KING&SHAXSON
ethical investing

Rebalance Update

June 2020

## General Overview

### USA

Focus in the US is still centred on COVID-19 as large parts of the country open up again. Initial evidence is that some states are recording high infection and death numbers again. As we mentioned in our last report the perception is that President Trump has not handled the situation very well. With racial tensions remaining high, Trump has got a lot on his plate. Later in the year we have the Presidential Elections, and although the most recent job data was not as bad as predicted, the market appears to have priced anything in regarding the outcome of this election. The bookmakers suggest Joe Biden is in a slight lead, but like the last campaign, President Trump retains his core support and the support of Mid America. It will all come down again to the electoral colleges, and if so then Mr Trump may likely gain a second term, even if he loses the popular vote, as he did when he was up against Hilary Clinton. When focus moves to the election it will be interesting to see the market moves.

### UK

Not much has changed in regard to the UK since our last meeting. The economy is opening up again and anecdotal evidence suggests that takeaway retailers are the early ones to benefit, with food outlets (The Golden Arches) seeing non-stop business. They have had a good bounce, the important issue now is will it last? In two months' time the Government's furlough scheme will end. Sadly it is predicted that a lot of people will be made redundant as companies adjust their business to the new normal. Will certain industries ever go back to how they once were? Will we continue to use public transport as much as we did previously? And as mentioned before, office property in certain areas of the UK may never see high occupancy levels again as we realise we don't need to be in the office to function.

The B word has re-appeared with more rhetoric appearing on the wires. It seems we are no closer to an agreement, with the BOE's Bailey telling UK Banks to prepare for a no-deal Brexit. The impact of coronavirus on the global economy would suggest a deal will be sought to reduce any further friction, but the UK government has confirmed they will not seek a delay. Our view is that this will once again go to the 11th hour, and we will either get concessions on both sides or we enter the world of WTO trading rules on 01/01/2021.

### EU

Apart from the other side of the B word coin, the ECB continues to support the economy, with more countries coming out of lockdown. We have also seen a €750 billion package announced for support across the EU, whilst individual countries such as Germany have announced packages to support their individual countries.

However the EU continues to pay the price for an enduring lack of structural reform, and once again the ECB is left to pump even more money into a malfunctioning system that only pushes asset prices higher and further away from the underpaid and underemployed workforce. To make matters worse,

the main engine of Europe, Germany, has seen their auto sector hard hit, which was already in cyclical and structural decline. The German government did produce a shock and awe budget package, but one that did not pander to the auto sector. Being mostly cuts to VAT and infrastructure spending, it will go some way to slow the decline but few doubt it will be enough to restart Europe's stalled economy.

**ROW**

In China President Xi has his own issues, (a la Trump) in Hong Kong. It appears that this time round China does not want to take a backward step in HK or vs Trumps America. This will continue to play out in the coming months, but recent data from China, post virus appears positive, although the validity of their data continues to be questioned. Most recently their employment data, with some economists suggesting it is closer to 80 million and not the circa 26 million that is quoted.

We are cautious on EM in general, with countries such as India and Brazil experiencing spikes in cases and the economic impact continues to be downgraded.

We think one interesting area in Asia is Japan. There are a number of exciting Japanese companies we have our eye on, with help from the Bank of Japan propping up markets, whilst the Yen remains an interesting proposition for its safe haven status.

**Equities**

The majority of the committee are feeling slightly more optimistic since our last meeting, with most of this optimism coming in the last week leading up to the virtual get-together. With all the stimulus that has been (being) provided it appears we are through the worst of COVID-19, and despite all the horrific loss of life things may not be as bad as first thought. Again, anecdotal evidence suggests that more social interaction does not always lead to an increase in the R rate just yet. We must mention though that Brazil, India and Russia are now facing the epidemic and reportable data is hard to find so we must not get complacent.

Talking of complacency, the committee felt that the recent rally in equity markets might be done, and in fact many equity markets had completed the V shape recovery that had been predicted by some commentators. The committee feels we may see a correction, but the worst is yet to come once the Quarter ends. The recent rally could have, in our view been driven by FOMO, where some investment houses were bearish initially but then realised they best get involved. We have also seen and heard that retail investors has been buying stocks, and a record number of new trading accounts have been opened in the UK. Our conclusion is that Equities are too high considering the level of uncertainty that still remains.

Although we still believe that stock picking and Fund choice is key. As we touched on in our previous report there are going to be big winners and large losers in this new world as companies streamline and move forward. Many M&A opportunities have arisen for companies that have cash in the bank (from not paying dividends/performing share buybacks or simply running a good business).

**Fixed Income**

Not much has changed in the Fixed Income asset class since our last report. Some members of the King & Shaxson bond team report that clients are selling into the rally, much like equities. This asset class remains highly valued and hard to buy at current levels. Although Central Bank activity swamps the market and will continue to support it moving forward, whilst negative rates in the UK is not off the cards just yet.

**Currencies**

Sterling has rallied slightly since our last report, but again nothing major and no real catalyst behind this except some dollar weakness. The $ will be in focus as we get closer to the US election, so it's an asset class we will be watching closely over the coming months. We are exploring opportunities in some of the safe haven currencies whilst we have no change of view on the Euro.

**Inflation**

There still remains a lack of inflation, albeit the slight bounce in the oil price will feed in later in the year, whilst we note that the price of Iron Ore has made headlines for reaching $100 as mines in Brazil come to a halt, but we think in the grand scheme of things it will be immaterial.

The committee noted that there is not enough cash being spent in the current climate to create inflation (we have the supply but not the velocity). Once lockdown ends, depending on how long the "release spending" lasts will lead us on this. If retail therapy and visits to restaurants/bars does not return to previous levels then inflation will remain elusive. The committee agreed that the UK Government would ideally like some inflation at some point given the amount of debt they have issued. One idea mooted amongst the Committee would be a rise in VAT to cover some of the UKs relief package. Something we have seen previously (although since our meeting it has been announced that the Chancellor s looking for a drop in VAT to boost the economy, but most likely a short term change).

**Cash**

The committee felt that taking risk off the table after the recent rally would be wise, and placing in to Cash. The biggest threat to this would be if we get Negative Interest Rates in the UK. We do not think this will happen but the BOE have stated that all options are on the table and this has not been ruled out. We will continue to monitor our options in this space but we have access to other cash like instruments in the Ethical space should we need a short term solution.

**Conclusion**

As with the previous meeting, we look to remain below our neutral level for bonds, and we favour reducing equities in the short term, infrastructure and cash being the beneficiaries. To repeat our recent mantra, stock picking is again key, and so is remaining nimble.

## Changes: Funds MPS

### Cautious portfolio

Fixed income asset allocation was unchanged, but with one change in funds held. We removed the Sarasin Responsible Bond fund and replaced this with the Kames Ethical Corporate Bond fund that we have held previously. The move was conducted due to reduced confidence in the Sarasin fund continuing to pass our Ethical screen. As with our process, we engaged with the team surrounding a few of the bonds held in the fund, but on completion of our interaction we felt it was prudent to remove the fund due to some of the holdings likely falling short of clients expectations.

Equity allocation was reduced from 42% to 38%. We added 2% to the Pictet Water fund as it offers good defensive holdings, given what we have mentioned above, this could benefit portfolios in the short to medium term. As with Fixed Income, we removed one fund, the Janus Henderson UK Responsible Income Fund, performance has been a drag on portfolios, and again some holdings were testing our ethical screen so we took the decision to disinvest. The monies raised were added to Cash,

which now stands at 14pc for the time being. Infrastructure and Clean Energy exposure was left unchanged.

## Income portfolio

Fixed income asset allocation was unchanged at 40pc, but with one change in assets. We removed the Sarasin Responsible Bond fund, and replaced this with the Kames Ethical Corporate Bond fund that we have held previously. The move was conducted due to reduced confidence in the Sarasin fund continuing to pass our Ethical screen. As with our process, we engaged with the team surrounding a few of the bonds held in the fund, but on completion of our interaction we felt it was prudent to remove the fund due to some of the holdings likely falling short of many clients expectations.

Equity allocation was reduced from 38pc to 30pc. As with Fixed Income, we removed one fund, the Janus Henderson UK Responsible Income Fund, performance has been a drag on portfolios, and some holdings were testing our Ethical screen, so we took the decision to disinvest. The vast majority of the proceeds were added to Infrastructure and Clean Energy, taking allocation in those sectors to 24pc. There was also a slight increase in Cash.

## Balanced portfolio

Fixed income asset allocation was unchanged at 30pc, but with one change in the fund makeup. We removed the Sarasin Responsible Bond fund, and replaced this with the Kames Ethical Corporate Bond fund that we have held previously. The move was conducted due to reduced confidence in the Sarasin fund continuing to pass our Ethical screen. As with our process, we engaged with the team surrounding a few of the bonds held in the fund, but on completion of our interaction we felt it was prudent to remove the fund due to some of the holdings likely falling short of many clients expectations.

Equity allocation was reduced from 48pc to 43pc. As with Fixed Income, we removed one fund, the Janus Henderson UK Responsible Income Fund, performance has been a drag on portfolios, and some holdings were testing our Ethical screen, so we took the decision to disinvest. We also slightly reduced exposure to the Stewart Asia Sustainability fund, increasing the Pictet Water Fund for defensive purposes. Infrastructure and Clean Energy increased by 1pc, taking allocation in them sectors to 15pc. There was also an increase in Cash to 12pc for the time being.

## Growth portfolio

Fixed income asset and fund allocation was unchanged at 10pc.

Equity allocation was reduced from 73pc to 66pc. As with our other portfolios we removed the Janus Henderson UK Responsible Income Fund, performance has been a drag on portfolios, and some holdings were testing our Ethical screen, so we took the decision to disinvest. We also slightly reduced exposure to the Stewart Asia Sustainability fund, but added 1pc to the Pictet Water Fund, which suits our preference for defensive purposes. Infrastructure and Clean Energy funds increased by 1pc each, taking allocation in them sectors to 15pc. Cash increased to 9pc for the current period.

## Adventurous portfolio

Fixed income asset and fund allocation was unchanged at 3pc.

Equity allocation was reduced from 79pc to 72pc. As with our other portfolios we removed the Janus Henderson UK Responsible Income Fund, performance has been a drag on portfolios, and some holdings were testing our Ethical screen, so we took the decision to disinvest. We also slightly reduced

exposure to the Stewart Asia Sustainability fund, and added some extra exposure to the Pictet Water Fund, which suits our preference for defensive purposes. Infrastructure and Clean Energy funds increased by 4pc taking allocation to 18pc. Cash allocation increased to 7pc.

## Changes: Direct Equity MPS

### Cautious Green portfolio

Fixed income asset allocation was unchanged, but with one substitution in assets. We removed the Sarasin Responsible Bond fund, and replaced this with the Kames Ethical Corporate Bond fund that we have held previously. The move was conducted due to reduced confidence in the Sarasin fund continuing to pass our Ethical screen. As with our process, we engaged with the team surrounding a few of the bonds held in the fund, but on completion of our interaction we felt it was prudent to remove the fund due to some of the holdings likely falling short of clients expectations.

REITs and Infrastructure allocation was left unchanged at 12pc. Equity allocation was reduced from 42% to 38%, we did this by removing our investment in Aviva as we feel risks to financial and insurance companies will remain elevated. We also reduced exposure to Asia by reducing our investment in Pacific Assets trust to 3pc from 5pc. Cash was increased to 14pc for the current period.

### Light Green portfolio

Fixed income asset allocation was unchanged at 30pc, but with one change in the fund makeup. We removed the Sarasin Responsible Bond fund, and replaced this with the Kames Ethical Corporate Bond fund that we have held previously. The move was conducted due to reduced confidence in the Sarasin fund continuing to pass our Ethical screen. As with our process, we engaged with the team surrounding a few of the bonds held in the fund, but on completion of our interaction we felt it was prudent to remove the fund due to some of the holdings likely falling short of clients expectations.

REITs and Infrastructure allocation was left unchanged at 11pc. Equity allocation was reduced from 51% to 47%, we did this by removing our investment in Aviva as we feel risks to financial and insurance companies will remain elevated. We also reduced exposure to Asia by reducing our investment in Pacific Assets trust to 3pc from 5pc. Cash was increased to 12pc.

### Mid Green portfolio

Fixed income asset and fund allocation was unchanged at 20pc.

REITs and Infrastructure allocation was left unchanged at 12pc. Equity allocation was reduced from 62.5pc to 57.5pc, the changes being - removing our investment in Aviva as we feel risks to financial and insurance companies will remain elevated. We also exited our long standing investment in Asos where we feel its heyday may be over, which also allowed us to reduce risk as per our want. As with other portfolios we reduced exposure to Asia by cutting our investment in Pacific Assets trust to 4pc from 6pc. Some of these proceeds were reallocated to the Pictet Water Fund, but Cash was the main beneficiary, increasing to 10.5pc.

### Dark Green portfolio

Fixed income allocation was unchanged at 3pc.

REITs and Infrastructure allocation was upped slightly to stand at 13.5pc. Equity allocation was reduced from 80pc to 75.5pc. We achieved this by removing our investment in Aviva as we feel risks

to financial and insurance companies will remain elevated. We also exited our long standing investment in Asos where we feel its heyday may be over, which also allowed us to reduce risk as per our want. As with other portfolios we reduced exposure to Asia by cutting our investment in Pacific Assets trust to 5pc from 7.5pc. Some of these proceeds were reallocated to the Montanaro and Pictet funds to increase exposure to impact assets, but Cash was the main beneficiary, increasing to 8pc.


## Disclaimer

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## Company Information

King & Shaxson Asset Management Limited (Reg. No. 3870667) has its registered office at 1st floor, Cutlers Court, 115 Houndsditch, London, EC3A 7BR. The Company is registered in England and Wales and is part of the PhillipCapital Group. King & Shaxson Asset Management Limited (FCA Reg. No. 823315) is authorised and regulated by the Financial Conduct Authority, 12 Endeavour Square, London, E20 1JN.