EPIM Brunel

Quarterly report – Q4 2020
Annual report – 2020

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Introduction

Welcome to this expanded edition of our EPIM Brunel investment review. In this report we will be covering information and events that influenced performance, not only in the fourth quarter of 2020, but across the entire year.

This should provide some helpful perspective and context around our investment decisions and the overall performance of the different portfolios.

The past year was defined by the COVID-19 crisis, which peaked globally in March and from which point central banks and governments deployed measures to support economies and protect jobs.

Global equities ended the year at record highs after a very strong quarter. This added to gains made during an historic rally after share markets crashed in March.

The Democratic win in the US election, the positive vaccine developments and rising stock prices have made investors very bullish. The last-minute Brexit trade deal also added to optimism.

With much good news now priced in, there is some risk of a near-term pull-back in share prices. That said, the outlook for corporate profits in the medium term is positive, and the yields on competing assets such as government bonds is very low. As a result, we are positive on equities on a 12-month view.

Market overview Q4 2020

- The Covid-19 situation deteriorated towards the end of the year. This means that the near-term economic outlook remains challenging, at least until the rollout of vaccines has reached a sufficient proportion of the population. However central banks and governments are deploying stimulus measures to offset the effects to some degree.
- The Democrats' election victory in the US, together with rising equity prices, have made investors very bullish. Global Equities finished the year at record highs.
- The UK and Emerging Markets were the two best performing regions in the fourth quarter.
- UK Corporate Bonds outperformed Government-issued Gilts.
- The US Congress finally approved a $900bn stimulus plan to support the economy, and to grant improved unemployment benefits to those out of work.
- The incoming Biden administration has said it will prioritise further stimulus spending, which should support growth in the near term.

The big picture in Q4

- Equities as a whole performed strongly in the fourth quarter, rising by over 10%.
- UK Equities were up by 12.2%, and Overseas Equities gained 8.4%.
- Within Overseas Equities, Emerging Markets returned 16.5%, while US Equities underperformed on relative terms, with a return of 7.0%.
- UK property REITs gained 6.9%, while the Absolute Return sector rose by 2.3%.
- In Fixed Interest, UK Corporate Bonds returned 4.0%, while Conventional Gilts were up 0.5% and Index-linked Gilts rose by 1.3%.
- The UK introduced a limited lockdown in November, along with many other countries who were battling a second wave of the virus.
- Containment measures to control the spread of Covid-19 have hampered the recovery in the services sector, especially hospitality and leisure, which includes pubs, bars and restaurants.
- Conversely, surveys of manufacturing sectors around the world continue to show a pickup in activity.
- China remains the global growth bright spot, with capital expenditure by state-owned enterprises driving gains. The fact that it has contained the Covid-19 more effectively than any other nation is also a major advantage.
- The good news elsewhere is that vaccines are being administered, and in the developed world the most vulnerable cohorts of society will be protected very soon.
- The housing markets in the UK and US are performing strongly. In the US, record-low interest rates are fuelling demand. In the UK, the government's temporary stamp-duty holiday has helped fuel a mini-boom in activity and price growth. This is likely to fade after the tax break ends on 31 March.

EPIM Brunel performance

EPIM Brunel PERFORMANCE												
	Q4	2020 YTD	1yr	2yr	3yr	4yr	5yr	2019	2018	2017	2016	2015
Cautious Portfolio	4.9	6.7	6.7	18.7	15.5	22.3	34.3	11.2	-2.7	5.9	9.8	2.5
Income Portfolio	6.8	6.8	6.8	22.3	17.2	26.6	42.2	14.5	-4.2	8.1	12.3	3.5
Balanced Portfolio	8.6	7.8	7.8	25.7	20.7	31.4	51.7	16.6	-3.9	8.8	15.4	3.3
Growth Portfolio	10.5	10.2	10.2	30.5	25.3	40.0	63.4	18.4	-4.0	11.8	16.7	4.7
Global Equity Portfolio	12.4	9.9	9.9	34.3	27.8	43.7	69.4	22.1	-4.8	12.5	17.9	5.4

All figures shown above are calculated to 31 December 2020.

Past performance is not a guide to future performance. Performance Calculation: All income is reinvested. Performance is shown inclusive of underlying fund charges but gross of Brewin Dolphin's investment management charge. Deduction of this charge will have the result of reducing the illustrated performance. The value of investments can fall and you may get back less than you invested. If you invest in currencies other than your own, fluctuations in currency value will mean that the value of your investment will move independently of the underlying asset.

Performance highlights Q4 2020

Asset Allocation

What worked and why?

The underweight position in UK Direct Commercial Property was particularly beneficial over the quarter. In addition, being underweight in bonds and overweight in Emerging Market equities boosted performance.

What didn't work and why?

The overweight position in Absolute Return was a drag on performance as it only returned 2.3% in the quarter, which was behind other asset classes.

Fund Selection

What worked and why?

Selection was very positive in the quarter, with standout performances from a number of UK holdings in Man GLG UK Equity Income, Ninety One UK Special Situations, Teviot UK Smaller Companies & Merian UK Mid Cap. US equities were also a strong source of outperformance with Legg Mason Royce US Small Cap Opportunities and Baillie Gifford American both doing well in the aftermath of the US election. PIMCO UK Corporate Bond and JPM Global Macro Opportunities also put in good performances.

What didn't work and why?

The holdings in Threadneedle European Select, Ninety One UK Equity Income and Lindsell Train faced headwinds after strong performances earlier in the year. BlackRock Gold & General fell back as weakness hit the price of gold and Henderson Absolute Return was a drag on performance.

Portfolio changes Q4 2020

Asset Allocation

In November we went further underweight UK equities, reduced the overweight to cash and increased the overweight to North American, European and Asian equities.

In December we further reduced the UK equity allocation and raised the US equity allocation.

Fund Selection

In November, we increased the Asia ex Japan equity allocation through the Fidelity Asia Fund, which provides a more growth-biased exposure within the Asia region.

We increased the European allocation by reducing our holdings in the MISM UK Equity and MISM UK Equity Income Funds.

In December, the increase in North American equities was funded by a further reduction in the MISM UK Equity and MISM UK Equity Income Funds. In addition, the Threadneedle European Select allocation was reduced and added to the HSBC Europe Index passive fund. Threadneedle has performed very well over the year but we feel that reducing the exposure to "quality" is the most appropriate approach given the potential for a cyclical upswing in the region's economy.

The assets in the Ninety One UK Special Situations mandate in the MI Select Managers UK Equity fund were transitioned and handed over to RWC UK Equity Income in December. This follows the manager's departure earlier in the year prompted a review by our fund analysts.

Performance against relevant benchmarks

- The Cautious model outperformed the IA Mixed Investment 0-35% Shares benchmark last quarter by 0.6% and rose by 4.7% in absolute terms.
- The Income model underperformed the IA Mixed Investment 20-60% Shares benchmark last quarter by 0.2% but rose by 6.5% in absolute terms.
- The Balanced model outperformed the IA Mixed Investment 40-85% Shares benchmark last quarter by 0.3% and rose by 8.3% in absolute terms.
- The Growth model outperformed the IA Flexible Investment benchmark last quarter by 1.2% and rose by 10.1% in absolute terms.
- The Global Equity model outperformed the IA OE Global benchmark last quarter by 2.5% and rose by 12.1% in absolute terms.

MI Select Manager fund weights

MISM FUND WEIGHTS			
Date	**MISM Fund**	**Mandate**	**Weight (%)**
31/12/2020	MI Select Managers Bond Instl Inc	Robeco Global Credits	26.91
		PIMCO UK Corporate Bond	35.09
		Insight UK Government Bond	29.46
		DWS US TIPS 10yr+	8.54
31/12/2020	MI Select Managers NA Equity Instl Inc	JPM US Equity Income	52.96
		Baillie Gifford American	42.30
		Legg Mason Royce US Smaller Companies	4.74
31/12/2020	MI Select Managers UK Eq Inc Instl Inc	Ninety One UK Equity Income	32.33
		Man GLG UK Equity Income	34.58
		Threadneedle UK Equity Income	33.08
31/12/2020	MI Select Managers UK Equity Instl Inc	JPM UK Equity Core	29.19
		RWC UK Equity Income	26.64
		Lindsell Train UK Equity	23.29
		Old Mutual UK Mid & Large Cap Crossover	11.78
		Teviot UK Smaller Companies	9.10

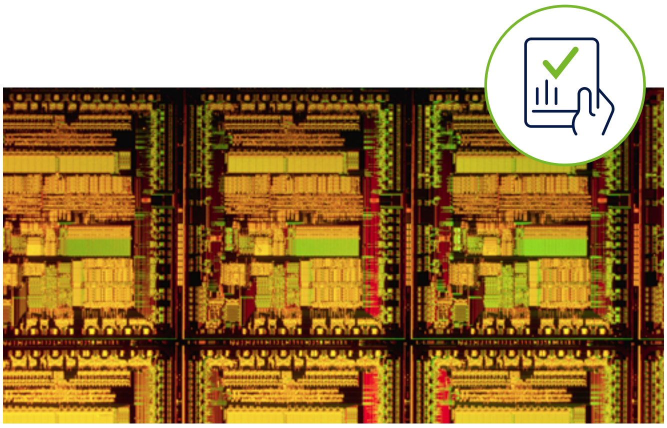
EPIM Brunel Service

Annual report – 2020

EPIM Brunel annual market overview 2020

- Despite the global pandemic and severe market crash in March, the year ended up for equities, although there was a wide disparity between regions. Asian equities gained almost 19%, and North America returned over 16%. On the other hand, the UK and Emerging Markets both fell 12% and 13% respectively.
- Bonds were up strongly in response to central bank stimulous with UK corporates and gilts up well over 8% and index-linked bonds up over 11%. Unsurprisingly, property was hit particularly hard, falling 9.5%. Other Alternatives ended the year broadly flat.
- On the geopolitical front, the year started with positive newsflow around the US/China trade war. But soon after, the spread of the coronavirus in China and beyond contributed to substantial falls in global equity markets. The Dow Jones Industrial Average plunged 37% during the height of the pandemic, before staging a stunning rebound, rallying by 63% to reach a record high at the year end.
- In the UK, the FTSE 100 started the year close to a record high, before falling by 25% in the three months to the end of March and then bouncing back somewhat on stimulus and news of an effective vaccine.
- Governments limited the damage by launching support programmes for workers. The UK, for example, contributed to the wages of 25% of the workforce. In the US, the emergency unemployment benefits paid to the jobless actually increased aggregate income, since the payments often exceeded the pay whilst in work.
- In addition, central banks were quick to instigate wide-ranging support initiatives, from support for borrowers and currency markets to lower interest rates and resumption of quantitative easing. During the peak phase of the first wave of the crisis, the US Federal Reserve was buying $1m worth of bonds every second. Central bankers have signalled to markets that rates will only be raised after inflation has sustainably returned to target levels. This means a “lower for longer” rates environment. Against this backdrop, the attraction of equities has grown.
- Biden’s win in the US presidential election in November saw global equity markets rally following a tight race. In the UK, a no-deal Brexit was avoided as an agreement on trade was finalised on 24 December, just a week before the transition period came to an end.

EPIM Brunel Performance highlights 2020



Asset Allocation

What worked and why?

Total allocation attribution was strong and positive across most models. The underweight position in Property and the overweight to North American equities were particularly helpful. North American equities benefited from a large exposure to the tech sector which was positively affected by the lockdowns.

What didn't work and why?

The mild overweight position to Cash was a small drag on performance.

Fund Selection

What worked and why?

Fund selection was strong over the year. The Baillie Gifford American strategy was the stand out performer, delivering returns over 120% during the year. The inclusion of LM Royce US Smaller Companies over the summer has also been a positive contributor. In the UK, Lindsell Train, Ninety One UK Equity Income and Threadneedle UK Equity Income have both put it solid relative performances in what was a difficult year. The holdings of Teviot UK Smaller Companies and Merian UK Mid Cap have performed very positively. The JPM Global Macro Opportunities fund has performed well in Other Alternatives.

What didn't work and why?

The holdings of Man GLG Japan Core Alpha, BlackRock Gold & General and Jupiter Absolute Return were a drag on performance. Jupiter was removed from the portfolios in early 2020. Man GLG Japan Core Alpha is a value strategy which has struggled in an environment that has not been friendly to the style of management. BlackRock Gold & General declined in response to lower gold prices.

EPIM Brunel Portfolio changes 2020

Asset Allocation change highlights

The Asset Allocation Committee has been overweight equities throughout 2020. As the pandemic struck it was felt likely that, despite the extraordinary near-term upheaval, the global economy would recover on the back of a swift response from central banks and governments. As sovereign bond yields lowered in response to monetary stimulus, so the tactical allocation to gilts was reduced. Property was taken further underweight as this seemed like one asset class that was undergoing a more fundamental re-evaluation.

In January, in the Cautious model, UK Corporate Bonds were reduced by 2.5% and Alternatives was increased by 2.5%. In the Growth model, UK Equities were reduced by 2.5% and Overseas Equities were increased by 2.5%.

In December, UK Equities were reduced from 30% to 27.5% in the Balanced model. International Equities were increased from 32.5% to 35.0%.

Fund change highlights

In the first quarter of 2020, Jupiter Absolute Return and JOHCM Continental European was removed and HSBC Europe Index, Muzinich Global Tactical Credit and BNY Mellon Short Dated High Yield Bond were introduced.

In the third quarter, Teviot UK Smaller Companies was announced in the MI Select Managers UK Equity fund and Legg Mason US Small Cap Opportunities was introduced in MI Select Managers North American fund. Blackrock Gold & General introduced as gold became more attractive against very low-yielding bonds.

In the fourth quarter, the assets in the Ninety One UK Special Situations mandate in the MI Select Managers UK Equity fund were transitioned and handed over to RWC UK Equity Income. This follows the manager's departure from Ninety One earlier in the year which prompted a review by our fund analysts.

Fidelity Asia was introduced to bring more of a growth tilt to the regional exposure.

Investment outlook

Cash

We recommend retaining a small overweight to cash, We want to have liquidity on hand to opportunistically add to positions in other asset classes in the event of market corrections.

Bond

After a big move up throughout August, the 10-year Gilt yield moved lower last month. The shift into risk-off We continue to think that the outlook for corporate bonds is superior to that of government bonds. However, the yield on offer is now so low that the risk/reward trade-off is no longer attractive. Therefore we advise a small underweight position.

In the fixed-income space as a whole, we favour global index-linked bonds, where we advise neutral positions. This asset class serves as a good hedge to protect against an increase in inflation.

Global Equities

Bullish sentiment and stretched valuations are a concern, as is the potential for tax hikes now that the Democrats have taken control of the Senate in the US. Nevertheless, we maintain a sizeable overweight in global equities. There will probably be a lot of volatility this year but at the end of the day, a backdrop of very accommodative central banks and rising profits is one that should see equities continue to push higher. Also, global consumer confidence is still somewhat depressed, and has lots of room to pick up as the economic and employment backdrop improves. Cyclical global equity rallies don't tend to come to an end until consumer confidence peaks.

Alternatives

A weighting to absolute return will provide some diversification benefits to portfolios if equities and bonds sell off together. While equity and bond prices have been negatively correlated since the late 1990s, there is the possibility that they both sell off in unison under certain scenarios. Furthermore, an allocation to absolute return provides some optionality to benefit from an increase in volatility.

UK Equities

The UK has been one of the strongest performing equity markets since the positive developments on vaccines in November. The UK has high weightings in financials and energy, making it a very value-orientated region. We have turned more bullish on cyclical value and therefore have warmed up to the UK. Moreover, sterling is a risk-on currency which should rally alongside the global equity market, supporting common currency performance.

US Equities

The US is heavily exposed to big tech, as well as the growth style more broadly, so a shift in favour of cyclical value is a headwind for its relative performance prospects. On this front, the US is underweight financials, energy, materials and industrials – all sectors that are highly sensitive to an improving economy, rising yields and increasing commodity prices. After this sector/style exposure, the second key part of the equation that underpins our less optimistic view is the dollar. The dollar tends to trade defensively, so a backdrop of stronger global growth should continue to pressure the dollar lower. Against this backdrop, we have trimmed our overweight position in the US relative to the benchmark.

Europe ex-UK Equities

As expected, the delays facing the rollout of the EU's jointly financed 1.8trn Euro recovery package have been overcome. This should help the euro to rally against the dollar. Europe ex-UK should also benefit from a shift in outperformance from growth to value.

Japan

The sector composition of Japan's economy is pro-cyclical. But the yen generally trades more defensively than other currencies. That may change somewhat in this cycle, but it still probably does less well than other currencies. Moreover, to become bullish on Japan, one should be somewhat optimistic with respect to domestic growth prospects v the rest of the world. On that front, we see now reason for the trend of the past 25 years to change.

Asia ex-Japan Equities

Asia ex-Japan is a cyclically exposed region. As global growth picks up, its currencies should appreciate against the dollar. Wide yield spreads should continue to lend support to the Chinese renminbi (RMB), and Asia ex-Japan currencies by association. Global investors, looking for ways to diversify portfolios at a time when traditional safe havens yield very little or are negative, will likely increasingly allocate capital to the Chinese fixed-income markets, also bolstering the RMB.

Emerging markets ex-Asia

EM ex-Asia equities have finally caught on, outperforming the global equity benchmark on the back of the surge in the oil price. For this category to sustain its performance, we'll need continued commodity-price strength. The good news is that oil demands is now outstripping production, which is beginning to slow the process of drawing down bloated global oil inventories. The region is a beaten down, cheap way to play a return economic normality, above-trend economic growth and a weaker dollar.

The value of investments can fall and you may get back less than you invested.

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If you invest in currencies other than your own, fluctuations in currency value will mean that the value of your investment will move independently of the underlying asset.

This information is for illustrative purposes only and is not intended as investment advice.

No investment is suitable in all cases and if you have any doubts as to an investment's suitability then you should contact us.

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