Homecroft Weatlh Portfolio Service

Portfolios Cautious-Adventurous

Quarterly Update - Q1 2020

In brief

- We first became aware of the novel coronavirus spreading quickly in China's Hubei province in mid-to-late January. By the end of the quarter, it had developed into a full-blown global pandemic. Many countries shut down huge swathes of their economies in an attempt to suppress the contagion.
- A recession now seems unavoidable. However, authorities have gone to great lengths to try to cushion the economic slowdown by rolling out comprehensive monetary and fiscal stimulus measures.
- It was a turbulent quarter for financial assets. Many fell sharply from record highs into bear-market territory before staging a partial recovery towards the end of the quarter.
- Portfolios were not immune to this volatility, posting negative returns over the quarter with higher-risk mandates recording larger losses than their lower-risk peers.
- High levels of market volatility and a rapidly evolving landscape led to increased activity within the portfolios, to take advantage of mispriced opportunities.

Global overview

There really is only one place to start our quarterly review; the Covid-19 pandemic that has spread throughout the world. From its origins in a Wuhan wet market in December, the Chinese state was slow to grasp just how quickly the virus would spread. It only ordered the first city-wide shutdowns in late January. Even then, other countries clung to the belief that China would contain it, hoping for a short, sharp supply-side shock to the global economy. However, one by one, new cases were reported across the world. Such phrases as 'self-isolation', 'social distancing' and lockdowns are now not only commonplace, but accepted by the vast majority as we trade basic freedoms for containing the virus. The virus is stretching the world's health services to breaking point and has brought the global economy to its knees, with the US now at the outbreak's epicentre.

It is now widely accepted that a global recession is upon us (defined as two successive quarters of negative economic growth). In response, central banks and governments have acted quickly to avert a global depression. Most have taken a wartime approach to measures; throw the kitchen sink at things now, and worry about the cost later. These rescue packages will dwarf those from the great financial crisis and will likely affect our lives for the coming decade(s).

Global economic data is beginning to catch up with current events, and the numbers reported are truly extraordinary. Over 10 million US workers have filed unemployment claims in the last two weeks (700,000 claims in one week was the previous high). In France, four million workers in the private sector have filed for benefits – this represents almost 20% of the private sector workforce. In the UK, over one million people have registered for working credits; many more will follow.

The US government signed off on a colossal $2 trillion rescue package. It includes loans for businesses, cities and states, as well as direct payments of $1,200 for most US adults. The aftermath of this response gave the Dow Jones its biggest one-day rise since 1933, when the Great Depression drew to an end. In the UK, the new Chancellor, Rishi Sunak, announced a £350 billion rescue package and promised to do 'whatever it takes' to cushion the inevitable fallout from the pandemic. It included a fiscal cocktail of help for businesses and the remarkable pledge to pay UK workers' wages for the first time ever. In Japan, both the central bank and government have long been big players in domestic financial markets, as they have tried to kick start a moribund economy. In response to the pandemic, the Bank of Japan has doubled its own equity-buying programme to an astonishing $112 billion for 2020.

Global companies now face huge cuts in their 2020 earnings, and governments and regulators are pressuring some sectors (banks specifically) to suspend their dividends. Other areas of the market are sure to see dividend cuts. Furthermore, with no clear end to the pandemic, companies cannot issue any guidance to investors as to future numbers. As a result, investors are trying to value companies without visibility on earnings or dividend policy. In some cases, they may not even know whether some companies have enough cash to survive a global lockdown of indeterminate length. However, financial markets have arguably priced in much of the 'here and now' uncertainty. Indeed, towards the end of March, investors had started looking at the aftermath, and what the world will look like in 6-12 months' time.

Investment performance

The Homecroft Portfolio Service faced an incredibly challenging environment over the first quarter of 2020. All mandates delivered negative returns on an absolute basis, and higher-risk portfolios recorded larger losses than their lower-risk peers. The escalation of the coronavirus pandemic has caused unprecedented disruption to the real economy and the consequences have been felt across capital markets. Central banks and governments have launched large stimulus policies in an attempt to avert the now unavoidable global recession from turning into an outright global depression. There is conjecture within the investment community over whether economic activity will follow a 'U-shape' recovery or whether we face a more prolonged period of economic malaise. The latter would, in all likelihood, generate second-round consequences. These could include increased business failures, less temporary and higher unemployment, and a lower level of trend growth than the market is pricing in. Much rests on the efficacy of the measures that governments have implemented to prevent the further spread of the COVID-19 strain of the coronavirus. This will ultimately influence how quickly the policies that are curtailing economic and social activity can be lifted.

Homecroft Wealth Portfolio Service Cautious

Tactical asset allocation was a negative contributor to performance during the first quarter. Coming into the quarter, the portfolios were positioned to be marginally risk-on. Through 2019, we enjoyed reasonably solid growth, with both low-risk and high-risk assets performing well. We expected this pattern of performance to continue through 2020, but at a more moderate pace. We, therefore, held underweight positions in cash and high-quality government bonds, preferring instead moderate overweight exposure to emerging-market debt, global high-yield bonds and equities.

This approach continued to serve us well through to 21 February, with all mandates in line or ahead of their benchmarks. However, the ferocity of the subsequent selloff was unprecedented. Equity markets moved from all-time highs to bear-market territory in the shortest period in history. In this environment, even a slight overweight in risk assets proved painful. The fact that we funded these overweight positions from lower-risk assets compounded matters.

So where does that leave us? The value of risk assets has fallen significantly as a consequence of the government engineered shutdown. However, the policies put in place by those same governments and central banks could give global economies enough fuel to bounce back when the lockdowns end. This being the case, we added marginally to equity positions in the middle of March, funded from emerging-market debt, which had held-up relatively well. As a result of this, we benefited from the market rebound during the last week of the quarter. We will continue to take opportunities as they arise to generate strong risk-adjusted returns for our clients over the medium to long term.

In terms of fund selection, the Vanguard UK Government Bond Fund was the strongest performer. It outperformed its index, vindicating the large weighting in the portfolio as a defensive asset. Positive returns were also driven by the Vanguard Global Bond Index Fund, as well as the Aberdeen Standard Investments (ASI) Global Inflation Linked Bond Tracker Fund, which outperformed its index. A reasonable weighting in cash via the ASI Liquidity Fund was positive, as the Fund was ahead of its index. The quality bias of the PIMCO GIS Global High Yield Bond Fund provided some ballast in our basket of high-yield bond funds. The L&G Emerging Market Government Bond Index Fund also outperformed.

Although equities were in negative territory, there were pockets of relative strength over the quarter. The Fidelity Asia Fund beat our reference benchmark. Within our basket of European funds, the quality bias of the Barings Europe Select Fund provided relative protection against its small-cap index. The T Rowe Price Continental European Equity Fund outperformed the broader European index. Pleasingly, the Fulcrum Diversified Core Absolute Return (DCAR) Fund, part of our basket of absolute return funds, was firmly in positive territory over an exceptionally difficult period for risk assets.

Homecroft Wealth Portfolio Service Moderately Cautious

Tactical asset allocation was a negative contributor to performance during the first quarter. Coming into the quarter, the portfolios were positioned to be marginally risk-on. Through 2019, we enjoyed reasonably solid growth, with both low-risk and high-risk assets performing well. We expected this pattern of performance to continue through 2020, but at a more moderate pace. We, therefore, held underweight positions in cash and high-quality government bonds, preferring instead moderate overweight exposure to emerging-market debt, global high-yield bonds and equities.

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Homecroft Wealth Portfolio Service Balanced

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In terms of fund selection, government bonds were positive, with the Aberdeen Standard Investments Global Inflation Linked Bond Tracker Fund outperforming its index. The quality bias of the PIMCO GIS Global High Yield Bond Fund provided some ballast in our basket of high-yield bond funds. The L&G Emerging Market Government Bond Index Fund also outperformed.

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Within alternative investments, the First State Global Listed Infrastructure Fund performed well, while the iShares Global Property Securities Fund performed in line with the global real estate investment trust index. Pleasingly, the Fulcrum Diversified Core Absolute Return (DCAR) Fund, part of our basket of absolute return funds, was firmly in positive territory over an exceptionally difficult period for risk assets.

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Portfolio activity

Over the quarter, we initiated changes in two phases at a tactical (short-term) level.

The first phase was in early February. We acknowledged that equities had performed strongly over 2019. We locked in some of those gains by trimming equities to reinforce our bond exposure in emerging-market fixed income. We reduced equities across Europe, Japan, Asia and emerging markets. Having had a neutral weighting in the UK, we added to UK equites and remained overweight in US equities. We increased emerging-market debt in local currency, bringing it up to the same weighting as the emerging-market debt hard currency position (denominated in US dollars). We reduced our basket of global high-yield bond funds. European high-yield bonds had performed particularly well and valuations were less compelling. We increased our exposure to alternative investments via global real estate investment trusts (REITs). Although the portfolio was risk-facing, with a preference for equities and bonds over cash, it was more defensive than at the end of 2019.

As the coronavirus crisis unfolded, equities moved rapidly into bear-market territory. We witnessed one-day moves the likes of which we had not seen since the 'Flash Crash' of 1987. The portfolio held up well with ballast in UK and global government bonds, and UK and European corporate bonds at the lower-risk end. Our alternative investments in global listed infrastructure and global REITs also afforded the portfolio relative protection. In addition, our basket of absolute return funds provided some downside protection.

Our second tactical re-orientation took place in mid-March. We added incrementally to US and UK equities. This meant we captured much of the subsequent rebound when the US rallied over a week on a scale last witnessed in the 1930s. We funded this re-positioning by scaling back our overweight position in local currency emerging-market debt, which held up well over the period. Although we made changes at the asset class level, there were no changes to underlying fund selection over the quarter.

Market outlook

To say that our economic and market outlook changed significantly over the course of the past quarter would be a significant understatement. In the course of a few weeks, the global economy has essentially shut down and economic growth estimates have cratered to levels below the 2008 financial crisis. Furthermore, we have seen daily gyrations in stock markets not witnessed in decades.

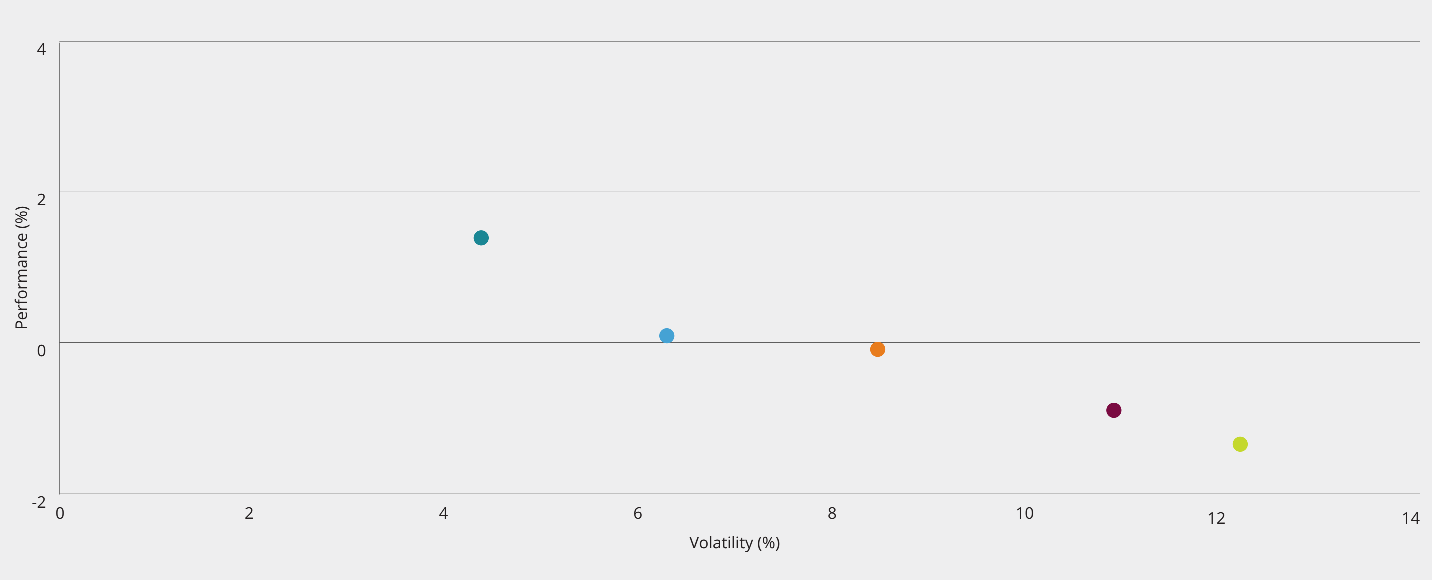
Understandably, this has prompted outright panic in markets. Consider the US equity market. During the quarter, it experienced three successive days of moves greater than 9% (twice down, once up) in March. Are we to believe that some of the world's largest companies were worth almost 10% less today than yesterday? And worth 10% more tomorrow? While we believe we have passed the point of 'peak panic', we do not believe we have reached the stage of 'peak pessimism' yet. Perhaps that will come when the immediate health crisis has abated, the dust has settled and the aftermath comes into focus. In the short term, unemployment claims have skyrocketed and we suspect corporate bankruptcies are likely to increase.

There has been much talk on the economic recovery. You may have read about a V-shaped recovery, a U-shaped recovery or a reverse J-shaped recovery. Clearly, much will depend on how effectively the coronavirus is contained, and thus how quickly society can get back to normality. This is a key reason why the broader Aberdeen Standard Investments economics team forecasts a (partial) recovery by the end of this year, but stops short of assuming a full recovery, even by 2021. We do not assume we will recoup all the lost output and, additionally, our assumptions are predicated on the virus being contained by the end of the summer.

Having been through many crises, it is important to remember that this one, like the others before, will pass. Decisions made in panic are seldom profitable. We would argue all our clients make an investment plan and stick to it; remember what your goals are and the timeframe you have. Almost all of us will remember the pain of the financial crash in late 2008, which bottomed out in early 2009. And all will know of the remarkable market recovery since then. We can look further back to the TMT (technology, media and telecoms) crash in the early 2000s, and to 1987 when markets fell circa 20% in one day. And we can all look at the subsequent recoveries in markets.

A diversified portfolio across geographies and asset-classes is often referred to as the one 'free lunch' in investment. We would also subscribe to 'time in the market' not timing the market. It's helpful to remember that there is only one person who will buy at the bottom, and only one who will sell at the top. Missing just a few of the best days of equity markets has a material effect on long-term returns. We aim to provide an investment portfolio that will create value over time. As such, we invest in companies and funds that have long-term horizons and will survive the inevitable market crashes that will come our way.

Annualised risk and return (3 years to 31/03/2020)



Source: Aberdeen Standard Capital
Please note: The chart shows the annualised volatility (risk) and annualised performance based on portfolio returns for Aberdeen Standard Capital's Conventional Managed Portfolio Service over the past three years to the date shown.

Key	Name	Performance (%)	Volatility (%)
●	Conventional Managed Portfolio Service 1	1.39	4.34
●	Conventional Managed Portfolio Service 2	0.09	6.25
●	Conventional Managed Portfolio Service 3	-0.09	8.42
●	Conventional Managed Portfolio Service 4	-0.90	10.85
●	Conventional Managed Portfolio Service 5	-1.35	12.15

Source: Aberdeen Standard Capital
Please note: The table shows the annualised volatility (risk) and annualised performance based on portfolio returns for Aberdeen Standard Capital's Conventional Managed Portfolio Service over the past three years to the date shown.

Current asset allocation (as at 31/03/2020)

	Portfolio Cautious (%)	Portfolio Moderately Cautious (%)	Portfolio Balanced (%)	Portfolio Moderately Adventurous (%)	Portfolio Adventurous (%)
Absolute Return Funds	6.95	7.41	10.21	7.37	2.50
Alternatives	3.75	4.79	7.26	9.33	9.01
Money Market	7.36	2.93	--	--	--
Equity	10.92	31.55	46.22	68.86	87.02
Fixed Interest	70.53	52.83	35.81	13.96	0.96
Cash	0.49	0.49	0.50	0.49	0.50
Total	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**

Source: Aberdeen Standard Capital

Holdings (as at 31/03/2020)

	Asset class	Portfolio Cautious (%)	Portfolio Moderately Cautious (%)	Portfolio Balanced %)	Portfolio Moderately Adventurous (%)	Portfolio Adventurous (%)
ASI Global Absolute Return Strategies	Absolute Return Funds	1.24	1.86	2.53	1.85	0.63
Fulcrum Diversified Core Absolute Return Fund	Absolute Return Funds	2.48	3.70	5.12	3.68	1.25
Invesco Global Targeted Returns Fund	Absolute Return Funds	1.24	1.85	2.56	1.84	0.63
SLI Global SICAV Absolute Return Global Bond Strategies Fund	Absolute Return Funds	1.99	--	--	--	--
First State Global Listed Infrastructure Fund	Alternatives	--	--	2.09	2.98	2.73
iShares Global Property Securities Equity Index Fund (UK)	Alternatives	3.75	4.79	5.17	6.35	6.28
Aberdeen Liquidity Fund	Cash & Money Market	7.36	2.93	--	--	--
Fidelity Asia Fund	Equity	0.70	1.79	2.61	3.71	4.70
Artemis Global Emerging Markets Fund	Equity	0.35	0.86	1.25	1.72	2.18
Barings Europe Select Trust	Equity	0.19	0.58	0.88	1.28	1.64
BlackRock European Dynamic Fund	Equity	0.32	0.93	1.38	2.06	2.54
Schroder European Fund	Equity	0.31	0.91	1.38	2.03	2.56
T. Rowe Price Continental European Equity Fund	Equity	0.30	0.88	1.34	1.96	2.55
Legal & General Japan Index Trust	Equity	0.62	1.83	2.74	4.06	4.91
Vanguard US Equity Index Fund	Equity	4.88	14.19	20.87	30.97	40.01
J O Hambro Capital Management UK Dynamic Fund	Equity	0.83	2.43	3.47	5.35	6.38
Lazard UK Omega Fund	Equity	0.83	2.43	3.50	5.35	6.46
Vanguard FTSE UK All Share Index Unit Trust	Equity	1.59	4.70	6.80	10.38	13.10
Legal & General Emerging Markets Government Bond (USD) Index Fund	Fixed Interest	3.36	3.98	4.77	3.52	0.48
Legal & General Emerging Markets Govt Bond Local Currency Index Fund	Fixed Interest	3.29	3.90	4.84	3.45	0.49
Schroder Euro Corporate Bond Fund	Fixed Interest	4.93	2.45	--	--	--
Standard Life Investments European Corporate Bond Fund	Fixed Interest	4.95	2.46	--	--	--
Vanguard Global Bond Index Fund	Fixed Interest	14.18	5.28	--	--	--
PIMCO Global High Yield Bond Fund	Fixed Interest	8.44	9.91	9.30	7.00	--
Aberdeen Standard OEIC IV Global Inflation-Linked Bond Tracker Fund	Fixed Interest	4.48	4.96	5.68	--	--
iShares Corporate Bond Index Fund (UK)	Fixed Interest	10.05	11.50	11.21	--	--
Vanguard UK Government Bond Index Fund	Fixed Interest	16.84	8.39	--	--	--
GBP Cash	Cash	0.49	0.49	0.50	0.49	0.50
Total		**100.00**	**100.00**	**100.00**	**100.00**	**100.00**

Source: Aberdeen Standard Capital

Aberdeen Standard Capital Limited, registered in Scotland (SC317950) at 1 George Street, Edinburgh EH2 2LL.

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