EPIM Brunel

Quarterly Review: 1 January 2020 to 31 March 2020

eden park
INVESTMENT MANAGEMENT

POWERED BY
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Introduction

Welcome to the EPIM Brunel investment review. In this report we will be covering information and events that influenced performance during the first quarter of 2020.

After stock markets hit all-time highs in January, the spread of the coronavirus outside of China impacted all global markets from February onwards, with falls averaging 20% over the quarter. Swift government and central bank responses to the crisis should help support markets going forwards but volatility will probably remain elevated.

This report will give some perspective and context around our investment decisions and the overall performance of the portfolios.

Contents

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Market overview Q1 2019

Around a quarter of the world was placed under lockdown

G20 nations launched $5trn in fiscal support packages

The Bank of England cut rates to 0.1%.

Central banks launched stimulus programmes to prevent a credit crunch

Government bonds outperformed equities

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

The big picture in Q1 2020

	Q1[1]	2020 YTD	1yr	2yr	3yr	4yr	5yr	2019	2018	2017	2016	2015
Cautious Portfolio	-7.5	-7.5	-2.5	2.4	3.5	14.3	14.9	11.2	-2.7	5.9	9.8	2.5
Income Portfolio	-11.3	-11.3	-4.9	1.0	1.9	16.1	16.7	14.5	-4.2	8.1	12.3	3.5
Balanced Portfolio	-14.4	-14.4	-7.2	-0.4	0.8	18.9	17.8	16.6	-3.9	8.8	15.4	3.3
Growth Portfolio	-16.8	-16.8	-8.9	-1.6	1.9	22.8	21.7	18.4	-4.0	11.8	16.7	4.7
Global Equity Portfolio	-20.2	-20.2	-11.1	-2.9	0.2	22.1	22.1	22.1	-4.8	12.5	17.9	5.4

- Global equity markets fell by an average of 20.3% over the quarter.
- Fixed Interest fared better; UK Corporate Bonds fell 5.6% while UK sovereigns generated a positive return with Index-linked Gilts up 2.6% and Conventional Gilts gaining 7% year to date.
- UK equities were harder hit than the rest of the world with a decline of 25.2% vs 16.6% for the rest of the world.
- Within Overseas equities, the Emerging Markets sector was a notable detractor, falling by 34.8%, while Japanese equities held up relatively well falling by 11.2%. US equities ended the quarter down 14.8%.
- Mimicking the equity markets, UK REITs fell 18.4% while UK Direct Commercial Property sustained a fall of 1.2% overall. Absolute Return fell by 6.6%.
- Governments around the world have implemented restrictions to help alleviate pressures on the health system. Now, a quarter of the world is living under some form of lockdown and global economies are taking a hit.
- Monetary policy has responded very quickly to the crisis with rate cuts, an increase in bond buying programs and liquidity support. Fiscal policy will play a bigger role with the G20 announcing plans to inject over $5 trillion into the global economy.
- The severity of past equity market declines has been more correlated with the length of the recession rather than the magnitude of the drawdown. We feel that buying stocks at these levels should reward investors over the long term.

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Performance highlights Q1 2020

Asset Allocation

What worked & why?

Being overweight North America and Absolute Return

There was relative outperformance in North American equities due to the overweight position. Absolute Return fell less than other asset classes during the sell-off.

What didn't work & why?

Being underweight cash and bonds

The underweight positions in "safe haven" assets, such as bonds and cash, hindered performance as equity markets fell over the quarter.

Performance highlights Q1 2020

Fund Selection

What worked & why?

- Baillie Gifford American continued to outperform with investors seeing value in tech stocks such as Netflix, Zoom and Amazon, during the Covid-19 outbreak.
- Lindsell Train, Ninety One UK Equity Income and Threadneedle European Select all have a quality bias which helped protect capital in tougher market environments.
- Fidelity Emerging Markets Fund has a defensive growth orientated strategy as it invests in companies with superior balance sheet strength, high corporate governance standards and high visibility on earnings.
- JPM Global Macro Opportunities has maintained a low level of risk throughout, predominantly achieved through short derivative exposures and defensive currency positions such as being long on Japanese Yen. The fund also added a small gold position. By sector, the bias is towards technology and the fund benefited from not holding energy stocks.

What didn’t work & why?

- Within UK equities, funds holding more domestically focussed firms suffered the most, such as Merian Mid Cap and Ninety One UK Special Situations.
- Listed property holdings (Schroder Global Cities Real Estate and iShares Global Property Securities) caused a drag to performance in addition to the corporate bond holdings (Pimco UK Corporate Bond and Robeco Global Credits) which sold off over concerns about corporate balance sheets.

Portfolio changes Q1 2020

Asset Allocation

- From 1st January 2020 there were some changes to the MSCI PIMFA Conservative and Growth indices.
- In the Conservative benchmark, UK corporate bonds were reduced by 2.5% and Alternatives was increased by 2.5%.
- In the Growth benchmark UK equities were reduced by 2.5% and overseas equities were increased by 2.5%.

Fund Selection

Fund	Asset Class	Action	Reason
Jupiter Absolute Return	Absolute Return	**Sold**	Over Q1 the Jupiter Absolute Return holding was removed following a downgrade to "Hold" by our Research Department after a period of disappointing performance. The proceeds had been allocated between the Muzinich Global Tactical Credit, Investec Diversified Income and BNY Mellon Global Short Dated High Yield funds. We expect these funds to generate a positive return for investors over the investment cycle with lower risk than equities.
Muzinich Global Tactical Credit	Absolute Return	**Bought**	
Investec Diversified Income	Absolute Return	**Increased**	
BNY Mellon Global Short Dated High Yield	Absolute Return	**Bought**	
JOHCM Continental European	European	**Sold**	The JOHCM Continental European fund was also liquidated. The performance of the JOHCM fund has been disappointing given the level of fees. In lieu of a suitable active fund with tilt to value stocks the allocation has been split between the HSBC Europe Index and Threadneedle European Select funds.
HSBC Europe Index Fund	European	**Bought**	

Focus on MI Select Manager Funds

MISM Funds – Covid-19 Volatility

- Reviewed Business Continuity Plans of the underlying manager’s
- Allowed the more defensive mandates to take up a larger share of the funds
- We took the opportunity to retain cash or allocate cash as managers found opportunities in the market

MISM mandate weights as at March end

UK Equity

Investec	24%
J.P.Morgan Asset Management	32%
Lindsell Train	29%
Old Mutual Asset Management	10%
New Smaller Companies Manager	5%

UK Equity Income

Columbia Threadneedle Investments	33%
Investec	35%
Man glg	32%

North American Equity

Baillie Gifford	42%
J.P.Morgan Asset Management	58%

Bonds

	8%
Insight Investment	35%
PIMCO	34%
ROBECO	23%

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Investment outlook

Investment outlook

Outlook	Asset Class	Reasoning
	UK equities	Cable is trading just above the levels seen last October when the market was most pessimistic about the odds of a no-deal Brexit. Since then, interest rate support has moved sharply in favour of the pound. Rate spreads are currently at 2015 levels, when the pound was trading in the 1.46-1.57 range vs. the dollar. We believe the pound has upside on a 12-month time horizon, which should support common currency relative performance. UK equities are also trading on historically very depressed valuations vs. Europe ex UK on 12m forward P/E. Against this backdrop, we consider the UK a deep value play.
	US equities	The prevailing view among investors is that the US is rich with good companies with attractive secular growth prospects that cannot be found in most other markets. The US is also in decade-plus long run of outperformance, and there has been no clear sign of a trend change. The US is well positioned to outperform if global equities correct, as it is defensive in nature. This defensiveness comes from both the currency, as well of from the fact that it has high weightings in defensive sectors and is rich in “quality” companies. We continue to recommend positioning for outperformance.
	European equities	Once the crisis simmers and demand for the dollar wanes, the euro should catch a bid from the fact the euro is more cyclical than the dollar, owing to the greater cyclical exposure of the Eurozone economy compared to the US. Still, there are headwinds facing Europe ex UK. Importantly, the region is highly reliant on tourism, which will be extremely hard hit over the coming quarters and may lag the broader economic rebound. As such, the benefit that Europe ex UK would normally derive from an eventual global economic rebound may be blunted somewhat. Meanwhile, although we foresee higher bond yields over the next year, the upside in Europe will likely be very limited, which will cap any net interest margin improvement for its banks.
	Japanese equities	After outperforming solidly as the coronavirus crisis intensified in Europe and the US, Japanese equities have moderately underperformed. The Bank of Japan has announced it will double its annual ETF purchases. The increase puts the BoJ on a possible course to overtake the Japanese state pension fund as the biggest holder of domestic stocks by the end of the year. But we doubt BOJ purchases will be enough to drive outperformance. What we need to see to turn bullish on Japan is a move higher in inflation, which pushes JGB yields higher. There are no signs of that occurring anytime soon.

Investment outlook

Outlook	Asset Class	Reasoning
↓	Asian ex Japan equities	As economic growth is tanking in the West, China is getting back to work. Against this backdrop, Asia ex Japan has outperformed the global equity benchmark since the crisis began intensifying in late February. On a 12m time horizon, there are several reasons to expect continued outperformance. China better positioned now to weather a global slowdown – exports as a share of GDP have dropped to multi decade lows. It is the 100th anniversary of the Chinese Communist Party next year. The authorities attach a lot of importance to these milestones and will do what they can to ensure that sentiment is positive around celebrations. State owned banks will do what is necessary to foster stock market stability. We were previously concerned that it would be difficult to generate positive news flow on the trade war front this year. But the trade war is now on the backburner until after the US election. Moreover, Trump's re-election odds are now highly uncertain. Joe Biden would not be easy on China, but we suspect he would be less tough than Trump. Finally, and similar to trends observed around the world, interest rate spreads have moved in favour of the RMB over the dollar. Despite these reasons, we suspect Asia ex Japan will underperform the US in the context of a global equity market correction, and so have trimmed our exposure. We anticipate raising weightings anew if/when we re-raise our global equity exposure.
↓	Emerging market equities	EM ex Asia has been by far the worst performing region since the coronavirus crisis heated up. Plunging commodity prices, particularly oil, has dragged the region lower. The recent OPEC+ decision to cut production puts a floor under prices, but is not enough to drive oil prices higher given the massive hit to demand due to the coronavirus crisis. We maintain a small exposure to EM ex Asia, and expect to take a more bullish view when we get closer to the economic turning point that will support higher commodity prices.
↑	Absolute Return	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 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.

Investment outlook

Outlook	Asset Class	Reasoning
	Bonds	At 30 basis points, 10-year Gilt yields are very low. Over time, the market should slowly price in that recovering economies will boost inflation pressures, which central banks will ultimately have to lean into. As this occurs, Gilt yields should move gradually higher. For now, however, we maintain Gilts at neutral. There is a high risk of an equity market correction, and Gilts still offer somewhat of a hedge, albeit much less so compared to past risk off phases. We expect default rates to pick up, mainly in the high yield sectors such as Energy, Retail, Leisure and Hotels. Investment grade corporates will not be immune, but rather than defaults we are likely to see more downgrades. Nevertheless, valuation is attractive, even after the recent rally. Meanwhile, central bank corporate bond buying programmes provide solid support. However, given our view that the odds of a correction in risk assets is high, we believe it is too early to add to credit exposure.
	Cash	We raise our cash weighting to overweight, funding this position with a reduction in our equity overweight. The odds of an equity market correction are elevated. We want to have liquidity on hand to quickly buy back in to risk assets if a correction occurs.

Appendix: Investment Performance

Portfolio Performance

Cautious

% to 31 March 2020	Q1[1]	2019	2018	2017	2016	2015	2014
Cautious Portfolio	-7.5	11.2	-2.7	5.9	9.8	2.5	9.8
IA Mixed Investment 0-35% Shares	-8.1	8.8	-3.4	5.0	9.0	0.8	5.4
Relative	0.6	2.4	0.7	0.9	0.8	1.7	4.4

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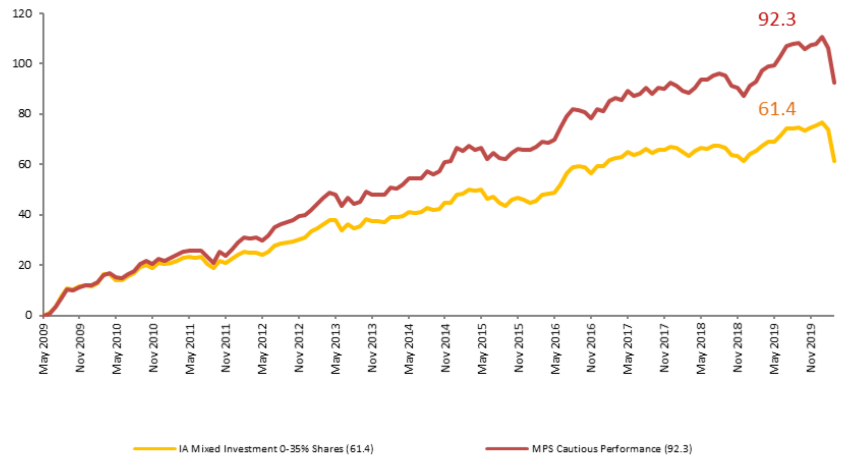
Performance since Inception



Asset Allocation as at 31 Mar. 2020

Bonds		48.0%
Equities – International		15.5%
Equities - US	10.5%	
Equities - Europe ex UK	2.0%	
Equities - Asia ex Japan	1.5%	
Equities - Japan	1.0%	
Equities - Emerging	0.5%	
Absolute Return		15.0%
Equities – UK		12.5%
Cash		4.5%
Commercial Property		4.5%

Source: Morningstar.

Performance and holdings may differ depending on your platform

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Portfolio Performance

Income

% to 31 March 2020	Q1[1]	2019	2018	2017	2016	2015	2014
Income Portfolio	-11.3	14.5	-4.2	8.1	12.3	3.5	8.8
IA Mixed Investment 20-60% Shares	-13.1	12.1	-5.1	7.2	10.5	1.4	5.1
Relative	1.8	2.4	0.9	0.9	1.8	2.1	3.7

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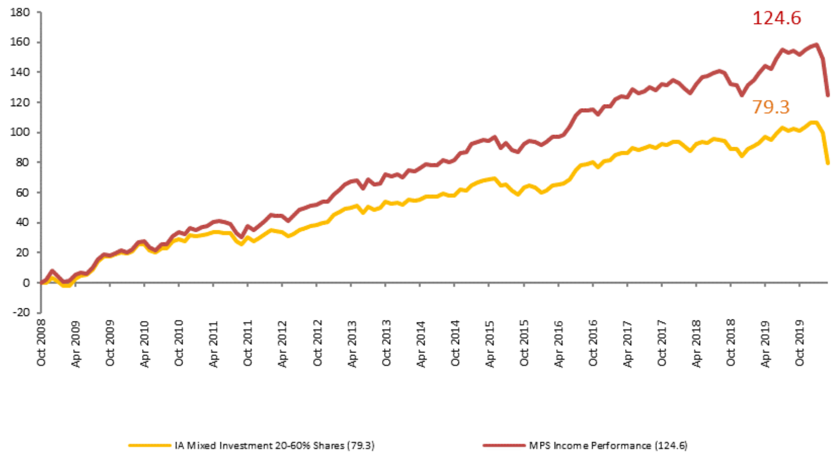

Asset Allocation as at 31 Mar. 2020

Bonds		32.0%
Equities – International		25.5%
Equities - US	16.5%	
Equities - Europe ex UK	3.5%	
Equities - Asia ex Japan	3.0%	
Equities - Japan	2.0%	
Equities - Emerging	0.5%	
Equities – UK		23.0%
Absolute Return		12.5%
Cash		4.5%
Commercial Property		2.5%

Source: Morningstar.

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Portfolio Performance

Balanced

% to 31 March 2020	Q1[1]	2019	2018	2017	2016	2015	2014
Balanced Portfolio	-14.4	16.6	-3.9	8.8	15.4	3.3	7.5
IA Mixed Investment 40-85% Shares	-15.2	15.9	-6.1	10.1	13.1	2.6	5.1
Relative	0.8	0.7	2.2	-1.3	2.3	0.7	2.4

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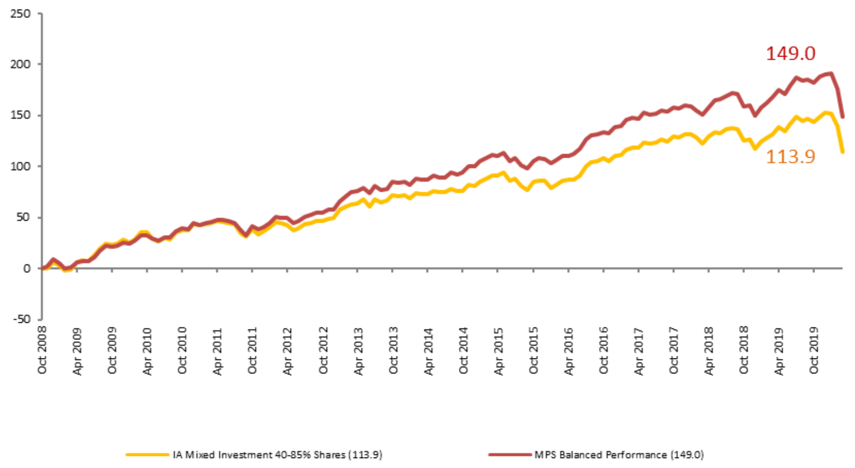

Asset Allocation as at 31 Mar. 2020

Equities – International		36.5%
Equities - US	23.5%	
Equities - Europe ex UK	5.5%	
Equities - Asia ex Japan	4.0%	
Equities - Japan	2.5%	
Equities - Emerging	1.0%	
Equities – UK		29.0%
Bonds		20.5%
Absolute Return		7.25%
Cash		4.5%
Commercial Property		2.25%

Source: Morningstar.

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Portfolio Performance

Growth

% to 31 March 2020	Q1[1]	2019	2018	2017	2016	2015	2014
Growth Portfolio	-16.8	18.4	-4.0	11.8	16.7	4.7	6.8
IA Flexible Investment	-15.5	15.6	-6.6	11.1	14.0	1.9	5.0
Relative	-1.3	2.8	2.6	0.7	2.7	2.8	1.8

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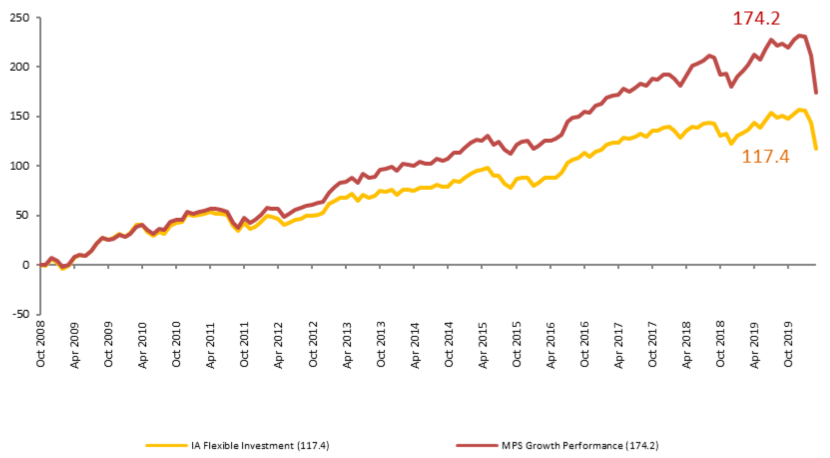

Asset Allocation as at 31 Mar. 2020

Equities – International		49.0%
Equities - US	31.0%	
Equities - Europe ex UK	7.0%	
Equities - Asia ex Japan	6.0%	
Equities - Japan	3.5%	
Equities - Emerging	1.5%	
Equities – UK		32.0%
Bonds		10.25%
Absolute Return		5.25%
Cash		2.0%
Commercial Property		1.5%

Source: Morningstar.

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Portfolio Performance

Global Equity

% to 31 March 2020	Q1[1]	2019	2018	2017	2016	2015	2014
Global Equity Portfolio	-20.2	22.1	-4.8	12.5	17.9	5.4	5.3
IA OE Global	-15.7	22.0	-5.7	13.9	23.4	2.3	7.0
Relative	-4.5	0.1	0.9	-1.4	-5.5	3.1	-1.7

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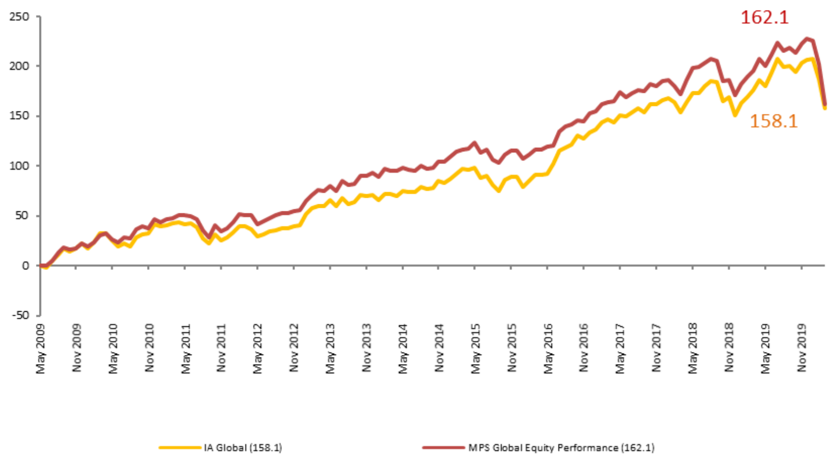

Asset Allocation as at 31 Mar. 2020

Equities – International		55.5%
Equities - US	34.5%	
Equities - Europe ex UK	8.0%	
Equities - Asia ex Japan	7.0%	
Equities - Japan	4.5%	
Equities - Emerging	1.5%	
Equities – UK		43.5%
Cash		1.0%
Bonds		0.0%
Absolute Return		0.0%
Commercial Property		0.0%

Source: Morningstar.

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