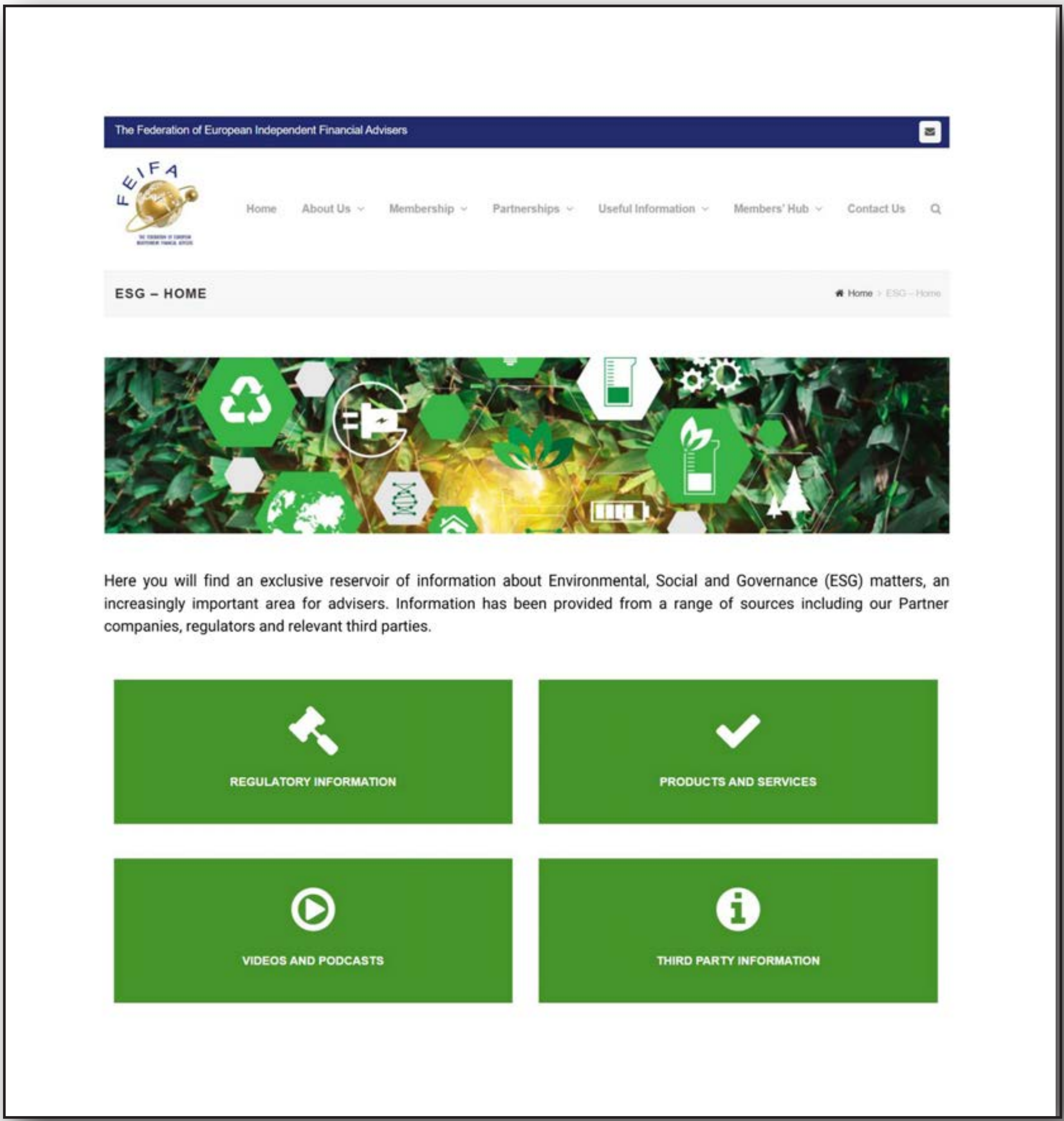
MARCH 2021

THE TRADE PRESS

The Federation of European Independent Financial Advisers



FEIFA launches unique ESG platform

See pages 8/9

ISSUE No 131
CONTENTS

The rise of green mining

Bedford Row Capital discusses.

Elon Musk: irrespective of your views of him, Elon is on a mission (no pun intended with SpaceX). He should be credited with creating the electric vehicle market and popularising new models of battery storage for the consumer market. The surge in demand for the production of both EVs and new batteries will require huge amounts of raw material and new factories and processes.

Electric vehicles are not new; in fact, they predate the combustion engine. First built in the 1830s by Robert Anderson it has taken over 175 years for EVs to become mainstream. Now all major car companies announced that within the next decades the combustion engine will be fully replaced by battery-powered cars. This shift from fossil fuel to battery power supports the Great Green Deal of reducing carbon dioxide emissions helping to reverse the climate crises. To meet this demand, the surge in the demand for battery minerals could be a paradigm shift for mining companies.[1] To meet this seemingly inexorable demand, sustainably, mining companies need to adapt.

Fundamental to both EVs and more efficient consumption of renewable energy is the underlying battery technology. New technology batteries are what make the Tesla accelerate in "insane mode" and hopefully, store community generated solar and wind power. Battery technology is consuming huge amounts of intellectual capital and raw material like lithium, cobalt, graphite and nickel; finite resources with an exponential growth in demand forecasted.

To combine both the potential commercial opportunity and do it in the "right" way, investing in the future of battery technology and the extraction of the core minerals must consider the impact the mining operations have on the environment. Green mining? Yes. We have seen a number of innovative mandates which combines both of these themes into asset-backed, high-yield investible propositions.

Green mining is a new, forward-thinking way of sustainably extracting minerals out of the ground with a less harmful impact on the environment. Listed companies like NQ Minerals, Altech Chemicals have put a lot of information in the market about the importance of these minerals. An Australian company called Energy Storage is focussing on the actual technology; all these companies offer new techniques and technologies to provide the required supply of crucial minerals but with a clear goal of doing it in a green manner. This has a positive impact on the whole value chain and creates unique opportunities for investors to participate in the inevitable green mining and battery technology evolution.

These companies are not only interesting from an income profile (in a world of low returns and increasing inflation) but from an impact perspective. Outcome focussed, these companies demonstrate a way forward for sustainable business in an exciting high growth sector of the economy. Professor Kevin Haines, BRC´s Head of Social Policy, sees it as the fundamental role of BRC´s commitment towards SDG/ESG to provide companies and investors with the expertise to achieve their commercial and impact goals. Beyond just high yield investments, these companies are working hard to do good.

For further information contact **Anella Veebel – anella@bedfordrowcapital.com**

[1] *https://www.miningweekly.com/article/battery-minerals-demand-surge-to-dwarf-anything-ever-seen-before-davis-2021-02-10/rep_id:3650*

Editorial Comment

Sustainable advice

The combined impact of COVID-19, ESG regulation and shifting consumer demands is creating rapid changes in the nature and delivery of advice. We are providing numerous services to help you in this regard.

Masterclass Webinars – you should already have received an email on these events, which take place later this month. Full details can be found **here** or you can simply register **at this link**.

ESG Platform – we launched this a few weeks ago; there is an article explaining its contents on page 8 and the platform can be found within our Members' Hub (**here**).

Articles – this issue has three articles focused on various aspects of "Sustainability" and numerous others looking at investment markets in the light of the global pandemic.
And I haven't even mentioned Brexit…!

Regards
Paul

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DID YOU SEE?...

In this section we will highlight any developments at FEIFA over the last month, which you may have missed, plus any potentially relevant and useful articles from our Associate Members and other appropriate sources. For articles in the Member's Hub, you will, of course, need your usual password.

FEIFA in the Media

- How did European advisers fare in 2020?

Members' Hub – Brexit

- Post-Brexit access regimes in EEA member states
- Ireland: update on insurance run-off regime
- Italy: limitations for UK banks and investments companies
- Brexit and Financial Services: 2021 update
- Beyond Brexit – what now for insurers' legacy business?
- Luxembourg: UK deemed equivalent

Members' Hub - ESG

- ESMA: legal framework for ESG ratings and assessment tools
- ESMA: final rules on SFDR
- Final rules on Sustainable Finance Disclosure Regulation
- ESG & investment – return on Sustainability
- Report on renewed sustainable finance strategy

FEIFA Associate Members' Articles

- Spanish wealth tax – part 1
- Spanish Wealth Tax – part 2

Luxembourg: your safe haven! – *Part I*

OneLife discusses.

Solid, innovative and transparent - Luxembourg, officially known as the Grand Duchy of Luxembourg, is one of the smallest sovereign states in Europe, bordered by Belgium, Germany and France, and one of the least-populous countries in Europe. And Luxembourg is far more than that. In the first part of this article, we will focus on its innovative character, its stability and fiscal transparency, before we shine our light on the impact of these characteristics on Luxembourg's primary industry, the financial sector.

On the 2020 European Innovation Scoreboard, which assesses the performance of countries in the field of **innovation** based on 27 indicators, the Grand Duchy came 5th and joins the EU **innovation** leaders[1]. In the Global Innovation Index 2020 rankings, Luxembourg is 18th and is together with China and Israel as the country ranking third in terms of creative outputs (venture capital, research and development, entrepreneurship, or high-tech production)[2].

Thanks to a purchasing power parity (PPP) of USD 112.875,12[3] in 2020 Luxembourg ranks first in the world and achieved a GDP per capita, expressed in PPS, of 263% of the EU average in 2018[4], with a general government net debt of EUR -2.90 billion and an unemployment rate of only 6.47% of its total labour force[5], making it **one of the most economically stable countries in the world**, if not the most stable.

The four credit rating agencies – DBRS Morningstar, Fitch, Moody's and Standard & Poor's – have confirmed Luxembourg's **triple A credit rating** despite the coronavirus pandemic. DBRS and Fitch consider that the economy ought to bounce back to pre-crisis levels in 2021 and confirms thereby that, despite the difficult economic context, the foundations of Luxembourg's economy remain solid. DBRS considers that the Grand Duchy ought to remain an attractive destination for investments and also acknowledges the Government's sustained effort in the field of fiscal transparency[6].

One of the direct consequences of the financial crisis of 2008 was a global push towards increased transparency in tax matters. Finance Minister Pierre Gramegna emphasises that Luxembourg did indeed adopt **fiscal transparency** "The country complies with all OECD and EU standards and guidelines on tax transparency, specifically in the area of exchange of information and administrative cooperation. […] These efforts have been recognised by the OECD Global Forum and the EU"[7]. Moody's states moreover Luxembourg's high degree of transparency as one of the reasons for its triple A rating[8]. In OECD peer reviews of tax transparency, **Luxembourg now enjoys the same ranking as Germany, the UK and the US.**

In the second part we dive deeper into the financial sector and what the aforementioned characteristics mean for the financial industry and its future ambitions. Stay tuned, stay safe and, if you already have some questions, please get in touch with OneLife at
https://www.onelife.eu.com/contact-us/

1 *European Commission, 2020, retrieved on 1/02/2021, https://ec.europa.eu/docsroom/documents/42981*

2 *The Global Innovation Index 2020, retrieved 11/02/2021, https://www.wipo.int/global_innovation_index/en/2020/*

3 *IMF, retrieved 11/02/2021, https://bit.ly/37gMKQZ*

4 *Eurostat, 05/03/2020, retrieved on 11/02/2021, https://ec.europa.eu/eurostat/documents/2995521/10474907/1-05032020-AP-EN.pdf/81807e19-e4c8-2e53-c98a-933f5bf30f58*

5 *IMF, retrieved 11/02/2021, https://www.imf.org/en/Publications/WEO/weo-database/2020/October/weo-report?c=178,137,&s=NGDP_R,NGDP,PPPGDP,NGDPRPC,NGDPPC,NGDPDPC,PPPPC,PPPSH,PCPI,PCPIE,TXG_RPCH,LUR,GGXWDN,GGXWDG,&sy=2018&ey=2025&ssm=0&scsm=1&scc=0&ssd=1&ssc=0&sic=0&sort=country&ds=.&br=1*

6 *Official website of Luxembourg, 29/09/2010, retrieved on 11/02/2021, https://luxembourg.public.lu/en/invest/competitiveness/economie-fitch-dbrs.html*

7 *PaperJam, 09/02/2021, retrieved on 12/02/2021, https://paperjam.lu/article/strategie-communication-gouver and 29/01/2021, edited on 01/02/2021 and retrieved on 15/02/2021, https://paperjam.lu/article/moody-s-certifie-triple-a-luxe*

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Investing in bitcoin – a safe investment?

Canaccord Genuity Wealth asks the question.

Bitcoin is the best known of the 1,800-odd cryptocurrencies. Its meteoric rise has drawn many investors, with some believing that the underlying blockchain technology (blockchain is a digital ledger in which transactions made in cryptocurrencies are recorded chronologically and publicly) could become one of the most powerful tools ever given to civilisation. But do investors understand the risks and does the underlying technology even matter?

Bitcoin investing - the risks

To us, any suitable investment requires a valuation methodology, safe custody and easy transferability. Bitcoin fails to meet these tests.

1. **Valuation:** bitcoin has no proper valuation method or underlying value. This is unlike equities which can be valued by their earnings or cash flow, bonds by yield, property by rental income and location and commodities by their industrial usage. There may be scarcity, because only a limited number of bitcoins is produced, but scarcity does not create value unless the product has an economic purpose. Should bitcoin be worth US$10,000, US$100, US$1m or 10 cents? There is no measurement to help make that decision.

2. **Safety:** other investments have custodians, registries, etc. to protect investors. With unregulated transferable cryptocurrencies such as bitcoin there is no central bank or public authority issuing or guaranteeing the asset. This is unlike central bank digital currencies (CBDCs) which are regulated. One astonishing statistic is that, at the time of writing, 20% of bitcoin has been lost, unrecoverable[1]. The private keys and digital wallets are inherently vulnerable, and intermediaries charge enormous amounts to deal with that basic safety issue.

3. **Transferability:** it takes a long time and huge efforts to buy or sell (particularly to sell) bitcoin. 'Mining' – where bitcoin transactions are digitally verified and added to the public 'blockchain' ledger – is highly time-consuming, whereas equities and bonds can be sold in a fraction of a second.

Regulation around bitcoin investing

It is no surprise that many governments, including South Korea, China and France are clamping down on cryptocurrencies such as bitcoin. And recent regulatory changes in the UK provide stark evidence as to the concerns for investors. The Financial Conduct Authority's near-total ban on cryptocurrency investment for UK retail investors shows that it is a matter of time before stronger restrictions are slapped on these assets in many parts of the world.

Bitcoin investment - the new gold?

Some adopters of bitcoin have heralded the asset as 'the new gold', suggesting it could be used as a defensive portion of a diversified portfolio. But gold has been around for thousands of years as a payment method and investment meaning there is some way of measuring its worth and the correlation with other asset classes. The extremely short history of crypto assets means this is impossible to do and the risk too high to warrant their inclusion in portfolios.

Theoretically, anything can go into a diversified portfolio (art, racehorses, timber) but most of these idiosyncratic assets have enough history to justify an analysis before placing them in a portfolio. Cryptoassets do not.

What is the outlook for cryptocurrencies?

Although cryptocurrencies seem to move up and down with risk appetite, their price graphs make the 17th-century tulip craze look like a triple-A rated government bond. More importantly, out of 1,800 outstanding cryptos plus any new cryptocurrencies issued in the future, are you confident you could pick the survivor?

Many governments and central banks have mentioned their desire to issue cryptocurrencies. It is therefore theoretically possible that such investments could be backed by a reputable country in the future, but until we can do due diligence on the terms of such cryptocurrency issuance and fully understand the motivation for governments doing this, investors may want to remain sceptical.

Blockchain may well be one of the technologies of the future (although it scores poorly environmentally, given the huge electricity consumption required for 'mining') but this alone doesn't warrant investing in bitcoin or other unregulated transferable cryptos for that matter, and there are countless other reasons not to.

For more information about CGWM's investment philosophy and outsourced investment solutions contact **Richard Burden – richard.burden@canaccord.com** or tel: **+44 (0)7624 499 590** or visit **our website**.

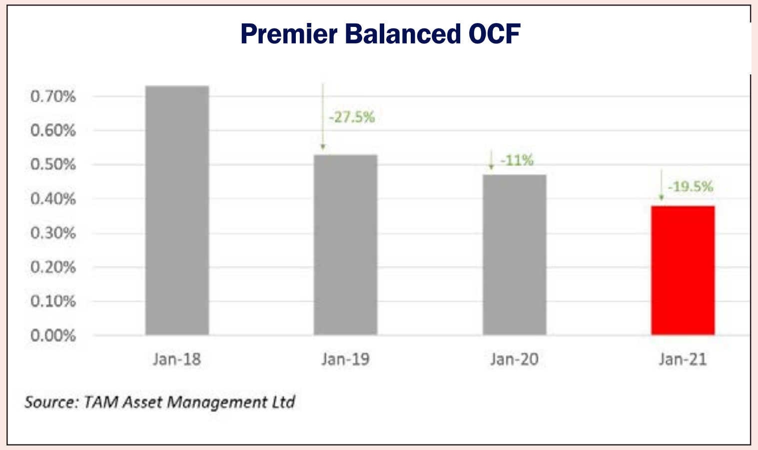
[1] *https://www.investopedia.com/ws/20-all-btc-lost-unrecoverable-study-shows/*

Another cost bites the dust

TAM Asset Management highlights fee reductions.

As we all know, the cost can be the deciding factor when it comes to a client choosing an investment.

Over the years, TAM has done its upmost to make that decision an easy one. How? Because of our continued efforts to cut costs for the end client, both in our management fees and the underlying OCFs of the funds selected for our model portfolios which can be seen below.



At the start of the year, we were pleased to announce a reduction in our mainstream investment portfolio AMC from 50 bps to 30 bps. This, together with the ongoing decrease in OCF charges, not only makes TAM one of the most attractive investment propositions available in the European market, it also makes TAM a fund of funds portfolio manager that can manage money for less than a 1% total charge.

As most retail fund classes are offered at 95 to 125 bps, this therefore means that the cost of buying a managed investment portfolio is now more or less equal to buying a retail fund.

The advantages to choosing an active investment portfolio far outweigh those for a passive portfolio, but one of the very few disadvantages to choosing an active portfolio has historically been the high price point. As you can see from the graph, such a disadvantage no longer applies, making an active investment portfolio the ever more attractive choice.

Gone are the days of fund picking for clients to save on costs, now IFAs can enjoy the solution of a well-established manager running a portfolio for the same cost, or even cheaper, than choosing the fund themselves.

And finally, we would like to remind readers that as a member of FEIFA, you can also enjoy a reduced AMC for our ESG investment portfolios of just 35 bps. To speak to us about our model portfolios and associated fees, please contact **Tom Worthington** at **tom.worthington@tameurope.com**

Unique ESG platform

Last month we announced the launch of our **online ESG platform**, exclusively for the use and benefit of our members. This can be found within the Resources section of our Members' Hub (**https://feifa.eu/members-hub/**) and also accessed directly at: **https://feifa.eu/esg-home/**. You will require your usual Members' Hub password in either case.

It is divided into four sub-sections, as detailed below – we have summarised the key content of each section and sub-section, which should hopefully help you find what you need even more easily.

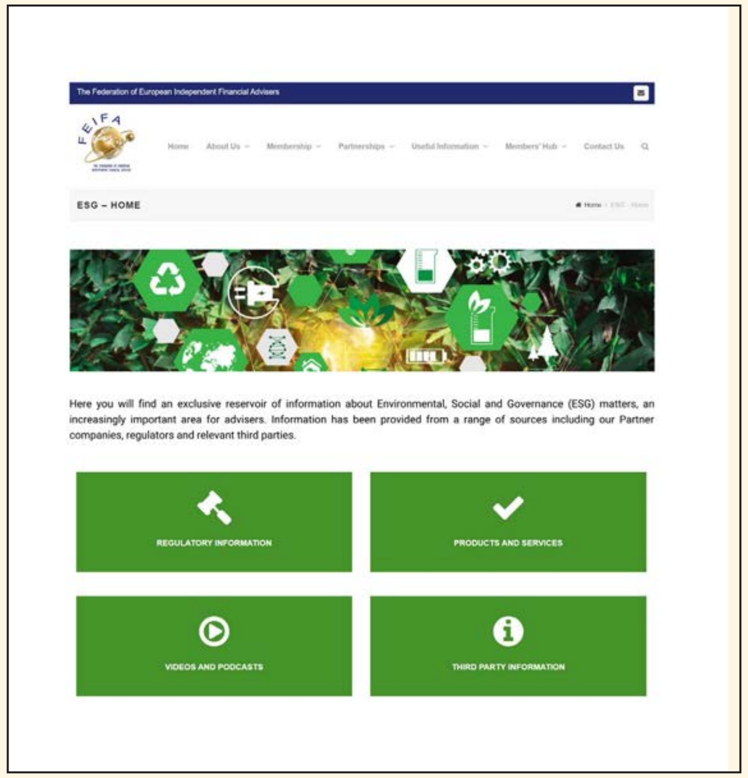
1. Regulatory Information
This area details, via a small number of links to relevant documents, the key regulatory aspects that you may need to know and/or reference. It includes the initial EU Action Plan from 2018 all the way up to the latest proposals, last month, for ESG ratings and assessment tools.

2. Third Party Information
Comment and information from the media and also other professionals, such as legal experts, providing wider context and far-reaching analysis and viewpoints.

3. Products & Services
Content from a number of our Partner companies can be found here. Below is a quick summary, with companies ordered by Partnership level and then alphabetically, as on the platform.

- ***Janus Henderson*** - a number of reports and an investment philosophy document are accompanied by a couple of interesting articles. There is also a video: "Deconstructing Sustainable Design".
- ***TAM Asset Management*** - some excellent generic documents and articles are joined with fund and product information. There is also a very useful ESG Questionnaire – that advisers can use with clients (or potentially incorporate into their existing factfinding).
- ***LGT Vestra*** - a couple of good articles/documents look at "Redefining the mainstream" and explore how regulations are bolstering the inclusion of sustainable investments. These are accompanied by another very useful client questionnaire.
- ***Prestige Funds*** (*added since launch*) - various strategy-related content: an adviser presentation for this quarter; a look at "private debt for a greener world"; an examination of renewable energy from farm/agricultural waste. There are also examples of a relevant finance trade and a project finance solution, a couple of articles and a link to fund information.
- ***Fidelity*** - some thought leadership content, including sustainable investing themes for 2021, is coupled with wide-ranging product information and details on the company's proprietary ratings system. There are also details on its "Water & Waste Exposure Tool" and "Client Support Tool", plus a podcast link: "The future of green investing".
- ***Dynamic Planner*** - a link to its independent ESG whole of market research, covering more than 36,000 funds, which can all be found in a single place.
- ***Guinness Asset Management*** - a "Sustainable Energy Webcast" along with a range of product documents and information, including an impact report, provide good breadth of content.
- ***Marlborough Group*** (*added since launch*) - a link to a full explanation of Marlborough's "Engagement Policy" can be found here, highlighting the individual ESG mechanisms used in each fund/strategy, and a brochure summarising the company's policies in this regard.
- ***PortfolioMetrix*** - here you will see a link to the company's responsible investing white paper, which covers areas such as terminology, ESG measurement and ratings agencies, relevant regulation and performance misconceptions and indicators.
- ***Tilney*** - a webinar and a podcast, on "Ethical investing's role in the global recovery", can be found; along with performance factsheets and relevant product information.

4. Videos & Podcasts
A dedicated section with visual training and information resources collated from a number of our Partner companies; including a look at the future of "green investing" and an analysis of sustainable energy. This section collates video content from the individual Partner sub-sections in one place, for your convenience.



This ESG platform will, of course, be an organic resource; we will be adding to it on a regular basis and keeping you updated about any new content. ***This will predominantly be communicated to you via the new "Did you see?…" section of this e-magazine (page 4)***.

Any feedback or questions please contact **Paul Stanfield – pstanfield@feifa.eu**

Are you ready for 10th March 2021?

LGT Vestra explains what you need to be aware of.

Clients are increasingly aware of the importance of Environmental, Social and Governance (ESG) investment and sustainable solutions, and as a result, financial advisers are beginning to incorporate a third dimension of investing, which includes 'non-financial preferences' in their clients' fact finds and discussions.

Not only do clients have a growing interest, regulators are also increasing the scrutiny placed on the subject and the investment community is responding with innovation and a range of solutions. The long and short of it is, the ESG/sustainable investment market is growing exponentially and, as a result, becoming increasingly complex and difficult for financial advisers to navigate.

So, what is the route map?

The introduction of the Sustainable Finance Disclosure Regulations (SFDR) will have far-reaching implications for asset managers, financial advisers and life assurance companies. Effectively, the SFDR affects financial market participants, which includes financial advisers who are required to take into account, sustainability risks and sustainability factors.

Due to the impending introduction of the regulation, research agencies are gearing up to analyse, profile and score ESG/sustainable solutions, which will provide more clarity on investments, allowing investors and financial advisers alike to make more informed ESG and sustainability related decisions.

When will it happen?
With regard to the timeframe, the SFDR comes into play in stages. The first by the 10th of March 2021 and the second by early 2022.

What disclosures will be required?
From 10th of March, the SFDR introduces new disclosure obligations at an entity level (financial market participants and financial advisers) as well as at a product level.

Company level disclosure
Market participants and financial advisers are required to disclose information related to sustainability risk, remuneration policies in relation to sustainability risk, and adverse sustainability impact.

- **Sustainability risk:** The need to disclose information on policies on the integration of sustainability risks in the investment decision-making process / in the investment advice or insurance advice.
- **Remuneration:** The need to disclose information on how remuneration policies are consistent with the integration of sustainability risks. The information is to be included in the existing remuneration policies.
- **Principal adverse impact:** the requirement to disclose how they consider the principal adverse impact of their investment decisions / advice on sustainability factors on a comply-or-explain basis. The sustainability factors are pre-defined in a template that according to the current Level II proposal consist of 32 mandatory indicators (16 are environmental and 16 social) and 18 voluntary indicators (11 are environmental and seven are social).

The indicators should apply across the whole reference period and not just a snapshot at the year-end to avoid window dressing.

So, what does this mean?
This regulation is all about both transparency and accountability, along with encouraging behavioural change in the investment sphere. It will undoubtedly shine a light on how companies behave in relation to their ESG and sustainability criteria themselves. This will give investors the ability to not only see how 'green' their adviser is, but also the credentials of their chosen investment manager and whether they 'walk the walk' as well as 'talk the talk'. It will be interesting to see how this plays out across Discretionary Fund Management firms.

For further information contact **Robert Hardy**, International Technical Director– **Robert.hardy@lgtvestra.com**

Haymarket Capital was founded in 2016 and is the exclusive global distributor of the Hanson Sustainable Income Fund.

Sustainable dividends

The Hanson Sustainable Income Fund was founded by the Hanson family with the aim of providing capital growth across the cycle and regular dividends. The fund aims to pay a 4% annual yield, which has so far been achieved. This is achieved by investing in dividend paying companies which have embraced sustainability in the areas of Environment, Society & Governance (ESG).

The fund is a UCITS V fund and is available across bond, pension, and investment platforms.

The fund's sustainable goal is to make 'a net contribution to sustainability' assessed by the investment manager, Arlington Capital's, proprietary 24 test sustainable scoring system that all holdings are subject to and scored on an annual basis. The fund has been on a sustainable journey asking key questions such as:

What shade of green does not come out in the wash?

How do you assess and measure sustainability?

Can your assessment add positive value to the investment proposition?

We believe that the sustainability of a business concerns the degree to which it reduces negative impacts on the natural environment through its operations and how it adopts business practices that positively contribute towards sustainable development.

Taking these questions in turn, 'greenwashing' is where companies pay lip service to the regulations but in reality, little change is made to their operations. To address this the fund decided that to adopt a sustainable objective to 'make a net contribution to sustainability'. To quantify and assess relative sustainability Arlington Capital adopted a sustainable scoring system that could make positive and negative assessments. The measuring system is holistic; with tests developed in the following areas: climate, resource efficiency, social, and governance as well as areas of excluded activities. Arlington believes that its 24-test system will enable it to look through greenwashing.

The third question is vital. Investors expect a return on their capital and sustainability must add value. There is much evidence to suggest that companies which have higher sustainable scores perform better than ones which do not. Arlington believes that sustainability helps them to identify risks which are vital in assessing the quality and resilience of a business model. They believe that companies which score positively have lower business risks and produce stronger returns. For the fund, that could mean they may have the ability to pay higher dividends.

A good example is Smurfit Kappa, Europe's leading packaging company. Smurfit is benefitting from the accelerating trends in e-commerce and increased demand for recyclable packaging. It has a net sustainability score of +19 / 24 and is raising its targets for energy efficiency and sustainable sourcing.

Looking at the markets for 2021 Arlington agrees with the UBS view that "from a regional perspective, we continue to see most potential upside in the UK". They expect a near 40% rebound in earnings in 2021, driven by the global economic recovery. Arlington believes that international investors will rotate back into UK equities driven by cheap fundamentals, a positive outlook for Sterling, earnings growth and an attractive yield.

The Hanson Sustainable Income Fund holds companies that can grow their earnings in this environment such as AT&T, Smurfit Kappa and Unilever and will weather any storm well. Our exposure to an element of recovery will help our more cyclical stocks like the oil companies. We are beginning to look again at those recovery stocks that will be able to dramatically improve their dividends in 2021 as life returns to normal.

We believe that by embracing the sustainable agenda companies will build more resilient business models and make a vital contribution in the transition to a green economy. The fund invests in large companies which dominate their sectors and have market-leading brands. We believe that these firms will enjoy stronger, more resilient margins than their competitors and their share prices should outperform. We will use any short-term volatility as an opportunity to build up positions in our highest convictions. This later point is essential in order to preserve capital in volatile markets.

For further information contact **Hugh Beaumont – hugh@hsincome.com** or on tel: **+44 (0)7815 948 353**.

UK SME sector: a lot tougher than it looks in the headlines

Prestige Funds discusses.

As we move into 2021 many of the unknowns of 2020 have become the knowns of 2021 - the US election has taken place and we have a new president sworn into office. An initial Brexit treaty has been negotiated and the UK has left the European Union. The UK is also leading the way in the deployment of new vaccines which signal the possibility of the end of the pandemic this year.

As a private debt manager, we have to look to the fundamentals, however, and we see much to be encouraged about, with huge fiscal stimulus programmes being rolled out in both the UK and US, our core markets. According to Goldman Sachs, the US is en route to 3%-4% GDP growth in 2021, with the UK forecast to see 5%-7% GDP growth.

A year of change and opportunity

The UK market sets out in 2021 with manufacturing PMI at a three-year high. Preparations are afoot to host a G7 summit in the country as well as the important UN Climate Change Conference. It is going to be a year of change and of opportunity for businesses on both sides of the Atlantic.

According to the UK's Office of National Statistics, aggregate national profit share (gross trading profits of the corporate sector) rose 23% to a record GBP126bn in the three months to September. For the first nine months of last year, according to the ONS, total corporate profits averaged GBP116bn a quarter, compared with GBP115bn in 2019. In other words, ***companies in the UK were more profitable during the pandemic than before it***.

While turnover has fallen, so have the bottom lines for many UK companies. Grants, tax deferrals and tax cuts, not to mention the employee furlough scheme, have all had a substantial impact on the UK corporate bottom line. This leaves many UK companies with the prospect of making considerable savings - the Office of Budget Responsibility expects UK companies to have saved around GBP30bn in cash in 2H 2020.

UK small businesses are resilient

The UK small business sector has proved very resilient under the twin threats of both Brexit and the pandemic: according to Goldman Sachs,

Continued on page 13

Recovery's winners and losers

As investors look ahead to a time when the pandemic will be over, Ed Smith and Sanjiv Tumkur, respective heads of asset allocation and equity research at Rathbones, question whether equity markets are in the midst of a great rotation from 'growth' to 'value'.

As vaccines dominated the headlines, a shift began where stocks that were seen as winners of the pandemic seemed to go out of favour, and investors rushed to embrace the cheaper 'value' stocks that have been hard hit by the pandemic. Is this a lasting change of heart that could impact on the long-term performance of your clients' portfolios? We don't think so. The last three significant rallies in value stocks happened in 2009, 2012 and 2016 when economic conditions were very different than they are today.

Those past value rallies occurred when leading economic indicators were depressed, when yields on corporate bonds versus safer government debt had spiked and when the broad market had experienced a large sell-off. None of those conditions are in place today. It's also unusual that the recent bounce in value stocks has not been driven by rising bond yields. If central bank bond buying programmes continue to keep a lid on yields, the policies could hold back any further rally in value.

Around half of the MSCI World Value Index is made up of companies in the financials, energy and materials sectors, the earnings of which haven't grown in aggregate since the global financial crisis. While there are undoubtedly attractive names in each of these sectors, we would be cautious about increasing broad exposure to them given the uncertainty ahead.

But what about the most expensive growth stocks? Should clients be worried about any exposure they have to them? We think it makes sense to reduce exposure to the most expensive growth stocks, while sticking with quality factors found in the cyclical companies (those that do better in an environment of broad economic growth) that lie somewhere in the middle of the growth-value spectrum. As for 'pure value' and 'deep cyclicals', whose prospects rest solely on the COVID recovery rather than any structural or fundamental drivers – we see these as unattractive for long-term investors.

Some sectors look more likely to benefit as the global economy recovers. In particular, the industrials sector has performed well recently due to its cyclical qualities. Elsewhere, the travel and leisure industry has been in the eye of the storm for much of the pandemic, so it could offer many opportunities if the economy picks up. However, these opportunities depend on how long it will take for working practices and consumer behaviour to return to normal.

For other industries, the outlook is more mixed. For example, oil should benefit from improving global economic growth due to higher oil demand and prices. Energy stocks bounced following the positive vaccine news but remain at historically low levels. While they could perform well during a recovery, the upside is tempered by longer-term uncertainty regarding the transition to clean energy. There is also a possibility that Iranian oil supply could re-enter the world market under a more dovish Biden presidency, and drive down prices.

In terms of regions, Japan's Nikkei 225 index has been one of the world's strongest-performing stock market indices in 2020, even beating the S&P 500. Its resilience can partly be explained by a combination of sector exposure, stocks that have 'growth' and 'quality' characteristics (especially low debt levels and high cash balances) and stable dividends, while also benefiting from a weaker yen.

Asia, and particularly China, have had a strong year, but we see reasons for caution on the prospects for this to continue in 2021. For one, Asian equities tend to outperform when the gap between the region's GDP growth and developed market GDP growth is increasing. The COVID vaccine would help consumption expenditure in Western countries more than elsewhere, as some emerging market countries may struggle to access sufficient numbers of vaccines at first.

The profits of Chinese exporters have been supercharged this year, picking up market share from countries with longer-term lockdowns, amid increased spending on electronics, furniture, and other household goods, particularly those offered by online sellers. In a vaccinated world, some parts — though not all — of this trend could unwind.

Focus on growth and quality

We still think it makes sense to keep a bias toward companies with a track record of persistently strong growth. However, with effective vaccines coming out, a more balanced stance is now warranted, moving more towards the middle of the value-growth spectrum — looking for quality companies that have cyclical characteristics, and are available at a reasonable price.

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UK SME sector: a lot tougher than it looks in the headlines

for every two businesses that have cut jobs during the pandemic, another has increased its employee base. Although 44% of firms have cut jobs last year, 62% have continued trading without interruption. This can be attributed in part to the fact that more than 80% of the UK economy is serviced based and it is also the world's second largest exporter of services after the USA.

Prestige Funds' SME lending partner Nucleus Commercial Finance was one of a small number of private lenders selected by the UK Government owned British Business Bank to deploy government guaranteed loans to small businesses last year. Since September 2020, Nucleus has lent almost GBP200m / USD 270m in this scheme.

Financing of small businesses through government-backed schemes has played a critical role in helping to support small businesses through these trying times - 98% say government support has had a positive impact on small businesses. Four out of five UK SMEs now feel they no longer require further government support to prevent further redundancies.[1]

How has the SME sector proved so resilient? Some business owners have demonstrated their readiness to take on external finance, and they have proved dynamic enough to change their business models to meet the new challenges presented by the pandemic. Many business owners tell us that these changes are likely to prove permanent, as they further embrace new and dynamic operating models.

Brexit: removal of uncertainty will be beneficial for SMEs

Brexit has also captured many headlines in the UK and Europe in Q4 of last year. For SMEs this has presented an additional challenge, and it is true there are some companies with heavy exposure to EU trade flows. But for the vast majority of UK SMEs Brexit will make little or no impact on the way they do business. Uncertainty has probably been one of the biggest worries for business owners.

At Prestige we focus our lending activities on companies with little to zero exposure to EU trade. But it is heartening to say that despite fears of a no deal with the EU throughout the course of 2020, less than 25% of SMEs were concerned about the negative impact of Brexit.[2]

SME owners are refocusing their efforts on either trading within the UK, or trading with countries outside the EU itself. From the government, they want to see a further trimming of red tape and additional financial support in terms of grants and tax reductions.

This positive narrative for SMEs is now being described as 'surthriving' - describing those firms that have embraced the changes forced upon them and have become more dynamic - according to data from FreeAgent only 21% of UK SMEs are now worried about the impact of Brexit, and 10% say the pandemic has ***actually opened up new opportunities***.

Last year was a testing time for many small business owners, but it has also proved that in the UK we have a diverse and opportunistic small business sector with the strategic support of a government that is prepared to do what it takes to shelter SMEs from the worst of the pandemic and pave the way for future successes in this sector.

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[1] *Small Business Britain - The Impact of Covid19 to Date (Goldman Sachs) Small Business Britain: The Impact of COVID-19 To-Date (goldmansachs.com)*

[2] *Survey data based on 500 SME interviews by FreeAgent, October 2020*

Outlook 2021: China equities

In a Q&A, GAM Investments' Rob Mumford discusses China capital market reform, the possibility of Chinese shares being de-listed in the US and his outlook for the market.

Will authorities address exuberance in China's equity markets given the focus on sustainable capital market development?

To create an equity culture the authorities will want to ensure bubbles do not form and disrupt the stable progression of the market. The pulling of the Ant Group initial public offering and focus on anti-trust reform at the large internet platforms confirms that Chinese authorities are willing to take tough decisions for the sake of a more stable long-term outlook. We would not be surprised to see steps taken to encourage a cooling of the market.

With US-listed Chinese stocks potentially facing de-listing, should investors be concerned regarding American depositary receipt (ADR) exposure?

In our view, no. The majority of large Chinese companies listed in the US already have Hong Kong listings and if they cannot abide by US disclosure requirements (or more companies are sanctioned due to military links) Hong Kong can become the primary listing with a minimum of formality (or in the case of the China telecom companies, the primary listings and liquidity pools were already in Hong Kong).

Should investors focus on domestic China shares or Hong Kong listed stocks (or China US-listed securities)?

We favour exposure to a blend of exchanges with a focus on portfolio construction (beta awareness) and a blend of styles (growth and recovery) in businesses with clear competitive edges and sustainable credit profiles. From a short-term perspective, we would urge caution in adding to new extended A-share positions. It is a retail dominated market (estimated at up to 90%) and when corrections occur, they can be aggressive while the Hong Kong market remains dominated by institutions and typically offers less volatility from a domestically induced consolidation.

What is our near and long-term outlook?

There is a tendency for investors to be overly concerned about China equity risks when valuations are attractive yet forget the same challenges when valuations are relatively expensive. With virus aftershocks recently rising in China, the timing of action to reduce exuberance may be pushed out slightly but we believe the issue of excess levels of indebtedness (and excess liquidity) is a near and present danger that needs to be addressed. Moral hazard has been gradually introduced into the credit markets as an essential aspect of capital market development. In order to create a sustainable equity culture in China, a similar exercise needs to occur in the equity markets. With inflation falling significantly of late, one area that could provide support to the market is a potential loan prime rate cut. Real interest rates have been climbing steadily and while the impact of interest rate shifts can be limited, this would certainly boost sentiment.

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Why remaining invested can outshine volatile markets

By Matthew Wintour, Head of Adviser Solutions, Brooks Macdonald.

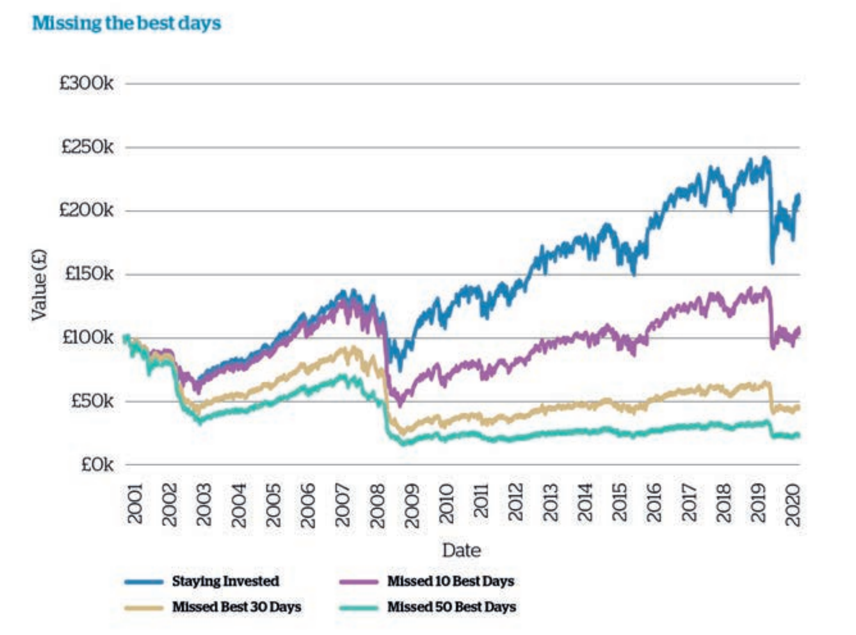
Over the past two decades, several major global events – including most recently the coronavirus pandemic – have prompted investors to flee financial markets, but data shows this could have been a mistake. When it comes to achieving long-term financial goals, investing – and remaining invested – tends to be the better option.

COVID-19 has had tragic consequences, with the loss of human life at the forefront of people's minds. The outbreak has seen widespread changes in human behaviour, with lockdowns and social distancing changing the way millions of us now live and work. This has had a dramatic knock-on economic impact with stock markets behaving in an extremely volatile manner at the start of 2020, creating a great deal of worry for investors.

Amidst heightened volatility, it is understandable that many are concerned about the impact on the value of their investments. But, while sharp declines in markets can naturally be disconcerting, if you want to give your clients' investments the best chance of earning a long-term return, then it's a good idea to practice the art of patience.

Trying to time the market can seriously damage your investment returns

When markets fall and fear dominates, it can be difficult to resist the temptation to sell out of the financial markets and switch to cash, with the idea of reinvesting in the future when feeling more positive about market prospects – trying to 'time the market'. But this is a strategy that carries with it the risk of missing out on some of the best days of market performance. And this could have a devastating impact on long-term returns.

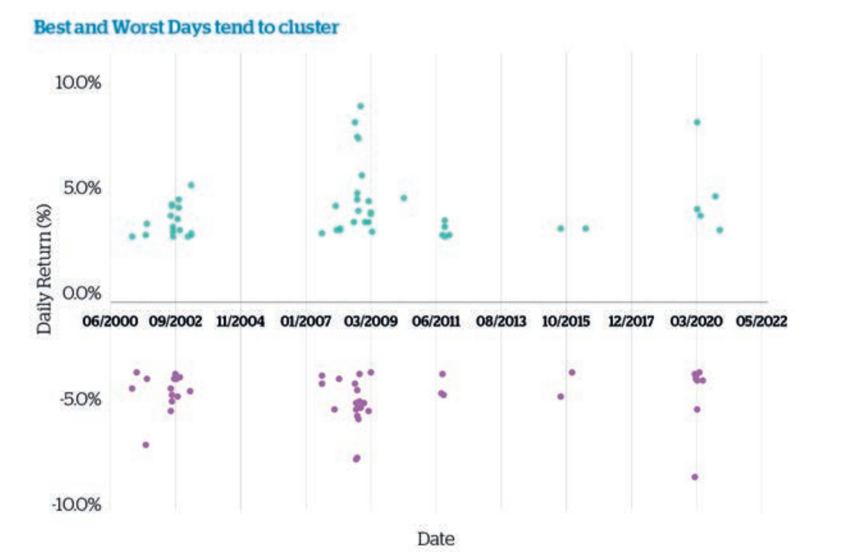


Source: Bloomberg, MSCI UK TR (MSCI: please see important information). Dates 01/01/01 to 01/01/21. Rebased to 100 at 01/01/01.

Remaining invested may be an emotional rollercoaster during times of market stress, but research shows time and again that this is the best investment approach over the long term.

For example, one study of US equity mutual fund investors showed that their tendency to try and time the market was a key driver of their underperformance (Dalbar, 2019)[1]. Despite temptations to switch into cash, data shows that missing out on just the 10 best market performing days can have a big impact on long-term returns, as the chart on the left demonstrates.

One of the most common reasons investors lose money is when they try to time the market. However, as the chart below left shows, the best and worst days of the stock market are actually much closer than you would think. Try to miss the lows and you'll probably miss the highs too because the best and worst days tend to cluster together.



Source: Bloomberg, MSCI UK TR (MSCI: please see important information), Dates 01/01/2001 to 19/01/2021. Chart shows 50 worst and 50 best days of one-day performance.

Keeping to an established and proven investment framework – and having the confidence to remain invested over the long term – increases your chance of earning a return

With the benefit of hindsight, we are now fully aware of the global impact of COVID-19, and the rapidity in which it has hit equity markets. While markets rivalled the speed of the virus in trying to price-in the near term damage, we expected they would also be swift to act when a tipping-point was seen to be close-at-hand. This expectation was played out in the market recovery over 2020 and continues into 2021.

If you try to time the market, there is a significant risk that you will miss the best days of performance. Yes, the journey may not be smooth - as with all investing, values can go down as well as up and neither is guaranteed - but the long-term returns support the case for looking past the short term news flow and remaining invested, even during volatile times.

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Source: [1] Dalbar (2019). 'Quantitative Analysis of Investor Behaviour'.

While the UK capital scored highly on its response to climate change, car-reliant Los Angeles dropped from first to 14th place.

London regains top spot in Schroders' Global Cities Index

London has returned to the top spot in the Schroders' Global Cities Index after scoring highly in its response to climate change in comparison to other cities in the index.

This year, the index has introduced a transport score into the ranking, with a particular focus on mass transit systems. As a result, car-reliant Los Angeles fell from first place last year to 14th position in 2021.

Cities in the Schroders' Global Cities Index are scored on four metrics: economic, environmental, innovation and transport. The ranking identifies cities with a combination of economic dynamism, excellent universities, forward-thinking environmental policies and excellent transport infrastructure.

The newly-introduced transport score has been designed to complement the environmental score, introduced at the last update in February 2020, as efficient transport is now seen as essential in providing social mobility. The index now has a heavy tilt to these two environmental and social factors. These two new scores give greater credit to cities that have sound environmental policies and good mass transit systems.

"London, as an example, scores well relative to other cities in its response to climate challenges," said Hugo Machin, a fund manager at Schroders who compiled the index. "London has scale, mass transit, strong universities and strong environmental policy to support its claim to be the best. Specifically, London is seeking to create an ultra low emission zone and put in place a solar action plan."

Risers and fallers

The introduction of a transport score and the recent introduction of the environmental score has diluted the economic score. The result is a downgrading of cities that are simply populous.

The negative impact has been on large industrial cities in China and large cities in North America reliant on road transportation. These cities tend to be post-industrial in nature. In the US, Chicago, Houston and Atlanta all dropped out of the top 30.

A city that has an efficient system for moving people, goods and data around will be more economicaly sustainable as inhabitants access more potential jobs. The transport score analyses data of five transport modes: sea, road, train, bus and air. Los Angeles performed particularly badly due to low score for access to rail, a key transport mode for the index. The city lacks a comprehensive rail network and the average walk time to a rail terminal in the city is 61 minutes.

Medium-sized cities, particularly in Europe, now rank higher. Stockholm, Madrid, Copehagen, Munich and Manchester all benefit from good public transport systems and improving environmental policies. They have also have sufficient scale to provide good employment opportunities.

Negative effect of the global pandemic

The Covid-19 crisis has had a profound impact on global cities. With many people forced to work from home during the pandemic, office owners will now have to compete even more aggressively for customers. Improved broadband speeds and communiction platforms, as well as the rise of flexible office providers, threaten traditional landlords.

"Cities will continue to be centres of innovation and entertainment as the health crisis subsides," said Hugo Machin. "The best cities will continue to evolve, encouraging open space and greener buildings. Human settlement requires planning and the majority of employment requires human interaction and the sharing of ideas. Cities that understand this will be best placed to thrive when competing for talent and capital. The aim of the Schroders' Cities Index is to quantify what makes a city successful."

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Currency update

Abounds of optimism shaped the last month as vaccine programme rollouts gave Sterling a boost, commodity currencies also saw some positives, and for the rest of the majors, it's been a rather average start.

GBP

The Pound was among the front-runner currencies throughout the month of February, scuffing the 1.40 mark against the US Dollar and bringing fresh highs to 2021. This break above 1.40 was the highest Sterling has been against the US Dollar since April 2018. The Pound has been steadily climbing since falling below 1.15 in March 2020, and has enjoyed over 20% appreciation in less than a year. This has mainly been attributed to the current success of the UK's vaccination programme, and post-Brexit uncertainty fading.

Despite UK economic data headed in a different direction to the Pound, investors don't seem too concerned, as all eyes were on were on Boris Johnson's address to Parliament and to the public in a televised briefing revealing the roadmap out of lockdown for England. Once again, although the development was in some way priced in, it did enough to help the Pound reach another new 34 month high against the Dollar of 1.4084. Reactions to Chancellor Sunak's Budget in March are being closely watched as the country, and the Pound, works its way through the spring. Investors will also be observing how on track the UK is with its four-step plan.

EUR

The single currency has struggled in the wake of a stumbling vaccine rollout. The Euro is facing a battle on more than one front too, falling to a month low against the US Dollar after it delayed the export of vaccines from the bloc, and then surprisingly triggered Article 16 of the Northern Ireland protocol. While outrage over this move was temporary, and more level headed discussions are taking place to smooth things over, it hasn't helped the Euro in the eyes of investors.

After that big news story, Europe has remained mostly off the radar. Investors will be looking ahead to how Mario Draghi shapes up as the new Italian Prime Minister, and in the coming months they'll be hoping his strengths in economic policies after his stint as President of the European Central Bank will come in handy at pulling Europe out of its rut.

USD

The US Dollar also had a rather average time, unchanged against major currencies. Economic data in the United States has been strong with regards to manufacturing and the service sector, bucking the trend of other major economies. Still though, the US Dollar has been feeling that risk sentiment is creeping back in, and as other currencies, particularly commodity-focused ones, gain more confidence, it simply slides towards the back.

Biden's first 100 days, and the economic stimulus he brings to the Capitol will be one for investors to keep a close eye on. The residential property market has remained strong up until now, but higher yield bonds are pushing up mortgage rates and could discourage buyers in the coming months. Also, worth noting will probably be frequent appearances from Federal Reserve leaders reminding investors that US interest rates are not going up.

To discuss a client's scenario in more detail, understand commission opportunities or refer a client please contact **Max Huseyin** from moneycorp directly on **+44 (0)207 828 7000**, or send an initial enquiry to **feifa@moneycorp.com**