global matters weekly

momentum

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Some things never change

by Michael Clough

In many ways, life has changed so much in recent weeks. Our usual routines suddenly seem distant memories. In other ways though, some practices haven't changed at all. The ongoing management of our portfolios and two key components which underpin this, asset allocation and manager research, have continued uninterrupted. Of course, the way we carry them out has changed. With asset allocation, we are no longer sat in one room together, rather all participating through video call and with manager selection, we are no longer meeting managers in person but instead through voice or video calls. Whilst several of our updates recently have considered our asset allocation thoughts, we haven't yet covered our approach to manager selection.

> *"Keeping on top of our managers in times like this is crucial"*

Keeping on top of our managers in times like this is crucial. Two questions are key. Firstly, have they performed as we would expect and if not, why not? Secondly, what changes have they made to their portfolio and why? For the first question, let me give the example of one of our quality equity managers, Evenlode. Given their philosophy we would expect them to protect capital more successfully than the broad market. Whilst they have performed in line with expectations, had they not, we would be scrutinising their portfolio to understand why. For example, were they carrying more cyclical risk, or economically sensitive positions than usual, and why was that? Exploring the second question gives further insights into the behaviours and style discipline of our managers. Let me use the example of RWC, one of our UK equity value managers. Recently they have been focussing on ensuring the balance sheets of the companies they own are sound and their businesses can survive this period, when markets are pricing many of them for significant financial distress. We would much rather hear this than see them hastily chase more value opportunities that naturally arise after big sell offs. Furthermore, if they have been initiating new holdings, do they fit their philosophy or are they investing in higher risk positions we would not typically expect? Importantly we do a lot of the work on the way in before investing in our managers and that means we typically don't get many surprises in times such as these.

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We have made some changes to portfolio asset allocations in recent weeks, but in recognition that we are just weeks into an episode that is likely to draw out over several months at a minimum, we have not yet moved risk up in size. That said, our underlying portfolio exposures will also move because we use active managers. As their portfolios evolve, so do ours. Of course, this makes ongoing monitoring essential. Whilst there are individual differences, broadly speaking we have witnessed managers putting cash to work in recent weeks. It has been encouraging that most of our managers have not been making wholesale changes to their portfolios. A common message has been the desire to fully stress test and reassess the balance sheet risks in all companies. Even value managers, whose opportunity sets have broadened greatly, have made minimal changes in aggregate.

> *"we have witnessed managers putting cash to work in recent weeks"*

We started working from home on Tuesday 17th March. Since then we have conducted calls with approximately one-third of all our managers. As long term investors, we have built up strong relationships over the years with managers. Such relationships help in periods like this, not least through one on one access to managers in a time when everyone is wanting updates. Regardless of extensive due diligence before investing with any fund manager, it is crucial to continue questioning and challenging them for reassurance. It is also important to regularly monitor risks and exposures in their portfolios, as our multi asset construct depends on each of them fulfilling their role as expected. Conversations are also important for information on markets which they study day in day out. We will be conducting many more manager meetings in the weeks to come. That will always continue to be part of our routine regardless of where we sit.

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Market Focus

- Global equities reverse some of the previous week's gains, but relatively contained
- Global employment numbers and service sector PMIs plummet
- Brent crude surged 36.8%, ending the week at $34.1 a barrel
- Gold fell 0.5% ending the week at $1620.8 an ounce

US

- US stocks ended the month and quarter with their worst performance since 2008. Consumer discretionary names were hit particularly hard
- A huge surge in the oil price, driven by expectations of an agreement between Russia and Saudi Arabia to reduce production, prompted a rebound in energy stocks
- The US printed 6.6 million weekly jobless claims, doubling the previous week's record number. Nonfarm payrolls fell 701K in March from a surprisingly low estimated fall of 100K
- US Treasuries returned 0.8% over the week, with their yield falling to the lowest level in a month as the Federal Reserve ramped up its purchasing program
- Officials warn the US death toll could reach around a quarter of a million from COVID-19
- US large cap equities fell 2.0% on the week

UK

- UK equities fell 2.1% last week
- The UK prime minister Boris Johnson has been admitted to hospital due to ongoing symptoms from COVD-19
- UK gilts fell 0.4% last week, with investment grade bonds returning 2.0%

Europe

- Germany's finance minister indicated that eurozone countries in need of recourse from the EU bailout fund and the European Stability Mechanism will not have to cut through as much red tape as during the GFC
- Equities fell back 0.4% last week as economic data points to a severe coronavirus-related recession this year
- The number of new COVID 19 cases in Italy, France and Spain appeared to slow last week as lockdown measures took effect. Encouragingly, Germany's doubling time of new cases is up to 18 days. The death toll across the major European countries stands at around 30,000
- Euro Area composite PMI fell to a record low of 29.7 (a reading below 50 marks economic contraction to put into context)

Rest of the World/Asia

- Chinese equities stabilised last week with better than expected PMI data and a rate cut providing some positive sentiment. The main index fell by 0.4%
- Japanese equities fell by 8.1% last week. The government intends to release its stimulus package in a two-phased approach, the first aimed at protecting jobs, the second focusing on a V-shaped recovery

Asset Class / Region	Currency	Cumulative returns Week ending 03 April	Month to date	YTD 2020	12 months
Developed Markets Equities					
United States	USD	-2.0%	-3.7%	-22.7%	-12.2%
United Kingdom	GBP	-2.1%	-4.9%	-27.7%	-24.4%
Continental Europe	EUR	-0.4%	-2.9%	-23.3%	-15.4%
Japan	JPY	-8.1%	-5.6%	-22.0%	-16.1%
Asia Pacific (ex Japan)	USD	-0.8%	-1.9%	-22.2%	-18.6%
Australia	AUD	4.7%	-0.2%	-23.2%	-16.0%
Global	USD	-2.6%	-4.1%	-24.3%	-15.5%
Emerging Markets Equities					
Emerging Europe	USD	6.1%	2.3%	-35.0%	-22.0%
Emerging Asia	USD	-1.4%	-2.0%	-19.8%	-15.6%
Emerging Latin America	USD	-5.9%	-5.9%	-48.8%	-44.7%
BRICs	USD	-1.3%	-2.2%	-22.7%	-18.3%
China	USD	-0.4%	-1.5%	-11.6%	-9.5%
MENA countries	USD	2.0%	2.0%	-23.3%	-24.2%
South Africa	USD	-3.2%	-4.5%	-43.0%	-43.0%
India	USD	-7.9%	-7.1%	-37.8%	-36.8%
Global emerging markets	USD	-1.2%	-2.0%	-25.1%	-20.9%
Bonds					
US Treasuries	USD	0.8%	0.7%	9.7%	15.7%
US Treasuries (inflation protected)	USD	1.6%	2.2%	4.2%	10.2%
US Corporate (investment grade)	USD	1.3%	-0.3%	-3.9%	5.2%
US High Yield	USD	-0.6%	-2.0%	-14.4%	-9.1%
UK Gilts	GBP	-0.4%	0.6%	7.7%	12.2%
UK Corporate (investment grade)	GBP	2.0%	1.6%	-3.8%	2.3%
Euro Government Bonds	EUR	-1.0%	-0.2%	0.1%	4.7%
Euro Corporate (investment grade)	EUR	0.1%	-0.1%	-6.3%	-3.5%
Euro High Yield	EUR	0.5%	-0.1%	-15.0%	-10.7%
Japanese Government	JPY	0.4%	0.4%	-0.1%	0.6%
Australian Government	AUD	1.0%	0.2%	4.4%	8.9%
Global Government Bonds	USD	-0.6%	-0.2%	2.9%	7.7%
Global Bonds	USD	-0.5%	-0.4%	-0.1%	5.0%
Global Convertible Bonds	USD	-1.9%	-2.0%	-11.0%	-6.8%
Emerging Market Bonds	USD	-1.8%	-2.0%	-10.5%	-5.0%

Source: Bloomberg. Past performance is not indicative of future returns.

		Cumulative returns			
Asset Class / Region	Currency	Week ending 03 April	Month to date	YTD 2020	12 months
Property					
US Property Securities	USD	-10.3%	-9.6%	-34.2%	-29.9%
Australian Property Securities	AUD	4.9%	-1.6%	-35.9%	-35.6%
Asia Property Securities	USD	-3.8%	-3.7%	-24.7%	-25.6%
Global Property Securities	USD	-6.7%	-7.0%	-32.5%	-28.0%
Currencies					
Euro	USD	-2.8%	-1.7%	-3.9%	-4.1%
UK Pound Sterling	USD	-1.5%	-1.4%	-7.8%	-7.2%
Japanese Yen	USD	-0.4%	-0.6%	0.1%	2.8%
Australian Dollar	USD	-2.9%	-1.7%	-14.6%	-15.8%
South African Rand	USD	-7.5%	-6.4%	-26.5%	-25.6%
Swiss Franc	USD	-2.5%	-1.3%	-1.2%	1.9%
Chinese Yuan	USD	0.1%	-0.1%	-1.8%	-5.4%
Commodities & Alternatives					
Commodities	USD	3.9%	5.6%	-28.2%	-27.7%
Agricultural Commodities	USD	-3.9%	-3.2%	-15.5%	-14.7%
Oil	USD	36.8%	50.0%	-48.3%	-50.8%
Gold	USD	-0.5%	1.4%	6.4%	25.6%
Hedge funds	USD	0.0%	-0.3%	-7.2%	-1.8%

Source: Bloomberg. Past performance is not indicative of future returns.

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