

– James Klempster, CFA

I received an email last month from Apple trying to sell me the new iPad. Tech sales are interesting; in essence the purveyor of the object you bought from them all too recently is informing you that it is now a little bit obsolete. Sure, it still works reasonably well but the newer version is incrementally better in every way.

As the consumer, all you have to do to access this new functionality is to ditch your existing kit and fork out for the new stuff. Imagine if fund management worked the same way. Inboxes would constantly be bombarded with messages along the lines of: “the fund we sold you a year ago is still pretty good but we haven’t updated the holdings since you bought it and while it will probably do an OK job, it’s no longer our best ideas. We will continue to let you know what’s going on in the portfolio (for a time at least) but it will drift further and further from optimal as time passes and at some point in the not too distant future, we will cease to support it entirely.”

So when we buy tech, we do so knowing that from the moment of purchase it is slowly sliding into obsolescence. It gets worse, though. The other interesting side to tech is that it is rarely supplied as a complete experience. Imagine if a fund were sold: “Out of the box, the fund only really performs a couple of pretty basic functions and so if you would like to take advantage of the really exciting features you will need to acquire more kit from other providers in our store. Some of these might be free and others you will have to pay for. Also, to have a full experience you may need to buy additional hardware...”

Fund managers are continually refining their asset class or company research models, for example. A manager may well test and re test their inputs and reach a conclusion that their process can be improved by tweaking it. Maybe the manager has started researching a new asset class that hasn’t featured in their portfolios before. The sunk cost required to do a decent job of this is significant, but it is borne by the manager.

Furthermore, when the manager decides that a holding should be sold or replaced with a better one, they make the change; rather than hold onto the good ideas to sell you via a ‘new release’ of their fund. As a result, actively managed portfolios are constantly evolving; processes are continually honed. As markets move and company prospects change, their relative attractiveness to different active managers changes and so their position may swell or contract in a manager’s portfolio. Investment managers charge regular ongoing fees rather than a large upfront cost. It is understood that the effect of the ongoing fee is that the manager is incentivised to continue to service a longstanding customer as if they were a fresh one.

Fund management companies should incentivise their fund management staff to make good long-term decisions in their clients’ best interest. There is no ‘designed obsolescence’ or product cycles; with a well-constructed fund, it is set up and run for the foreseeable future – for the benefit of investors. Clearly there have been examples in the past where this has not occurred, but in the vast majority of instances the intent of the manager is earnest even if the results don’t compete with the best out there.

The beauty of a well-run fund is that they should be forever young. Fund managers should assess their portfolios constantly to see if they believe them to be well positioned to weather the challenges they expect tomorrow. Such regular regeneration should mean that the portfolio continues to reflect cutting edge thinking, meaning that investors do not have to experience the cost, inconvenience and out of the market risk by selling a ‘stale’ holding and moving to something fresh.

The Marketplace

- Germany managed to avoid a technical recession in Q3 with a GDP growth reading of 0.1%
- The large-cap Dow Jones Industrial Average and S&P 500 reached record highs over the past week
- Brent crude rose 1.3% to \$63.3 a barrel
- Gold rose 0.4% to \$1467.7 an ounce

Market Focus

US

- Initial jobless claims printed above expected (215k) at 225k, their highest level since June of this year.
- The US producer price index (PPI) rose by 0.4% (vs an expected 0.3%) in October and the core measure rose by 0.3% (vs 0.2% expected).
- The chairman of the Federal Reserve (Jerome Powell) gave indications that the Fed was on pause with regards to cutting rates, also mentioning that the manufacturing downturn wasn't seen to spill over into the wider US economy.
- The main US equities index returned 0.9% over the past week, placing its year to date performance at 26.0%.

Europe

- Germany's final consumer price index (CPI) measure remained at 0.1% month on month, with the year on year figure at 0.9%.

- European equities gained along with the US equities rally over the past week as the possibility of a US-China trade deal increased.
- Euro government bonds returned 0.2% over the past week, whilst their investment grade counterparts lagged behind at 0.1%.

UK

- The Q3 GDP of the UK was disappointing in comparison to expectations, printing 0.3% vs an expected 0.4%, resulting in its slowest annual rate in a decade.
- Inflation data in the UK was weaker than expected, falling 0.2% month on month. Retail sales also fell by 0.1% in the month of October.
- UK earnings data was softer than expected with basic wage growth 20 basis points below estimates at 3.6%, however, unemployment did fall back down to 3.8%.
- Moody's lowered the UK economic outlook from stable to negative due to the political and social divisions that have caused the UK's inability to make policy decisions.

Asia/Rest of The World

- China's October economic data release indicated weakness across the board, with a number of data points below expectations, such as industrial production which was 70 basis points below expected at 4.7% year on year.
- Japan's GDP for Q3 was 70 basis points lower than expected at 0.2% quarter-on-quarter.
- Private consumption in Japan was printed at 0.4% (vs 0.6% expected) quarter-on-quarter, with the new sales tax increase likely influencing this data, while business spending was in line with expectations at 0.9%.

Asset Class/Region	Currency	Currency returns			
		Week ending 15 Nov. 2019	Month to date	YTD 2019	12 months
Developed Market Equities					
United States	USD	0.9%	2.8%	26.0%	15.9%
United Kingdom	GBP	-0.6%	1.0%	12.5%	7.7%
Continental Europe	EUR	0.2%	2.6%	25.0%	17.8%
Japan	JPY	-0.4%	1.8%	16.2%	6.2%
Asia Pacific (ex Japan)	USD	-1.6%	0.7%	13.0%	11.2%
Australia	AUD	1.5%	2.5%	25.1%	23.5%
Global	USD	0.7%	2.3%	23.4%	14.9%
Emerging markets equities					
Emerging Europe	USD	-1.1%	1.2%	26.5%	23.6%
Emerging Asia	USD	-1.7%	1.0%	11.8%	10.1%
Emerging Latin America	USD	-1.8%	-3.0%	7.7%	7.6%
BRICs	USD	-2.7%	-0.6%	13.1%	10.8%
MENA countries	USD	1.1%	1.7%	3.0%	3.3%
South Africa	USD	0.0%	3.1%	3.5%	4.8%
India	USD	-0.6%	-0.6%	7.9%	13.9%
Global emerging markets	USD	-1.5%	0.7%	11.1%	9.7%
Bonds					
US Treasuries	USD	0.7%	-0.8%	7.3%	10.3%
US Treasuries (inflation protected)	USD	0.2%	-0.3%	7.9%	9.0%
US Corporate (investment grade)	USD	0.7%	-0.5%	13.3%	15.0%
US High Yield	USD	-0.1%	0.1%	11.9%	9.4%
UK Gilts	GBP	0.7%	-1.5%	8.2%	9.8%
UK Corporate (investment grade)	GBP	0.5%	-0.5%	10.4%	10.5%
Euro Government Bonds	EUR	0.2%	-1.0%	7.7%	9.5%
Euro Corporate (investment grade)	EUR	0.1%	-0.2%	6.3%	6.1%
Euro High Yield	EUR	-0.2%	0.2%	9.3%	7.5%
Japanese Government	JPY	0.1%	-0.7%	2.1%	3.4%
Australian Government	AUD	1.0%	-0.3%	9.5%	12.7%
Global Government Bonds	USD	0.6%	-1.3%	5.6%	8.8%
Global Bonds	USD	0.5%	-1.0%	6.2%	8.7%
Global Convertible Bonds	USD	0.2%	0.9%	8.8%	7.1%
Emerging Market Bonds	USD	0.4%	-0.4%	9.0%	10.6%

Asset Class/Region	Currency	Currency returns			
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Property					
US Property Securities	USD	1.4%	-2.1%	24.8%	17.5%
Australian Property Securities	AUD	2.6%	1.3%	20.0%	19.2%
Asia Property Securities	USD	-4.5%	-4.0%	7.8%	11.2%
Global Property Securities	USD	0.1%	-1.9%	19.8%	16.3%
Currencies					
Euro	USD	0.3%	-0.8%	-3.5%	-2.3%
UK Pound Sterling	USD	1.1%	-0.2%	1.3%	1.3%
Japanese Yen	USD	0.4%	-0.7%	0.8%	4.2%
Australian Dollar	USD	-0.6%	-1.1%	-3.3%	-6.2%
South African Rand	USD	0.8%	2.5%	-2.3%	-3.2%
Swiss Franc	USD	0.8%	-0.3%	-0.7%	1.7%
Chinese Yuan	USD	-0.2%	0.4%	-1.9%	-1.0%
Commodities & Alternatives					
Commodities	USD	-0.4%	1.1%	8.1%	-0.1%
Agricultural Commodities	USD	-0.5%	-0.2%	-4.3%	-6.1%
Oil	USD	1.3%	5.1%	17.7%	-5.0%
Gold	USD	0.4%	-3.0%	14.5%	21.0%
Hedge funds	USD	0.0%	0.3%	6.5%	4.6%

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