NDL momentum

Weekly Digest

4 November 2019

Stick or Twist?

– *Michael Clough*

31st October was meant to be the day the UK finally parted ways with the European Union. It came as little surprise that the deadline was extended, again. As our first Weekly Digest following this date, I had been lining up a thrilling article on Brexit, or rather pondering how to actually make it thrilling. In the end, I felt I could no longer do this, which I'm sure will dishearten readers.

Fortunately something else happened over the weekend. Unfortunately though, after a phenomenal victory against New Zealand the weekend before, South Africa proved too much for England and manager Eddie Jones in the Rugby World Cup final. Although it wasn't the result England wanted, players and fans will surely look back positively in the weeks and months to come on getting to the final. Let's not forget just over one year ago there were calls for Mr Jones to face the sack after a poor run of form including England's worst ever performance at the 2018 Six Nations Championship. In the face of adversity, Jones remained focused. He knew England had the squad to succeed. It just needed patience, faith in the philosophy and commitment to the process. Had England sacked Jones last year, who knows what would have happened this year. My guess is we wouldn't have done nearly as well as we did.

As investors in third party funds, at any time there are always, and will always be, managers that are underperforming. No fund manager outperforms all the time. However, having the discipline to stick with underperforming managers can be hugely rewarding over the long term. Of course, blindly backing underperformers in a portfolio in the hope they will turn around is not the approach we'd advocate. One must do thorough due diligence, analyse the data and ask the difficult questions. But if you remain confident in that manager's ability going forwards to do what they were introduced to do, then backing them might just be the best thing you could do. Two of our deep value equity managers (which we blend alongside quality and growth managers) have endured a torrid time of late, Schroders in the UK and Contrarius on a global scale. Over the past year, they have fallen meaningfully behind their respective benchmarks. Both have suffered sustained periods of underperformance before, both have recovered, and both have delivered strong long term returns for our clients. Back in 2011, Schroders underperformed by 11%. Over the next two calendar years their strategy outperformed by 23% and 25%. Of course, as readers will know, investing in 'value' stocks has not been kind to investors since the 2008 financial crisis, but do we take these episodes of severe underperformance and just assume they'll bounce back? Of course not. We have met with Schroders three times so far in 2019 and Contrarius twice. We continue to believe these are two of the strongest deep value managers in their respective markets.

Of course, sometimes it is not prudent to keep the faith. We sold one of our alternatives managers during the summer of this year following a period of underperformance. We ultimately concluded we had reduced conviction in the manager going forward and favoured other incumbent strategies. Since we made this decision, it has proceeded to fall a further 9%, thus validating our decision (so far).

Sticking with managers can be difficult and leave you red-faced at times during periods of underperformance. We don't mind this. Ultimately if we believe they have the appropriate team and process to recover, we are happy to be patient. After these past few weeks, I think the country is probably happy we stuck with Eddie Jones last year, despite the disappointment on Saturday. Perhaps it is now time to stick with him again.

The **Marketplace**

- The Federal Reserve cut rates for a third time in four months
- Flows into European stocks outpaced those of US equities over the week
- Brent crude fell 0.5% to $61.7 a barrel as inventories rose by 1.22m at the US's largest storage hub
- Gold rose 0.4% to $1509.2 an ounce

Market **Focus**

US

- The October jobs report exceeded forecasts, adding 128,000 jobs, with unemployment hovering around its 50-year historic low.
- President Donald Trump stated that the US was "ahead of schedule" when referring to the US-China trade deal talks.
- The US Federal Reserve cut the base rate by 25 basis points as expected, although forward guidance led economists to reduce their expectations for future rate cuts.
- A strong monthly jobs report on Friday, helped equities move higher for the fourth consecutive week. The S&P 500 and Nasdaq Composite Index both reached new highs over the week. Meanwhile, volatility reached a four-month low.

Europe

- The European Central Bank held rates at their historic low, with outgoing President Mario Draghi stating that Eurozone governments now need to place more emphasis on fiscal policy for economic growth.
- Confidence indicators in the Eurozone were broadly weaker than expected.
- Nonetheless, stocks rose to a 22-month high as the EU granted a further extension to the UK's Brexit leave date, along with positive asset inflows into the region.

UK

- The UK's request for a three-month extension to Brexit was granted.
- MP's have now agreed to a general election on the 12th December.
- UK equities fell by 0.4% over the week, underperforming global equities.
- UK gilts delivered negative returns over the week at -0.2%, with their investment grade counterparts flat.

Asia/Rest of The World

- The Bank of Japan kept its policy rate the same but strengthened its forward guidance, stating that it expects short and long-term rates to remain at their current levels or lower.
- The Bank of Canada also held rates steady at 1.75%, interpreted by economists as dovish.
- China's October PMI's for manufacturing printed 49.3 (vs an expected 49.8), the lowest reading since February and the non-manufacturing PMI came in below expected at 52.8 (vs 53.6).

Past performance is not indicative of future returns.

Source: Bloomberg. Returns in local currency unless otherwise stated.

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Asset Class/Region	Currency	Currency returns			
		Week ending 1 Nov. 2019	Month to date	YTD 2019	12 months
Developed Market Equities					
United States	USD	1.5%	1.0%	23.8%	13.5%
United Kingdom	GBP	-0.4%	0.7%	12.2%	6.6%
Continental Europe	EUR	0.5%	0.7%	22.7%	14.6%
Japan	JPY	1.1%	0.0%	14.2%	4.7%
Asia Pacific (ex Japan)	USD	1.5%	0.5%	12.8%	12.8%
Australia	AUD	-1.0%	0.1%	22.2%	19.2%
Global	USD	1.3%	0.8%	21.6%	12.6%
Emerging markets equities					
Emerging Europe	USD	2.1%	1.6%	26.9%	25.4%
Emerging Asia	USD	1.7%	0.5%	11.3%	11.8%
Emerging Latin America	USD	1.1%	1.6%	12.9%	7.3%
BRICs	USD	1.9%	0.9%	14.8%	13.7%
MENA countries	USD	-1.6%	0.0%	1.3%	0.3%
South Africa	USD	-1.9%	0.3%	0.7%	3.4%
India	USD	3.1%	0.8%	9.5%	20.4%
Global emerging markets	USD	1.3%	0.7%	11.1%	10.8%
Bonds					
US Treasuries	USD	0.5%	-0.2%	7.9%	11.2%
US Treasuries (inflation protected)	USD	0.2%	0.1%	8.3%	9.6%
US Corporate (investment grade)	USD	0.6%	-0.2%	13.7%	15.1%
US High Yield	USD	-0.1%	0.1%	11.8%	8.4%
UK Gilts	GBP	-0.2%	-0.5%	9.3%	10.6%
UK Corporate (investment grade)	GBP	0.0%	-0.3%	10.7%	10.2%
Euro Government Bonds	EUR	-0.1%	-0.3%	8.4%	10.1%
Euro Corporate (investment grade)	EUR	0.1%	0.0%	6.5%	6.1%
Euro High Yield	EUR	0.0%	0.0%	9.1%	6.4%
Japanese Government	JPY	0.5%	0.4%	3.3%	4.8%
Australian Government	AUD	-0.3%	-0.1%	9.7%	12.5%
Global Government Bonds	USD	0.7%	-0.1%	7.0%	9.8%
Global Bonds	USD	0.6%	-0.1%	7.2%	9.4%
Global Convertible Bonds	USD	0.7%	0.3%	8.2%	5.8%
Emerging Market Bonds	USD	-0.1%	0.1%	9.5%	10.8%

Source: Bloomberg. Past performance is not indicative of future returns

Asset Class/Region	Currency	Currency returns			
		Week ending 1 Nov. 2019	Month to date	YTD 2019	12 months
Property					
US Property Securities	USD	0.3%	0.0%	27.4%	21.6%
Australian Property Securities	AUD	-0.5%	0.5%	19.1%	20.4%
Asia Property Securities	USD	2.0%	0.7%	13.0%	19.3%
Global Property Securities	USD	0.8%	0.3%	22.5%	20.3%
Currencies					
Euro	USD	0.8%	0.1%	-2.5%	-2.2%
UK Pound Sterling	USD	0.9%	0.0%	1.5%	-0.5%
Japanese Yen	USD	0.5%	-0.2%	1.3%	4.1%
Australian Dollar	USD	1.3%	0.3%	-1.9%	-4.0%
South African Rand	USD	-2.8%	0.3%	-4.3%	-3.8%
Swiss Franc	USD	1.0%	0.1%	-0.3%	1.6%
Chinese Yuan	USD	0.4%	0.0%	-2.3%	-1.6%
Commodities & Alternatives					
Commodities	USD	0.8%	1.7%	8.7%	-1.9%
Agricultural Commodities	USD	0.6%	0.5%	-3.6%	-6.5%
Oil	USD	-0.5%	2.4%	14.7%	-15.4%
Gold	USD	0.4%	-0.2%	17.8%	22.3%
Hedge funds	USD	0.1%	0.0%	6.2%	3.2%

Source: Bloomberg. Past performance is not indicative of future returns

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