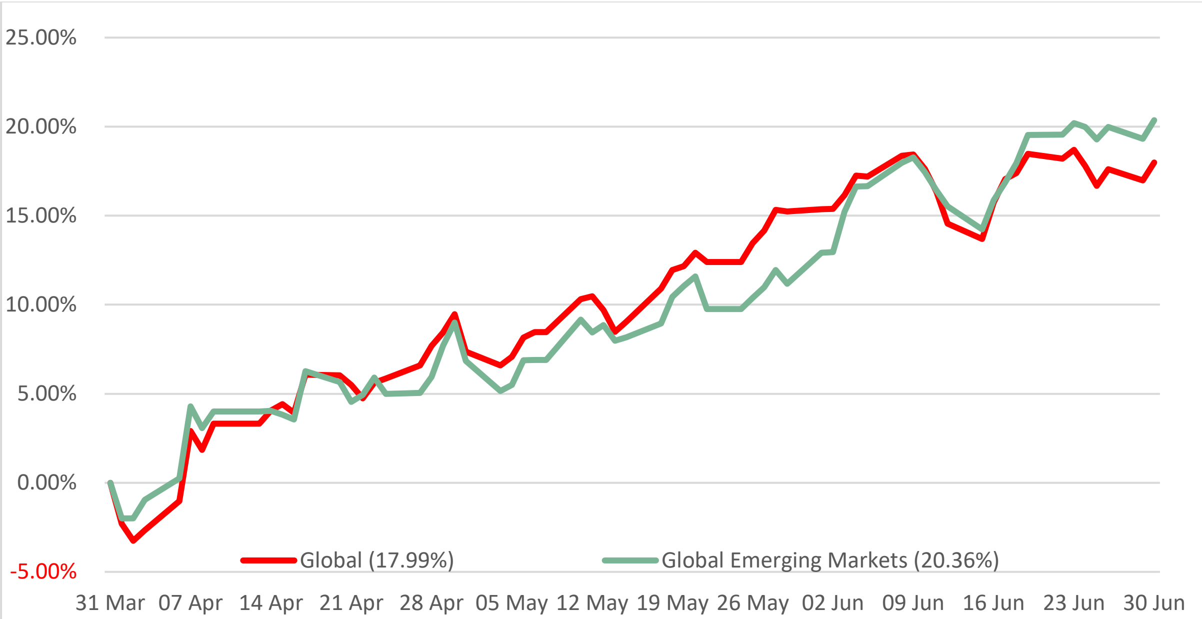
EMERGING MARKETS

The economic crisis caused by Covid-19 has been extreme and unusual in many ways. One example of this is that it did not affect the usually more volatile emerging market economies as much as it did their western counterparts during the initial reaction to the pandemic. Some of this can be put down to their experiences with other respiratory diseases such as SARS which meant that they acted much more rapidly, and with greater action. Of course, with the sector including a very broad range of economies, there was a wide variation in the level of impact.

Since the global recovery took hold just before the quarter began, emerging markets have slightly lagged behind countries like the US and those in northern Europe. To a large degree this is because emerging market economies face a distinct set of challenges. One major factor is that many rely very heavily on tourism and with international flights effectively falling to zero as the crisis hit, so did visitor numbers. It is also the case that many developing economies have a reliance on migrant labour and casual, informal activities which are greatly impacted by travel restrictions as well as fears about the virus. Another aspect is the fall in oil prices which has been a particular issue for those economies built around the export of the commodity which have faced shutting down production or potentially selling at a loss.

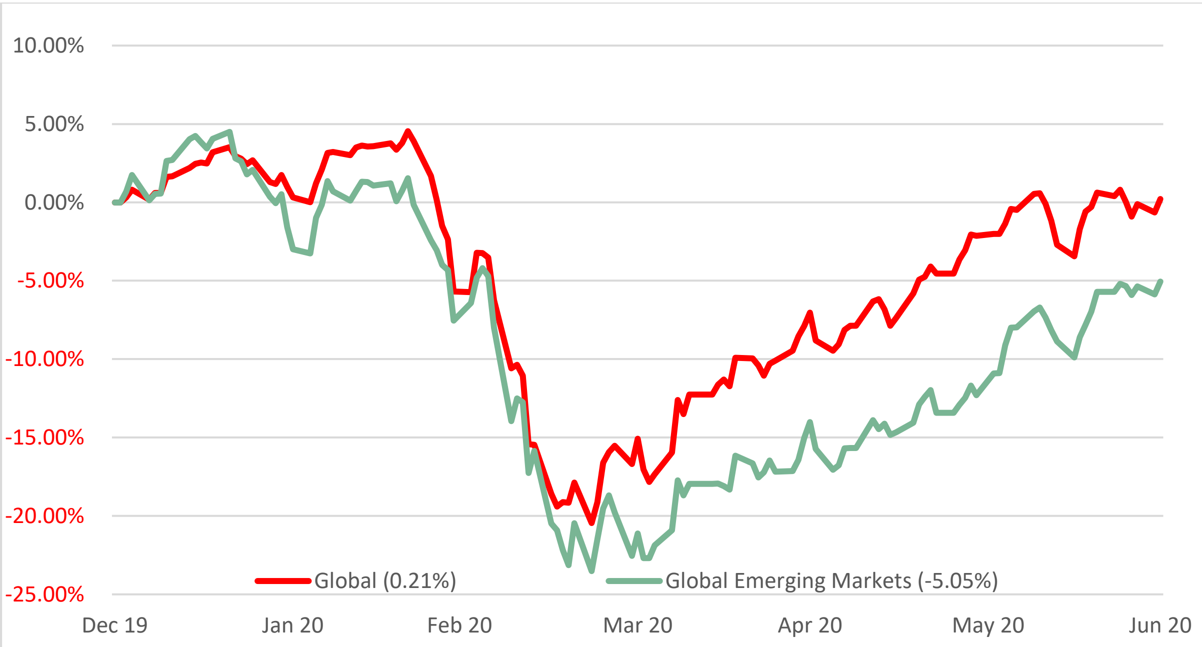
A further issue is that emerging markets often do not have the ability to issue the giant stimulus packages that many countries have put in place to protect their economies. Despite this, many emerging counties are investment grade rated, or are close to, and have shown the ability to sensibly manage their finances. Those with strong central banks will be able to provide sufficient liquidity to prevent a surge in inflation which would hinder their chances of a relatively rapid recovery. This makes a strong argument for the use of active rather than passive strategies in this area as this should allow managers to use their local knowledge to seek out regions and companies that can prosper despite these difficult conditions.

Sector comparison: Global and Global Emerging Markets – 3 month performance



31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global and Global Emerging Markets – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

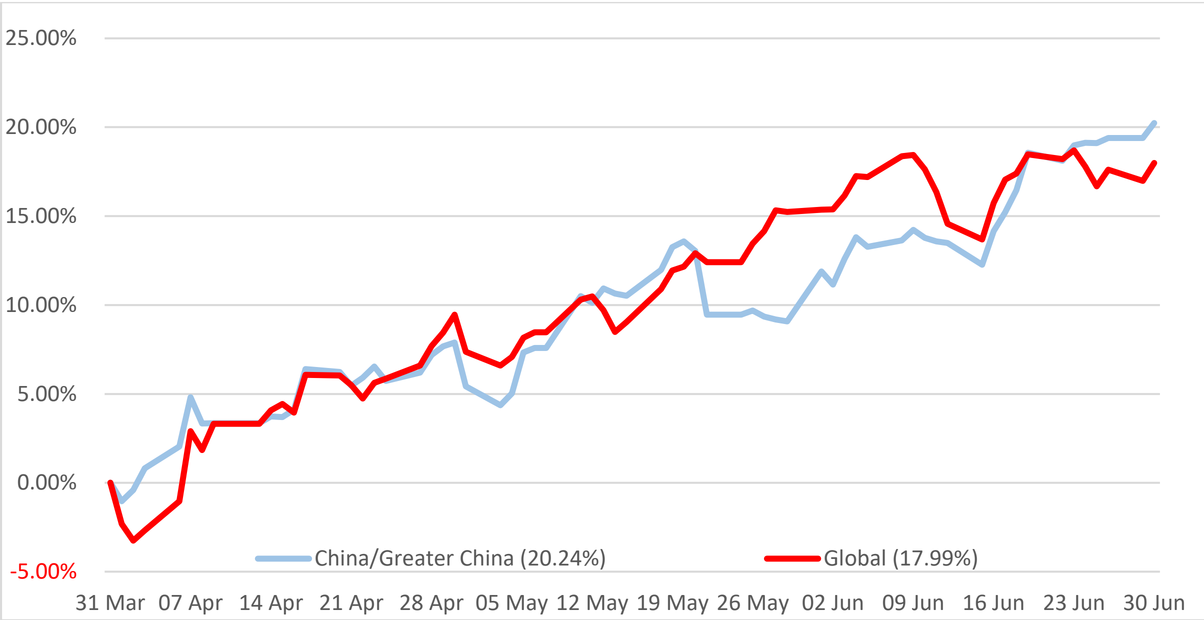
ASIA PACIFIC/CHINA

In much the same way as the broader emerging market sector, China and other Asia Pacific economies have enjoyed a strong recovery since the peak of the crisis in March. China also benefitted by falling less than other economies thanks to their decisiveness in imposing harsh restrictions to slow the spread of the virus in conjunction with a rapid deployment of stimulus measures. A spike in cases towards the end of the quarter is cause for concern, however, not just for China, but also for what it might mean for other countries.

China recently announced that it is scrapping its economic growth target for 2020. This is the first time since 1990 (when records began) that it has not set a growth goal and it coincided with the news that their economy had fallen by 6.8% in the first quarter of the year. Although the country has been successfully evolving from a reliance on external demand to one more based on the internal consumer, exports still make up a large part of their economy and in this respect the outlook for China and the wider region has been undermined by the increasingly aggressive rhetoric from Donald Trump.

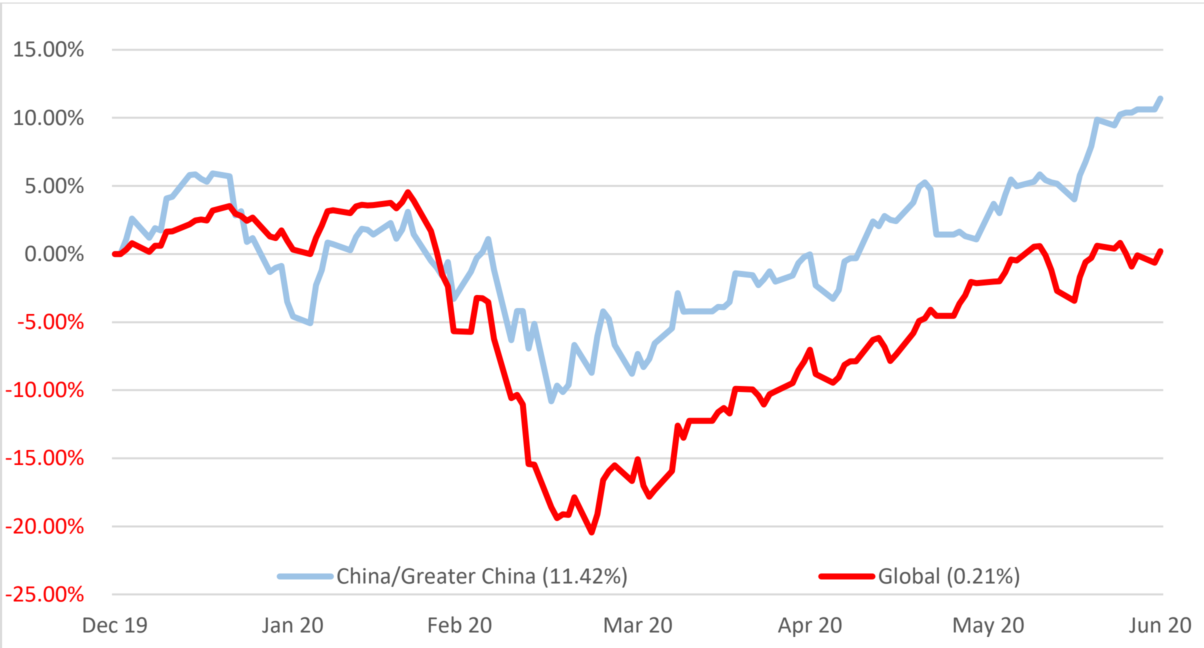
The US president has stepped up his war of words (and actions) and having imposed controls on the use of foreign-supplied parts in US electricity infrastructure in May, he doubled down by tightening controls that specifically target Huawei over concerns about their links to the Chinese government. As he seeks a second term, it appears that Trump is intent on using these fears to ramp up the nationalist sentiment that was so successful for him at the last election. This has the potential to not only undermine much of the work that went into reversing the negative effects of the original trade war but also hinder the international cooperation that could be essential in the fight against the virus.

Sector comparison: Global and China/Greater China – 3 month performance



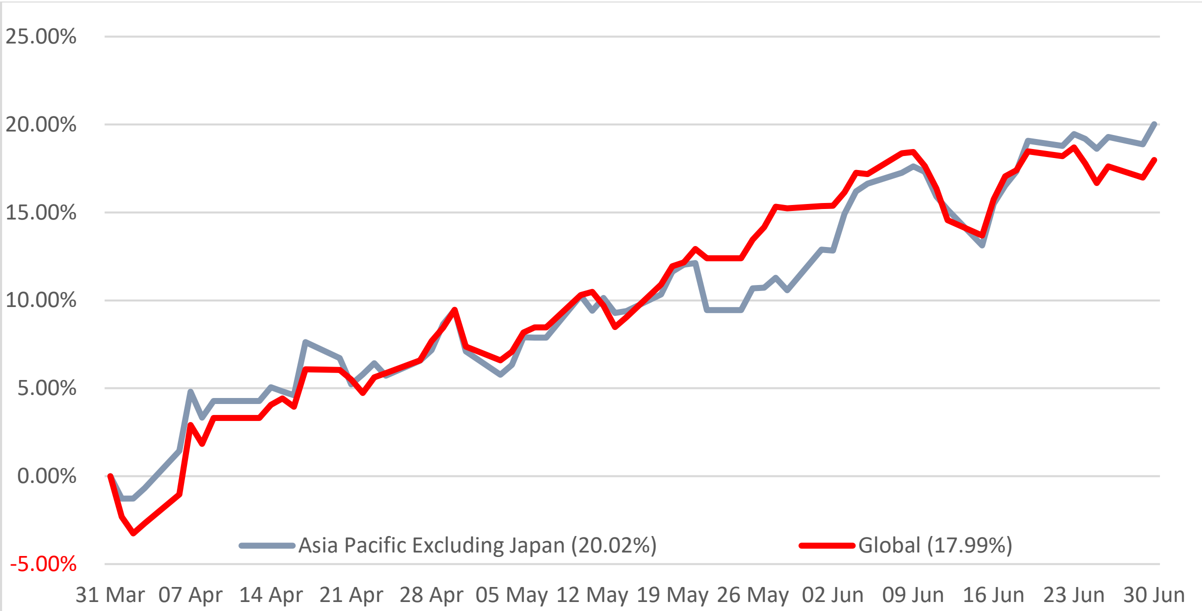
31/03/2020 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global and China/Greater China – YTD performance



31/12/2019 – 30/06/2020 Data from FE fundinfo 2020

Sector comparison: Global and Asia Pacific Excluding Japan – 3 month performance



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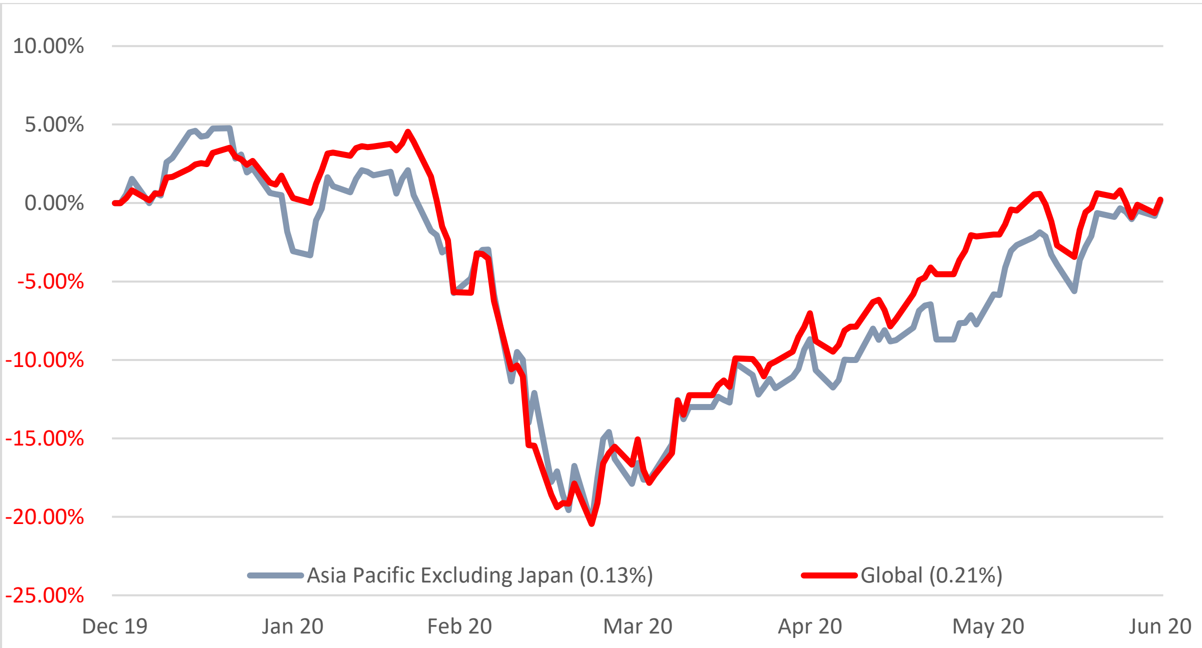
Sector comparison: Global and Asia Pacific Excluding Japan – YTD performance



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COMMODITIES

Like many other risk assets, commodity prices have recovered from their extreme lows seen in March. While it was positive quarter for oil prices, it was also an extremely volatile period. In April, the West Texas Intermediate, the benchmark for US oil, turned negative for the first time in history as May futures contracts came up for expiry. However, as countries began to emerge from lockdown, oil prices continued to strengthen. By the end of the quarter, the price of West Texas Intermediate Crude was up to $40 a barrel, doubling in price over the quarter and up over 400% since the lows of $9 a barrel hit during April.

It was a better quarter for investors in oil and gas companies, as energy was the best performing sector in the S&P 500 index in April and rallied from the extreme lows in March. However, year-to-date, the energy sector remains rooted to the bottom still.

The price of Gold continued to rise over the quarter and provided a positive return, although most of the return came in the first few weeks and then range trading thereafter, before finishing the quarter at $1791, up 14%. Silver, which had registered heavy losses in the first quarter, had a strong second quarter and was up 30%. On the back of this, investors in mining companies, particularly those invested in gold miners, saw strong returns over the period by rising over 50%.

ALTERNATIVE STRATEGIES

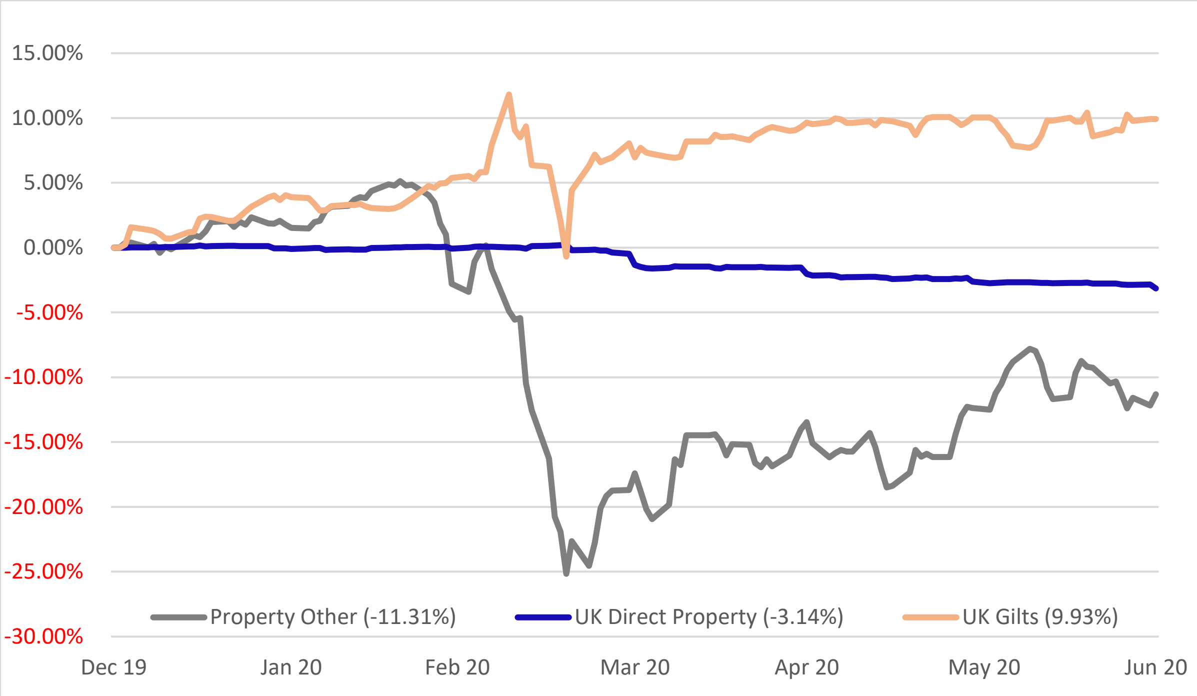
UK Direct Property

The financial, economic, social, corporate and medical effects of Covid-19 (along with many other factors) are likely to be felt for a long time to come as the world starts to adapt to “the new normal”. The property market is feeling effects too – this isn’t an equity, debt, cash or commodity story only. Social distancing is wreaking havoc on many parts of the property market. As the virus swept across the country, only essential business (read “supermarkets” and “pharmacies”) on the high street stayed open whilst offices, factories, industrial units and leisure facilities were forced to close. As at the end of June you still cannot get a pint, go for a swim and workout, get your hair cut, or take a loved one out and enjoy a meal in a local restaurant, whilst many stores that have re-opened are doing so with limited staff numbers, enforced queuing and other constraints that didn’t exist only 4 months ago….

This “new normal” will change employees and employers perceptions and realities of what “work” is when it comes to how businesses operate going forward. With millions furloughed and millions more working from home, it makes sense that managers will review their needs and demands for property – including office space for instance. Social distancing has forced alternative ways of working. Commuting is very difficult if you rely on public transport for instance.

It is not surprising the property market has been hurt significantly in the second quarter, and first half of this year. Most open-ended bricks and mortar property funds have been suspended for the entire quarter as “material uncertainty” clauses have made it difficult for the valuers to be able to put a true price on the portfolio of properties in the funds. It makes sales and purchase transactions difficult to proceed. With uncertainty surrounding transparency of pricing and uncertainty of rent collection, the property market has really felt the strain. According to many sources, parts of the market will not be able to price correctly for several more months to come.

Sector comparison: Property Other, UK Gilts and UK Direct Property – YTD performance



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Cash / Money Markets

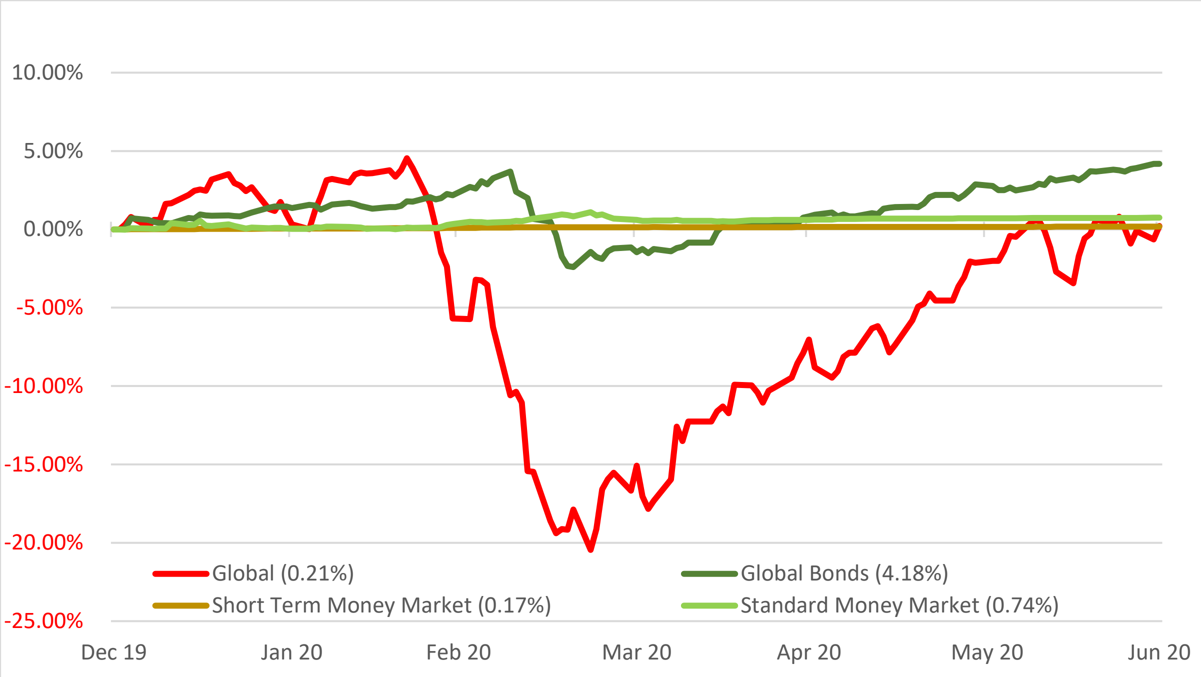
This sector experienced the absolute inverse of the conditions from the previous quarter; where money market assets provided a critical stabilising factor in the first three months of the year, they have trailed world markets since April. Of course, this should not be taken as a criticism, the purpose of the sector is to act as a diversifier to help dampen the effects of spikes in volatility and it has more than achieved this goal.

The greatest challenge ahead is what the Bank of England decide to do about interest rates. With the rate of inflation in April falling to 0.8%, almost half of the 1.5% in March, the Bank will be keen to correct an inflation level that is well below their 2% target. If they decide to take action by introducing negative interest rates for the first time in their history it will further reduce the already low yields in the sector.

The issue for the bank is that conditions are obviously far from usual and they won't want to take drastic action if they think that the situation will improve in a relatively short timeframe. This was certainly the case at their latest policy meeting when they left interest rates at 0.1% on the view that the economic damage caused by the pandemic may be less severe than they had feared.

In assessing our allocations to this sector we need to consider the benefits it brings within a diversified portfolio, and balance the understanding of its potential to reduce overall returns with our view on the outlook for world markets as we head into the second half of the year.

Sector comparison: Global, Short Term Money Market, Global Bonds and Standard Money Market – YTD performance



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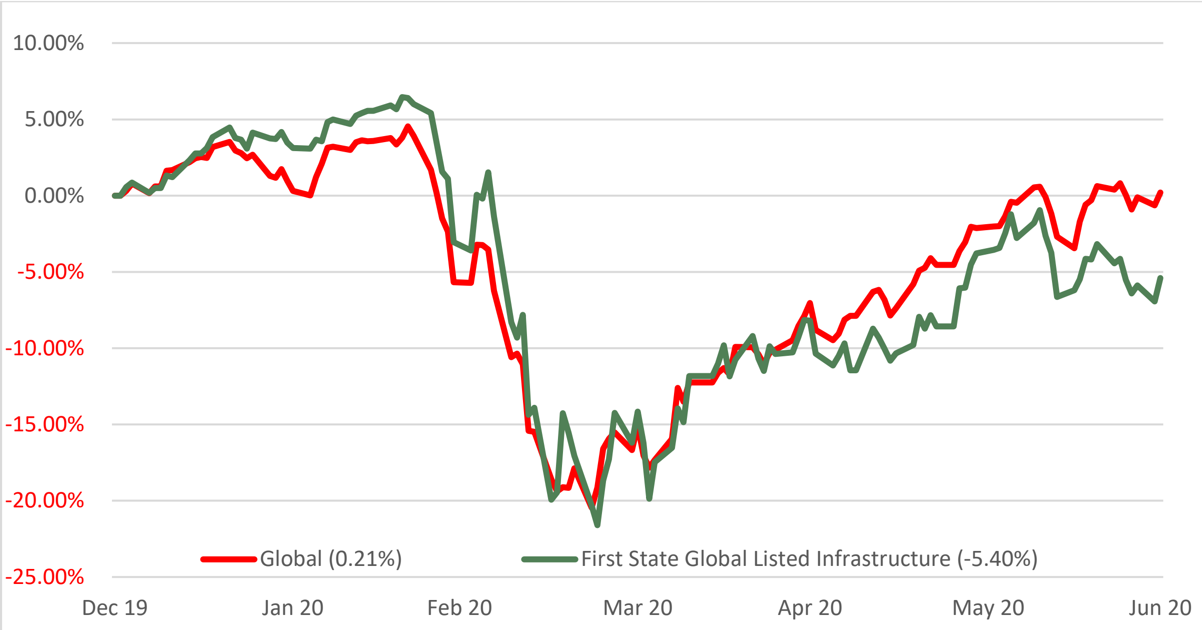
<u>Infrastructure</u>

The infrastructure market has been hit – quite hard – by the global pandemic that is Covid-19. Airports have pretty much shut for instance; the use of railways have fallen dramatically; schools have not operated. Revenues coming in from these parts of the infrastructure space are down massively. Projects – such as roads have been worked upon as staff have been furloughed or laid off. It is not surprising parts of the market have been hit.

On the other side of the infrastructure story – utilities for instance – have been seen as a relative safe haven as they are regulated and have – arguably – stable income streams. Infrastructure assets tend to have a higher level of dividend income and in a world where income is falling, could be seen as a place of interest. Infrastructure assets could be used by governments of the world to help kick-start economies too. New roads to be built, existing roads to be improved. Railways to be enhanced. New runways at airports given planning permission for instance.

The coronavirus has hugely slowed down global economies, and recessions abound. As governments try to get money back into the economy, they could incentivise businesses via infrastructure spend to adopt the production of “green” energy, or make businesses reduce their carbon footprints. This can help finance departments change their capital expenditure plans. Big projects – such as infrastructure ones (originated by governments for example) can certainly assist in employment, rejuvenation and economic growth.

Sector comparison: Global and First State Global Listed Infrastructure – YTD performance



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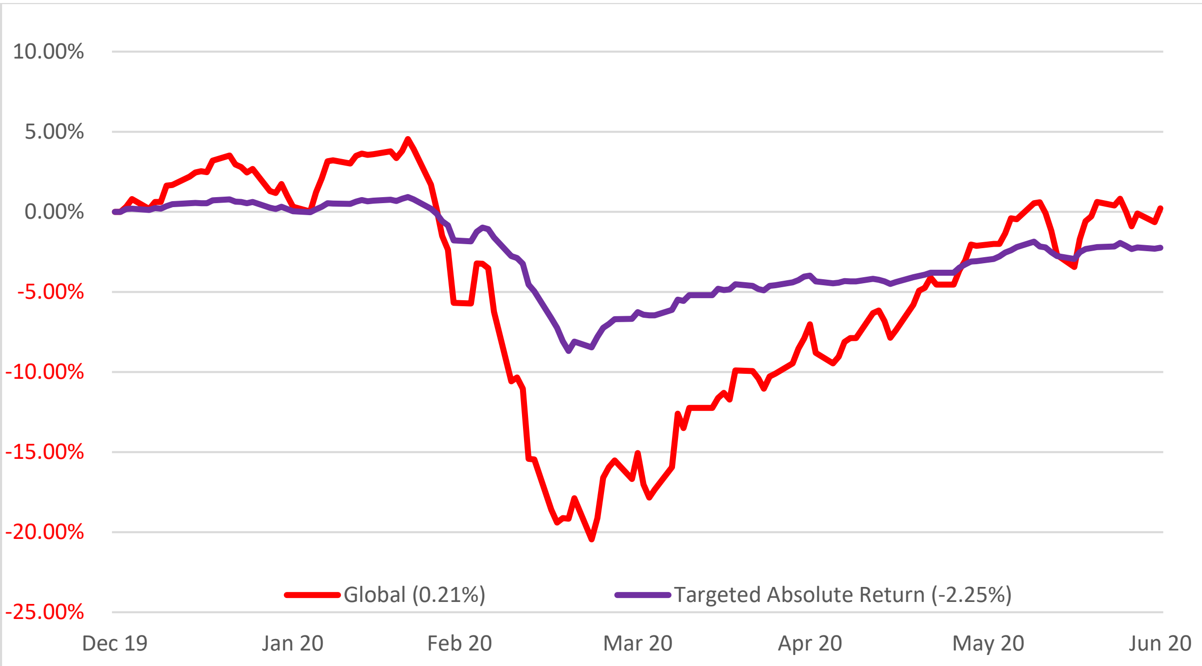
Targeted Total Return

The Targeted Total Return sector is diverse by its nature and so it wasn't surprising to see a wide range of returns from strategies. Some of the strongest performers over the quarter had higher allocations to equities and consequently were among the weakest performers during March. The risks around the use of derivatives were plain as those with the most extensive derivatives use tended to have marked performance (both positive and negative), while the funds more focused on the use of traditional asset classes tended to fall in between.

Sector comparison: Global and Targeted Absolute Return – YTD performance



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