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Keeping you informed matters

Annual Investment Review

January 2021

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Outlook

With the help of central banks once again, major global economies performed much better than expected in 2020. This was contrary to expectations due to the impact of Coronavirus. With vaccines now approved for distribution, hopes for a more stable year ahead have risen, although obstacles remain for growth to return.

2020 will no doubt be remembered as the year the Coronavirus pandemic swept around the globe and brought life as we know it to a standstill. As a result of the virus, many key events that would normally have provided defining moments for markets, have been little more than footnotes under the virus dialogue.

At the start of the year, many investors were understandably in a more positive frame of mind. Expectations were that the global economy was set to improve and the laggards from recent years would have an opportunity to recover.

The trade war between the US and China had reached an initial Phase 1 agreement. The Trump Administration were shifting their focus to the Primaries in a US Election year and history suggested that the incumbent President running for a second term would win, with Trump seen as the more market-friendly of the candidates.

Here in the UK, we saw a decisive General Election with an 80-seat majority won by the Conservatives. This gave Boris Johnson his mandate to "get Brexit done". International investors, who had shunned the UK market since the EU Referendum in 2016, showed signs of returning.

Germany had avoided a technical recession in 2019 and its focus was on reinvigorating manufacturing through the auto industry with a structural shift away from higher carbon emitting vehicles. Italy, the long-term problem child of Europe, appeared to be on a more stable footing, and Spain and France had fared well with their inward focus on domestic markets.

In emerging markets, while Chinese growth had fallen significantly over the last several years, the size of the economy and expected growth of between 5% and 6% was enough to keep investor appetite for exposure to the region.

As we now know, this hope for a more stable, predictable year was soon forgotten as the world faced the full impact of Coronavirus. Economies were closed as populations were placed under some of the most draconian restrictions in peacetime.

With these national lockdowns to prevent the spread of the virus, a rapid economic collapse followed in February and March as businesses closed doors and global supply and demand chains ground to halt.

Without wishing to dwell on the massive loss of life and inevitable long term social impact from the virus as this crisis continues, we recognise that it is the unprecedented actions of governments and central banks to stem the financial losses in Q1 that provided the springboard for recovery over the rest of 2020.

The scale of this unprecedented stimulus is hard to fathom. The US Federal Reserve for example, has purchased assets equivalent to nearly 13% of its GDP in 2020. That's more than $9 trillion in liquidity to shore up the economy, which is equivalent to creating 22% of all the US Dollars issued since the birth of the nation. The figure for the European Central Bank is 12% of GDP and the tallies for the Bank of England and the Bank of Japan are 14% and 8%, respectively.

Despite this attempt to avoid financial Armageddon, markets have remained at the mercy of the virus as it has evolved over the course of the year. As new cases rise and lockdowns follow, markets have been volatile. On positive news, such as the roll-out of vaccines, markets have rallied.

During all of this, we have seen some astounding price movements in certain assets, with the gap between the winners and losers widening each day.

Technology stocks have been the story of the year. With some fearing a "bubble" at the start of the year, it is the tech giants that have enabled our adjustment to life under lockdown.

With the increase in use of social media, online shopping, entertainment and working from home, the structural shift to a heavier reliance on technology for industry, entertainment and the environment has accelerated.

As a major component of the US market, technology stocks have led the charge and new records have been achieved in the indexes of the largest listed companies such as the Dow Jones Industrial Average, S&P 500 and Nasdaq Composite.

Conversely, the global travel and leisure industry has suffered severe damage. With international travel bans, airlines have been largely grounded and some have failed or required bailouts. Bars, restaurants and cinemas have been forced to close, leading to massive job losses in the sector and impacting service led economies such as the UK, where the recovery has not been as strong.

The defining news of the latter part of 2020 was all about the vaccines. Major events such as the toppling of Donald Trump in the US election or a Brexit trade deal in the 11th hour, have been mere subplots to the virus story. We believe this will remain the case now well into the summer, so we continue to evolve our strategies around various scenarios related to the distribution success, or otherwise, of the vaccines.

While a vaccine is not universally available just yet, we recognise the potential social and economic benefits reach far beyond the first individuals who receive it. In the UK, we have spent £280 billion to protect against the virus. While critically dangerous to certain groups, it is relatively mild for the majority.

By inoculating the most vulnerable first, the hope is that the need for draconian restrictions can be removed and businesses can reopen. Confidence in sectors such as hospitality, travel and leisure should return, knowing that lockdowns are no longer the only defence against the impact of the virus.

Other changes we have seen as a result of the lockdowns should prove more positive long term, such as the acceptance of remote working practices, which could lead to a more mobile and flexible workforce.

With the inauguration of US President Elect Joe Biden, it will be a welcome change from the leadership that inspired events at Capitol Hill at the start of January. There will be a more conventional President in the White House and he inherits a relatively strong market, despite the burgeoning debt taken on to tackle the virus.

Like all global leaders, Biden’s priority will be to bring the virus under control and get the population vaccinated. However, Biden is also expected to be more diplomatic in both domestic and foreign affairs than his predecessor. While Democratic views are closely aligned to Republican when it comes to matters such as international trade, it is hoped that his more pragmatic and statesman-like approach will create a more benign business environment.

The fear remains, however, that the tech giants will be in his crosshairs, but after a year like this when they have been instrumental to living with COVID, Biden may be more reluctant to put Silicon Valley on notice. There may be more regulation to come, but the breakup of big tech is looking less likely for now.

Brexit brings its own possibilities for the UK now that an initial trade agreement with the EU has been reached. International investors may be drawn to the UK once again. While we are more positive on the outlook, we still need to understand what the long-term impact will be to key industries such as the finance sector.

Negotiations were disproportionately skewed towards fishing, a relative minnow in trade terms, rather than financial services. But we are more confident that London’s place won’t be challenged just yet by the likes of Paris or Frankfurt from what we have seen.

China is well ahead of the US and Europe in terms of its recovery. Data is expected to show that China has recovered all lost output by the start of the new year. Premier Xi Jinping has also stated that he wants to double the size of the economy by 2025. While this may seem fantastical based on recent growth, the trade war with the US and pandemic has allowed time for the Chinese to focus on developing their domestic market.

Finally, we continue to watch the “green revolution”, as economies and industry adjust to the evolving demands of the population as consumers, and guardians, of the environment. Technology will inevitably play a big part in this, but countries such as the UK along with our northern European neighbours could well be leaders in this movement.

Key facts about the world

United Kingdom

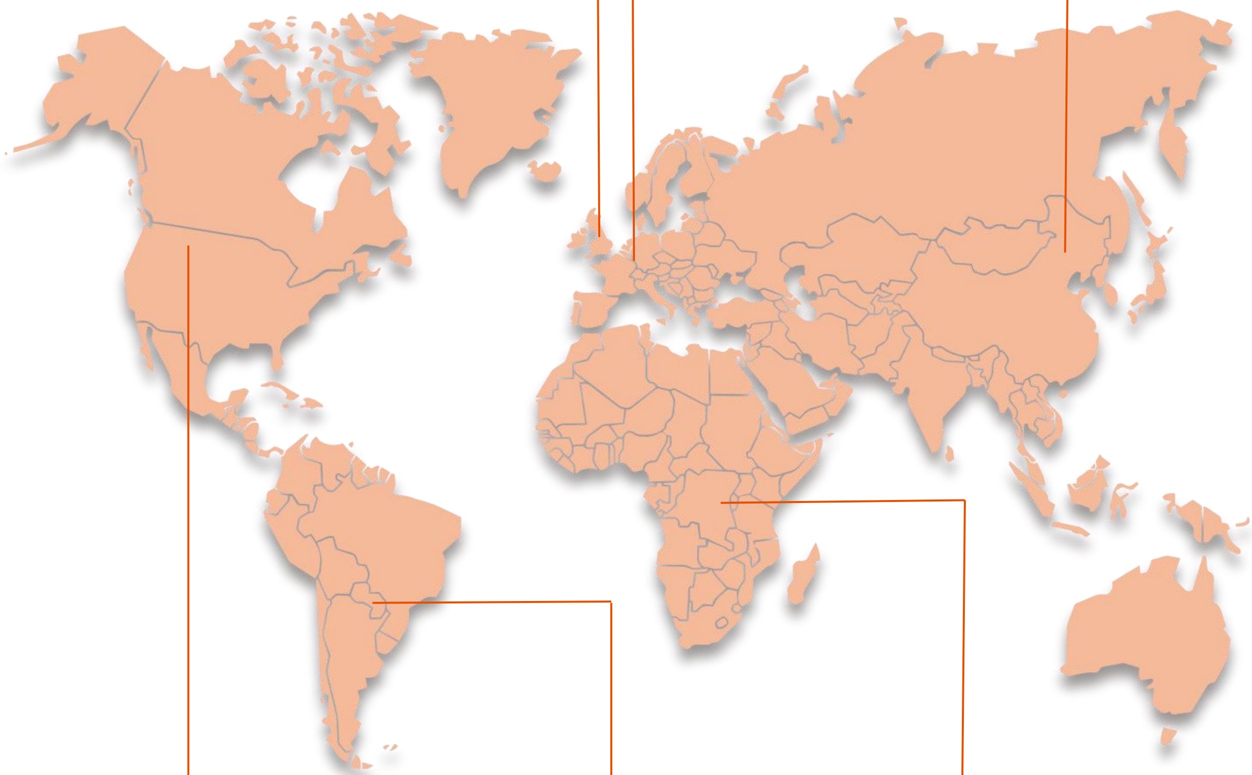
- Economic growth falls as result of repeated lockdowns
- Global leader in vaccine development and rollout
- 11th hour Brexit trade deal agreed with EU

Europe

- Discord delayed EU Budget and COVID rescue measures as Poland and Hungary threatened veto
- ECB expected to cut already negative rates further and extend monetary stimulus beyond 2021

Asia

- China leads global COVID recovery with aim to double size of economy by 2025
- South-east Asia hardest hit by pandemic, but expected to catch up strongly led by bank and energy companies



North America

- Democrat Joe Biden wins US Elections
- Tech companies lead global recovery
- Digitisation of many areas of the economy, including the green revolution, set to continue

South America

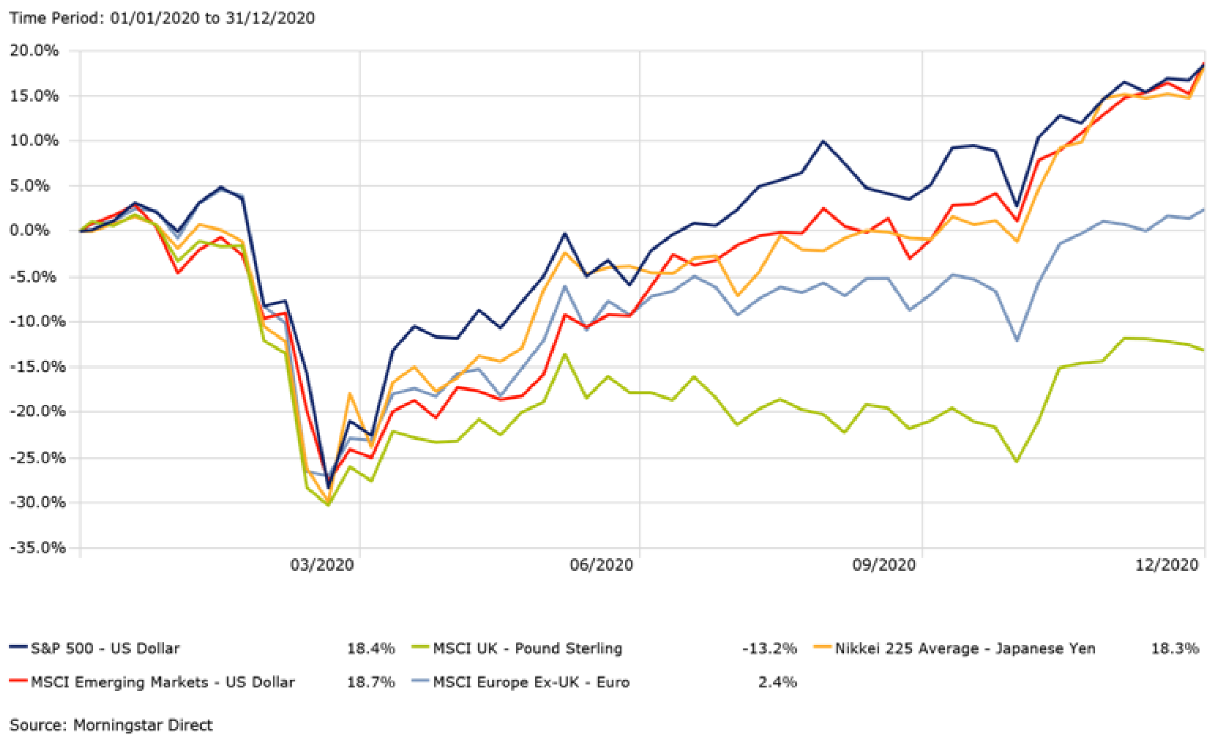
- Recovery in most major Latin American economies from COVID downturn to be amongst slowest in emerging markets
- Limited ability to implement additional stimulus

Africa

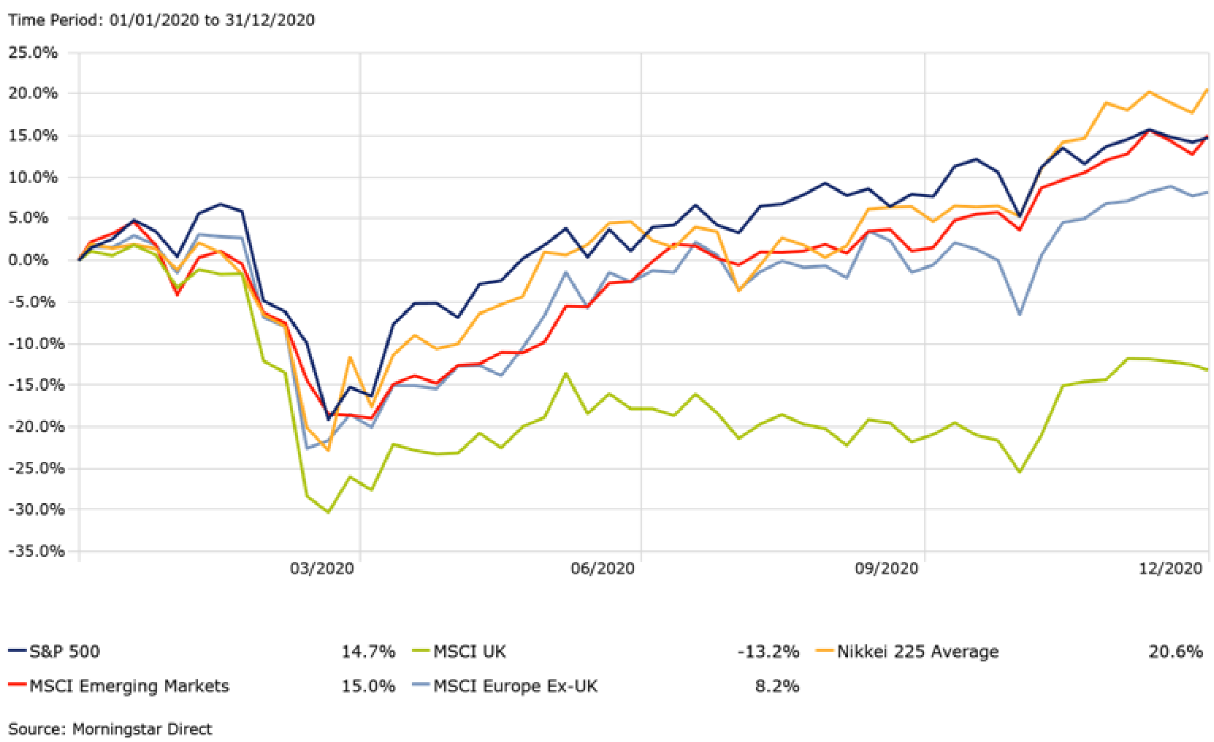
- In West and Central Africa, decline in growth driven by oil exporters as demand and prices plunged
- Investment in digital economy and infrastructure essential to recovery hopes

2020 in charts

Major market movements in local currency (1 year)



Major market movements for sterling investors (1 year)



NB Gross/total price return

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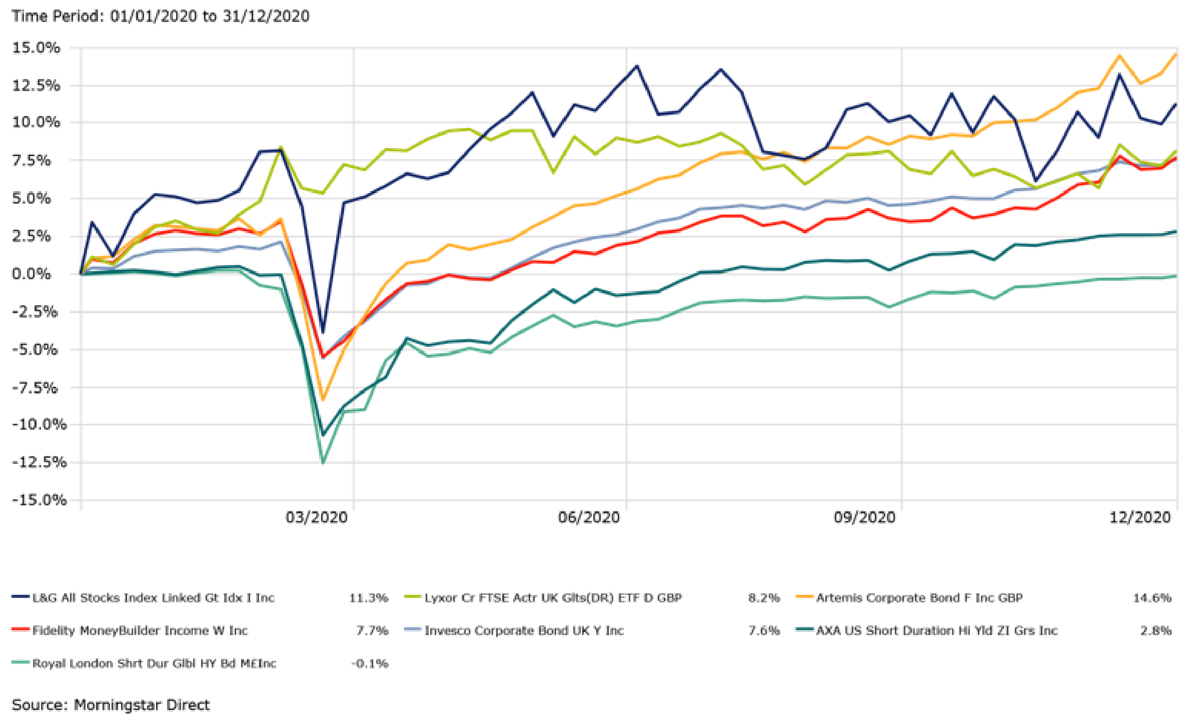
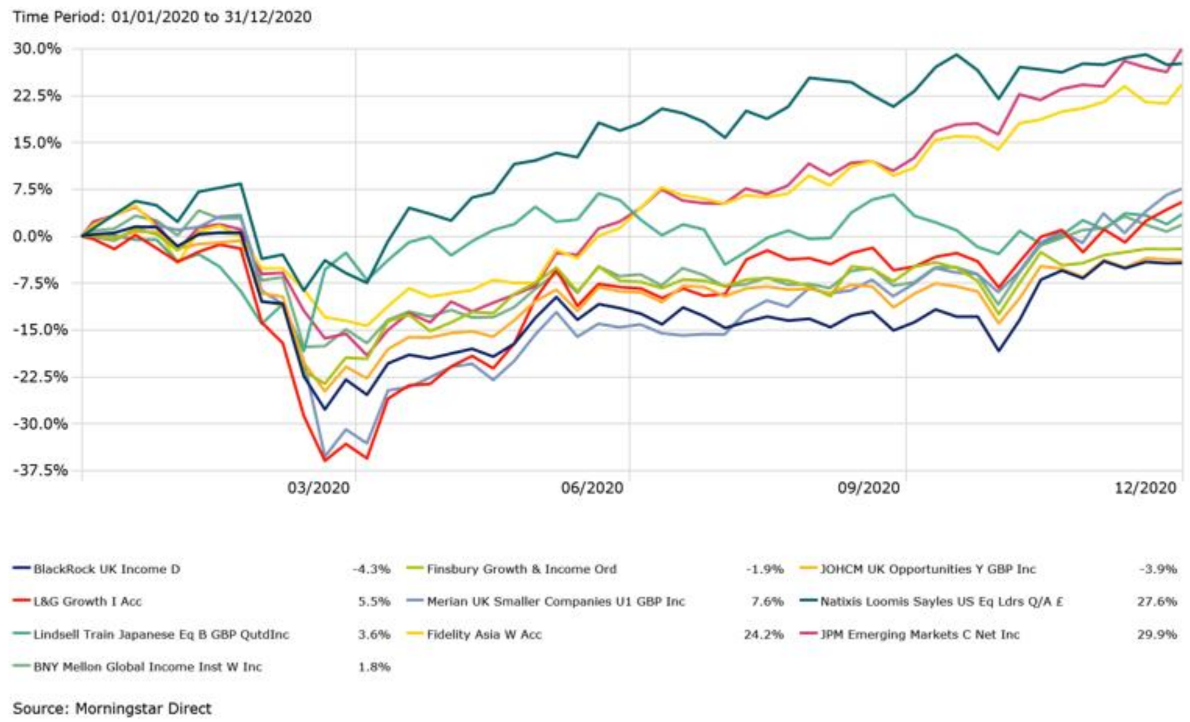
2020 in charts

Model Growth Returns Fixed Interest (1 year)



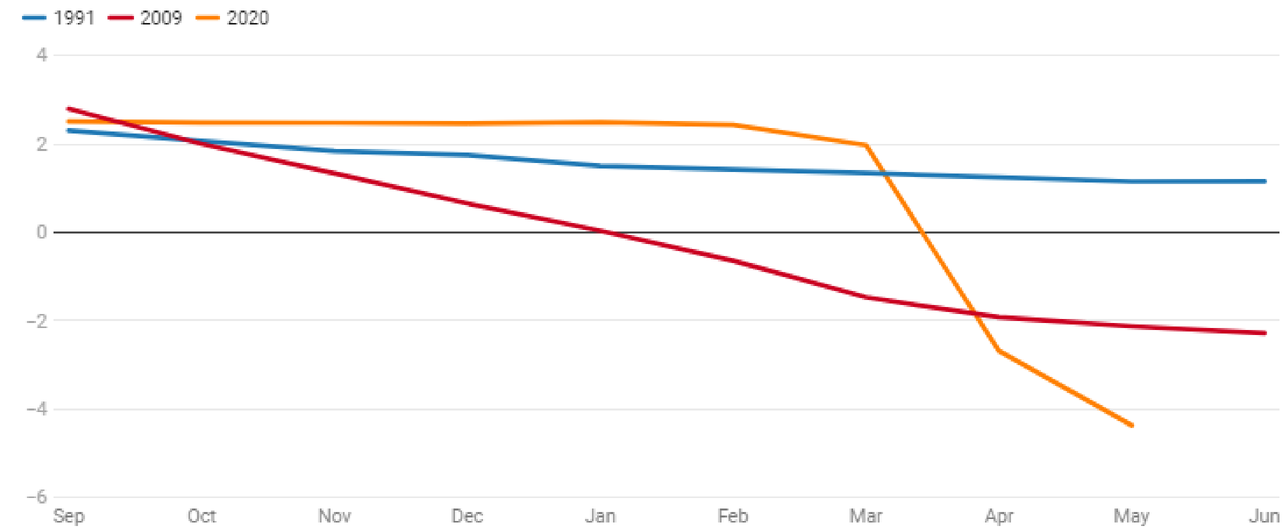
Model Growth Returns Equity (1 year)



NB Gross/total price return

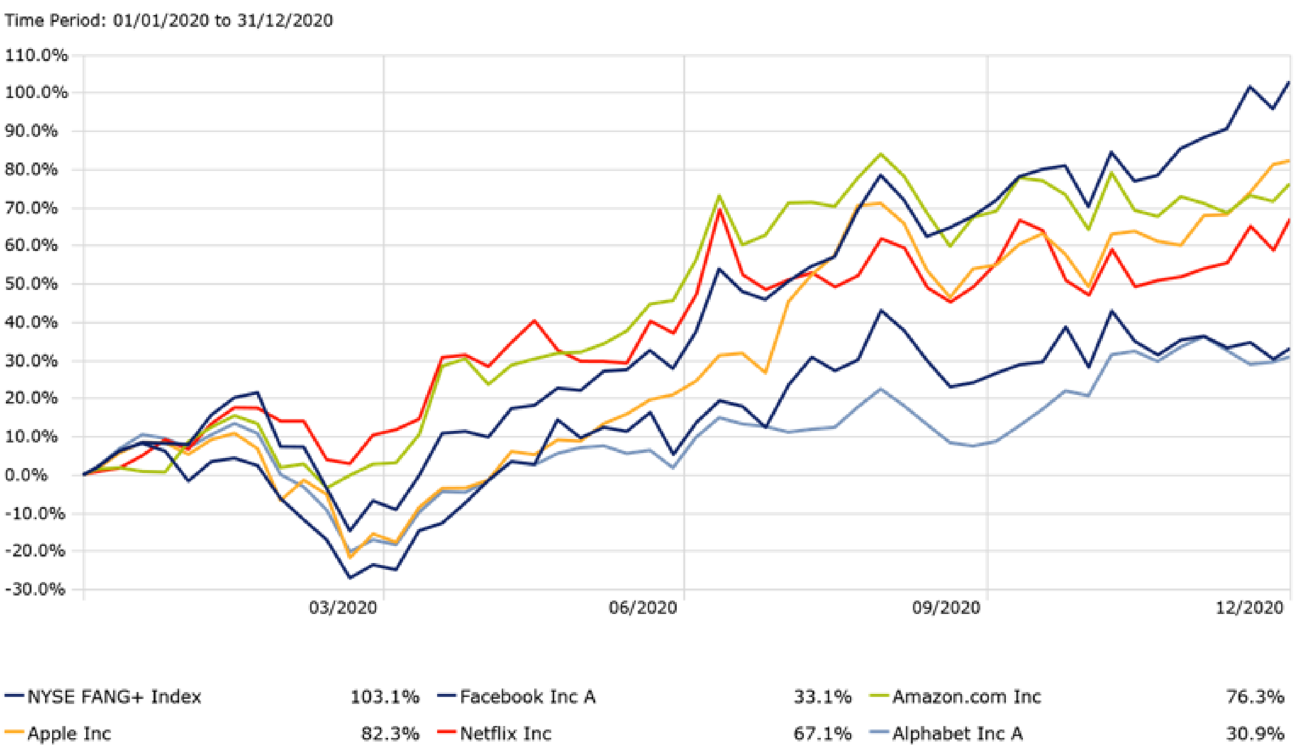
2020 in charts

Covid Accelerated Economic Downturn



Source: World Bank, consensus forecasts of global GDP (percent). The COVID-19 recession saw the fastest, steepest downgrades in consensus growth projections among all global recessions since 1990

Large US technology companies lead the recovery



Source: Morningstar. NYSE FANG+ is an index of the 10 biggest tech companies today; Facebook, Apple, Amazon, Netflix and Alphabet's Google, Alibaba, Baidu, NVIDIA, Tesla and Twitter

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2020 performance review

COVID to recovery

- Equities perform well post COVID recession in March
- Government and central bank stimulus acts as springboard for recovery
- Tech stocks lead recovery once again
- But bond yields fall further as uncertainty remains
- Pound at mercy of Brexit/EU Trade Agreement news
- Vaccine news dominates

From COVID recession to technology rally

Q1 was dominated by the COVID recession as global growth collapsed and financial markets plummeted. The UK was one of the worst impacted markets, down over 30% towards the end of March, before government and central bank intervention lead to a sharp, largely synchronised V-shaped recovery globally.

A defensive position in UK gilts added to strategies at the start of the year to offset existing equity risk performed very well during the sell-off, as did the index linked bonds. More recently and throughout the recovery it has been the corporate bonds that have provided the best of the returns in this asset class as expectations for a substantial rise in business failures and subsequent defaults faded. The Artemis fund, newly launched in October 2019, has been outstanding, up over 14% for the year.

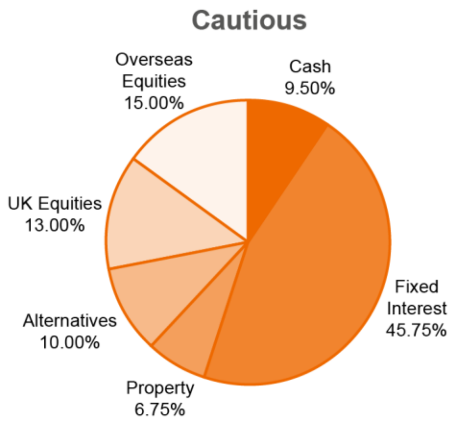
While the UK lagged both its developed and emerging market peers throughout the year, a late rally on positive vaccine news and Brexit progress helped those sectors and stocks left behind recover some of the lost ground. In particular, the Merian UK Smaller companies (+7.6%) and L&G Growth (+5.5%) provided a positive return well ahead of the wider market, which closed for the year down over 14%. International equity markets were much stronger, with the Natixis Loomis Sayles US Equity Leaders +27.6% thanks to its technology exposure and the JP Morgan Emerging Markets fund +29.9% and Fidelity Asia +24.2%, all areas we remain comfortable with for 2021.

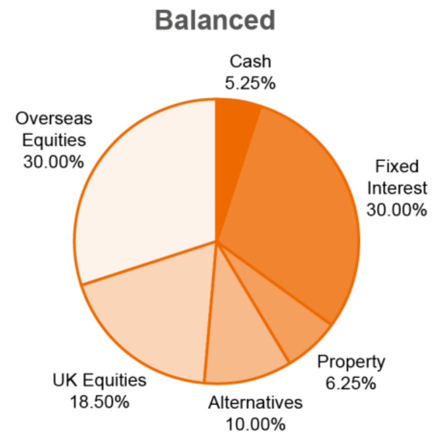
While property returns have been disappointing for most of 2020, the BMO Commercial Property Investment Trust saw a significant rally as the economy began to reopen. Providing there is any sign of "normal" day to day life with a successful rollout of the vaccine, we believe the remaining losses can be recovered over the coming year. Similarly, those sectors of the market such as income and value companies that underperformed during the lockdowns, should see a further return to favour with "business as usual" expected into the summer.

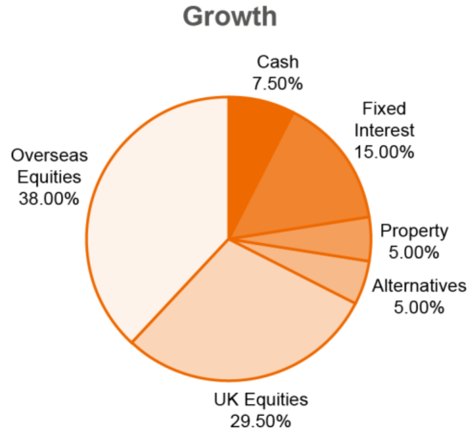
SECTOR	Q4 2020	1 year to 31/12/20	1 year to 31/12/19	1 year to 31/12/18	1 year to 31/12/17	1 year to 31/12/16	5 years (annualised)
IA OE UK Index Linked Gilts	0.1%	11.9%	5.9%	-0.5%	2.2%	25.1%	8.6%
IA OE £ Corporate Bond	3.3%	7.9%	9.5%	-2.2%	5.2%	9.7%	5.9%
IA OE Property	-0.3%	-3.8%	-0.8%	2.9%	7.6%	-2.0%	0.7%
IA OE UK Equity Income	15.6%	-10.9%	20.1%	-10.5%	11.5%	9.1%	3.1%
IA OE UK Smaller Companies	21.7%	7.0%	25.4%	-11.8%	27.1%	8.5%	10.3%
IA OE North America	7.8%	16.4%	24.6%	-1.2%	10.5%	30.1%	15.6%
IA OE Europe Excluding UK	9.8%	10.5%	20.4%	-12.2%	17.5%	17.1%	10.0%
IA OE Japan	9.1%	13.9%	17.1%	-11.3%	17.8%	23.5%	11.5%
IA OE Asia Pacific Excluding	13.3%	19.9%	15.8%	-9.8%	25.3%	26.0%	14.6%
IA OE Global Emerging Markets	15.5%	13.6%	15.7%	-11.5%	24.5%	31.6%	13.8%

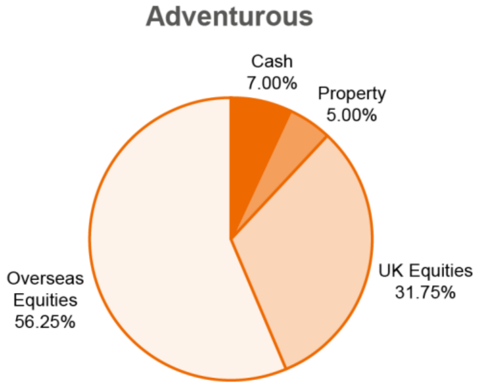
Source: Morningstar, bid-bid pricing, net income

The positioning of our core strategies

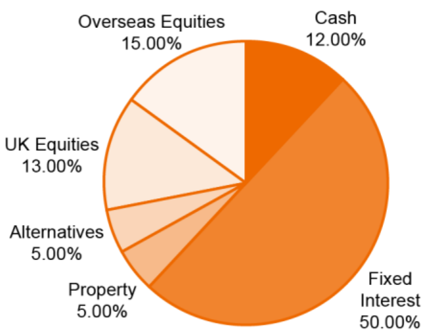




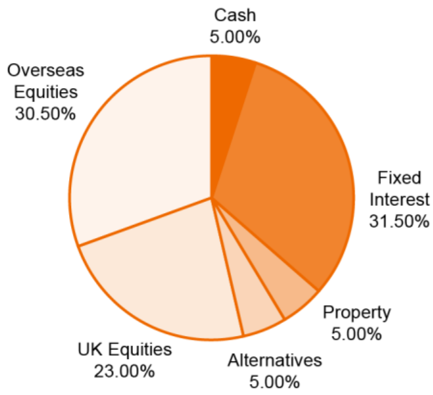




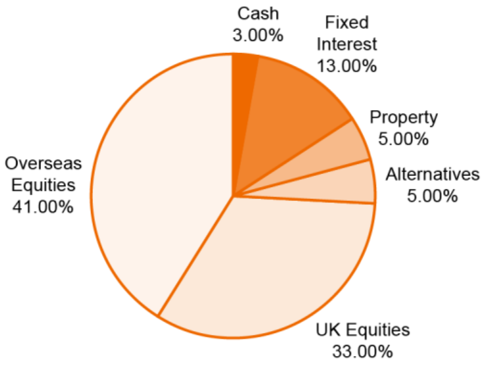
Ethical Cautious



Ethical Balanced



Ethical High Growth



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