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Hub News

EVERGREEN INVESTING
Waste and Water

POST COVID
Building Resilience

What lies ahead?

Adjusting to a world with Covid-19

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WELCOME

Our last issue of Hub News came out in March, when many were still hoping that the pandemic would be short-lived and its impact minimal. That has proved optimistic to say the least. We are still weighing the economic fallout from the crisis four months later and there remains little clarity on the ultimate price for Covid-19.

Nevertheless, there are some interesting trends emerging. It has notably accelerated the adoption of e-commerce, the digital transformation and perhaps most surprisingly, the energy transition. Usually, the green agenda falls by the wayside at times of economic crises. This time, green issues have been front and centre of government plans to 'build back better'. It shows how far the agenda has moved in just a few years.

In this month's Hub News, our contributors explore these issues in greater depth. Ninety-One looks at why sustainability will be key in a post-Covid world, with companies needing to look at their E, S and G to thrive. Square Mile discusses its ESG research process, while five Schroders fund managers talk about the main ways they expect Covid-19 to change the way we live and work.

It is clear that big government is back and with it, chunky deficits and low government bond yields. A number of our contributors also address the income dilemma and potential solutions – AXA Investment Managers discusses high yield bonds, while Jupiter's Jason Pidcock discusses Asian Income.

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
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INVESTING IN THE FUTURE OF WATER AND WASTE

The provision of clean water and the removal of waste is a social imperative crisis or no crisis, says, Bertrand Lecourt, Portfolio Manager on the Fidelity Sustainable Water & Waste Fund.

While markets have been highly disrupted by large sell-offs and significant volatility across the board, the long-term structural drivers for water and waste provision remain firmly in place. It's important for investors to realise that even when the economy stops, one of the key services in society is the provision of clean water and the removal of waste. The virus has undoubtedly attacked people's ways of life, but one of the pillars of society, namely, how we manage our water and waste will not go away.

More than half the world's population live in cities. Rapid urbanisation is still underway in developing markets, while developed markets are dealing with increasing pressure on old infrastructure. Rising environmental regulation and health standards are also creating compelling opportunities for investors. The theme of water and waste is a structural global megatrend that impacts us all on a local level. It is a story of people and the planet - the planet needs water and waste management, and always will. There is no economy without water and there is no sustainable economy without waste management.

WATER AND WASTE – DIFFERENT INVESTMENT OPPORTUNITIES, ON COMMON GROUND

The unique combination of investing in water and waste together provides access to two complementary sectors which benefit from secular growth trends. Investments made across the two value chains vastly increases the investment universe, whilst providing greater diversification benefits compared to other investment vehicles that only focus on one of these sectors. Despite the human need for both water and the flip side of consumption, waste management, water and waste are hugely under-researched sectors globally. The combination of the two sectors also offers investors relatively defensive access to global equity markets and can serve as a strong diversifier from having no exposure to sectors such as technology, communications and financials.

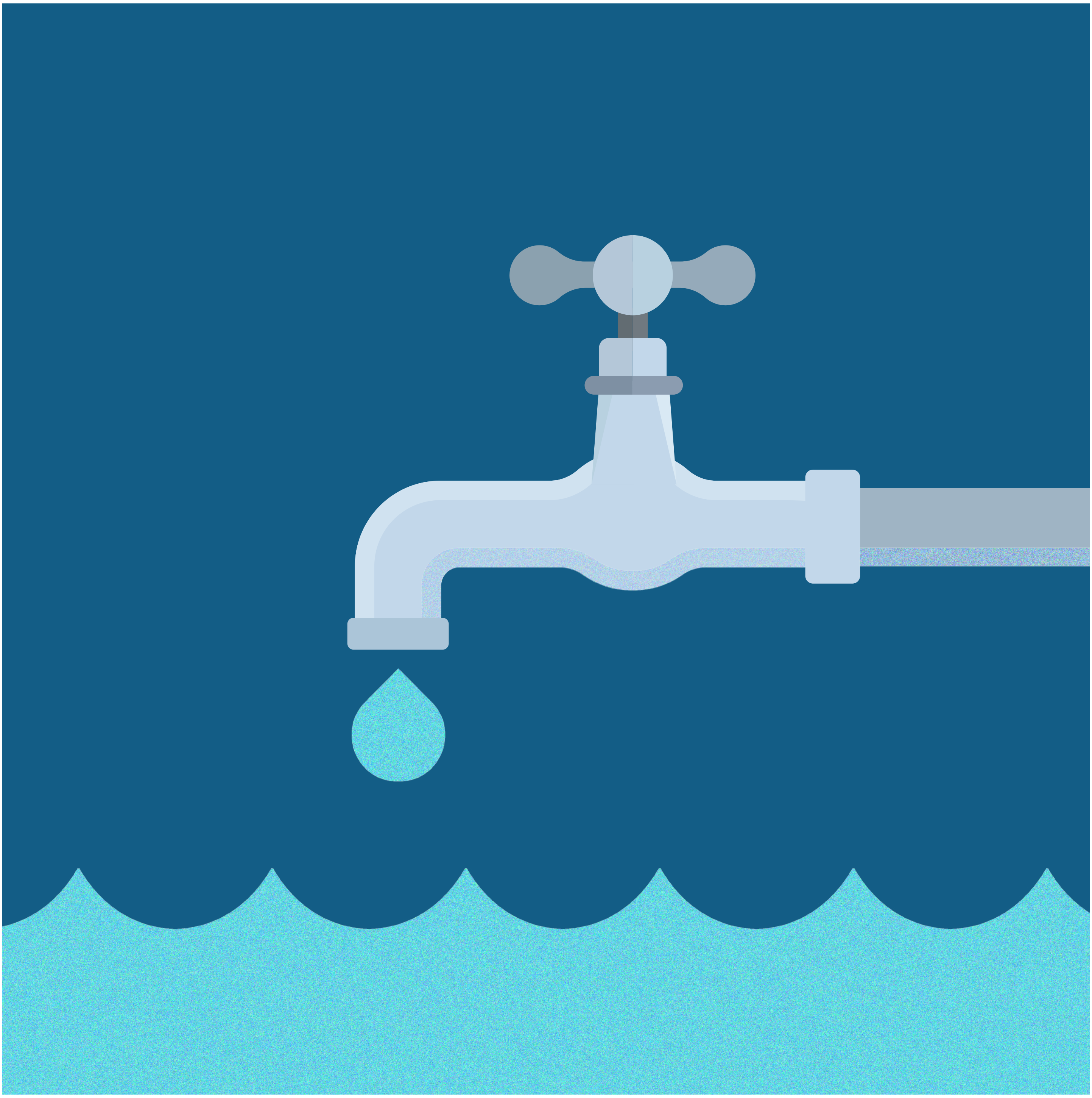
THREE REASONS TO COMBINE THE WATER AND WASTE SECTORS

1. Water and waste-related companies share many key drivers of demand such as growing global population, increasing urbanisation, growing consumption and supporting regulation.
2. Processes involved in the water industry can create waste, while the waste industry uses a lot of water – think about waste water produced in households or the amount of water required to clean bottles for recycling.
3. Covering both the water and waste sectors means finding complementary yet differentiated companies and a wider opportunity set. Spotting opportunities in one theme might highlight opportunities in the other.

THE FIDELITY SUSTAINABLE WATER & WASTE FUND

The Fidelity Sustainable Water & Waste Fund is the first UK fund to combine the water and waste sectors, aiming to deliver strong risk-adjusted returns across the cycle from a global universe of sustainable opportunities. The fund adopts a global equity strategy with a focus on quality and growth, analysing companies across the entire water and waste management value chains. These companies benefit from powerful structural growth drivers relating to the ever-increasing demand for clean water, as well as the need to manage waste from a growing population. The investment universe currently comprises a total of around 330 companies that are actively monitored for inclusion in the portfolio. By investing in companies which operate with high standards of corporate responsibility and overall ESG objectives, the fund can further protect and enhance investment returns for clients over the long term.

We always need to make sure that we have the right infrastructure in place for provision of water and waste removal.



Regulation around the sector isn't going away either. We cannot escape who we are as human beings and in that respect, sanitation will always be key. To run a good economy, we need a healthy economy and as long as that continues to be the case, water and waste will continue to be important. The fundamentals behind these two sectors are still solid, and therefore the investment case for water and waste is still as relevant today as it was before the global pandemic. Therefore, beyond the bleak, short-term outlook, there are causes for optimism.

THE FLAWS OF "CYCLICAL THINKING"

Cyclical change separates markets into growth companies and value companies. Structural change separates the market into winners and losers. Losers don't revert...they go bankrupt. It's important to recognise the difference, says Randy Dishmon, Senior Portfolio Manager at Invesco.

I get asked all the time about my "outlook" for the market. My answer has been the same for nearly 20 years: "I don't have one." I don't...for good reason. I've not yet met the person who can consistently predict what the market is going to do, but even more importantly: I don't buy the market. In my view, the question itself is the real problem. I believe it shows a critical flaw in a person's thinking – the only reason to ask that question is to attempt to time the market...a perfect example of what I call "cyclical thinking." I don't like cyclical thinking. I believe it is one of the main enemies of the successful long-term investor.

Successful investors, in my view, have to be expert at recognising the difference between cyclical and structural trends. At the core of my investing philosophy is this: I look for structural trends. Simply put: "How is the world changing?" A perfect example that I've been investing in for my entire career is the rise of e-commerce. That's represented a steady change in the way business is done – it's not a cycle that leads to four years of e-commerce being favoured and then a mean-reversion to four years of brick and mortar retail outperforming. That's the difference: cyclical change separates markets into growth companies and value companies. Structural change separates the market into winners and losers. Losers don't revert – they go bankrupt. Like I said, it's important to recognise the difference.

So, here's my outlook, but not for the market...for the structural growth trends that I believe are changing the world.

- **Move to the cloud.**
  I believe the shift toward cloud-based tools and services will continue stronger than before. Prior to Covid-19, it was considered a "nice to have." It is now considered essential. As one CEO recently told me, "If I don't get to the cloud like yesterday, I don't have a business tomorrow." I see this as a once-in-a-generation type shift that is changing the way every company on the planet does business. Not many things do that.

- **Rise of e-commerce.**
  E-commerce is accelerating. It has become the only option in a Covid-19 world, and post-Covid behaviour will likely still favour not going to the store as much. Every crisis in the past 20 years has sped up the market share gains of e-commerce. I don't expect this to be any different.

- **The electronification of money.**
  This trend actually started in 1950 with the first credit card, and it has grown globally unbroken at a rapid rate for over 60 years. I expect it to accelerate during this Covid-19 environment and continue afterwards. Why? Ever look at money under a microscope? Don't.

- **Diagnostics and research.**
  It's been on the rise for two decades and will again accelerate as a result of this environment, in my view.

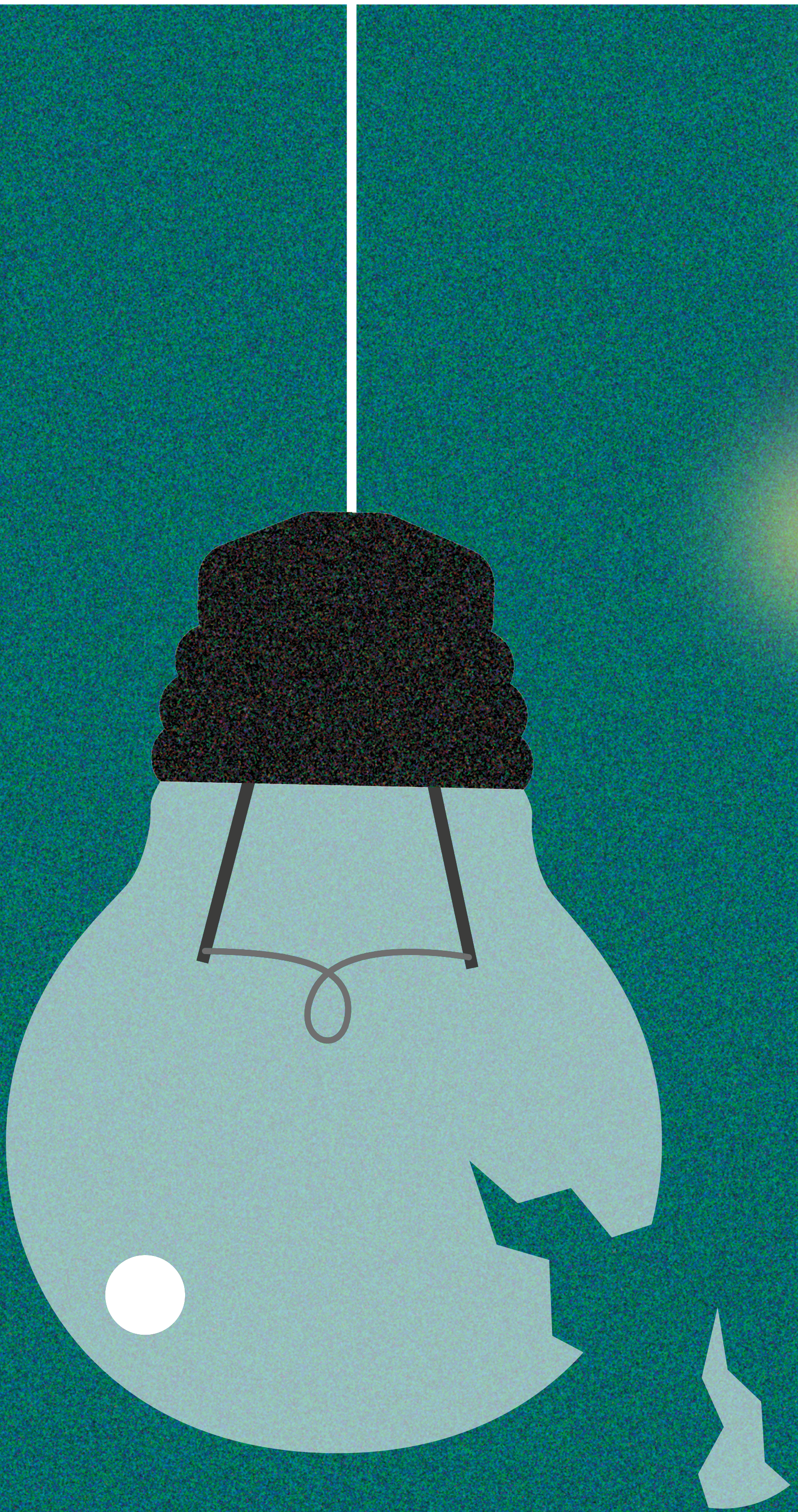
I expect all of these trends to continue for at least the next decade – that kind of compounding makes short-term concerns meaningless to my investment process.

MORE INFORMATION

For Randy, one of the greatest benefits of global investing is that he can buy anything, anywhere in the world. The Invesco Global Focus Fund (UK) is a compilation of his best 30-40 ideas that fall within several long-term structural growth trends.

To learn more about the fund and Randy's investment process, visit: **invesco.co.uk/globalfocus**

"It's not a cycle that leads to four years of e-commerce being favoured and then a mean-reversion to four years of brick and mortar retail outperforming."



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. The Fund may use Stock Connect to access China A Shares traded in mainland China. This may result in additional liquidity risk and operational risks including settlement and default risks, regulatory risk and system failure risk. As the fund has a concentrated number of holdings, investors should be prepared to accept higher risks. The fund may use derivatives (complex instruments) in an attempt to reduce the overall risk of its investments, reduce the costs of investing and/or generate additional capital or income, although this may not be achieved. The use of such complex instruments may result in greater fluctuations of the value of the fund. The Manager, however, will ensure that the use of derivatives within the fund does not materially alter the overall risk profile of the fund. Although the Fund invests mainly in established markets, it can invest in emerging and developing markets, where there is potential for a decrease in market liquidity, which may mean that it is not easy to buy or sell securities. There may also be difficulties in dealing and settlement, and custody problems could arise.

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Change
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Asset Management

SPORTING CHANCES: WHY SUSTAINABILITY WILL BE KEY FOR COMPANIES IN A POST-PANDEMIC WORLD

Matt Evans, Portfolio Manager on Ninety One's UK Sustainable Equity Fund, explains why companies will have to be high achievers across all the corporate disciplines – from financial targets; to environmental – to thrive in a post-crisis world.

As lockdowns ease and the global economy emerges from semi-hibernation, companies face stern tests on many fronts. Perhaps more than ever, how businesses cope will depend on their performances across multiple dimensions.

The companies with the best chances of emerging strongly from this challenging period are the Jessica Ennis-Hills and Katarina Johnson-Thomsons of the business world: high achievers across all the corporate disciplines – from financial targets; to environmental-, social- and governance-related areas; to impact and stakeholder engagement. In salute to Great Britain's gold-medal-winning heptathletes, we discuss seven areas in which UK companies will need to be on their game – and that UK equity investors should keep a close eye on.

1. PEOPLE-FIRST APPROACHES

The coronavirus has reminded everyone just how material the 'S' of ESG (environment, social and governance) can be. Among the social factors considered in ESG analysis, labour policies and practices will need to be assessed particularly carefully. With the coronavirus remaining a threat, high standards in health & safety will be critical; missteps could see businesses forced to shut up shop. And with millions of UK workers getting used to very different ways of working, a commitment to (and competence in) staff training will be essential. Inadequate or mismanaged training could have disastrous consequences, and not only financial ones.

Companies have a clear moral obligation to do the right thing by employees. But there is also a compelling investment reason to seek businesses with good labour practices: those that emerge from the current crisis with a motivated and appropriately skilled workforce are more likely to recover faster.

2. ACTION ON DIVERSITY

Diversity merits a separate mention. George Floyd's tragic death in the US has sparked an essential global debate about fairness and access to opportunity. We can expect closer scrutiny of companies' diversity records and policies in the months ahead. What comes next is likely to go beyond asking whether businesses have achieved industry-average levels of diversity. We have a long way to go to provide everyone with equal opportunity, regardless of ethnicity, gender and physical ability. Consumers, authorities and the general public will be demanding leadership, new thinking and advances in best-practice from the business community. Corporate laggards in this regard risk reputational damage and a potential consumer backlash.

3. SUPPLY-CHAIN RESILIENCE

Another key 'S' factor at present is the supply chain. Analysis of the UK companies in our investment universe reveals wide variations in policies and practices – from companies with minimal oversight of suppliers' environmental and labour policies, to those that require business partners to adhere to their own standards and that monitor closely to see that they do. Global supply chains are extremely fragile right now, so the more resilient a company can make theirs the better. Adding to supply-chain threats, trade tensions are escalating again between the US and China. If ever there was a time to focus on companies with supply-chain best practices, this is it.

4. BOARD QUALITY

Robust governance (the 'G' of ESG) will be crucial in the months ahead. Companies are having to make major decisions amid tremendous uncertainty, and these decisions will need constant monitoring by boards. Having independent and experienced board members that support, challenge and appropriately incentivise management teams will be a major advantage.

"Businesses that emerge from the current crisis with a motivated and appropriately skilled workforce are more likely to recover faster."

5. COLLABORATIVE MANAGEMENT TEAMS

One benefit of being a UK equity investor in times like these is that the United Kingdom's governance code and culture encourage a collaborative, supportive approach between shareholders and companies. That should help, because it can enable companies to adapt more quickly to new conditions. But some management teams (and indeed some shareholders) embrace this spirit of cooperation more than others. Those that do will have an advantage, especially if economic conditions deteriorate and changes need to be implemented at speed.

6. ENVIRONMENT AND BIODIVERSITY

In the early weeks of the pandemic, there was widespread speculation that environmental considerations would take a back seat, given the need to protect lives and livelihoods. Increasingly, it seems more likely that companies' environmental impacts and policies will be examined more closely than ever in the months and years ahead. Many experts, including some at the United Nations[1], believe health crises in human societies are closely linked to the degradation of the natural world and loss of biodiversity. Moreover, the coronavirus has done nothing to alter the fact that radical changes to the way we produce and consume are needed to avert a climate catastrophe. We all have a part to play in protecting the natural world, and we know the terrible consequences of failing to act.

7. POSITIVE IMPACT

If any good comes of the coronavirus, we may hope that this tragedy has cemented – and perhaps accelerated – the trend for businesses to think more deeply about their role in society, and their obligations not just to shareholders but to all current stakeholders, future generations and the natural world. We expect companies to be increasingly held to account for their societal and environmental impacts by consumers, authorities and investors, and for these groups to require businesses to actively seek ways to make a positive difference.

Our engagements with UK companies reveal that they are at very different points on this journey. Some have intricately mapped their impacts and are able to measure them robustly; others have given scant consideration to the wider effects of their products, services and operations. There are clearly risks for the latter group. But we see tremendous opportunities for companies that can demonstrate they fully merit a social license to operate, and that are valued as engaged stakeholders who contribute positively. Rather than being at the expense of financial returns, we think impact targets can be complementary to them.

In our experience, there seems to be a growing acknowledgement among businesses, investors and the wider public that sustaining success – at a corporate or national level – is ultimately a team sport. Long may that last.

For more information on the Ninety One UK Sustainable Equity Fund and to access the Fund's Impact Report visit: **https://weare.ninetyone.com/UKSustainableEquity**

[1] *Source: https://news.un.org/en/story/2020/05/1064752*

RETIREMENT

THE RETIREMENT INCOME MARKET

At the time when clients might be deciding to ease up on their working hours the adviser's life becomes more challenging, says Lawrence Cook, Head of UK Intermediary Distribution at Sanlam. Here's what they need to consider.

Every stage in a client's life can have its complications but there is no doubt that as a client approaches that moment of decumulation, advice can get a bit more complicated.

There are after all quite a few moving parts. Many advisers intuitively understand all these moving parts. Part of the commercial issue here is that if it's all intuitive and we don't explain it, then clients may not understand the tremendous value they get from their adviser.

Annual allowance, Lifetime allowance, Benefit crystallisation, Income tax, Capital gains tax, Inheritance tax, Investment markets, Tax wrappers, Withdrawal rate, Sustainability of income, Investment strategy. And the list goes on...

We're now a long way from 'Why don't you save £20 per month into this endowment savings plan Mrs Jones?'. Financial advice has changed and decumulation is so much more involved than the relatively simple accumulation phase. But unless the client perceives the strategic financial planning of today to be very different to selling Mrs Jones a product, why would they be willing to pay for it? In other words - be prepared to show your workings, which will help illustrate the value of your advice. They don't have to know how to calculate a Sharpe ratio or work out their pension input period, but they should know all the key headings and the expertise you are providing.

Returning to our main theme here, decumulation, many of us are grappling with how to manage the many issues to be considered.

In particular how are we tackling the polar opposite risks of sequencing of investment returns and longevity & price inflation? When I was a director at a DFM (acquired by Sanlam in 2019) I spent many hours developing a proposition with our chief investment officer. We were pretty pleased with our work after working diligently in the lab. We had consulted with a number of advisers and we proudly presented our new shiny service which did a good job of managing sequencing risk and longevity. However, hardly anyone recommended it to their clients. Why?

Partly, it was a solution in search of a problem that many advisers did not know they or their clients had. With the FCA promising a thematic review into retirement income advice, this is probably changing and quite quickly.

The other reason I think it failed, other than a lousy sales strategy of mine, was that ultimately the answer to our decumulation challenges is not to be found in a product from an investment house. I now understand this is primarily an advice issue not a product issue. For all those financial advisers that already knew this, sorry.

We have all the products we need. It is how we use them to manage the risks for clients that really counts. Let us look at sequencing risk in particular.

FIGURE 1: SEQUENCING RISK

As the client builds her pot up towards retirement the risk of a bad run of investment returns increases – sequencing risk.

If you're not familiar with it, the simple table below shows that it is not the investment return by itself that matters but the order in which it happens. It is no good saying to an investor 'I had all the right notes, I just played them in the wrong order'. The order matters, a lot.

This example illustrates the point. 4% investment return in nine out of ten years with the one exception being -30%. I have just changed the order. I then subtract a client withdrawal of £25,000 per year. Hey presto: the client in scenario one now knows sequencing risk is a big deal with only £198k left after ten years whereas clients experiencing scenario ten have £287k left. Same total investment return, totally different outcome. It doesn't matter what example you use, it makes the same point.

FIGURE 2: INVESTMENT RETURNS OVER A TEN YEAR YEAR PERIOD WITH ANNUAL WITHDRAWALS

	SCENARIO 1	SCENARIO 2	SCENARIO 3	SCENARIO 4	SCENARIO 5	SCENARIO 6	SCENARIO 7	SCENARIO 8	SCENARIO 9	SCENARIO 10
YEAR 0	£500,000	£500,000	£500,000	£500,000	£500,000	£500,000	£500,000	£500,000	£500,000	£500,000
YEAR 1	£325,000	£495,000	£495,000	£495,000	£495,000	£495,000	£495,000	£495,000	£495,000	£495,000
YEAR 2	£313,000	£321,500	£489,800	£489,800	£489,800	£489,800	£489,800	£489,800	£489,800	£489,800
YEAR 3	£300,520	£309,360	£317,860	£484,392	£484,392	£484,392	£484,392	£484,392	£484,392	£484,392
YEAR 4	£287,541	£296,734	£305,574	£314,074	£478,768	£478,768	£478,768	£478,768	£478,768	£478,768
YEAR 5	£274,042	£283,604	£292,797	£301,637	£310,137	£472,918	£472,918	£472,918	£472,918	£472,918
YEAR 6	£260,004	£269,948	£279,509	£288,703	£297,543	£306,043	£466,835	£466,835	£466,835	£466,835
YEAR 7	£245,404	£255,746	£265,690	£275,251	£284,445	£293,285	£301,785	£460,509	£460,509	£460,509
YEAR 8	£230,220	£240,976	£251,317	£261,261	£270,822	£280,016	£288,856	£297,356	£453,929	£453,929
YEAR 9	£214,429	£225,615	£236,370	£246,711	£256,655	£266,217	£275,410	£284,250	£292,750	£447,086
YEAR 10	£198,006	£209,639	£220,825	£231,580	£241,921	£251,865	£261,427	£270,620	£279,460	£287,960

The table above is about sequencing returns from day one of regular withdrawals. But the sequencing risk issue starts earlier, in the years running up to that point.

One can argue that de-risking investment portfolios in the last few years means the client misses out on the massive compounding effect of investment returns in those years. That is of course true but what is the investment there for? For most clients it is there to deliver a lifestyle the client desires - not to risk that goal in the hope they can get even more. We can say then it is a risk trade-off.

If in the last few years of accumulation the investment portfolio suffers, say, a 30% fall, that can have a material impact on the lifestyle it can provide at the client's retirement date. Or it means deferring retirement. Neither of those outcomes are optimal. Therefore, if the portfolio value is pretty close to achieving the financial planning objective then de-risking the investment strategy makes sense. You are trading off potential investment return for reducing the risk of failing to achieve the planning objective. That feels like an insurance premium worth paying.

Once we get to that moment of taking money out and not putting it in, things start to a look a bit different. Not just the hard numbers but psychologically for the client. A good friend of mine who has worked in financial services all his life recently told me he had just started to decumulate and he said it felt 'weird'. The cosy saving part of accumulation had shifted to one of 'have I got enough?' and 'will it last?' type of thinking. The positive aspect to this kind of thinking is that it tends to make clients a little cautious about their spending which is helpful: it means their funds are less likely to be depleted through reckless spending. However, our role of course is to help clients steer a path that gives them comfort but helps them achieve the lifestyle they want.

The question we need to answer then is 'what is the appropriate investment strategy for decumulators?' Of course this will vary according to the client but there are some guiding principles worth considering.

To combat longevity and price inflation risk over the long term, most would agree that investing in equities has to be the answer. We can debate how much but the principle remains that it is only equity investment that has a sustained track record in beating inflation and is likely to help us avoid outliving our money. In fact if you look at any serious study, it would tell you that investing - perhaps - 100% in equities is the right answer, probably.

The key word is 'probably' of course. Saying to a client 'it's ok; your retirement is probably going to be ok' isn't really what they want to hear.

What I mean by probably is that based on historical investment data an equity-based strategy more likely than not will be better than other strategies. A probabilistic basis is a sensible approach. We can gauge levels of probability using stochastic modelling. It avoids being tempted into giving absolute answers to questions which do not lend themselves to such certainty.

We are probably not going to recommend a 100% equity portfolio for the majority of clients. This is because of the potential severe impact of poor investment returns in the early years (see fig. 2 above). A big drop in those early years is a risk worth trying to mitigate because of the scale of its potential impact. This suggests having some of the portfolio in lower-risk assets. That much is perhaps obvious. However what is just as important is the order in which you sell down assets to meet client income needs. Selling equities in the short term makes little sense as these tend to be volatile. It makes more sense to rely on assets that tend to exhibit lower volatility.

If you are using a multi asset portfolio, then simply taking say a 4% withdrawal across all asset classes, this is likely to be sub-optimal. In most years equities tend to be the best-performing assets class so selling these and maintaining the asset mix is illogical. It might be better to sell down bonds in the early years and leave equities to grow over time. Beyond the short term, say five years, we can then start to withdraw money from equities once it has had a chance to grow and possibly overcome any short term sequencing risk horrors.

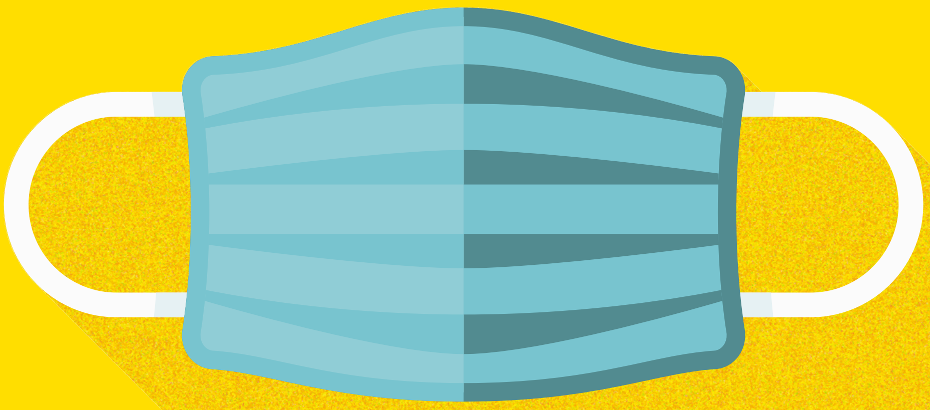
The implication of all this for risk profile and asset allocation is that we start with say 50%/50% equity/bond allocation but gradually shift to perhaps 80%/20% over time as we sell down bonds in the early years. That is an evolution of investment planning from the traditional approach but logically this is a sensible strategy to manage decumulation risks.

"Ultimately the answer to our decumulation challenges is not to be found in a product from an investment house."

POST-COVID

WHAT WILL THE WORLD LOOK LIKE AFTER COVID-19?

Five Schroders fund managers reveal the main ways they expect Covid-19 to change the way we live and work.



The coronavirus pandemic is acting as a catalyst, accelerating a number of trends, such as an increase in the number of people working from home and higher levels of e-commerce. Whilst some of the impacts of Covid-19 will be temporary, there is a growing sense that we are now at a pivotal moment and many of the changes will become permanent.

We spoke to five fund managers to find out what they think will be the most significant long-term impact of Covid-19.

Robin Parbrook is a fund manager specialising in Asian equities

"Covid-19 is going to have a number of significant impacts on how we live and work. This is more of an acceleration of trends that were already there, rather than a sudden change in behaviour. This could include the end of the 9-5 working week, the end of office life as we know it. If not our children, then certainly our grandchildren, will find it very peculiar that anyone would choose to get on a packed train at 8.30 in the morning to go and work in an office with thousands of other people when you didn't actually need to. During the current crisis, Schroders has 98% of its workforce working very successfully from home. The technology to do this has been there for some time, Covid-19 merely accelerated the process."

"The other key change will be the return of "big" government. The only way to get out of this hole is to spend money and government expenditure is going to come back to the fore. Big government is back and governments are going to play a much

"Big government is back and governments are going to play a much bigger role in society, whether we like it or not."

bigger role in society, whether we like it or not. As someone who can remember the 1970s, I'm not too keen on this idea. However, younger generations, such millennials and Generation Z seem quite open to this change."

Alex Tedder runs the global equities team and specialises in disruption

"Covid-19 is going to act as a catalyst for automation. This was already happening before the outbreak of the virus, particularly in parts of Asia, and now there will a rapid adoption of automation in areas that previously haven't been automated, such as the service sector. You will see a lot more artificial intelligence (AI) than we currently have. This is something that I'm very excited about and something that is significantly underestimated by the market today."

"During the current crisis technology has really come to the fore. We have had to use it and it's actually worked really well, which for me is tremendously positive. Adoption rates in areas of technology such as communications, e-commerce, automation and remote healthcare soared during the pandemic because we didn't have any other options. These trends are all set to accelerate further once the pandemic is under control and there is a huge amount of growth potential in these areas."

John Bowler is a fund manager and specialises in healthcare innovation

"The Covid-19 pandemic has shone a light on the growing importance of technology for the healthcare sector. During the crisis, telehealth (the distribution of healthcare-related services via electronic devices such as smart phones and laptops) has been essential. These services are not only providing better patient outcomes, but are doing so in a more cost effective manner. And while these technologies were available before the pandemic, Covid-19 has accelerated their take up, which will undoubtedly continue once the crisis is under control. We are now at a positive inflection point where we will start to see genuine innovation and advancement across the sector."

"Patients are now experiencing the benefit and convenience of online consultations with doctors, and healthcare providers are also realising the benefits as they replace lost income from cancelled face-to-face consultations with virtual consultations. I believe we are at the start of a transformational shift in knowledge and technology. Increased use of digital health services will also serve to democratise the management of healthcare and well-being, providing individuals with the tools and data to take greater responsibility for their own personal health."

Tom Walker is a fund manager, specialising in global cities

"Technology has allowed huge numbers of people to work from home during the current lockdown, supplanting the need to be in an office on a daily basis. As such, we envisage that there will be fewer people who work in the knowledge economy travelling into city centres each day. Although the urban core will still be vital to the effective running of a global city's economy, office buildings in secondary locations, outside of the urban core, will be most at risk of being repurposed. With higher numbers of people working from home, it will make no sense for businesses to maintain these type of offices."

"The way we use buildings in global cities will change. However, this is nothing new. In London, for example, old warehouses by the side of the Thames that were once used for storing commodities brought to the city's port by ship, have been repurposed as high-end luxury housing. Covid-19 has accelerated the move to online shopping and data centres and warehouses are increasingly replacing the need for shopping malls in many cities. Most companies will prioritise their offices in the most connected locations or use flex office alternatives. This was already happening as flexible working ensured only the best connected offices remained relevant."

Isabella Hervey-Bathurst is a fund manager who specialises in climate change

"Covid-19 has led many businesses to re-evaluate their priorities. People are working from home where they possibly can and meetings and conferences have become virtual ones, This crisis will make businesses re-evaluate the necessity of what they would previously have considered "business as usual" practices. And this could just be the start. We think it is quite possible that we could see some more permanent changes in how we work, and that could be good for the climate."

"Climate-focused investments are no longer as dependent on policy support as they were a decade ago. However, that support remains important in accelerating progress, particularly in areas such as heavy industry where the economics of decarbonisation technologies are not yet compelling without regulatory intervention. We are hopeful that the current crisis could prove the springboard for the climate transition that scientific consensus tells us is becoming increasingly urgent."

Please remember that the value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.

THE ADVANTAGE OF FLEXIBILITY

Jim Leaviss, manager of the Global Macro Bond fund, at M&G Investments, discusses how he has been investing through the crisis and the prospects for fixed income markets today.

HOW HAVE YOU ADJUSTED THE GLOBAL MACRO BOND THROUGH THE CRISIS?

"As we came into 2020, trade wars were already causing a slowdown in growth. There were other signs of pressure in the global economy: Germany had had a couple of quarters of zero growth and inflation rates were below target; the yield curve was negative. As a result, we were already wondering whether credit spreads should be as highly valued as they were. Equally, we were also asking whether government bonds should have sold off so quickly.

As a result, we moved from an underweight position in government bonds and got rid of most of our corporate bond exposure. When the crisis hit, we had almost zero in emerging markets, credit and high yield. We also had duration of around eight years. We can't claim to have anticipated the pandemic but we responded to unrelated warning signals."

WHAT HAS HAPPENED SINCE?

In March and April, we saw a complete reversal of valuations. It wasn't quite the global financial crisis, but we did see significant distress in fixed income markets. It was an opportune moment to add back risk. As a result, we took government bond exposure lower, raised investment grade credit to 50% of the portfolio, high yield to 20% and emerging markets to 15%. This wasn't a question of knowing whether the recovery would be V-shaped or L-shaped, but just that at some stage there would be a recovery, given the actions taken by central banks, and that this would be positive for risk assets.

We needed to be selective. There have been some defaults – Argentina, for example, Hertz in the US. That said, it is clear that governments don't want companies to go bust and the ECB, Bank of England and Federal Reserve are providing a backstop.

WHAT HAS HAPPENED TO INCOME ON THE FUND?

This is a fixed income fund and people buy fixed income for yield. This crisis may have prompted investors to reevaluate the way they look at equity versus bond yields as dividends are cut. The yield on a corporate bond can't be cut without the company defaulting.

Yields on government bonds have moved down significantly. The yield tipped below 0.5% for US treasuries and, even today, a 10-year gilt pays just 0.15%. However, the yields on some corporate bonds started to look attractive, peaking at over 4% in March. In many cases they weren't there for long, but it presented an opportunity.

The question is whether defaults are priced in. It should be said that defaults are relatively rare for investment grade companies. In the 1980s, we saw 3-4% of investment grade companies default over a span of five years, the highest level in history. At one point, investment grade markets were suggesting a default rate of 18% within one year – and 40% for higher yield. Was capitalism going to end? If not, we saw that we would outperform by being invested in corporate bonds.

We found that even short-duration high quality corporate bonds were sold off, when these should have been the most solid area. Often they were being sold in order to raise money because they were the most liquid option.

ARE COMPANIES STILL ISSUING NEW BONDS?

March was the high point in history for corporate bond issuance. Even though investment bankers and fund managers were all at home, there was real demand for the asset class, while companies also wanted to lock in long-term borrowing. Companies drew down credit lines and borrowed aggressively. It was also possible to pick up a new issuance premium. Companies issuing new bonds tended to be doing so at around a 50bps premium to their existing bonds.

ARE YOU ANTICIPATING MORE ACTION FROM CENTRAL BANKS?

If the global economy doesn't recover, central banks will do more. That said, it is notable that while the Bank of England and Federal Reserve cuts rates, the ECB didn't. This suggests they don't think negative rates are very effective – there are always unintended consequences.

As it stands, central banks are buying up a lot of the new issuance. The Bank of England has bought more gilts than the Treasury has issued. It is effectively borrowing from itself – quantitative easing is soaking up the excess supply.

"It wasn't a question of knowing whether the recovery would be V-shaped or L-shaped, but just that at some stage there would be a recovery, given the actions taken by central banks, and that this would be positive for risk assets."

The government may ultimately make banks or insurance companies buy more government bonds.

WHAT IS YOUR POSITIONING TODAY?

We are more tentative on risk, but still in a broadly 'risk on' position. We are reducing those areas that have rallied a long way. Today, the bond markets are more finely balanced and therefore stock selection has become a lot more important.

We went into March with a lot of US dollar exposure to take advantage of the flight to safety. The dollar rallied throughout the early weeks of coronavirus, but this has started to tail off again. Investors expected the Eurozone to be in a far worse position and therefore no longer need the safe haven quality of the US dollar. Equally, the US appears to have the worst coronavirus problem, plus rioting and dysfunctional government.

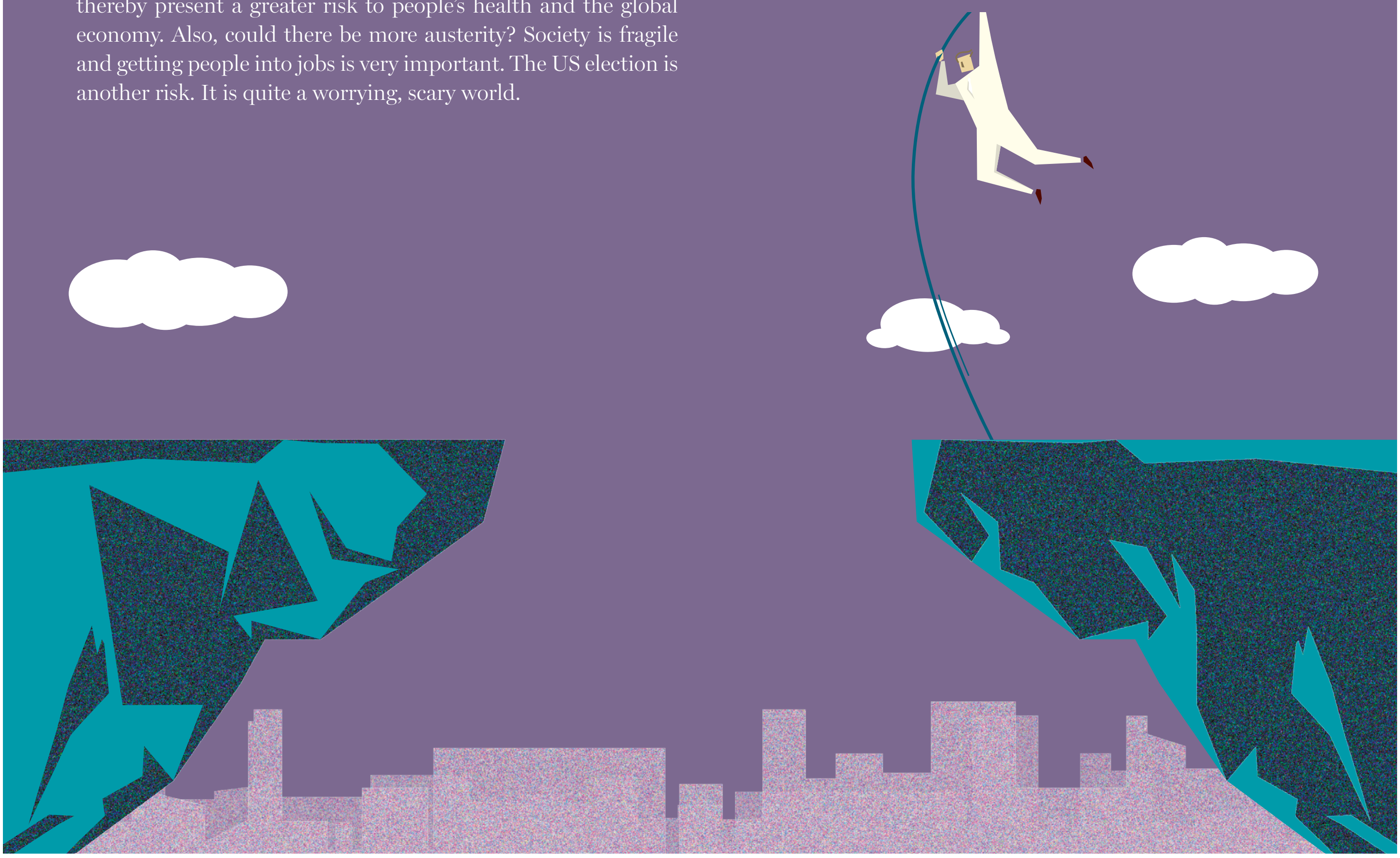
WHAT KEEPS YOU UP AT NIGHT ABOUT THE CURRENT SITUATION?

Certainly, the potential for the virus to become more serious and thereby present a greater risk to people's health and the global economy. Also, could there be more austerity? Society is fragile and getting people into jobs is very important. The US election is another risk. It is quite a worrying, scary world.

HOW DO YOU SEE THE ROLE FOR A FLEXIBLE FIXED INCOME FUND?

It depends on the client. Some people want to allocate to individual asset classes within fixed income. We find that many clients would rather we took the strain: we have the time, the access to information. Flexible bond funds can help take away responsibility for allocating to different areas at a complex moment.

Listen to Jim's podcast 'Uncle Jim's World Of Bonds' - **https://podcasts.apple.com/gb/podcast/uncle-jims-world-of-bonds/id1511287804**



For Investment Professionals only

A LONG HISTORY OF LOOKING TO THE FUTURE

Even through uncertain times we remain focused on helping investors realise their investment goals. Nobody knows what's around the corner, but throughout our 89-year history our priority has always been on helping to create positive financial futures for our clients.

We will continue to focus on sustainable investing and invest in companies that aim to deliver meaningful societal and environmental outcomes, and engage with our clients to keep them informed and involved. Together we can look forward to a brighter future.

Capital at risk

M&G INVESTMENTS

GO EAST FOR EQUITY INCOME

Equity income investors in Western developed markets have been bombarded by announcements of dividend cuts and suspensions, as companies grapple with a severe hit to earnings from Covid-19 and lockdowns. Where, then, can investors go to achieve a more attractive income from their equity portfolio allocation? Jason Pidcock, fund manager of the Jupiter Asian Income Fund discusses the prospects for dividends in the Asia Pacific region.

Dividends across the world are undoubtedly being impacted by the Covid-19 pandemic, but significantly less so in the Asia Pacific region. Why are companies cutting dividends? I see three fundamental reasons: earnings weakness, balance sheet weakness, and regulatory pressure. The first point is addressed by fiscal and monetary stimulus, which has been enormous and ought to lead to higher economic growth and higher earnings growth for many businesses from the back end of 2020 and into 2021.

In the Asia Pacific region, meanwhile, balance sheets remain relatively strong. Regulatory pressure to cut dividends is now quite common in parts of the world, particularly for financial companies in Europe, but it is relatively much less of an issue in Asia Pacific nations – and in any case it's certainly possible to find attractive income opportunities outside of the financial sector.

Forecasting right now is trickier than normal, but there are several sectors in the region that I believe are likely to be more resilient to drastic dividend cuts. These include technology - because of companies' very strong balance sheets and reasonably resilient earnings; plus a number of basic consumption plays such as food & beverages, personal hygiene and supermarkets; and some utilities, telecoms businesses and infrastructure companies.

Although dividends for 2020 are sure to be lower than those seen in 2019, I'm optimistic that Asia Pacific as a region will be relatively resilient, while strong active stock picking should lead to portfolios even more exposed to robust, consistent dividend payers. That is something I am absolutely focused on in the portfolios that I manage, adding to positions with the right combination of dividend resilience in the short term and long-term total return prospects.

In summary, the low base for economic activity and company earnings in Q1/Q2 this year should, in my view, mean that dividend growth from Asia Pacific companies in 2021 could be quite exciting.

If you require any further information or have any questions, please do not hesitate to contact the Jupiter intermediary support team.

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RESILIENT INCOME FOR A POST-COVID WORLD

Income has been one of the first casualties of the Covid-19 outbreak. The UK market has been hit particularly hard, with around half of UK companies cutting, deferring or cancelling their dividends. For Toby Ross, co-manager of the Baillie Gifford Global Income Growth Fund, this underlines the importance of a broad opportunity set and a focus on resilience.

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

For a number of years, loose monetary policy has allowed weaker companies to continue paying dividends – sometimes from debt – and limp on through relatively benign economic conditions. However, the crisis has brutally exposed the limitations of this approach, with significant dividend cuts by some of the world's largest companies, particularly in vulnerable sectors, such as oil.

Toby Ross, co-manager of the Baillie Gifford Global Income Growth Fund, believes that the crisis has brought to a head many of the structural changes in the global economy already under discussion in his team. The portfolio's income mandate precludes some of the high-growth names that feature in other Baillie Gifford portfolios, such as Scottish Mortgage, but the Baillie Gifford growth DNA still runs through the fund, with meaningful weightings in areas such as technology, healthcare and niche industrial businesses, rather than the traditional fare of income portfolios.

"We are not focused on the big businesses of yesterday that tend to dominate the FTSE 100. We want to see how companies will look in ten years' time", says Toby. "As long-term income investors it is not just about yield this year, but also how a company will perform in times of stress and the resilience of that income. The crisis has shown why it's so important. It has exposed those businesses that are not in control of their own destiny, that are over-distributing or where growth prospects are weak."

This has seen the fund deliver a very different income experience through the crisis. Toby estimates that the fund's income is likely to fall around 10 per cent this year, and it is likely that this will be a far better outcome than will be seen from many UK funds and others in its global peer group.

He has not significantly altered the positioning of the fund during the crisis: "The changes we have made include taking advantage of the sell-off to buy businesses we'd admired, but where the price had previously been too high. This includes financials, such as T Rowe Price or Hargreaves Lansdown. These were companies where the market panicked."

That said, there were a few holdings where the dividend growth prospects were notably dented by the virus and what has followed. In particular, Toby sold out of two European banks. "We saw the massive influence of state aid and there was a danger that politics could have started to intrude on their decision-making." On the whole, the team has had to look at each business on its merits. "We always ask whether in five or ten years that business is going to be stronger? Will it be meaningfully larger and better?"

In general, it is not the Baillie Gifford style to react by backing away from companies. The firm sees itself as a provider of long-term capital to businesses and wants to support management teams through difficult periods. Toby gives the example of Amadeus, which provides technology to the travel industry. Understandably, it has had a difficult time, but he believes it is likely to come out of the crisis with a larger market share. "In the near term, we just sit out the volatility in the share price."

Roche is currently the fund's largest holding. This is partly a reflection of recent good performance: Roche has had a 'good crisis' with its diagnostics capability seen as an important factor in Germany's successful response to the virus. However, for Toby, this success didn't happen by accident and is not confined to its response to Covid-19. "There was a culture that underpinned it. A culture of scientific discovery, a willingness to make – and learn from – mistakes and a forensic focus on research."

He believes income fund managers need to guard against retreating into "stodge and safety", even with the outlook so uncertain. While it may feel comfortable in the short term, it is likely to be unhelpful as the economy restarts.

The team has always worked with a checklist for income resilience – the template shown in the box-out. While this doesn't predict the next crisis, it does help the team create an all-weather portfolio that should prove resilient in difficult times: "We need to be able to trust the management teams of the companies in which we invest, that the companies can grow and ride out different scenarios."

The team is also focused on engagement. It launched a responsible version of the portfolio in 2018 and uses the same analysis across both portfolios. This also helps ensure resilience, uncovering those companies and their management teams that are acting sustainably for the longer term.

The breadth of global opportunity is always helpful for delivering income, particularly in a crisis. However, it is not enough in itself. The Baillie Gifford Global Income Growth Fund identifies those companies that can compound growth and

"We are not focused on the big businesses of yesterday...we want to see how companies will look in ten years' time"

income over decades, and will not only last through this crisis, but the next one as well. It has just faced its biggest test and is proving the resilience of its philosophy.

FIGURE 1: CHECKLIST IN ACTION: ROCHE

	Weak		Strong
Fat or thin margin business	0-10%	10-20%	>20%
How stable has Operating Cash Flow been, including Working Cap, swings, historically?	Volatile	Some instability	Like a rock
How capital intensive is growth?	Highly	Moderately	Not at all
Payout Ratio	>66%	33-66%	0-33%
Balance sheet strength if called upon to fund dividend?	Weak	OK	Fortress
Management/Board attitude to defending absolute level of dividend?	Don't care	Try a bit	Try very hard
Is the business structurally shrinking or growing?	Shrinking	Trundling	Growing
Are there any external impediments to paying dividends (e.g. regulators?)	Yes	Not really	No
How does it stack up on the sector-specific considerations?	Warnings	OK	Looks great

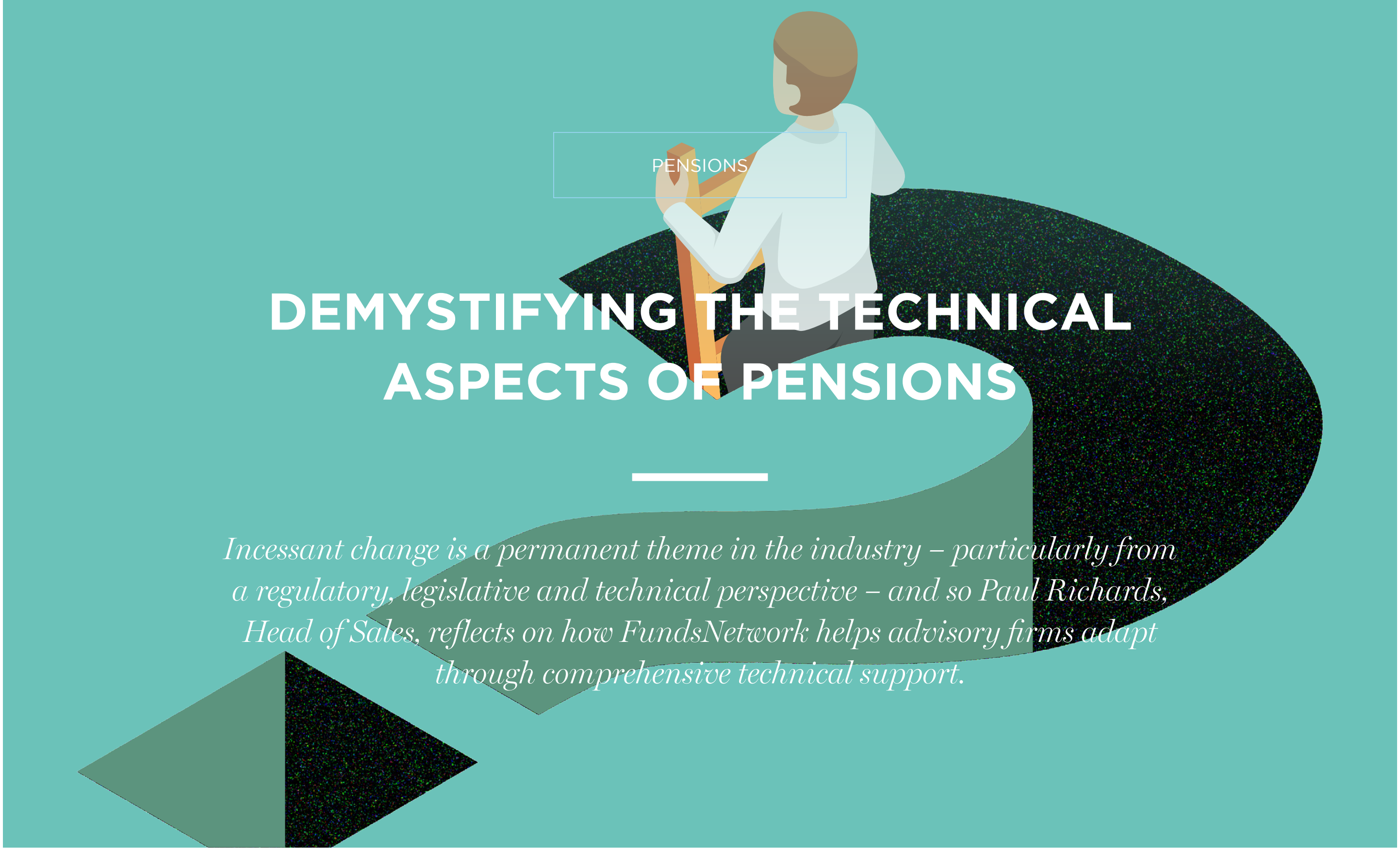
FIGURE 2: ANNUAL DISCRETE PERFORMANCE (%) TO 30 JUNE EACH YEAR

	2016	2017	2018	2019	2020
Fund Class B Inc*	13.7	23.8	5.7	12.6	7.2
Benchmark**	14.0	23.0	9.4	10.1	5.7
Sector Average***	9.6	19.2	3.6	8.4	-2.6

Performance source: StatPro, FE, FTSE, total return in sterling. Returns reflect the annual charges but exclude any initial charge paid.
Global Income Growth Fund ** FTSE All-World Index * IA Global Equity Income Sector*

Past performance is not a guide to future returns.

The manager believes the FTSE All-World Index is an appropriate benchmark given the investment policy of the fund and the approach taken by the manager when investing. In addition, the manager believes an appropriate performance comparison for this fund is the Investment Association Global Equity Income Sector. More details on the fund can be found at **www.bailliegifford.com**



PENSIONS

DEMYSTIFYING THE TECHNICAL ASPECTS OF PENSIONS

Incessant change is a permanent theme in the industry – particularly from a regulatory, legislative and technical perspective – and so Paul Richards, Head of Sales, reflects on how FundsNetwork helps advisory firms adapt through comprehensive technical support.

WHY IS PROVIDING TECHNICAL SUPPORT TO PRACTITIONERS SO IMPORTANT?

We've seen a deluge of new pension regulation over the last five years which has led to more demand for advice. We think it's vital that advice practitioners are on top of all the intricacies that go hand-in-hand with the reforms. We therefore offer wide-ranging technical support in this space, drawing upon the considerable expertise and experience of our pensions team.

WHO CAN BENEFIT FROM THIS SUPPORT?

Our aim is to assist all advisers and paraplanners, no matter how experienced or new to the industry they may be. For example, we offer a broad range of training videos designed to help anyone studying for CII exams or who simply wants to boost their knowledge. We cover the JO5, RO4, RO8, AF1, AF3 and AF7.

We also recognise that even the most knowledgeable individuals occasionally need guidance on the more complex areas of pension legislation. Pensions and divorce, for instance, is a complex area where we are frequently asked to clarify the rules. We've produced an in-depth guide on this subject which is available on our 'Technical matters' hub.

WHICH OTHER TOPICS ARE POPULAR AT THIS TIME?

The pension lifetime allowance and beneficiary flexi-access drawdown death benefits are areas currently at the top of the list.

We've developed two new support packages on these subjects where our tax and pension experts discuss key considerations when assessing client options.

DO YOU HELP ADVISERS EXPLAIN THE TECHNICAL ASPECTS OF PENSIONS TO CLIENTS?

Yes, in order to save advisers time and money, we've produced several client-facing guides for use in meetings and other communications. These downloadable guides cover topics such as pension tax relief, the 'carry forward' rules, income drawdown, annuities, the annual allowance, the tapered annual allowance and the lifetime allowance.

HOW CAN ADVISERS ACCESS THIS SUPPORT?

Our support is available in a number of ways. Firstly, our technical experts can run sessions on specific areas as it's important to hear firsthand the issues practitioners are facing. Secondly, we put a lot of work into our website and there really is a wealth of good quality information to be found at **fundsnetwork.co.uk/technicalmatters.**

FIXED INCOME

WHY SHORT DURATION STRATEGIES MAY HELP NAVIGATE THE CURRENT MARKET ENVIRONMENT

While central bank stimulus measures are likely to keep bond yields low, short duration strategies may be a means to deal with this new environment.

WHATEVER IT TAKES

Central banks and governments around the world have put in place unprecedented monetary and fiscal stimulus in reaction to the economic threat posed by the Covid-19 pandemic.

These measures, combined with broadly risk-off sentiment, are likely to keep yields low, even negative, at the more 'safe-haven' end of the fixed income spectrum. This means lower scope for return and higher vulnerability to interest rate risk.

Although yields have bounced back more recently, a great deal of uncertainty remains over the longer-term impact of this unprecedented policy support and the shape and timing of the recovery, therefore, we expect volatility to continue in the near term.

WHY SHORT DURATION STRATEGIES COULD HELP YOU MITIGATE RISK

Short duration strategies could help to navigate this uncertainty. As a result of recent market turmoil, short duration bonds are now appearing to show value and as a result, there is potential for a pricing rebound.

Short-dated assets could benefit from attractive valuations and risk premiums in the primary market as companies have restarted to issue bonds at attractive levels. In fact, despite warnings about disappointing first-quarter results, many companies are taking action to fight the negative impact of the coronavirus crisis on their earnings, notably through capex reduction, dividends/share buy-back cuts and a review of their operating costs.

Furthermore, companies are proactively drawing down on revolving lines of credit and other sources of financing to put cash on the balance sheet. On the downside, rating downgrades are rising, and financial leverage will increase despite all these measures.

"A great deal of uncertainty remains over the longer-term impact of this unprecedented policy support and the shape and timing of the recovery."

OUR FIXED INCOME VIEW

The global bond market is not homogenous and different opportunities and risks will appear over the period ahead.

While central banks and government stimulus is massive for corporates, ratings agencies have started to re-assess companies' fundamentals to the downside and some sectors – like energy, airlines, automotive and leisure – will be strongly impacted.

US corporate bonds are relatively attractive as they have widened twice as much compared to Europe[1]. Meanwhile, the primary market has reopened with very attractive premiums on high quality names. In Europe, all sovereign issuers should benefit from central bank support, even if the Eurozone's sustainability could again be questioned in the coming months and the debt level is a legitimate concern.

Despite limited inflationary risk for the coming months, we believe US and French inflation-linked bonds are attractive as they have violently repriced the inflation outlook. Emerging markets have suffered strong outflows that have impacted performance given the liquidity issues.

AXA IM'S SHORT DURATION BOND STRATEGY

We offer a range of short duration strategies which aim to meet your needs, whether you are looking for a higher yield or to combat inflation.

Our short duration strategies generally invest in bonds with maturities of five years or less and seek to capture high current income with low overall volatility. The result will be portfolios with a duration that is generally below three years.

Visit our website **adviser.axa-im.co.uk/fixed-income**

[1]Source: AXA IM as at 6 April 2020

ESG:
THE NEW NORMAL

ESG integration and Responsible investment have moved squarely to centre stage, taking the spotlight within the investment industry, says Square Mile.

Although a focus on ESG integration and Responsible investment could be considered a recent phenomenon, these two trends have roots that can be traced back to as early as the 18th century, when the Quaker and Methodist movements imposed ethical guidelines to influence how their adherents spent or invested their money. In spite of this long history, the recent years have been a turning point for these two investment approaches as they have entered mainstream asset management.

This seismic shift has led to a proliferation of funds labelled 'responsible' or 'sustainable', while ESG factors are now increasingly integrated into the investment processes of funds across all sectors of the market. This has been driven by three key factors.

First, there is an increasing legislative and regulatory focus on tackling issues such as climate change or corporate behaviour. Second, as investors take steps to become more responsible citizens in other aspects of their lives, they also demand to understand how their money could be invested for good.

Finally, leaders within the asset management community itself are increasingly emphasising the important role the industry has as a whole, in reconsidering how we assess securities to fully ascertain their impact on society and the environment, and how this process can be improved.

There is no doubt that ESG integration and responsible investment are here to stay, but with all new trends, there has been confusion and misinterpretation surrounding the broad terminology applied to these approaches to investments. There are worries over 'greenwashing' within the industry. There has never been a greater need for clarity and consistency, to ensure that the needs and preferences of clients can be met.

With incoming MiFID II regulation, which require an assessment of each client's ESG preferences into their suitability tests, it is of crucial importance that advisers are confident in their understanding of the terminology around ESG and responsible investing.

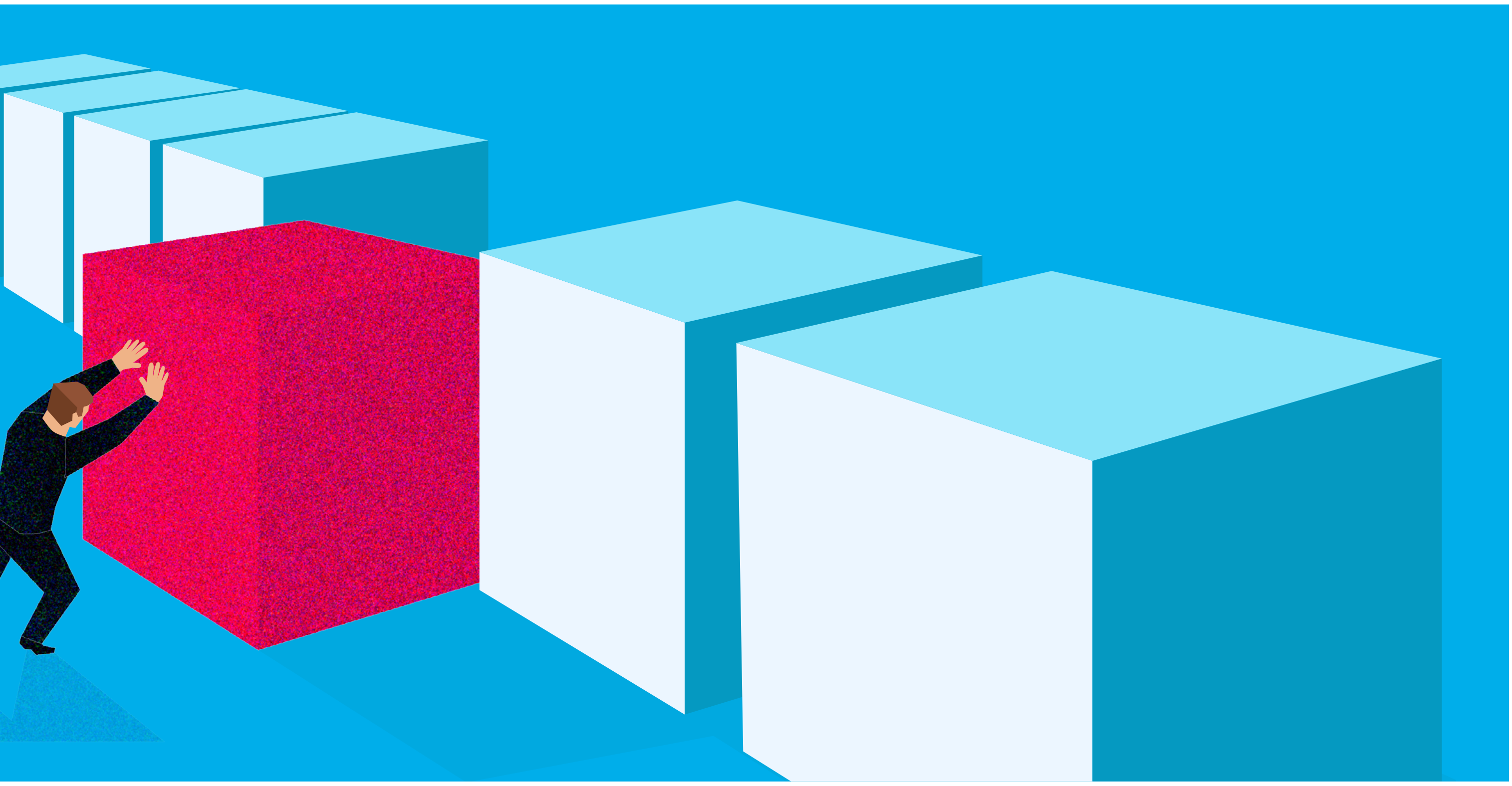
ESG should be seen as a fundamental input into the company analysis to better establish the potential risks these factors have on an investment and how they can be mitigated. That said, it is important to emphasise that ESG analysis in itself does not produce better outcomes for either society or the environment and is not limited to funds with 'sustainable' or 'responsible' objectives in their mandates. ESG is simply another lens through which to consider risks at both a company and fund level.

Responsible investment focuses on outcomes: what the fund is trying to achieve beyond a monetary objective. Essentially, these funds will have the ability to contribute to a positive outcome for society, the environment or to avoid harm, alongside their aim to deliver positive financial returns, and can be grouped into three categories.

First, and most commonly associated with responsible investing, is 'exclusion'. These funds actively exclude 'sin-stocks' which have a negative impact on society and/or the environment, for example, tobacco or oil companies. Second, 'sustainability' includes funds that reward and encourage positive change and are leaders in sustainability. Finally, the 'impact' category includes companies that have a positive impact on society and/or the environment.

The investment industry is experiencing a rapid shift in the way it views itself and its responsibilities within wider society, but the need for a consistent and communal language is only one piece of the puzzle. While advisers are increasingly aware of these themes, a recent survey by Square Mile highlighted that only 39% of advisers have integrated ESG considerations into their centralised investment proposition.

However, this will change, as new regulation is implemented governing advisers' approach to recommending ESG and responsibly invested products. This is likely to have significant repercussions for the financial adviser community; compelling advisers to disclose information on the ESG characteristics of each financial product under consideration and describe how the client's ESG preferences have been considered in the financial advice process. Furthermore, those companies providing



portfolio management services will have to explain how ESG preferences have been accounted for in the selection of portfolio holdings.

There is no doubt that advisers are overloaded with information on ESG integration and responsible investment. Given how subjective this area can be coupled with some level of confusion in the wider market, the issue arises of how to best match a fund to a client's needs. At Square Mile, to help provide clarity on these two themes and to support advisers during their fund selection process, we have developed two initiatives: ESG integration assessments and Responsible ratings.

Our ESG integration assessments are applied at a company and a fund level. In both instances, they are based on information received from the fund groups through a proprietary questionnaire which is then overlaid with our analysts' qualitative intelligence.

At a company level, we seek not only to understand how an asset manager integrates the consideration of these factors in its investment processes, but also to what extent these are applied consistency across the business. Additionally, we assess if and how ESG factors are considered in the management at an individual fund level, focussing on how they are used as an input to the process, how they impact research, portfolio construction and risk management processes. At both a company and a fund level, Square Mile allocates one of seven scores from 0, where ESG considerations have no material influence on the management of the investment company or fund, through half-point grades to 3 where they are fully integrated into processes and philosophy.

As with the increasing number of groups and funds adopting ESG principles, there has been a proliferation in funds that are responsibly driven, whose objectives go beyond purely financial returns, aiming to contribute to a positive outcome for society and/or the environment. To help advisers identify funds that can fulfil their clients' goal of both a positive impact on their financial wellbeing and the wellbeing of the world around them, Square Mile has also introduced Responsible ratings.

An evolution of our existing research process, the Responsible ratings identify those funds that have a responsible outcome or target incorporated into their objective and in which Square Mile is confident that its manager has the ability to meet both their objectives. While ESG considerations are applicable to all funds and groups and are viewed as separate assessments, they provide valuable input into framing our understanding of the fund managers approach to Responsible investment.

The investment industry is continually evolving, with a combination of investor demand, impending regulatory changes and a recognition of its responsibilities within the wider society being driving forces for change. As ESG and responsible investment become mainstream, there is incredible potential for good, but it can be only be successful if the industry develops a clear and communal language, thereby creating greater clarity for the fund selection process.

Jake Moeller, Senior Investment Consultant, Square Mile

For more information, visit the Square Mile website
www.squaremileresearch.com

"As investors take steps to become more responsible citizens in other aspects of their lives, they also demand to understand how their money could be invested for the greater good."

ESG MULTI-ASSET

ESG BUILDS MOMENTUM IN MULTI-ASSET

There are still relatively few options for multi-asset investors who want an Environmental, Social and Governance (ESG) focus. With its Future World Multi-Index range, the LGIM Asset Allocation team aims to fill this gap. Justin Onuekwusi and Andrzej Pioch discuss how they've built the new funds.

The momentum behind sustainable investing has gathered pace in recent years: a confluence of increasing awareness, regulatory pressure and stronger environmental reporting have seen flows directed towards environmental, social and governance (ESG)-focused investments.

There are early signs that the Covid-19 crisis may have accelerated this trend. The most recent Pridham Report (2020) showed that ESG and ethical funds took the lion's share of investment in the early part of this year and as the crisis started. Recent Morningstar figures show that these type of funds have outperformed their peers throughout the crisis so far. (https://www.ft.com/content/46bb05a9-23b2-4958-888a-c3e614d75199)

However, as yet, there has been relatively little in the multi-asset space for ESG investors and certainly not at a lower price point. Legal and General Iinvestment Management's (LGIM) Asset Allocation team sought to address this gap with the launch of its Future World Multi-Index funds in April 2019, applying the same disciplines used across its Multi-Index funds, but with an ESG agenda.

In doing this, it calls on LGIM's 'Future World' range. This is a collection of index funds, built on three pillars: long-term thematic analysis, the integration of ESG factors, and active ownership. The funds cross themes, asset classes and geographies and have been designed to help identify new opportunities, while also managing risk effectively.

ESG WEIGHTING

The funds include a range of index building blocks and apply an ESG 'tilt' based on a proprietary scoring mechanism. The funds are similar to traditional, well-diversified index funds but with a higher weight to companies that score well against environmental, social and governance criteria.

The Asset Allocation team, comprising economists, strategists and fund managers, uses these building blocks to deliver an ESG multi-asset solution for its investors. Justin Onuekwusi, who manages the funds alongside Andrzej Pioch, says: "We saw there was a growing demand from our client base to take the foundations of our existing portfolios – suitability, cost-effectiveness, diversification and dynamic asset allocation – and create a sustainable version."

The two funds are targeted at risk profile 4 and risk profile 5 clients. They offer a similar level of diversification to that found in the group's standard Multi-Index funds - including equities, fixed income securities, money market instruments, and alternatives such as property. The result is two funds tilted to reduce exposure to companies associated with poor ESG practices and provide greater exposure to those with better practices.

The Future World Multi-Index funds will perform differently to the main Multi-Index range. For example, the funds will generally be lower weighted to energy companies, which can influence relative performance.

NO 'ONE SIZE FITS ALL' ON ESG

The criteria for the funds is that at least 50% will be in investments that incorporate the Future World principles or that clearly define a set of ESG criteria, but also include assets such as government bonds or alternatives which have been shown to enhance diversification of a multi-asset proposition.

Pioch says: "There are so many terms being used and there is no 'one size fits all' for ESG investment. Clients have different convictions and we need to be very clear and transparent about what the fund does and what it does not do when it comes to ESG. As such, we asked ourselves how we could deliver a fund that has a tilt towards ESG, excludes the worst 'sin' stocks and has a greater emphasis on those with lower carbon emissions, a more diverse workforce and better practices."

He says this is possible because of the metrics that are now available, which allow them to assign scores to individual companies. In this way, they know how their funds are scoring. "This wouldn't have been possible ten years ago. These statistics were patchy and expensive to get hold of."

He admits there are areas where data is still hard to come by: "In real estate investment trusts and infrastructure, for example, it is not as easy to get information as it is for equities or credit. However, these areas are valuable to their diversification properties." Nevertheless, he is clear that in aggregate the funds offer a markedly better ESG profile than a standard fund.

STEWARDSHIP

As one of Europe's largest asset managers, LGIM has long taken its stewardship responsibilities seriously. Its engagement programme runs across the entire group, incorporating both the Future World Multi-Index funds and the standard Multi-Index range. The company, through its Investment Stewardship team, votes on all shares, rather than outsourcing. The most recent annual statistics show the company's ESG team has analysed 16,000 companies under its proprietary scoring methodology.

The company is willing to back its views with conviction, including voting against 3,864 board directors globally last year. "We take a stance and don't simply abstain," says Pioch. It recently sold out of Exxon Mobile from its future world fund range because of its weak performance in tackling climate change.

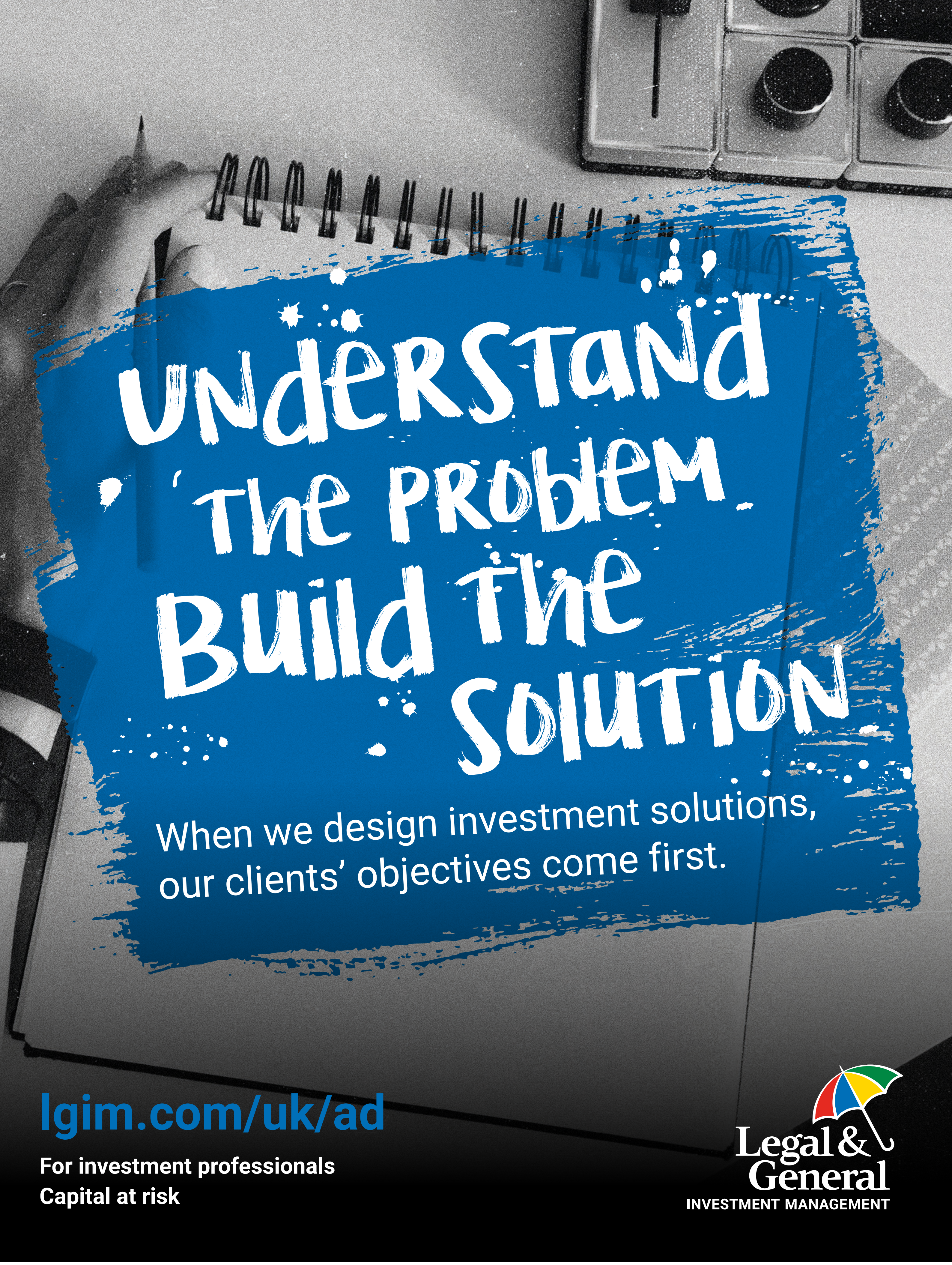
There is also Future World Protection List, which excludes those companies that it believes exhibit the greatest risks, including controversial weapons manufacturers, 'pure' coal manufacturers and violators of the United Nations Global Compact.

CHANGING INVESTOR PREFERENCES

Although much of the early demand for ESG funds has come from defined contribution schemes, Onuekwusi says that this is spreading all the time: "In particular, social factors are becoming more important - employee rights and how companies support their workforce, plus gender and racial diversity issues - are likely to be increasingly reflected in investor preferences."

He points to new obligations under MiFID that may require advisers to ask clients about their ESG preferences. Having workable ESG options for clients will be a necessity. The Future World Multi-Index funds, combining risk-targeting with enhanced ESG credentials, add a welcome option in an under-served area.

"There are so many terms being used and there is no 'one size fits all' for ESG investment. Clients have different convictions. As such, we asked ourselves how we could deliver a fund that has a tilt towards ESG, excludes the worst 'sin' stocks and has a greater emphasis on those with lower carbon emissions, a more diverse workforce and better practices."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JAPAN EQUITIES

Sophia Li
FSSA Investment Managers

SEARCHING FOR SUSTAINABLE RETURNS IN JAPAN

Japan's weak economy is no reason not to invest, says FSSA Investment Managers; company profits are growing fast.

Despite the perception that there is no growth in Japan, there are many companies that have been able to adapt and grow despite economic headwinds, and have delivered sustainable earnings growth and attractive shareholder returns. We aim to address some of the most common investor concerns about Japan equities and highlight the opportunities for sustainable growth in this market, one of these concerns is discussed below.

ECONOMIC GROWTH IS NOT A REQUIREMENT FOR CORPORATE GROWTH

Theoretically, a fast-growing economy bodes well for corporate earnings and stock prices, and vice versa. Because of this, investors often cite Japan's weak economy and deflationary environment as reasons they have been reluctant to invest in Japan equities. However, the data suggests that these concerns may be unfounded. Although Japan's nominal GDP has grown by just 4% since the late '90s peak, Japan Inc's corporate profits have grown by 180% over the same period.

At FSSA Investment Managers, we believe that Japan contains many "hidden gems" – companies that are able to grow strongly, despite the macro backdrop. How is this possible? Our research indicates that high-quality franchises that are dominant in niche sectors can sustain strong and consistent earnings growth without relying on leverage or macro conditions. Often, these companies incorporate some combination of the following characteristics: innovation, disruption, overseas expansion and astrong focus on return on invested capital.

Even in declining sectors, there are singular companies that have beaten the odds and delivered steady returns for investors. One such example is specialty furniture retailer Nitori, the largest furniture brand in Japan. Weak domestic consumption and deflationary price expectations might reasonably challenge any domestically-focused retailer. However, Nitori has continually innovated – from product design to new store formats – to secure new areas of growth.

As Akio Nitori, founder and chairman of Nitori, reportedly said, "Economic growth is never a part of our growth assumptions." This supports our view that there are no sunset companies, only sunset industries. We believe that successful investing in Japan is about seeking out these "hidden gems" in a large and deep universe, rather than simply buying the index. As a highly under-researched market, we believe that Japan offers the perfect opportunity for bottom-up active investors to generate alpha.

Sophia Li, FSSA Investment Managers

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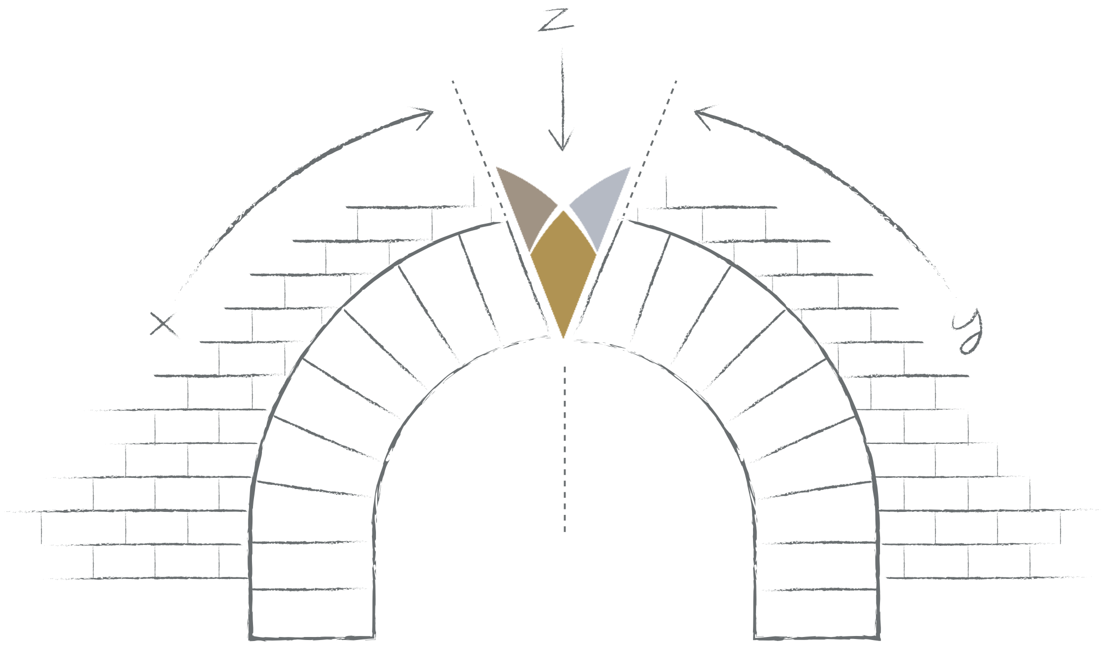

In uncertain markets, a solid foundation is paramount. The BNY Mellon Long-Term Global Equity Fund can act as a keystone, aiming to provide long term stability for any portfolio, to better withstand the market forces that may come its way.

BNY Mellon Long-Term Global Equity Fund

Managed by:

WALTER SCOTT

The value of investments can fall. Investors may not get back the amount invested.

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