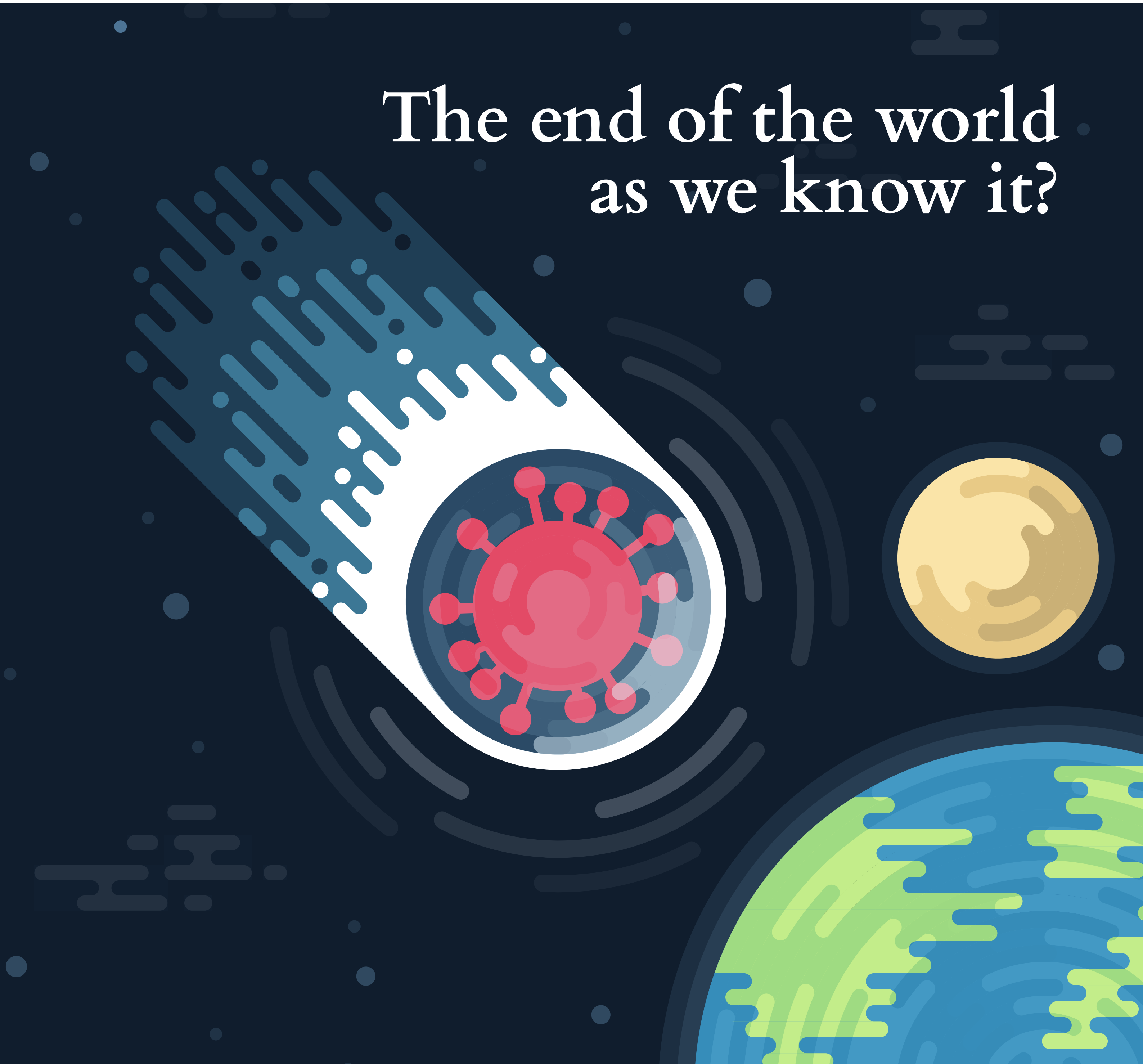
ISSUE 45 SPRING 2020

Hub News

CLIMATE INVESTING
Think positively

TOUGH MARKETS
Hold your nerve



CONTENTS

CISI CHARTERED INSTITUTE FOR SECURITIES & INVESTMENT ENDORSED CPD

WELCOME

This magazine hits your desks at a time of global uncertainty. As it stands, even the brightest minds are debating the likely impact of the coronavirus both on humankind and on the global economy. Much of this magazine was written before the virus wreaked havoc on financial markets. It feels like a long time ago now.

Nevertheless, many of the themes in this magazine are timeless. Investing sustainably will not be derailed by the coronavirus. In fact, it may become more important as it has become clear the speed at which companies with poor business models can be derailed by a rogue incident. Those companies with excessive debt, poor products, irresponsible practices have been found out.

Equally, it has once again demonstrated the power of diversification. It is a reminder than it is impossible to quantify every risk and assess its impact. Those holding a range of assets and bringing in appropriate checks and balances to a portfolio have fared far better through the market sell-off.

Inevitably, it appears, the next few months will be tough, but advisers have weathered these crises before and will weather them again. It is when the advice community really earns its spurs, keeping people invested through tough times, preventing them making silly mistakes and, most importantly, preserving their long-term wealth.

As always, we hope you find the magazine an illuminating and insightful read. Please send any thoughts or feedback to **enquiries@adviser-hub.co.uk.**

Cherry Reynard
Editor
www.adviser-hub.co.uk

SEEKING BIG OPPORTUNITIES IN UK SMALLER COMPANIES

While the shape of the UK economy shouldn't be the defining factor to a firm's share price performance over time, it can certainly make a difference to the smoothness of the ride. Invesco's UK equity fund managers Jonathan Brown and Robin West consider the outlook for the UK economy and why UK smaller companies with organic growth are well positioned to capitalise on both the highs and lows.

Political and economic uncertainty defined 2019 for UK equity investors. The lack of visibility over our future trading relationship with the European Union and a paralysed minority Government weighed particularly heavily on the UK smaller company sector due to its greater exposure to the domestic economy. Insecurity has seen the sector shunned, with international investors particularly reticent to invest. Companies that source their revenues from the UK have underperformed companies with substantial interests outside the UK despite underlying corporate earnings stability.

Meanwhile, sterling weakness has increased costs for many domestic businesses. The UK Smaller Companies equity sector, notwithstanding the UK General Election bounce in share prices, has been trading more cheaply than its 20-year average.

We believe the year 2020 is set to be different. The recently published Deloitte CFO Survey showed the largest increase in optimism in the survey's eleven-year history for Q4 2019[1]. This is a clear signal of business sentiment changing in the wake of the election.

Our longer-term view for the global economy, however, is more cautious. In more recent weeks, it has become apparent that coronavirus, or Covid-19, could pose a serious challenge to global economic growth. It's a fluid situation but concerns over the impact of the outbreak have intensified. The impact on the global economy will become clearer as companies outline how an exogenous shock such as this affects their business by way of disruption to global supply chains and forcing customers to stay at home.

So far, it remains difficult to quantify how far the virus will spread and how deep its economic impact will be. What is clear, however, is that the virus is exposing the vulnerabilities of globalisation itself.

It should not be forgotten that the main driver of financial markets, and share prices in general, is liquidity rather than the economy. So, whilst the short-term outlook for corporate profit growth has become more difficult, interest rates and the potential for more creative forms of economic stimulus, such as increasing government spending or quantitative easing, to name a few, should continue to be supportive for equities.

INVESTMENT PROCESS

We spend a significant amount of time meeting companies and prefer to invest in those with "self-help" characteristics. This can include restructuring stories, where a fundamentally good business has lost its way, but has the potential to rehabilitate itself under new management. We also like businesses that have scope to roll out a successful concept more widely, or companies that can consolidate a fragmented industry and derive a benefit from increased scale.

We also seek companies that are exposed to higher growth niches within the wider economy. These niches are often too small to make a significant difference to a large-cap company but can represent a very significant opportunity for a smaller business.

For stock pickers the smaller companies end of the equity market is an exciting place to be. Significantly lower stock analyst cover compared to larger companies allows us to find genuine mispricing, while a high proportion of founder-ownership encourages management to focus on long-term shareholder value creation.

Our analysis is focused on the sustainability of returns and profit margins, which are vital for the long-term success of a company. We continue to look for businesses with "pricing power" by assessing positioning within supply chains and having a clear understanding of how work is won and priced. It is also important to determine which businesses possess unique capabilities, in the form of intellectual property, specialist know-how or a scale advantage in their chosen market.

"It should not be forgotten that the main driver of financial markets, and share prices in general, is liquidity rather than the economy."

[1] *Source: Deloitte, January 2020.*

More information
For more from Jonathan and Robin on UK smaller companies, including their outlook for 2020 and examples of companies they've been investing in, visit **invesco.co.uk/uksmallers**

Investment risks
The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested. Securities of smaller companies may be subject to abrupt price movements and may be less liquid, which may mean they are not easy to buy or sell.

Important information
This article is exclusively for use by Professional Clients in the UK and is not for consumer use. Please do not redistribute. All information as at 9 March 2020 and sourced by Invesco, unless otherwise stated.

Where individuals or the business have expressed opinions, they are based on current market conditions, they may differ from those of other investment professionals, they are subject to change without notice and are not to be construed as investment advice.
This article is marketing material and is not intended as a recommendation to invest in any particular asset class, security or strategy. Regulatory requirements that require impartiality of investment/investment strategy recommendations are therefore not applicable nor are any prohibitions to trade before publication. The information provided is for illustrative purposes only, it should not be relied upon as recommendations to buy or sell securities. Issued by Invesco Asset Management Limited Perpetual Park, Perpetual Park Drive, Henley-on-Thames, Oxfordshire RG9 1HH, UK Authorised and regulated by the Financial Conduct Authority. EMEA1842/2020.

CLIMATE INVESTING: THINK POSITIVELY

Deirdre Cooper and Graeme Baker, Co-Portfolio Managers on the Global Environment Fund, say there is real positive action to decarbonise the economy and investors can benefit.

From record temperatures in the Antarctic to the row over the presidency of the UK-hosted COP26 climate talks, it's easy to become despondent about climate change. Now the coronavirus crisis, and subsequent oil-price crash, have sparked speculation that efforts to cut emissions will be delayed further.

Yet amid the scary headlines, there is still much to be optimistic about the world's transition to a greener future. There's an enormous amount still to do to meet emissions targets. But we believe there are at least three reasons for investors to think (and act) positively. After all, negativity will get us nowhere – it's time for forceful, positive action on climate change.

1) **Political and business momentum is becoming unstoppable**
We're starting to see political responses to climate change that would have been unthinkable a few years ago. European industrial policy is now based entirely around the low-carbon economy, with the bloc's leaders looking to halve emissions by 2030. Meanwhile, the UK has brought forward a prohibition on the sale of petrol and diesel cars by five years to 2035 at the latest. The present market turmoil may delay green policies slightly, but we think they are very unlikely to derail them. In fact, we would not be at all surprised if the stimulus programmes likely to follow the

coronavirus pandemic strongly emphasises green technologies and ultimately accelerate the energy transition.

The response from some sections of the business community has been equally impressive. Confounding most forecasts, new data show that global carbon emissions from energy plateaued in 2019 as developed economies abandoned coal in favour of wind, solar, natural gas and nuclear — the first time in a decade that carbon emissions from energy have not increased. Meanwhile, UK energy providers generated more electricity from zero-carbon sources in 2019 than from fossil fuels, for the first time since the industrial revolution.

This acceleration of climate action is widening the opportunities for investors. We think there are some great decarbonisation enterprises with solid business models, impressive technologies and defensible competitive positions. Of course, there are also companies that don't have these attributes, which is why we recommend a highly selective approach. But the assumption that a climate-focused portfolio need be high risk is totally outmoded, in our view.

In fact, we'd argue quite the reverse: that a well-constructed environmental portfolio can help balance the climate risk in other investments. What's more, investing in decarbonisation companies should have a positive impact by aiding the transition to a lower-carbon economy.

2) **The focus is shifting to positive investment**

There are also encouraging signs that more investors are recognising that divesting from carbon-intensive businesses is not, by itself, sufficient. Our recent Planetary Pulse survey found that investors are keen to use their savings positively to help tackle climate change. Some 61% of UK pension fund members said they would be willing for a proportion of their workplace pensions to default into environmental investments.

That's good news because, as the director of the United Nations Environment Programme says, "we need to catch up on the years in which we procrastinated." 'Catching up' means a massive and immediate acceleration of efforts to tackle climate change, or else the 1.5C goal will be out of reach by 2030.

This shift in emphasis towards positive investment is good for the planet, because it raises the likelihood of meaningful action being taken. It's also good for investors in decarbonisation, because it will strengthen the tailwind behind the businesses that are shifting the global economy to a lower-carbon model. Specifically, we need to spend heavily on: transforming our energy infrastructure; electrifying transport and other systems; and vastly improving energy efficiency. There are investment opportunities across all three of these pathways to a lower-carbon world.

3) **The risk of positive shocks may be rising**

Though worrying from a planetary point of view, there is a positive investment case to be made from the fact that current efforts to tackle climate change are "utterly inadequate", according to the UN. We're spending only about one-quarter of the US$2.4 trillion required each year to stop temperatures rising dangerously. That's already driving growth for select businesses, but the additional spending required to achieve the Paris Accord emissions targets would put their growth into hyperdrive.

It remains to be seen whether the full investment will be made. But the UN's dire assessment increases the likelihood of regulatory, technological or consumer-choice shocks to get emissions on track. Such shocks would be positive for decarbonisation companies and negative for businesses with high climate-risk exposure. To illustrate the growth potential of decarbonisation businesses, cutting emissions sufficiently to achieve the 1.5C goal would mean increasing wind and solar's share of the energy mix from 7% to 70%. The proportion of electric cars on the road would need to reach 100%. That isn't our base case but, after a torrid 2019 for the electric-vehicle value chain, we think 2020 could mark a turning point for the electric car.

As an aside, these shocks would only be felt meaningfully in listed equities, which immediately price in changes in expected growth. Green bonds and private infrastructure – other ways that investors might seek exposure to decarbonisation – won't respond in anything like the same manner, largely because their returns are contracted, which makes their valuations fairly stable.

Let's close with one more positive for investors. Our analysis shows that the consensus is forecasting lower growth for decarbonisation companies than for the market overall. To us, that makes no sense. But it also suggests opportunities to invest in businesses whose potential the market is yet to recognise. If that doesn't sound like a reason for investors to look forward more positively, we're not sure what would.

All investments carry the risk of capital loss.

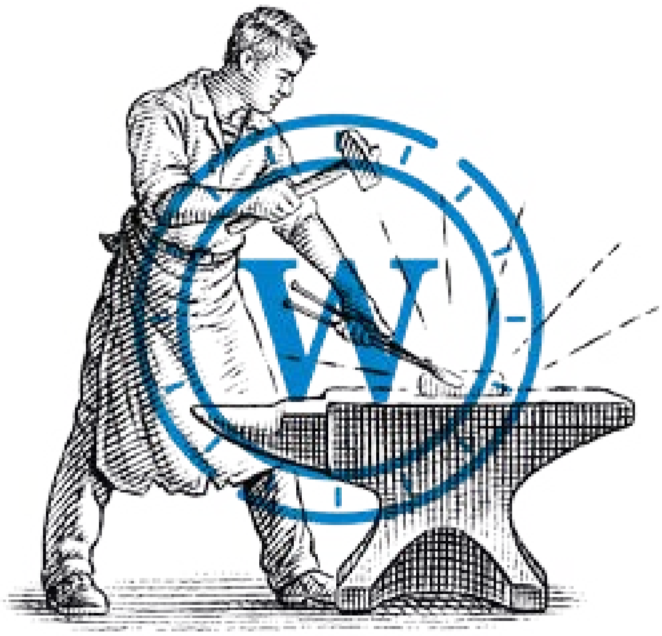
"We think there are some great decarbonisation enterprises with solid business models, impressive technologies and defensible competitive positions."

Ninety One

Previously Investec Asset Management

Important information

Ninety One is authorised and regulated by the Financial Conduct Authority.
Investments involve risk; losses may be made.


W

...IF IT'S NOT HURTING YOU ARE NOT DOING IT RIGHT

Lawrence Cook, Head of UK Intermediary Distribution at Sanlam, discusses the 'if it's hurting it's working' school of thought.

Don't panic that this is some sadistic ritual from an ancient cult. It's rather more prosaic than that.

"...If it's not hurting you are not doing it right" was a comment from a compliance officer referring to implementation of MIFID II for financial services firms. His contention was that firms who have breezed through MIFID II are very likely not to be up to speed with the ramifications of the raft of obligations contained in these regulations and if they were, they would be feeling a lot of pain. The difficulty with such comments is that they may have some general use but are not particular or specific. My own experience is that it really depends on who you speak to.

In a recent meeting with a successful IFA wealth management business the managing director proudly explained how the business had developed and was set to reach new heights in the coming years. It was going swimmingly until the operations director answered a couple of points about where the business was experiencing pinch points. She explained how each time the advisory model portfolio was reviewed it led to a long chain of administration which was increasingly difficult to manage, so much so she was worried about being able to do what clients had been promised.

This led to a longish conversation about what clients want and what they are paying for. That of course also depends on which client you speak to, with clients coming on board in recent years much more likely to say they had a planning experience, while longer-established clients might focus more on how the adviser arranges their pension and investments.

This is a common evolution in advisory businesses. Strategic, holistic financial planning has come a long way in the last ten years and is now common as the core offering for advisers. Therefore, positioning the up-to-date client proposition with older clients is particularly important. In times past the adviser may have 'given away' technical information when making the sale. Now the sale is the advice, not the product. When things are apparently free, they tend not to be valued or even noticed.

The mistake is thinking that the technical stuff is of interest to clients. It may be intriguing to some but it's a minority interest. That is not to say that technical knowledge and application is unimportant, quite the opposite. Practitioners can easily get carried away with their enthusiasm. Our own Chief Investment Officer, Phil Smeaton, remarked last week that it dawned on him earlier in his career that attendees at a client event were not interested in his vast knowledge of markets. No one had asked him anything interesting about markets or stocks at all. Does that mean we don't value the knowledge? No of course not but clients assume we know it; it's what they pay us for.

Back to our IFA conversation. We agreed that clients don't particularly value paperwork and administration. They wanted the benefits but not the job itself. The benefits of course are ensuring portfolios remain in line to achieve a client's objectives and risk tolerance.

One of the temptations is to make fewer changes, leading to less paperwork but that can't run for too long: clients start to wonder whether anyone's hand is on the tiller, let alone the potential regulatory tension.

We went on to consider wider business issues:

1. Growing the business without adding lots of new people - scale it up
2. Keeping in touch with clients about their needs, not just completing paperwork
3. Freeing up paraplanning and administration resource to support business demands
4. Freeing up advisers to take on more clients
5. Price of the client proposition

1. Growth and scaling up

One of the challenges for adviser businesses can be their own success with most advisers sitting on a healthy client book. For our IFA, the MD was reluctant to add more people and considering other alternatives. That means each adviser being able to drive more revenue into the business. While there were a number of contributory factors, the key was a lack of time available to see new clients and get in touch with top clients.

2. Keeping in touch with clients

The quarterly review of portfolios lends itself to making contact with clients. However, in practise this is mostly done via email and there is no value contact happening that might help understand how clients' circumstances and needs may be changing. A lot of time is spent by the administrators and sometimes the advisers simply chasing up paperwork to implement portfolio changes.

3. Freeing up paraplanning and administration resource

The paraplanners currently spend too much of their time supporting administrators. Getting them focused back on writing reports would be valuable to the business as it would free up advisers to spend more time with clients. There is a worry about staff retention if the current state persists.

4. Freeing up advisers to see more clients

The advisers are struggling to find time to develop new business and are concerned about their ability to respond in timely fashion to existing clients, let alone bringing on new clients. They are frustrated they have become involved in too much report writing and bogged down in supporting the administrative function.

5. Price of the client proposition

The MD was keen to provide a cost-competitive offering and felt that, having grown considerably over the last ten years, they could cope with pricing lower than the typical financial advisers in his region. The focus was on lowering the investment management fees.

The next consideration was whether using a discretionary service from a third party would help. The initial concern was cost and whether they could add any value. Views on discretionary services costs are typically out of date. The emphasis today is about how a third party can supply a discretionary service to support the IFA's proposition rather than simply buying an off-the-shelf DFM model solution.

This led us to conclude that an approach that could do the following would greatly assist in dealing with our pinch points identified above;

- An investment solution that incorporated the existing IFA advice model including risk profiling
- A discretionary service included which would remove the need for client permission for portfolio changes
- The design of the investment solution reflecting the IFA's own investment approach
- Could be managed on the wrap platforms they were already using at an acceptable price
- The ability to change all client portfolios at the same time, particularly when markets are distressed or there is a concern about a specific holding

It was felt that this was possible and discussion progressed to feasibility. The by-product of this is the domino effect through the business; the administrators having time to do their work, free from managing portfolio changes, leaving paraplanners to do paraplanning, leading to advisers being confident they could deliver a good service and take on more clients.

The cost of the overall client proposition also took a more strategic turn. The focus had previously been on protecting the adviser charge fee and therefore pressure was brought to bear elsewhere in the value chain. The owner of the business felt that he needed to consider what a buyer would value most - his current adviser charge fee or the asset management fee.

HOW CORONAVIRUS IS TURNING THE SPOTLIGHT ON SUSTAINABLE INVESTING

The unrelenting march of the coronavirus reminds us that environmental and social problems are increasingly clear financial risks that investors need to manage appropriately.

It is difficult to start any article without referring to the threat presented by the coronavirus sweeping across countries. The human impacts are clearly devastating for anyone affected, even if the overall impact is at present relatively small in the context of major pandemics through history.

The economic and financial impacts are also proving significant. Less than two months after the first reported case, the OECD lowered its forecast for global GDP growth in 2020 by one-fifth in response to the virus.

The speed and scale of downturns in stock markets mirror this response. Since the 1970s there have been four periods during which global equities have fallen more than 10% in five days: the 1987 crash; the 2008 global financial crisis; the 2011 eurozone crisis; and the first few months of 2020.

That market response contrasts with the effect of similar crises in the past. Notably, major equity indices rose while Spanish flu raged in 1918-19; the end of the Great War provided a boost but stocks were relatively unaffected even before its end.

The world is a very different place to that of 1918, or even that of a decade ago when the spread of swine flu coincided with a 40% rise in the Dow Jones Industrial Average.

Companies are more dependent than ever on the Licences to operate society provides, supply chains are more complex and connected than ever, social and environmental tensions are more acute than in the past, and regulation is accelerating to address growing imbalances between corporate success and social needs.

COMPANIES DON'T OPERATE IN A VACUUM

The changing backdrop underlines the importance of sustainability to the investment industry. If they ever did, financial markets no longer exist in isolation from social or environmental challenges. Companies' fortunes are intrinsically tied to their ability to navigate changes in the societies on which they rely.

We have long argued that companies don't operate in a vacuum. Their success reflects their ability to adapt to challenges and trends in the societies to which they belong. That is more true now than ever; social and environmental challenges, and investment drivers, are increasingly overlapping.

As a result, environmental and social problems are increasingly clear financial risks, moving up corporate agendas to drive long-term strategy and growth plans. As investors, our ability to examine companies and separate winners from losers has improved as corporate sustainability reporting has become mainstream.

BOILING POINTS AHEAD

A spectrum of social and environmental pressures will reach boiling points in the next decade, for example, looking beyond the current crisis:

- **Climate change will either reshape the physical environment or the global economy.** The International Panel on Climate Change has warned that we have a decade to roughly halve global greenhouse gas emissions. Failure to make a significant move away from fossil fuels will tie the world into escalating physical damage, rising sea levels, less agricultural land and more volatile weather. In the 1960s, emissions were half of what they are today. Returning to that relative level by 2030 - when the world's population will be more than twice as large and its economic output roughly ten times bigger – will require capital reallocation on a huge scale and drive disruption across every industry.
- **Technological advances will reshape the role of workers.** PwC estimates that artificial intelligence could put 30% of jobs at risk by the 2030s, demanding new skills and rendering existing roles redundant. Changes comparable to those which played out over centuries during the industrial revolution will be forced into less than a generation.
- **Social unrest puts political stability and economic systems at risk.** Social unrest has already reached unprecedented levels across the world. Pressures that have been building over the last decade are spilling into breaking points in developed economies as well as emerging. Policymakers can either respond by taking steps to rebalance the economic playing field that has created uneven economic gains, or have changed forced upon them.

Any of these trends alone will have a major impact on economies and industries. Together they represent a cocktail that could reshape stock markets and redefine the investment industry. Understanding those trends and aligning investments to them will be vital. We believe that sustainable investment is becoming a requirement, not a choice.

SUSTAINEX: OUR INNOVATIVE INVESTMENT TOOL

We also believe that growing impacts also demand innovative thinking and more robust investment tools. Off-the-shelf ESG ratings, subjective assessments and lazy rules of thumb have to be replaced by new approaches. This will involve everything from defining and assessing corporate sustainability, to quantifying and comparing companies, to building portfolios and helping investors understand the impacts their portfolios have.

For our part, we have invested heavily in developing tools to help our analysts, fund managers and clients navigate the turbulence ahead. Last year, we detailed the SustainEx framework we have developed to quantify companies' social and environmental externalities, putting a monetary figure to the positive and negative impacts companies have on society. We have rolled that framework out across over 10,000 companies, providing an objective basis on which to assess impacts and risks through an economic lens.

THE PENDULUM IS SWINGING BACK

That journey will continue. The investment industry became increasingly focused on dissecting financial data for much of the last few decades, emphasising measures of how much money companies make, over how they make money and how sustainable those profits will prove. The pendulum is swinging back; we believe asset managers need to refocus their investments lenses now more than ever.

Andrew Howard, Head of Sustainable Research, ESG, Schroders

"Companies are more dependent than ever on the Licences to operate society provides, supply chains are more complex and connected than ever, social and environmental tensions are more acute than in the past."

'BEST-IN-CLASS' IN HIGH YIELD BONDS

M&G has recently launched a version of its ESG Global High Yield Fund in the UK. James Tomlins talks about how the group is marrying principles and profit in corporate credit.

WHAT WAS THE GENESIS OF THIS FUND?

In 2014/15, we started to look at applying sustainable principles to a high yield strategy. This culminated in the Luxembourg-domiciled M&G ESG Global High Yield Fund, launched in 2017. The M&G Global High Yield ESG Bond Fund is a carbon copy of that fund. In deciding on the right approach for the fund, we considered a range of options, including impact, exclusion and best in class.

For us, we had to find a balance between being ideologically pure, but not having a lot of practical success, and taking a more flexible approach, which may not have the impact we'd hoped. We decided we wanted something in between.

We also found that a lot of sustainable investment is designed exclusively for equity investors and trying to apply that analysis to public credit markets was difficult. It was like putting a square peg in a round hole.

WHY DID YOU SETTLE ON AN ESG APPROACH?

Impact works well in the private debt space, but it is more difficult in a fund with daily dealing. Green bonds work well for quasi-sovereigns, but there are only a handful of green bonds and there have been some high-profile disasters. We thought it too concentrated and risky. We had seen how a 'best-in-class' approach worked well in global equities, so thought this might be the right approach.

However, of the thousands of companies in the high yield universe, there tends to be a skew to the medium and lower end of ESG scores. Only 5% of companies get the top two scores. This gave us a practical problem of diversification and risk problems.

HOW DO YOU STRUCTURE YOUR APPROACH?

We eventually decided on a three-stage screen. The first layer fully excludes companies in breach of the United Nations Global Compact Principles: that is areas such as child labour and corruption. A second layer filters out a number of sectors such as: alcohol, tobacco, gaming or nuclear. Companies in the portfolio can't have material exposure to these areas. Generally speaking, we wouldn't be able to invest in a duty-free retailer because that is too much exposure to tobacco and alcohol, but we could invest in a supermarket, for whom it is only a small part of their business.

Finally, the fund excludes any companies that lag their wider industry on ESG credentials. For this, we look at areas such as energy efficiency and pollution, plus governance, working conditions and product safety.

HOW DO YOU DECIDE ON THOSE GOOD AND BAD COMPANIES?

For the exclusions side, we use MSCI, which provides consistent data and good coverage. This is the straightforward part. The more difficult element is the ESG assessment, giving an holistic score for individual businesses. This is an internal process.

We score businesses in each sector and weight them in the portfolio according to that score. We weight the portfolio purely based on ESG scores, over and above the investment considerations.

We are skewed to companies with a positive plan for change. We wouldn't invest in companies exploiting the Canadian tar sands, but we would invest in, say, Total, which is working hard to decarbonise and move away from fossil fuels. We are happy to provide capital for them to do that. This is an ongoing debate for ESG investors, whether to tackle or exclude, but ultimately these companies have to transition.

"We find that big can be beautiful. We are among the biggest corporate bond investors in the market. Therefore, we get an audience and the conversations are very positive."

IS ENGAGEMENT IMPORTANT TO YOU AS WELL?

Yes, we have very targeted engagements with companies on specific issues. Debt holders are in a unique position. They aren't owners of the business and therefore don't have the same power of veto. They simply decide to lend or not lend. That said, we find that big can be beautiful. We are among the biggest corporate bond investors in the market. Therefore, we get an audience and the conversations are very positive. We are pushing on an open door.

For example, we recently had a big win with a Czech company that hadn't put a proper board structure in place. With our encouragement, they implemented a market-standard governance structure. We also worked with Iceland on their response to the palm oil problem. If companies want to do the right thing, we want to help them.

We can show clients what we have achieved. Engagement isn't just firing off an email. It is targeted - we may only have ten running at a time. We are trying to enact meaningful change.

PRIOR TO THE COVID-19 OUTBREAK, YIELDS HAD DROPPED SIGNIFICANTLY THIS YEAR. WHAT IS THE OUTLOOK NOW?

Certainly, at the start of the year we had seen yields dip to an all-time low in Europe, with the US not far behind. We have taken a cautious approach as a result. We didn't foresee the coronavirus, but we saw that the market was priced for perfection and valuations left no margin for error.

Bond prices have come down significantly since and we now have risk budget ready to deploy. It is clear that, valuation-wise, recession is fully priced in, plus a spike in default rates. The question now is whether it will be a deep or shallow recession. Discretionary spending should come back fast as long as people don't lose their jobs. There will also be pent-up activity from the fiscal support from governments. We see it as a reasonably good entry point.

NO SECRET SAUCE TO RESILIENT INCOME, JUST CAREFUL ASSET SELECTION

The Baillie Gifford Multi Asset Income Fund has been designed as a drawdown option, delivering a robust income stream while protecting capital. Manager James Dow talks about how his team is finding resilient income in a low interest rate world.

AS WITH ANY INVESTMENT, YOUR CLIENTS' CAPITAL IS AT RISK.

Pension freedoms created a new dilemma. Investors were no longer compelled to buy an annuity and were able to look for an investment product that could deliver resilience of income without them having to give up their capital.

While it is impossible to recreate the guaranteed nature of annuity income with an investment product, it's possible to come close to replicating its regular income stream.. This is the aim of the Baillie Gifford Multi Asset Income Fund, which has been designed to deliver long-term resilient income while preserving capital after inflation. However, in today's low interest rate environment, that isn't easy.

James Dow insists there is no secret sauce, no magic asset class that will do the job. It's about diversification, looking globally, and employing careful asset selection. "As well as equities we can invest across many different asset classes, including investment grade and high yield bonds, emerging market debt, property and infrastructure", says Dow. "We have a huge universe of options picked from across the globe."

He sees this as contrasting sharply with some of the existing UK-only equity income funds that investors rely on for income. UK income investors often gravitate to the big income players, such as BP and Shell. This can leave them exposed to individual sectors and to lower growth companies.

A key part of income resilience, says Dow, is in the different characteristics of each asset class and the way they are blended. For example, infrastructure – currently a major position in the portfolio – has its own specific drivers, which may be very different to those that drive high yield bonds, or global equities.

Dow says: "The fund was a number of years in preparation. The product group looked at the income, capital and diversification characteristics of certain strategic asset allocations. We looked at what would give the long-term income stream we need for a given level of risk. We settled on a blend of approximately one-third equities, one-third bonds and one-third 'real assets'".

From there, the team will take tactical positions, although the strategic asset allocation is important to keep the fund anchored. "It keeps us from any temptation to bet heavily on red." That said, the fund is flexible. Exposure to an asset class can be zero if its prospects look particularly unattractive, while the fund can take meaningful overweights relative to the long-term strategic allocation. "In practice, we've been running the fund for just over two years and deviations from the strategic asset allocation have been no more than 5%-10%" he adds.

"At the height of last summer's trade tensions, we were running an allocation of 27%-29% on equities. We saw that markets were just a bit too bearish and we reallocated another 6%-7% into equities. That played out well throughout 2019."

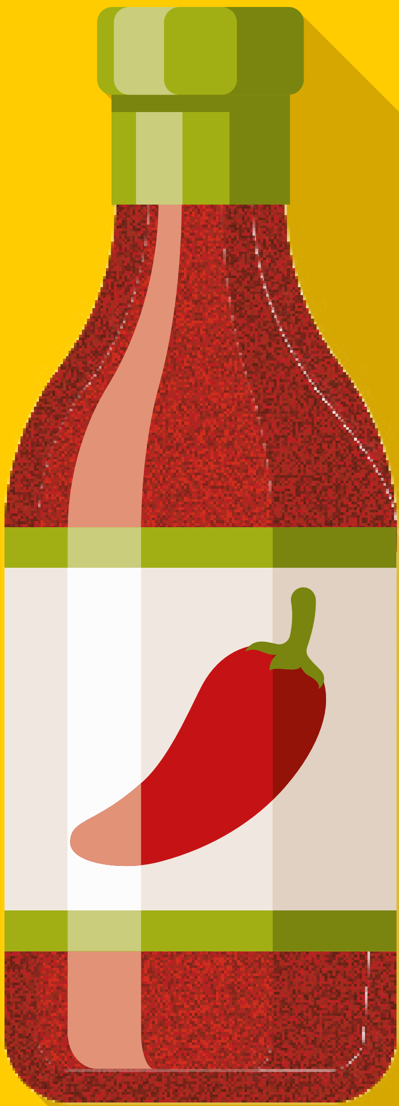
The asset allocation is determined by the Multi Asset Income portfolio construction group, which brings together investors who specialise in equites, fixed income, or real assets. It decides how much is given to each asset class after taking into account the views of the asset class experts who are responsible for researching individual securities. In this way, top-down and bottom-up are seamlessly integrated.

As with many Baillie Gifford strategies, the fund draws heavily on the expertise of the broader group. Its members will contribute ideas that fit the fund's targeted outcome. The group's infrastructure specialist will give ideas on renewables or US utilities, for example. Each expert has considerable autonomy over the companies they propose for the fund, and will give a view on the asset class as a whole. "It's not arms' length," Dow says. "We work as a team."

Dow's specialism is equities, so how does he ensure dividends are robust? A 'dividend dependability' checklist is compiled for each company, comprising 12 to 14 metrics that are considered good predictors of dividend strength. These include elements such as volatility of operational cash flow, or the capital intensity of a company's growth. Does it need to put significant cash back into the business to make it work? Do the board and management have the right attitude? Dow says some have dividend payouts as an afterthought, whereas some make it a priority. "Balance sheet strength is core. Thin, low-margin businesses are not resilient", adds Dow.

He labels this a 'pre-mortem'. The team wants to ensure that a company can pay income for the next 10-20 years, not just the next 12 months. This generally means steering clear of economically-sensitive companies: "We are avoiding those that may only be resilient for a year or two. We don't like deeply cyclical businesses; we don't like companies that need a lot of capital to grow – inevitably, they have to choose between cutting their dividends and growth. Most choose to grow."

“We are avoiding those that may only be resilient for a year or two. We don’t like deeply cyclical businesses; we don’t like companies that need a lot of capital to grow – inevitably, they have to choose between cutting their dividends and growth.”



That means the fund tends not to have holdings in banks or oil companies. It also won’t have many of the ‘usual suspects’ of an income portfolio. This philosophy extends to government bonds. The team will generally avoid countries where the structure of public debt is unsustainable in the longer term.

The biggest overweight position in the portfolio is currently in infrastructure. Dow says: “We think infrastructure is a really attractive, stable source of income. On the other side, we are underweight high yield bonds. We believe that valuations are quite high and the risks are probably skewed to the downside. We’re not being sufficiently compensated for taking the risk.” This has proved to be a helpful position in the current downturn.

And, summing up the objectives of the Multi Asset Income Fund, he says: “We aim to be a one-stop shop for investors and to take advantage of all different types of income. This fund should give good stable income while providing the capital protection that comes with diversification and careful stock selection. For drawdown investors, it should be a useful option.

The objectives stated are not guaranteed.

Please note, this article was written in early March, ahead of the considerable disruption in markets wrought by the coronavirus outbreak. As such, some of the statements may now be out of date. We would be grateful if you could bear this in mind as you’re reading.

RE-PLATFORMING

A TRANSFORMATION, SHAPED BY ADVISERS

Fidelity FundsNetwork has just enacted one of the largest re-platforming projects in the industry. It talks about what it means for clients.

At Fidelity we are committed to helping independent financial advisers run efficient and profitable businesses, while serving the needs of their clients. Insight and feedback from users of Fidelity's adviser platform, FundsNetwork, led us to embark on a multi-million-pound investment programme which consisted of a wide range of propositional and capability enhancements to improve client experience and support the advice process. A key element of this programme was to develop our underlying platform.

This exercise – now complete – represented one of the largest re-platforming projects in the industry and we have received extremely favourable feedback from advisory firms on the developments made. These enhancements are, of course, just part of our twenty-year journey in supporting firms.

Critical to our development programme has been the distinctive way we've worked with advisers. In addition to consultation with firms, we shadowed advisers and administrators in their offices, observing first-hand how they operate day-to-day. By taking on board how they use their systems, we formed a deeper understanding of the solutions we needed to build into our platform.

A few examples of recent developments:

- Advisers now benefit from a consistent suite of investment options across the entire product range. Importantly, this consistency spans all wrappers and accounts
- We've made our charging simpler and more consistent, ensuring clients receive even greater value for money
- To reduce time spent on back-office administration, you'll now find fully-integrated quote and new business processes, improved bulk switching options, simplified 'next generation' CGT client reporting and much more
- To complement the depth of reporting advisers can access at a client level, we now provide visibility across a firm's entire client bank, enabling advisers to analyse their book

Separate to this investment, we continue to assist advisers through providing comprehensive technical support on key advice and business topics, particularly around retirement in the wake of the pension freedoms.

In addition, news of the coronavirus in recent weeks has contributed to increased market volatility. With the continued impact on global markets, your clients may be concerned about their investments. Our coronavirus hub brings together some useful insights and expert opinions from Fidelity and several fund partners to help you reassure your clients.

Looking to the future, we're only too aware that change in the industry is likely to continue apace. We're already finalising the roll-out of further upgrades to client reporting, pension reporting, as well as improvements to our DFM capabilities and pension phased drawdown. And looking at how our technology can further integrate with advisers' back office and CRM systems, to name but a few.

Now could well be a good time to take a closer look at how our transformation can benefit your business: **www.fundsnetwork.co.uk**

THEMATIC INVESTING

THE EVOLVING ECONOMY – A FRESH APPROACH TO EQUITY INVESTING

The way that companies do business has changed dramatically over the last 20 years, but many investors' approach to equities has remained the same, says AXA Investment Managers.

These days, companies are increasingly global and multi-sector in their approach, which means that investors could be missing out on potentially higher equity returns by continuing to base their equity allocation decisions purely on traditional geographic or sector approaches.

We've identified five multi-decade growth themes that we believe will have a radical impact on the way that equity investors access long-term growth, which we call the Evolving Economy: automation, the connected consumer, ageing and lifestyle, clean tech, and transitioning societies. While these structural themes are not new, we believe we're still in the relatively early stages of accessing their investment potential.

COMPANIES ARE CHANGING…

The combination of irrevocable demographic shifts and the relentless pace of technological change is steadily forcing companies to change their business models to meet the constantly evolving needs of their clients and customers globally.

So for investors, selecting 'technology' companies gives very little insight into the true nature of those companies' long-term prospects and risks, given the ubiquity of technology across industries.

Take the example of a technology company that has evolved its product offering to include smartwatches that can measure your heart rate or sleep patterns, and link to devices to continually monitor your blood sugar levels – this defies easy categorisation into traditional technology or healthcare investment classifications.

Similarly, the automotive sector no longer simply manufactures cars. The automotive industry can instead refer to manufacturers developing clean technologies which will impact resource sustainability, automation tools that are paving the way towards driverless cars, and companies keeping pace with the demands of today's connected consumers by developing options for personalisation and connectivity with smartphones.

…AND EQUITY INVESTMENT NEEDS TO KEEP UP

To give investors better access to the potential opportunities of this corporate evolution, we have evolved our existing collaborative research structure by adding a specific coverage of the five Evolving Economy growth themes.

So rather than limiting our team's expertise to the traditional barriers of sector classifications, we have appointed a research lead for each of the five Evolving Economy themes to effectively collaborate on investment ideas.

"For investors, selecting 'technology' companies gives very little insight into the true nature of those companies' long-term prospects and risks, given the ubiquity of technology across industries."

For example our **'ageing and lifestyle'** research lead covers all manner of companies catering to the implications of ageing demographics – from companies selling products to the affluent older population, which accounts for an increasingly large proportion of consumer spending, to financial companies helping millennials build long-term savings plans, or to real estate companies specialising in retirement homes or hospital facilities.

Similarly, our **'transitioning societies'** research lead looks at companies serving the changing consumption patterns of societies across frontier, emerging and developed markets – from healthcare companies providing access to medicines, to clean technology companies and infrastructure projects.

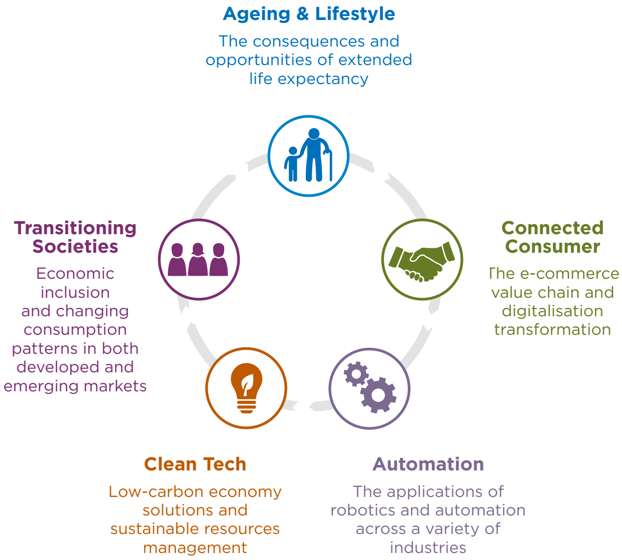
This multi-faceted approach intends to give investors fully diversified and quantifiable exposure to growth opportunities across the Evolving Economy. Using our proprietary thematic exposure database we can quantify companies' varying levels of exposure to each of our five themes, across a universe of c.11,000 companies, c.100 sub-themes and c.1,400 sub-industries[1].

LONG-TERM ACTIVE INVESTMENT IN THE EVOLVING ECONOMY

Once we've identified companies that have some exposure to each of these areas of structural growth, we look for businesses that we believe can benefit from these growth trajectories and that we believe are likely to generate attractive returns over the long term for our investors.

In this respect we stay true to our fundamental bottom-up stock analysis at Framlington Equities – we still care very much about the details like returns on invested capital and free cashflow generation to ensure sustainable long-term growth outcomes for our investors. What's changing most, in terms of evaluating companies that are exposed to these themes, is the need to be more multidisciplinary and collaborative in terms of sector knowledge.

FIGURE 1: THE EVOLVING ECONOMY



SO WHAT DOES THE EVOLVING ECONOMY MEAN FOR INVESTORS?

Ultimately, companies and the individuals they serve will continue to change over the coming decades. We believe that the Evolving Economy is about identifying the best of these long-term equity opportunities, regardless of how companies are defined geographically or from a sector perspective.

[1]*Source: AXA IM as at 31 November 2019*

SQUARE MILE FUND DASHBOARD: A COMPREHENSIVE VIEW

Square Mile discusses its new Fund Dashboard, designed to present fund information in a concise, consistent and intelligent way.

Every adviser has a different approach when choosing the best fund options for their clients. For instance, one adviser may view performance as the most important element, another may value ESG and another may find ratings essential when selecting a fund.

As a result, advisers are often drowning in information, and whilst there is a wide range of fund material available, there are relatively few options which draw this together in a readily digestible format. To tackle this, Square Mile have partnered with FE fundinfo to develop the Fund Dashboard, a visual snapshot designed to provide an easy-to-interpret overview of core fund information to help advisers assess a fund's ability to meet their clients' investment needs.

The Fund Dashboard will allow advisers to look, first and foremost, at the area most important to them, whilst providing an awareness of other key elements of the fund which they may not have previously considered. Square Mile have consulted extensively with the wider industry to determine which areas should be included, and the resulting development provides a comprehensive view to support informed fund selection based on five key elements:

1. **Opinion:** A combination of qualitative and quantitative assessments of a fund's ability to meet its objective based on Square Mile's fund ratings and FE fundinfo's Crown fund ratings, respectively.

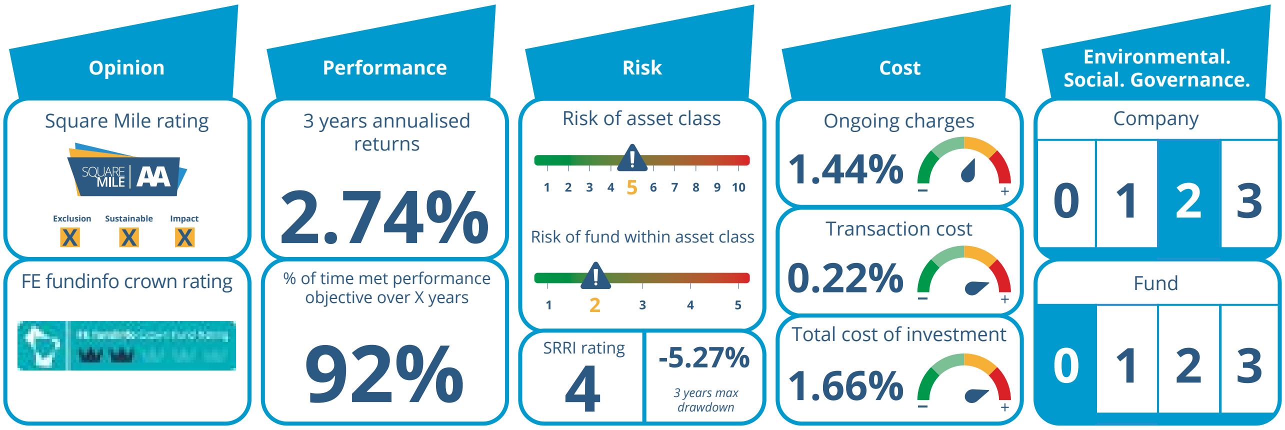
2. **Performance:** A representation of a fund's absolute annualised return during the timeframe outlined in its objective, and its performance versus its objective.

3. **Risk:** An assessment of the risk of the fund and the asset class it invests in, as well as its Synthetic Risk and Reward Indicator (SRRI) profile and the fund's maximum drawdown within the period stipulated in its objective.

4. **Cost:** An overview of the fund's ongoing charges, its transaction costs and total cost of ownership.

5. **ESG credentials**: An evaluation of how Environmental, Social and Governance (ESG) factors are being considered at both a company and a fund level, based on Square Mile's ESG integration assessment.

FIGURE 1: AN ILLUSTRATIVE EXAMPLE OF THE FUND DASHBOARD



Source: Square Mile and FE fundinfo

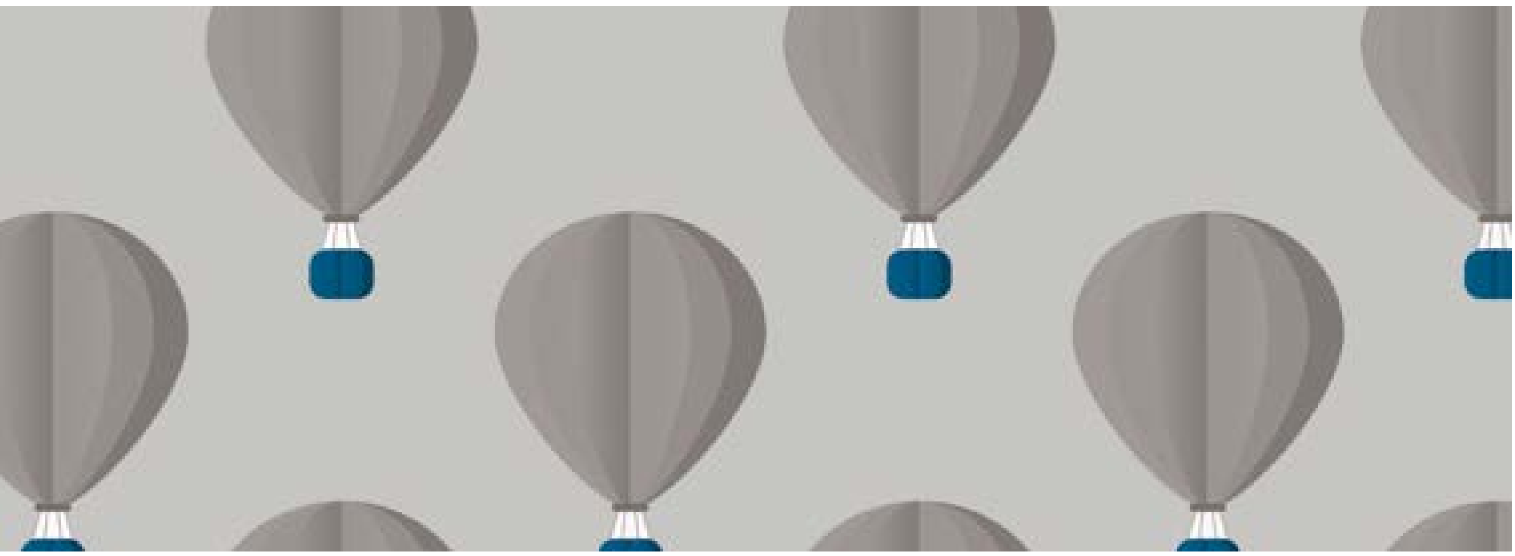
Square Mile have gone through a rigorous process to determine the most suitable fund information to display within the Fund Dashboard that will be most relevant to advisers. This has been based on both Square Mile's research analysts' knowledge of the market, as well as consulting with advisers, asset managers and the Investment Assocation to ensure it is fit for purpose. However, this will be an iterative process, and Square Mile will continue to seek feedback from the market to ensure the Fund Dashboard remains beneficial for advisers in making informed fund decisions best suited to their clients' needs.

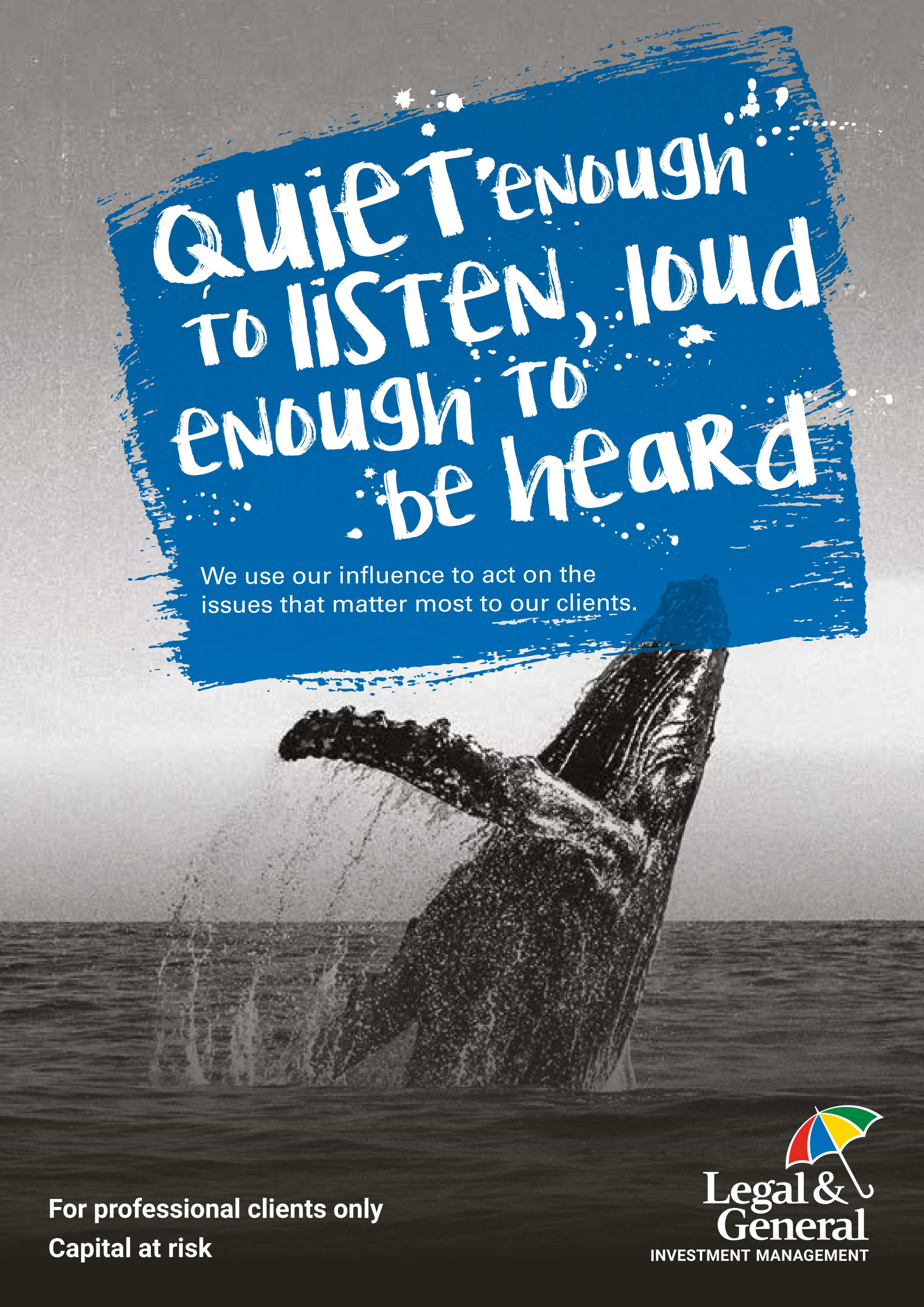
Square Mile's focus has always been on helping the market to deliver better client outcomes and they believe this concept will enable advisers to present fund information in a concise, consistent and intelligent way to their clients. The Fund Dashboard has been designed to be intuitive, but Square Mile will provide guidance on how to navigate it; to help advisers to understand and convey key concepts to their clients.

The financial services market is constantly evolving with layers of regulation being implemented, distribution becoming increasingly complex and adviser firms continuing to focus on delivering better outcomes to their clients. From an adviser perspective there is no straightforward answer to choosing a fund and selecting the right fund for a client is driven by a variety of factors. Advisers have a duty to be transparent when it comes to recommending funds to their clients and Square Mile hopes that the Fund Dashboard will help combat these challenges.

"The Fund Dashboard is a visual snapshot designed to provide an easy-to-interpret overview of core fund information to help advisers assess a fund's ability to meet their clients' investment needs."

The Fund Dashboard will be launching on the Square Mile Academy of Funds in Q2 2020. For more information on this initiative please contact us at **info@squaremileresearch.com** or **020 3700 7393**.




Quiet enough to listen, loud enough to be heard
We use our influence to act on the issues that matter most to our clients.
For professional clients only
Capital at risk
Legal & General
INVESTMENT MANAGEMENT

HOLDING YOUR NERVE IN DIFFICULT MARKETS

These are precarious conditions for all asset allocators. On the one hand, the wrong positioning could lead to losses, but on the other, clients may be asking why they did not take advantage of potential buying opportunities further down the line. Chris Teschmacher, fund manager of the Legal & General Multi-Asset Total Return Fund, discusses his strategy for dealing with difficult markets.

STAY TRUE TO YOUR INVESTMENT BELIEFS

Teschmacher says that in challenging conditions, his team is maintaining confidence in the investment beliefs they have spent many years researching and building. "At times like these it is easy to lose your head, but we have done our stress tests just for moments such as these. If we abandoned those findings now, we would be giving up all the accumulated knowledge over many years. These principles will help us navigate volatility."

STAY DIVERSIFIED

Structural diversification is core to all the LGIM portfolios, says Teschmacher. While there is a lot of price volatility, market dislocations may present themselves, but they may disappear as quickly as they arrived. There may be opportunities amid the volatility, but investors need to be careful that they can execute on any ideas and are not misled by irregular pricing in markets caused by poor liquidity.

He says: "We are structurally diversified, across geographies and asset classes. We aim to spread our risk. In the recent market dislocation, we have seen traditional safe-haven assets, such as sovereign bonds, deliver positive returns in spite of low starting yields. Investors had questioned whether they would prove defensive because of this low starting yield, but they have acted as they should."

HIGH-QUALITY MACROECONOMIC ANALYSIS

LGIM has an experienced and well-resourced team. It promotes both specialism and collaboration, which allow for a more informed and differentiated understanding of markets.

This has been particularly important in the recent coronavirus outbreak. Teschmacher says: "It is tempting for everyone to look at the latest news on the coronavirus all the time. However, rather than have lots of people chipping in with an opinion, we have a handful of designated experts who are looking exclusively at the impact of the coronavirus.

"They can do all the research and form a view. If everyone has a view, we would simply get the market consensus. In this way, we get a clear, consistent and hopefully differentiated view."

The coronavirus research is led by our economists, including our specialist in Chinese economics. They immerse themselves in the latest research, including calls with eminent epidemiologists and virologists. Teschmacher adds: "We want to get as close to the front edge of the research as we can, but also want to make sure that other trade ideas don't get forgotten."

BE AWARE OF LIQUIDITY

Idiosyncratic trades can behave in unexpected ways at times of crisis, says Teschmacher. "These trades are often poorly rewarded in volatile conditions. Pricing can be less robust because liquidity is less robust. As such, that makes us inclined to focus our efforts on broader asset allocation decisions where we believe liquidity is higher and price transparency is better."

THE IMPORTANCE OF TEAM

The LGIM team is split into three main components. A team of economists look at the world economy, country by country and sector by sector. At the moment they will be looking at the impact of the quarantine at the sector level within economies as well as the ability of governments to provide fiscal support and as a result which economies will be hardest hit.

Strategists look at which asset classes are likely to be most affected, given the prevailing economic climate.

Fund managers then package these conclusions into different portfolios and Teschmacher's fund is perhaps the most dynamic of the group's offering.

"In this portfolio we aim to capture both long-term trends and short-term opportunities, as well as capturing alternative risk premiums. We then need to bring it together effectively as a portfolio." These basic rules apply whatever the financial market weather.

"It is tempting for everyone to look at the latest news on the coronavirus all the time. However, rather than have lots of people chipping in with an opinion, we have a handful of designated experts who are looking exclusively at the impact of the coronavirus. They can do all the research and form a view."

ASIA'S ECHOES OF THE PAST

Teera Chanpongsang, portfolio manager on the Fidelity Asia Fund, discusses the outlook for Asian equities in light of the coronavirus pandemic.

With over 20 years of experience investing in Asia, I have invested through both the Asian Financial Crisis in 1997-98 and the global financial crisis (GFC) in 2008. When it comes to periods of market downturn, and financial crises, each one is different and nuanced with differing causal effects. This time is different again. It is not about over-leveraging, but it is a global pandemic that we are facing. What began as an outbreak in China has now assumed a global scale. It is not financial distress, rather it is uncertainty about individual health and fear about personal wellbeing everywhere.

We are seeing sharp declines in global equities as news of global contagion unnerves investors. Going forward, the level of action that each government takes to contain a sharp rise in new cases, and its impact on the actual contagion will impact investor sentiment.

ALL EYES ON ASIA'S RECOVERY

I believe Asian countries (such as Hong Kong, China, Singapore, Thailand, Taiwan) are prepared and have a high level of risk awareness which is evident in their day to day responses. Asian corporates appear to be in good shape and have very low debts on their balance sheet. Therefore, these economies are likely to recover quickly. However, the level of recovery depends on each economy's reliance on global economic growth as well. I strongly believe that Asian countries, particularly China, are now on the path to recovery. Nearly 80% of production in China has come back and is expected to be at 90% by the end of March. However, the global economy might decelerate significantly and that would have a huge impact on demand.

We should not overlook the long-term structural shifts like e-consumption - anecdotal evidence from Fidelity analysts as well as data releases in China showed that online transactions accelerated during this tough time. Consumers will be even more interested in buying life insurance and health insurance, furthering the structural penetration of insurance in China and let's not forget the ongoing development of innovative drugs in China, which the government will certainly keep promoting.

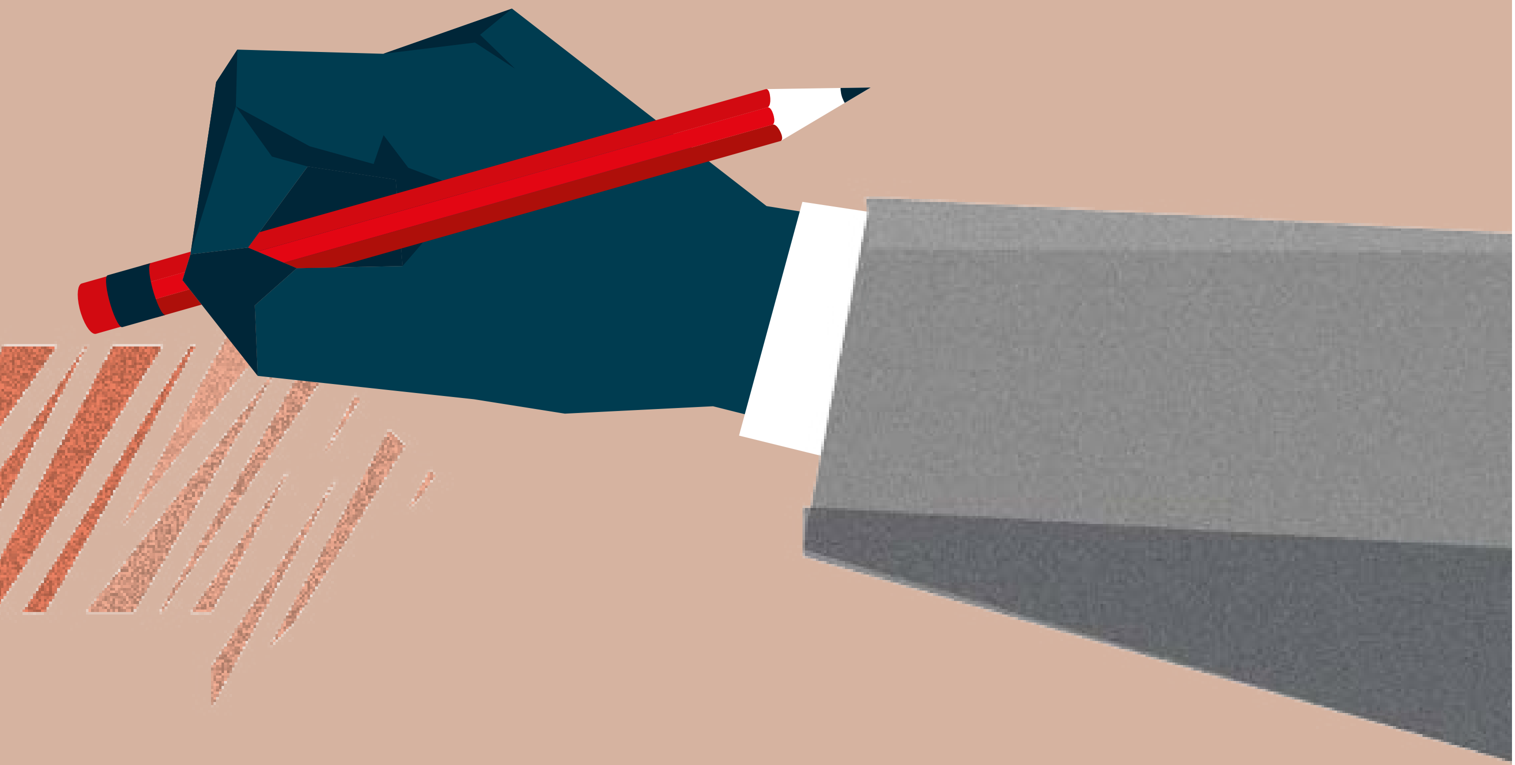
PORTFOLIO POSITIONING

I continue to spend most of my time in 1:1 meetings with corporates to evaluate current impact of the outbreak and my bigger concern is the expected weakness in the global economy.

I remain overweight domestic growth stories such as financials in emerging countries like India and Indonesia, which have a low penetration of financial products. I prefer AIA Group as it is the best-in-class private sector insurer with room to grow as China opens up in 2021 and the addressable market increases three-fold.

On a stock-specific basis, I am overweight consumer discretionary and consumer staple sectors and underweight industrials, materials and energy sector. The demand pattern is cyclical in nature and there is no catalyst for a structural growth in demand.

> *"Nearly 80% of production in China has come back and is expected to be at 90% by the end of March. However, the global economy might decelerate significantly and that would have a huge impact on demand."*



LOOKING FURTHER AHEAD

In the short term, headlines about the acceleration of new Covid-19 cases in the developed countries like the US and UK will fuel investor fear and market volatility, particularly as global markets continue to be highly correlated.

Nonetheless, I believe Asia offers long-term structural growth opportunities for long-term investors. I continue to look for companies that can deliver sustainable earnings in the long-term. I do not own companies that have high levels of debt. Stock selection will be the main driver of alpha generation for investors in the long term, while we navigate short-term spikes in volatility.

For the latest insight and market commentary from Fidelity, please visit professionals.fidelity.co.uk

About the manager

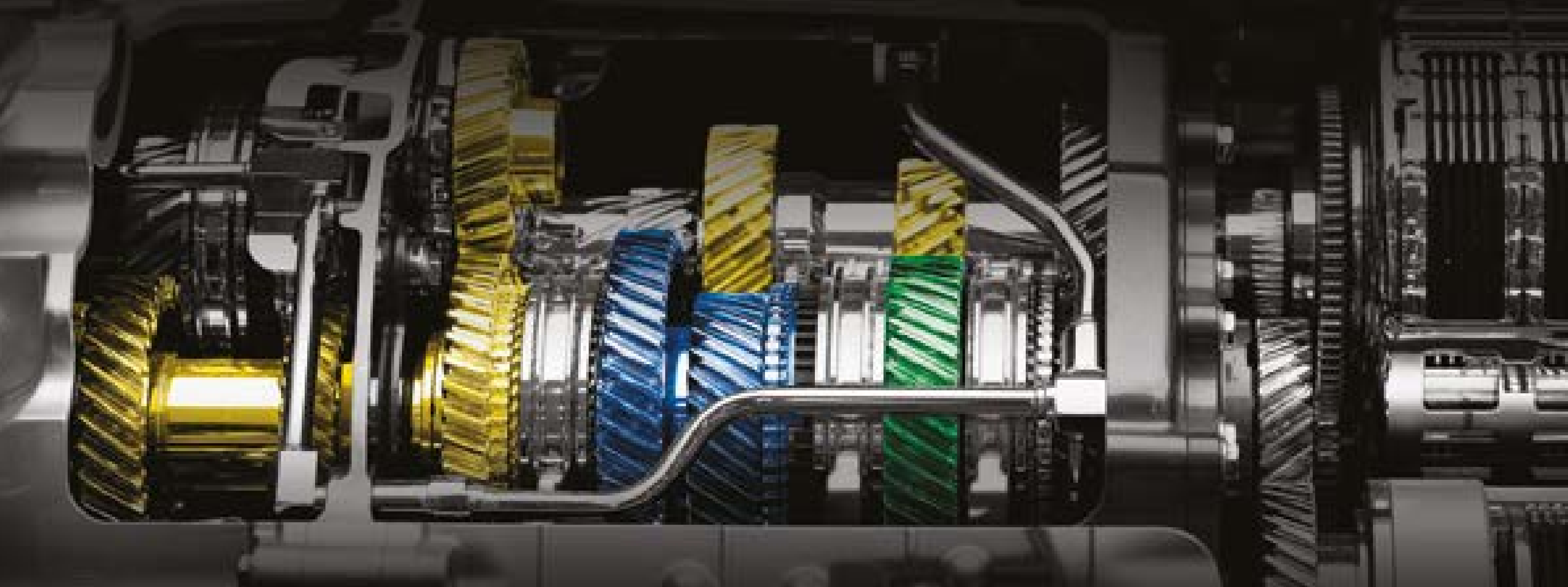
Teera Chanpongsang joined Fidelity in 1994 as a research analyst. In 1998, he was appointed portfolio manager of the Fidelity Thailand Fund (SICAV), which he managed until September 2004 before moving to London to run the Fidelity Global Telecommunications Fund (SICAV). Teera relocated back to Hong Kong in 2007 to start our Emerging Asia strategy and he has managed the Fidelity Emerging Asia Fund (SICAV) since its launch in 2008.

He also managed the Fidelity India Focus Fund (SICAV) from 2009 to and 2013 and has run the Fidelity Asia Fund since 2014. Prior to joining Fidelity, Teera was general manager at Chi Cha Group, Bangkok. He graduated from Chulalongkorn University, Thailand, with a Bachelor of Art (Accounting) and also holds an MBA degree from University of California, Berkeley.


For investment professionals only
Ahead of the trend
Growth spotting in Asia's $300bn* fashion market
What was once just Made in China is now designed, made and consumed in China. Our analysts were quick to spot that rising consumer wealth and a desire for quality created an opportunity for local fashion brands to cater specifically to local tastes. It's just one example of how our presence on the ground across Asia helps us find investment ideas that have been turning heads for more than 50 years.
The value of investments can go down as well as up so the client may get back less than they invest. Changes in currency exchange rates may affect the value of an investment in overseas markets.
Find a new perspective on Asia at professionals.fidelity.co.uk
Fidelity™ INTERNATIONAL
*Source: Statista: China apparel market, Sep 2019. Issued by Financial Administration Services Limited and FIL Pensions Management, authorised and regulated by the Financial Conduct Authority. Fidelity, Fidelity International, the Fidelity International logo and F symbol are trademarks of FIL Limited. UKM0919/CSO9295/24864/0320A

Engineered around you and your clients

Aviva Investors Multi-Asset Funds



Precise: five global multi-asset funds carefully designed to suit different risk appetites

Efficient: bespoke blending of active and passive strategies, ensuring your investment works as hard as possible

Dynamic: managed by a global business – bringing together over 35 years' experience in multi-asset investing

Bringing it all together for today's investor
avivainvestors.com/maf

Risk rated by:

The value of an investment and any income from it can go down as well as up and can fluctuate due to changes in currency and exchange rates. The funds invest in derivatives which may have the effect of magnifying investment gains or losses. Investors may not get back the original amount invested.

For today's investor

AVIVA INVESTORS

For professional clients and advisers only. Not to be distributed to or relied on by retail clients. Ratings are no guarantee of future performance and can change. The Aviva Investors Multi-asset Fund range comprises the Aviva Investors Multi-asset Fund I ("MAF I"), the Aviva Investors Multi-asset Fund II ("MAF II"), the Aviva Investors Multi-asset Fund III ("MAF III"), the Aviva Investors Multi-asset Fund IV ("MAF IV") and the Aviva Investors Multi-asset Fund V ("MAF V") (together the "Funds"). The Funds are sub-funds of the Aviva Investors Portfolio Funds ICVC. With effect from 4 June 2018, share class R3 was renamed share class 2. For further information please read the latest Key Investor Information Document and Supplementary Information Document. Copies of these documents and the Prospectus are available in English free of charge on request or on our website. Issued by Aviva Investors UK Fund Services Limited, the Authorised Fund Manager. Registered in England 1973412. Authorised and regulated by the Financial Conduct Authority. Firm Reference 119310. Registered address: St Helen's, 1 Undershaft, London EC3P 3DQ. An Aviva company. www.avivainvestors.com RA19/1047/21082020

SUSTAINABILITY: A CHANGING MINDSET

The EU has put sustainable investment at the heart of its regulatory agenda. First State was recently given the top group score by Square Mile at the launch of its Responsible Ratings service. Will Oulton, Global Head of Responsible Investment at First State Investments, discusses with Cherry Reynard the group's approach.

When the EU looked at how it could deliver its sustainability agenda – for example moving energy creation and unsustainable business activities from 'brown' to 'green' in order to meet the Paris Agreement commitments by the EU - it sought to mobilise private capital to achieve its aims. This has prompted a vast range of initiatives and has given the sustainability and sustainable investment agenda unprecedented momentum.

We are now witnessing the early stages of global capital moving away from the most polluting energy generation and environmentally impactful industries to those that are less so. A recent report from Deloitte (https://www2.deloitte.com/us/en/insights/industry/financial-services/esg-investing-performance.html) showed that across the globe, the percentage of both retail and institutional investors applying environmental, social, and governance (ESG) principles to at least a quarter of their portfolios jumped from 48% in 2017 to 75% in 2019. It estimates that ESG-mandated assets in the United States could grow almost three times as fast as standard mandates and are likely to comprise half of all professionally managed investments by 2025. A similar pattern is happening across Europe.

A CHANGE OF MINDSET

For the investment management industry, it requires a meaningful rethink of its approach from solely measuring performance relative to a benchmark; to being measured on a range of metrics, including the extent to which they achieve or contribute to sustainability goals. Advisers need to start to consider how they will gain access to and interpret such information. As part of MiFID II rules, retail investors need to be given the opportunity to express their preferences on sustainability.

Where is that information going to come from and what will it look like? While there are some specialist advisers, many will be starting from scratch in building sustainability preferences into their investment propositions and recommendations. We have already seen a number of discretionary fund managers hiring people for such roles, but many advisers may not have the capacity to bring in specialists.

It is fair to believe that when given the option, most people will choose a sustainable option rather than investments which may include companies that would be considered to be controversial, and environmentally or socially harmful. This is also likely to become progressively more important for future generations and, for advisers, change the conversation they have with their clients. The University of Cambridge's Institute for Sustainability Leadership for example looked at 2000 investors in the USi and found they had more tolerance for potential underperformance if they got a beneficial environmental or social outcome.

One of the long-standing industry challenges has been that of definition. The UK Investment Association developed a definitional framework in late 2019 which is very helpful. It addresses the problem of the alphabet soup of names and descriptions currently associated with sustainable investment. This should be an important tool for the retail market and their advisers in delivering more clarityto them. Morningstar has also built a system for rating the sustainability of funds which can also be helpful, however it should be incumbent on investment managers to provide investors with appropriate and clear information allowing them to compare products in a meaningful way.

FIRST STATE'S APPROACH

While First State has a number of successful specialist sustainability funds, all of its fund ranges are run to high ESG integration standards. First State takes its reputation for leading practice seriously, and wishes to contribute to the increasing quality of markets in which it operates, while also acknowledging that there are a number of risks to the continuing development of this part of the market.

The concept of "greenwashing" is a threat to investor confidence in this area. Investors need to be able to trust the information they receive from fund manufacturers and distributors. There have recently for example been concerns regarding companies included in passive ESG ETF's and funds due to the selection of their benchmarks. There is a risk in benchmark selection that they may include companies which, would not generally be considered to be "sustainable" businesses.

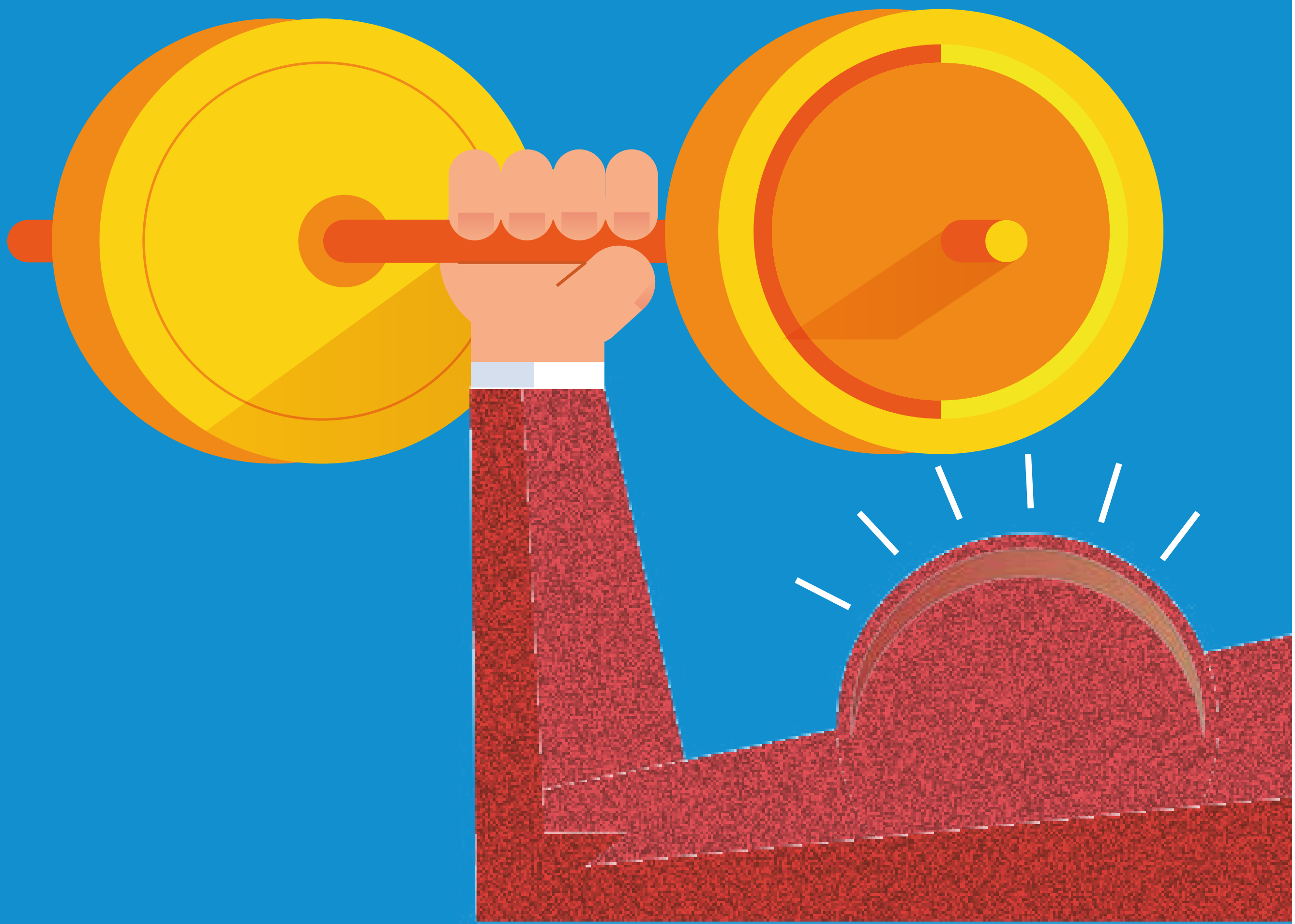
First State is working hard to bring transparency and accountability to an ESG integration process that has been adopted across the business. Its Responsible Investment & Stewardship Report is part of this communication as it shows how it goes about integrating ESG issues into investment processes and uses case studies by way of examples to bring this process to life. It reports on engagements with investee companies, to protect the value of clients' assets both directly and through working with industry peers collaboratively.

In this way, First State is making a contribution to help shape and develop the market on this important issue. Here is a recognition that our purpose, and that of our industry, is to make a real difference to society and we should all strive to remember that in the decisions we make each day.

MULTI-ASSET INVESTMENT

MULTI-ASSET INVESTING: THE POWER OF A STRONG TEAM

Drawing on a broad, multi-disciplinary team gives Aviva Investors' multi-asset fund managers a unique advantage says Sunil Krishnan.



The Aviva Investors multi-asset team is unashamedly collegiate in its approach – Sunil Krishnan, Head of Multi-Asset Funds at the group doesn't believe it is possible to run a strong multi-asset portfolio without a broad range of analytical resources and specialist analysis. It is a model that plays to Aviva Investors' multi-disciplinary strengths.

Krishnan says the group's strategy has been designed to deliver long-term risk-adjusted performance, but also to be robust in the face of unexpected problems – the coronavirus being an apt example. It also needs to be able to react to information in a timely way.

This starts with a strong long-term framework. "To our mind, this is too important to leave in the hands of conventional wisdom or to outsource. It is important to manage it in-house," according to Krishnan. "As such, we bring in solution design specialists and portfolio managers to get this right."

In building resilience, the group takes a firmly global approach, even though many of its investors are in the UK. This gives the portfolio managers more options. For example, they have been using US Treasuries to build defensiveness into portfolios. This position has benefited from the growing importance of the US government bond market globally and the strength of the US dollar. This was true during the pivot to lower US interest rates during 2019, but has been turbo-charged during the recent volatility as investors again seek the safety of US assets.

"If times get tough, US Treasuries are likely to do more than UK gilts to protect a portfolio because they have international attractiveness," Krishnan points out. It has also been useful to hold alternatives to equities during a lengthy period of UK equity underperformance linked to Brexit uncertainty.

"Looking globally gives us better access to a range of corporate profiles. This has helped performance. Growth does not come from just one place, and we need to build in long-term diversification. Longer term, growth is not just found in equities, but can be found in emerging market debt too, for example." The group also includes areas such as absolute return funds, which are designed to defend capital during periods of market volatility.

There are seven professionals who oversee the balanced and multi-asset funds for the group. The team brings in multi-asset and macro specialists, plus fixed income specialists and implementation specialists. They all provide insights which drive the funds' core allocations.

DYNAMIC MANAGEMENT

The funds also use dynamic management, tilting the portfolio from time to time. While the funds are flexible, Krishnan is clear that they will not fundamentally change the allocation at a moment's notice. He says: "Setting expectations is one of the most important things advisers do, along with determining an individual's appetite for risk. They establish with clients what is reasonable to expect in terms of long-term returns. As fund managers, we don't want to jeopardise that by making drastic changes to the risk parameters."

Equally, he says, trying to time the market should not be a dominant source of portfolio risk. "When we go through market weakness or a risk event, the rebound can be vigorous and difficult to time. Actively controlling position sizes can smooth returns, but if we had taken the portfolio out of equities entirely, we could miss early recovery periods, which are large drivers of long-term returns. We want to ensure that the profile of portfolio volatility is at largely in line with the profile an adviser recognises."

DEEP EXPERTISE

The Aviva Investors multi-asset team will often stray from its home turf when taking positions. At times it has held large weightings to Australian government bonds, for example, and emerging market debt. For Krishnan, the support of specialist teams across the business is vitally important. This can also help with decision-making in illiquid markets: "As markets become more volatile, those with detailed knowledge can tell us where there are pockets of liquidity. Rather than making the buy/sell decision in an unthinking way, and then getting poor pricing, they can make sure we get it right."

Normally, the asset allocation committee meets monthly, drawing on feedback from the individual fund managers and making decisions on tactical positions. However, in more volatile markets – such as those prompted by Covid-19 – it may meet more frequently, bringing in external insight where necessary. This will be set against the backdrop of the team's existing assumptions. The committee members will discuss how those new events reshape those assumptions and the likely impact on the portfolio.

Krishnan gives the example of the team's equity positioning in 2019. "There were genuine fears last summer on whether the global economy would be in recession in the second half of the year. August was a period of real market weakness and we debated the likelihood of recession, much of which hinged on the US/China trade war. We saw that emerging US data were not as bad as some had feared. We're not diplomatic experts, so we brought in some external experts to guide our thinking on the US/China trade war. We felt it was going to step back from the brink. It suggested market concerns on recession were unfounded."

The team saw the underlying strength of the US economy was still in reasonable shape, even though manufacturing was sickly. It took the opportunity to add risk back into portfolios. This proved very important in the funds' overall performance over 2019. The same approach informs risk management in more adverse circumstances such as the current time.

Responsible investing is also an important consideration across the multi-asset portfolios. Aviva Investors was a founding signatory of the UN Principles for Responsible Investment in 2006. The group believes it is crucial to use active management to make a difference, and even where the multi-asset team uses passive funds, they are active owners, ensuring that shares held are voted in line with our values. Environmental, Social and Governance (ESG) considerations are fully integrated into the multi-asset investment process, with members of the ESG team participating in the asset allocation committee and working with the team to understand the investment process.

The next goal for the group is integrated reporting. It is currently a significant priority for Aviva Investors as a whole and it wants to be able to provide this by the end of the year. The ambition is full transparency.

"As markets become more volatile, those with detailed knowledge can tell us where there are pockets of liquidity. Rather than making the buy/sell decision in an unthinking way, and then getting poor pricing, they can make sure we get it right."

adviser-hub

Free marketing and business support

AVIVA INVESTORS · AXA Investment Managers · BAILLIE GIFFORD · BNY MELLON INVESTMENT MANAGEMENT · Fidelity INTERNATIONAL · First State Investments · FundsNetwork · Invesco

PARTNER DETAILS

AVIVA INVESTORS
t: 020 7809 6521
e: BDEUK@avivainvestors.com
w: avivainvestors.com/en-gb

AXA INVESTMENT MANAGERS
t: 020 7003 2345
e: LONClientServices@axa-im.com
w: axa-im.co.uk

BAILLIE GIFFORD
t: 0800 917 4752
e: trustenquiries@bailliegifford.com
w: bailliegifford.com

BNY MELLON INVESTMENT MANAGEMENT
t: 020 7163 8888
e: salessupport@bnymellon.com
w: bnymellonim.com

FIDELITY INTERNATIONAL
t: 0800 368 1732
e: premierline@fil.com
w: professionals.fidelity.co.uk

FIRST STATE INVESTMENTS
t: 020 7332 6500
e: enquiries@firststate.co.uk
w: firststateinvestments.com

FUNDS NETWORK
t: 0800 414 1 81
e: FNWnewadviser@fil.com
w: fundsnetwork.co.uk

INVESCO
t: 01491 417 600
e: salesadmin@invesco.com
w: invesco.co.uk

JUPITER ASSET MANAGEMENT
t: 020 3817 1063
e: intermediary-sales-support@jupiteram.com
w: jupiteram.com

LEGAL & GENERAL INVESTMENT MANAGEMENT
t: 0345 070 8684
e: fundsales@lgim.com
w: lgim.com/uk/ad

M&G INVESTMENTS
t: 0800 328 3191
e: advisorysales@mandg.co.uk
w: mandg.co.uk/adviser

MERIAN GLOBAL INVESTORS
t: 020 7332 7524
e: clientservices@merian.com
w: merian.com

NINETY ONE
t: 020 3938 2000
e: enquiries@ninetyone.com
w: ninetyone.com

SANLAM
t: 0117 975 2093
e: salessupport@sanlam.co.uk
w: sanlam.co.uk/financial-advisers

SCHRODERS
t: 020 7658 3894
e: advisorysalesdesk@schroders.com
w: schroders.co.uk/adviser

SQUARE MILE RESEARCH
t: 020 3700 7397
e: info@squaremileresearch.com
w: squaremileresearch.com

We would love to hear your feedback on this issue of Hub News. If you would like to contact us on this or any other matter, our details are below.

Tel: 020 3004 4479
Email: enquiries@adviser-hub.co.uk

Adviser-Hub
4th Floor, 33 Sun Street
London, EC2M 2PY