QuotedData

Monthly summary | Investment companies

December 2019

Economic & Political Roundup

Kindly sponsored by Polar Capital and Allianz

A collation of recent insights on markets and economies taken from the comments made by chairmen and investment managers of investment companies – have a read and make your own minds up. Please remember that nothing in this note is designed to encourage you to buy or sell any of the companies mentioned.

Roundup

Growing optimism around US-China trade negotiations saw US stocks register their best monthly performance since June. The dollar benefitted from this uptick in demand for US assets, having lost value over October. Sterling held its own following last month's rally, though all eyes are on the upcoming general election.

Global

Separating oscillations from material uncertainty

Susan Noble, chair of AVI Global, says trade war between the US and China is affecting economic growth in both countries and, by extension, the rest of the world's economy and equity markets. Capital Gearing's chairman, Graham Meek, says the trust's "dry powder" holdings, including cash and short-term bonds, provides valuable optionality to turn-up risk exposure when the underlying climate improves. Elsewhere, the manager of Scottish Mortgage discusses gathering evidence of cracks in the dominance of some of China's leading internet platforms. These fissures have come from dynamic newer companies, not regulators or public discontent.

UK

General election looms

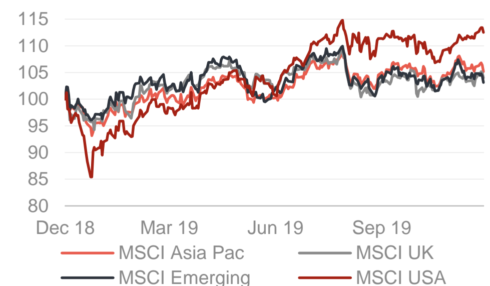
Several UK-focused funds review the last few months in their outlook statements as the general election approaches. Chelverton Growth's manager, David Horner, says the low point in sentiment was probably reached three months ago. Since then, as the likelihood of "no-deal" receded and a "deal" of some form looked probable, we have passed the nadir. Mark Barnett, manager of Perpetual Income and Growth…

Exchange Rate	29/11/19	Change on month %
GBP / USD	1.2925	(0.1)
USD / EUR	0.9076	+1.2
USD / JPY	109.49	+1.4
USD / CHF	1.0002	+1.4
USD / CNY	7.0325	(0.1)

Source: Bloomberg, Marten & Co

MSCI Indices rebased to 100

Time period 01/12/2018 to 29/11/2019



Source: Bloomberg, Marten & Co

	29/11/19	Change on month %
Oil (Brent)	62.43	+3.7
Gold	1463.98	(3.2)
US Tsy 10 yr yield	1.7758	+5.0
UK Gilt 10 yr yield	0.697	+10.8
Bund 10 yr yield	(0.362)	(11.5)

Source: Bloomberg, Marten & Co

NB: this note has been prepared by Marten & Co and is for information purposes only. It is not intended to encourage the reader to deal in the security or securities mentioned in this report. Please read the important information at the back of this note. QuotedData is a trading name of Marten & Co Limited which is authorised and regulated by the FCA. Marten & Co is not permitted to provide investment advice to individual investors.

UK (continued)

… notes that over the third quarter, UK employment data remained robust, with the unemployment rate below 4%. The chairman of Shires Income. Robert Talbut, discusses the equity income sector, noting that dividend yields are high and the gap between equity yields and bond yields remains at very high levels. He adds that the under-performance of value / yield has thrown up many attractive yield opportunities in companies that should prove resilient in a downturn. We also hear from Aberdeen Standard Equity Income, Baillie Gifford UK Growth, Blackrock Smaller Companies, Gresham House Strategic, Montanaro UK Smaller, Schroder Income Growth, Troy Income & Growth and Value and Income.

. . . .

Japan

Accession of Crown Prince Naruhito seen as a significant boost to morale.

Karen Brade, chair of Aberdeen Japan, says the slowdown in China this year, has had a consequential impact on the Japanese manufacturing and service sectors. While the relative strength of the yen might be dampening exports, Karen notes that it is encouraging some companies to invest abroad. She adds that many companies continue to commit capital to long-term expansion. Baillie Gifford Japan's chair, Nick AC Bannerman, leads with what he says was a significant boost to the country's morale earlier in in May when Crown Prince Naruhito acceded to the throne on the abdication of His Majesty Emperor Akihito. The onset of the new era is expected to encourage a fresh focus on innovation and revitalisation of the economy. Eiji Saito, Naohiro Ozawa and Michiko Sakai, managers of JPMorgan Japan Smaller, discusses several themes that underlie the trust's long-term investment thesis. On a cautionary note, the mangers note that Japanese companies are sensitive to economic cycles in overseas markets and, although they do not expect a recession, a failure to achieve a positive outcome for the current range of trade issues would pose a headwind.

. . . .

China

There has been a clear slowdown in Chinese economic activity.

Dale Nicholls, manager of Fidelity China Special Situations, provides a detailed account of the state of play in China. In addition to his market review, Dale discusses the US-China trade conflict and the country's economic outlook. On the latter, he says there has been a clear slowdown in Chinese economic activity. While trade war uncertainty has clearly weighed on business sentiment, tighter credit conditions, especially around some of the so-called "shadow banking" sectors has also played a part.

. . . .

Biotech and healthcare

The US Food and Drug Administration had another record year for new drug approvals in 2018.

In their market review, Biotech Growth's managers, Geoff Hsu and Richard Klemm, discuss the sector's recent market underperformance. They attribute this to general macro concerns about the economic outlook and concerns about the potential for drug pricing regulation, particularly in light of the upcoming 2020 U.S. presidential election. These concerns resulted in a net outflow of approximately U.S.$7.5bn from biotechnology/healthcare funds during the review period. The sector is at an important inflection point, as new platform technologies spur innovation and make more diseases amenable to treatment. Elsewhere, Syncona sees a rich pipeline of opportunities around to found new companies with the ambition of taking products to market, including across areas such as gene therapy, cell therapy, small molecules and biologics. Sven H. Borho and Trevor M. Polischuk, managers of Worldwide Healthcare,

say that the overall fundamentals of the healthcare industry remain overwhelmingly positive. The secular tailwind is as strong as ever, from more people (from global population demographics), more innovation (from unparalleled technological advancements), more drugs (from record number of approvals), and more money (from increasing gross domestic spend on healthcare). They also note that the U.S. Food and Drug Administration (FDA) has just had another record year for new drug approvals. 2018 marked the second consecutive year in which the FDA has approved a record number of new molecular (or biological) entities, with 59.

. . . .

Infrastructure

High demand from unlisted investors for core infrastructure investments.

HICL Infrastructure say that the market for core infrastructure investments continues to be very competitive, characterised by high levels of demand from unlisted investors for good quality infrastructure assets. Sequoia Economic Infrastructure Income says it has operated in a relatively calm environment over the last six months with tightening lending margins and bond spreads since the volatility of the corporate bond and loan markets in the fourth quarter of 2018. The trust adds that primary market issuance in the infrastructure loan markets has been exceptionally strong, with deal volumes of $264bn over the last six months, split approximately 30% in the North America, 36% in EMEA, 15% in Asia, and 19% in the rest of the world.

. . . .

Other

We have also included comments on Europe from Montanaro European Smaller; global emerging markets from Templeton Emerging Markets and Utilico Emerging Markets; Asia ex Japan from Asia Dragon, Henderson Far East Income and Schroder Oriental Income; Latin America from Aberdeen Latin American Income; India from Aberdeen New India; the flexible investment sector from Caledonia Investments, Henderson Alternative Strategies and Personal Assets; leasing from Doric Nimrod three; renewable energy infrastructure from NextEnergy Solar; property – debt from Real Estate Credit Investments and property securities from TR Property.

. . . .

Contents

4	Global (thoughts from AVI Global, Capital Gearing and Scottish Mortgage)
6	United Kingdom (thoughts from Aberdeen Standard Equity Income, Baillie Gifford UK Growth, Blackrock Smaller, Chelverton Growth, Gresham House Strategic, Montanaro UK Smaller, Perpetual Income and Growth, Schroder Income Growth, Shires Income, Troy Income & Growth and Value and Income)
16	Europe (thoughts from Montanaro European Smaller)
16	Japan (thoughts from Aberdeen Japan, Baillie Gifford Japan and JPMorgan Japan Smaller)
18	China (thoughts from Fidelity China Special Situations)
19	Global emerging markets (thoughts from Templeton Emerging Markets and Utilico Emerging Markets)
23	Asia ex-Japan (thoughts from Asia Dragon, Henderson Far East Income and Schroder Oriental Income)
26	Latin America (thoughts from Aberdeen Latin American Income)
27	India (thoughts from Aberdeen New India)
28	Flexible investment (thoughts from Caledonia Investments, Henderson Alternative Strategies and Personal Assets)
29	Debt (thoughts from Alcentra European Floating Rate Income and TwentyFour Income)
32	Leasing (thoughts from Doric Nimrod Three)
35	Biotech and healthcare (thoughts from Biotech Growth, Syncona and Worldwide Healthcare)
43	Infrastructure (thoughts from HICL Infrastructure and Sequoia Economic Infrastructure Income)
44	Renewable energy infrastructure (thoughts from NextEnergy Solar)
45	Property – debt (thoughts from Real Estate Credit Investments)
46	Property securities (thoughts from TR Property)

Polar Capital Technology Trust plc

Digital Disruption: Transforming the world bit by bit

Twenty years after the dawn of the commercial internet, nearly every sector is now being challenged, improved or replaced by disruptive technology. The Polar Capital Technology Trust – managed by a team of dedicated technology specialists – has a proven track record with the ability to spot developing technology trends early on and to invest in those companies best placed to exploit them.

Find out more about how the
Polar Capital Technology Trust
is helping to transform the world bit by bit.

London Stock Exchange Ticker: PCT

Visit **polarcapitaltechnologytrust.co.uk**
Available to purchase through all major platform providers, stockbrokers and/or your financial adviser.

Capital at risk and investors may not get back the original amount invested.
Important Information: This advert constitutes a financial promotion pursuant to section 21 of the Financial Services and Markets Act 2000 and has been prepared and issued by Polar Capital LLP. Polar Capital is a limited liability partnership with registered number OC314700, authorised and regulated by the UK Financial Conduct Authority ("FCA"). The value of your investments (including the income from them) can go down as well as up. This does not constitute investment advice. If you are unsure of any issue, you should speak to a financial adviser.

AS FOCUSED ON DIVIDENDS AS YOU ARE

The Merchants Trust PLC

The Merchants Trust aims to provide a rising income by investing in large UK companies with the potential to pay attractive dividends. Although past performance is no guide to the future, we've paid a rising dividend to our shareholders for 37 consecutive years, earning us the Association of Investment Companies' coveted Dividend Hero status. Beyond a focus on dividends, Merchants offers longevity too. This year we celebrate our 130th anniversary, making us one of the oldest investment trusts in the UK equity income sector. To see the current Merchants dividend yield or to find out more about us, please call or have a look at our website.

A ranking, a rating or an award provides no indicator of future performance and is not constant over time. You should contact your financial adviser before making any investment decision.

1889 – 2019

0800 389 4696 www.merchantstrust.co.uk

INVESTING INVOLVES RISK. THE VALUE OF AN INVESTMENT AND THE INCOME FROM IT MAY FALL AS WELL AS RISE AND INVESTORS MAY NOT GET BACK THE FULL AMOUNT INVESTED.

This is a marketing communication issued by Allianz Global Investors GmbH, an investment company with limited liability, incorporated in Germany, with its registered office at Bockenheimer Landstrasse 42-44, D-60323 Frankfurt/M, registered with the local court Frankfurt/M under HRB 9340, authorised by Bundesanstalt für Finanzdienstleistungsaufsicht (www.bafin.de). Allianz Global Investors GmbH has established a branch in the United Kingdom which is subject to limited regulation by the Financial Conduct Authority (www.fca.org.uk).

Global

(compare Global funds **here**)

Susan Noble, chair of AVI Global:

The challenges continue unabated. The macroeconomic situation remains difficult. The trade war between the US and China is affecting economic growth in both countries and, by extension, the rest of the world's economy and equity markets. Political tension remains high, not least in Europe. At the time of writing, the UK is dealing with an uncertain outcome of the Brexit process and now also an unscheduled general election.

. . . .

Graham Meek, chairman of Capital Gearing:

German residential property has been a significant portfolio theme and positive contributor over the last 3 years. We started to reduce the position in the spring due to concerns around the rising politicisation of rents; with hindsight we should have reduced further. In June, a draft law was proposed by the Berlin state government to introduce a 5 year freeze on rental increases. As a result of this process three holdings with significant Berlin exposure fell by more than 20%. Fortunately, the majority of our exposure was to property outside Berlin and, after some recovery later in the period, the aggregate German residential holdings were only down circa 1%. We continue to believe these assets offer attractive long term return potential but the risks have clearly risen.

The large portfolio of US Index linked bonds delivered returns in excess of 10%. This was a combination of currency gains and falling yields; the former driven by Brexit concerns and the latter by actual and anticipated interest rate cuts. This asset class will continue to play a central role in portfolio construction but in the short term it seems unlikely to repeat such marked gains.

The company continues to hold in excess of 35% of the portfolio in cash, treasury bills and short dated high quality sterling debt. In relative terms these holdings were a drag, at a time of strong gains elsewhere in the portfolio. However, we value the stability and optionality of this “dry powder” highly. We look forward to a time when either the equity market or the bond market offers materially better value, and will deploy this dry powder when this emerges.

. . . .

Manager’s report for Scottish Mortgage:

Whilst the short term oscillations of markets frequently contain little meaning and much noise, we always endeavour to winnow through events to discern if beneath emotions and market positioning there have been structural changes that we should reflect in our portfolio. The last six months have seen markets become so concerned at the current low levels of global economic growth and political harmony that the equities of preference have been those perceived to possess minimal sensitivity to the perils of stagnation. This is, though, no more our preoccupation than the equally common perception of twelve months ago that US economic growth was so formidable that interest rates would rise remorselessly.

But we must acknowledge underlying concerns where they exist. The most significant may be gathering evidence of cracks in the dominance of some of the internet platforms that we have invested in both heavily and successfully in the last decade. This suggests that their longevity may be more questionable than we thought. But there is an irony

here. It's not in the US that these fissures have emerged despite market nerves provoked by regulatory and media scrutiny. Instead the issues have been in China. The threat to incumbents has come neither from regulators nor public discontent but from extraordinary dynamism. The major casualty has been Baidu (once a very significant holding) and the major disruptor has been Bytedance. That we own a holding in the unquoted Bytedance is some compensation.

The contrasting relative fortunes of Baidu and Bytedance are not isolated examples of a divergence between quoted and unquoted competitors. Contrary to the mood of the moment our experience has been that in both underlying progress and valuation, our unquoted companies are generally outperforming their listed counterparts. It is common knowledge that there are high profile examples of unquoted or recently listed companies that have suffered serious problems but it seems to us that generalising from these distinctly colourful sagas is misguided. The flaws of their business models were not impossible to identify.

....

United Kingdom

(compare UK funds **here**)

Thomas Moore, manager of Aberdeen Standard Equity Income:

Market review

The financial year was marked by persistent anxiety over economic stagnation and geopolitical tensions. This drove a wide divergence in share price performance within the UK equity market which was unhelpful for our performance. The portfolio suffered from its heavy exposure to small/ mid-cap stocks which were out of favour for most of the period. It was also hit by its limited exposure to large-cap defensive/growth stocks and some company-specific disappointments. Looking ahead, low valuations and robust dividend prospects make us positive on the outlook for the portfolio.

The slight advance in the UK equity market over the 12 month period masks considerable volatility along the way as political events, notably the US-China trade war and Brexit, hit investor sentiment. In this environment, company-specific developments took a back seat to macro events, causing large-cap defensive sectors to lead the market and small and mid-cap cyclical sectors to lag.

The financial year started on a sour note, with the FTSE All-Share Index delivering a double-digit percentage decline in the last quarter of 2018; its weakest quarterly performance since the depths of the Eurozone crisis in Q3 2011. The weakness in global stock markets coincided with the inversion of government bond yield curves, meaning that long-dated bonds yielded less than short-dated bonds. These market signals indicated growing expectations of a global economic recession. Central bank policy responded by turning increasingly dovish in order to support economic growth. The US Federal Reserve shifted its policy stance first to pause and subsequently to cut rates in July and September. This helped to lift global stock markets.

Politics remained the primary focus in the UK, with Prime Minister Theresa May being forced to delay the UK's departure from the EU and then to resign. Her successor, Boris Johnson, took a more hard-line approach to negotiations, emphasising his willingness to allow the UK to leave the EU without a deal. This political whipsawing was reflected in a weakening in the value of sterling against the US dollar and the underperformance of the FTSE 250 Index and Small Cap Index against the FTSE 100 index. Weak sterling enhances the earnings of companies with significant overseas sales, a feature of the large-cap FTSE 100 Index, which derives around 80% of its revenues from outside the

UK, in contrast with smaller companies, whose revenues tend to be far more weighted towards the domestic economy.

Since the year end, investors have become more sanguine about the global outlook, helped by a thawing in US-China trade relations at the same time as a continuation of dovish Federal Reserve policy and signs of a bottoming in US economic data. In the UK, Prime Minister Boris Johnson has managed to negotiate a fresh Brexit deal and will fight for an overall majority in the forthcoming General Election. While there remain multiple different potential political outcomes, the probability of a no-deal Brexit is now considered to be much reduced. This has helped to broaden the performance of the stock market beyond the large-cap defensive sectors that dominated during the year under review.

Outlook

The prolonged period of intense investor pessimism we have experienced has led to a polarised stock market in which stocks perceived as low risk are trading at very high valuations while stocks regarded as higher risk are trading at very low valuations. This valuation divergence is the most extreme it has been for more than 10 years and we therefore see it as an opportunity to build positions in robust businesses that will ultimately deliver strong performance as risk aversion subsides.

Past performance is, of course, no guide to the future, but when we have observed a similar situation in the past, we have recovered strongly once investors become less anxious and shift their focus away from momentum investing and back to corporate fundamentals. Increased confidence levels would benefit many of our holdings, in particular those stocks whose earnings and valuation multiples are linked to global economic growth, such as resources, industrials and financials. Specifically, the political uncertainty relating to Brexit and the US-China trade war has weakened activity levels and depressed valuation multiples across many of our holdings. We would expect share prices to respond very positively to any resolution to these political matters. In addition, we remain confident in the sustainability of the portfolio's income generation and expect the portfolio to deliver solid revenue growth in 2020. We have seen some evidence of a change in mindset since the beginning of September at which point conditions have become noticeably more benign for our investment process. Although uncertainty is still elevated, investors are showing signs of becoming less nervous, particularly in relation to the risk of a no-deal Brexit. We have also benefited from a noticeable increase in the number of holdings meeting or beating consensus analyst expectations and a reduction in the number of stocks missing expectations.

. . . .

Manager's report for Baillie Gifford UK Growth:

It has been a tumultuous six months in world politics and economics, and UK investors continue to be chiefly preoccupied with what the denouement of the drawn-out Brexit negotiation process will look like. Depending on the noises coming from Westminster on any given day, the All-share swings from one direction to another - either favouring or eschewing domestically (or internationally) exposed equities; investor behaviour is seemingly more influenced by short-term moves in the value of Sterling than fully considering the specifics of the underlying constituent companies.

Even more than usual, it feels like we live in interesting and uncertain times - times of technological, societal, political and economic disruption. Rather than despair, however, we think this presents an exciting backdrop for bottom-up growth investors such as ourselves. The pace of change in many industries is quickening and this will likely increase the divergence between those companies which adapt and thrive and those which fall by the wayside. In this volatile and news-driven environment, more than ever, our chances of picking the winners will be greatly aided by cultivating the

resilience to remain patient and resolutely focused on understanding long-term, structural changes. If we are successful, superior investment returns will follow.

. . . .

Ronald Gould, chairman of Blackrock Smaller Companies:

The outlook for the UK equity market is unclear, with potential for significant volatility as the impact of a UK election and further Brexit negotiations play out in the economy. Globally, growth also looks set to be constrained as geopolitical tensions increase, trade tensions, especially between China and the US continue to rumble and economic data worsens. However, supportive monetary policy, with the ECB and the US Federal Reserve cutting rates, has at least partially mitigated the risk of a global recession in 2019 and our manager expects the global economy to continue to grow albeit at a much slower rate.

. . . .

David Horner, manager of Chelverton Growth:

Market review

In the past year the impact of the uncertainty resulting from the grinding "Brexit" process has finally begun to impact on our companies. The significant reduction in share prices, seen across the entire market, has been amplified in the small company "value" segment, the area of the market in which this company is largely invested.

In the past year the UK economy has grown, albeit slowly, and employment has continued to rise. We have finally started to observe some real wage increases. The tortuous Brexit impasse has created a very negative, indeed toxic, atmosphere which has adversely affected both business and consumer confidence.

However, when meeting up with companies one does not get any sense of the doom and gloom that one sees in the media. Generally, people are getting on with making their businesses more efficient, more profitable and more resilient.

Hopefully, when we finally see a resolution of the Brexit process, the country and the companies we are invested in can get on with managing within a much more certain and predictable environment. There is a feeling within the investment community that once Brexit is resolved, or more precisely the high profile and public aspect of the first phase is resolved, then there will be a release of pent-up demand that has been held up waiting for something to happen.

The portfolio is invested in small AIM traded or unquoted companies whose business is largely conducted in the UK and therefore the strength and growth of the UK economy is by far and away the most important determinant of our underlying companies' success.

Across the larger funds managed by Chelverton, investing in companies outside of the FTSE 100, the "low point" was probably reached about three months ago. Since then, as the likelihood that "no-deal" receded and that a "deal" of some form is probable, there has been a strong rally in share prices and investor sentiment. As ever, it is the larger companies, valued in excess of say £1bn, that react first, then over time this ripples down the market.

One factor that endorses our view of value has been the very significant increase this year in the number of takeovers of UK companies by overseas businesses at healthy premiums. Whilst this is unlikely to impact the type of company in our portfolio, it is, on one level, encouraging confirmation of the deep value that we believe currently exists.

It is a well-documented view that UK and Overseas investors are very "underweight" in UK equities, all waiting for a resolution of the "Brexit" impasse. In addition, analysts say

that the relative ratings between "Growth" companies and "Value" companies are as wide as they have ever been. History shows that these extremes of valuation do not last forever.

. . . .

Graham Bird and Richard Staveley, managers of Gresham House Strategic:

Market commentary

It has been a turbulent six months for UK equity markets facing both domestic and global headwinds, with continued and increasing political uncertainty in the UK, exacerbated by negative headlines emanating from the Woodford saga with a global economic backdrop of concerns over trade-wars and potential economic slowdown.

1. **Increasing political uncertainty**

The initial Brexit delay from March 2019 to October 2019 was designed to avoid the uncertainty of a no-deal and give parliament time to produce a co-ordinated outcome for the country. However, rather than stabilise the situation, the summer has ended up providing a marked increase in political and economic uncertainty. We have witnessed a change of Prime Minister, Supreme Court rulings, a revised but rejected Brexit deal and now a snap general election. The lack of clarity on the outcome of these processes makes it difficult for both investors and operating companies to make investment decisions. This has been a key ingredient to the state of paralysis that both the UK economy and markets currently find themselves in. Given the context of all-time highs in US equities, global asset-allocators have continued to reduce UK equities exposure to very low levels vs history.

2. **The fall-out from the Woodford saga**

The UK fund management industry was dominated by one story over the summer: the fallout from the crisis at Woodford Investment Management. Whilst we do not need to regurgitate the story here, the collapse of one of the UK's most renowned investment managers did little to help investor confidence in UK equities or their managers, in particular at the smaller, less liquid end of the market.

These two factors drove accelerating outflows from UK SMID funds over the summer at the fastest rate for five years, putting pressure on valuations (as funds sold to meet redemptions) and at the same time drying up liquidity and buying interest. This allowed equities to drift down further indiscriminately on 'no news'. As a result, small-caps (the most illiquid of equities) have de-rated against their larger peers.

3. **The global backdrop**

The global backdrop to UK specific issues has been souring economic data - especially industrial. Both domestic and international economic indicators have declined into the autumn and the drivers of these are multi-faceted. The US faces the ongoing uncertainty of an unsettled trade war and growing impacts of tariffs which are now starting to have a real impact. It looks increasingly as if the US presidential race next year will be another divisive battle, with Trump likely to face an equally polarising candidate from the Democrat party. The other engine of the global economy, China, also impacted by the trade war, has already been slowing down as the gradual transformation of their economy, from being dependent on infrastructure build and high levels of credit support evolves. The Eurozone, beset by long-term structural issues, is also struggling as Germany's strong export base finds weaker end-market conditions: "Germany's central bank warning the country's economy may have shrunk for its second consecutive three-month period" in October 2019. Significant monetary policy support looks increasingly like 'business as usual' rather than temporary. The IMF has cut its global growth forecast by 0.3% in the last six months and now expects global growth to fall to 3% in 2019, its slowest rate since the Global Financial Crisis. The

common theme here is that near-term visibility is worsening, making it more difficult for companies to make decisions. The inversion of the yield curve, a regular, if not early and approximate indicator of near-term recessionary conditions, certainly highlights bond market positioning given this economic backdrop.

The UK and global issues described in this report have, of course, impacted company earnings and we are on track for the weakest year of the current bull market for UK corporate earnings. The number of profit warnings we flagged in the Q3 factsheet has worsened; UK companies have now issued 235 warnings in the first nine months of 2019, the highest third-quarter sub-total since 2008 and the EY profit warning stress index is at a score of 96, a level not seen since the first quarter of 2009.

This market commentary is an important context to the portfolio performance described below. While positive for the six months to 30 September 2019, the performance was weaker than the performance of the preceding 24 months. A protracted period of domestic and global uncertainty is affecting decision making and demand in UK businesses and households - as reflected in the 30% of UK profit warnings, citing delayed or cancelled contracts. As a result, companies and markets alike have had a difficult six months. The sharp rise in profit warnings citing accounting issues is a further worrying sign and a signal that the economy is cooling. This compares with a previous average of 3%. It is worth considering that these sorts of problems often come to the fore at times of increasing economic stress, with the current peak exceeding the previous high of 9% of accounting-related warnings issued in 2007. Many of the issues described here are on-going and will run into 2020, underlining our belief in the need for cautious analysis of investment opportunities focusing on value, underpinned by fundamentals, downside scenario testing, cash generation, strength of balance sheets and a cynical eye on the promise of above average growth by small company management teams.

Outlook

Given the continued uncertain economic and political outlook, there are many reasons to remain cautious in relation to investment activity. However:

- The biggest determinant of future returns is the entry valuation. UK equities are very cheap relative to history and other international markets. Within the UK market, the smaller company discount has widened and is now wider than it has been for many years.
- Structural factors, such as the introduction of MiFID II in 2018 have, in our view, exacerbated inefficiencies at the smaller end of the market, providing a greater number of opportunities for discerning investors to find hidden value. These inefficiencies are, in our view, persisting for longer.
- Fallout from the Woodford crisis is likely to lead to many open-ended funds taking a more cautious approach to smaller companies and illiquidity. This may lead to technical factors which create opportunities to acquire attractive assets at appealing prices from market participants selling for non-investment reasons.

. . . .

Manager's report for Montanaro UK Smaller:

Review

Over the past six months, Brexit has continued to dominate the investment landscape. Although equity markets reacted positively to the change in prime minister, this did nothing to alter the parliamentary arithmetic that makes getting a Brexit deal through the House of Commons difficult.

A result of this has been the continued outperformance of the UK's largest companies, which source much of their revenue overseas, compared to the more domestic focus of UK SmallCap.

Besides Brexit, there were some notable reminders that events overseas have the potential to influence the trajectory of markets. A rise in the VIX index (a measure of market volatility) during the summer was influenced by President Trump's Trade War related tweets. Meanwhile, oil prices spiked by over 20% after an attack on Saudi Arabia's oil infrastructure, the largest move in the price of Brent crude since Saddam Hussein invaded Kuwait in 1990.

Furthermore, worries about global growth increased with economic data pointing to a slowing world economy. Bond yields continued their decline with the staggering consequence that the total market value of negative yielding debt reached over $16 trillion.

Outlook

It has been 96 years since a pre-Christmas election in the UK. In 1923, the result was a hung parliament. The outcome may be similar this time, although investors hoping for a removal of "Brexit anxiety" must surely wish that some element of certainty emerges from polling stations.

It is worth remembering that the UK remains home to many high quality businesses. With sterling weaker than it has been in a generation, equity valuations cheaper compared to many other stock markets and economic data weakening in countries such as the US, it may be that investors will look at UK SmallCap once again.

. . . .

Mark Barnett, manager of Perpetual Income And Growth:

The UK equity market posted a positive return over the six-month period to 30 September 2019. However, as has tended to be the case in recent reporting periods, this headline return masks periods of underlying volatility. Global markets were driven by persistent concerns of a slowdown in economic growth and the fluctuation of US-Sino trade tensions. Meanwhile a trend noted in previous periods continued; internationally orientated sectors within the FTSE 100 continued to lead market performance.

Political uncertainty surrounding negotiations for the exit from the European Union (EU) dominated the domestic agenda. During the period sterling served as the bellwether for the perceived likelihood of a “no-deal” exit. The value of sterling versus international currencies remained weak, with the prorogation of Parliament in August pushing the pound to just US$1.20.

Amid this persistent domestic uncertainty, the Bank of England’s Monetary Policy Committee voted unanimously on four occasions to hold the UK base interest rate at 0.75%. Latterly, officials signalled the potential for a future interest rate cut following the UK’s exit from the EU. Economic data released during the period, showed a slowdown in economic growth during the first half of 2019, a result of weaker business investment and slowing global economic growth. The UK economy expanded in the third quarter, avoiding recession. Employment data remained robust, with the unemployment rate below 4% and more than 800,000 labour market vacancies.

Outlook

The performance of the UK stock market is likely to be determined by the same macroeconomic and political forces that have dominated sentiment for the past few years. The political uncertainty in many regions has been especially difficult to navigate recently and has been a major headwind to portfolio performance given the extreme

polarisation of company valuations that has emerged. I have commented previously that this differential between highly rated global non-cyclical stocks and depressed domestic economically sensitive shares is substantial. This differential sits at a multi-year high and offers the most glaring opportunities within the UK stock market. The portfolio is positioned to take advantage of this perceived mispricing and retains large portfolio weightings in insurance, real estate, retail and support services.

The extent of this mispricing is perhaps most clearly highlighted by the spread between dividend yields and corporate bond yields over the past ten years. Over this period, dividend yields have remained broadly flat, whilst corporate bond yields have declined markedly. A 650bp (6.5%) shift in the yield differential over the period is notable and represents another strong endorsement of the attraction of equities to an asset neutral investor at the moment. It is also very likely a significant factor behind the strong re-emergence of merger and acquisition activity in recent months. The range and breadth of deals witnessed from industrial and especially financial buyers is clear evidence that there is value available in UK listed companies that can be exploited with finance from accessing the debt markets at very attractive yields.

In recent weeks sentiment within the market has been extremely volatile as perceptions around a political deal have shifted. This has resulted in a marked change in the composition of the stock and sector leadership, which has favoured the current positioning within the portfolio. Clarity regarding the outcome of the negotiations with Brussels would clearly benefit the performance of the UK stock market and especially this portfolio. The level of pessimism which is discounted in the valuations of many holdings is anticipated to result in material revaluation opportunities from current levels as and when the political fog clears.

....

Manager’s report for Schroder Income Growth:

The All-Share rose by 0.4% in what was a mixed period for global stock markets. The final calendar quarter of 2018 was one of the worst quarters for global equities in many years as fears over the outlook for the world economy came to a head against the backdrop of tightening global monetary conditions at the time, US-China trade tensions and European political uncertainty. Equities globally bounced back sharply in Q1 in response to dovish commentary from central banks, with the US Federal Reserve (Fed) and European Central Bank (ECB) tempering expectations for tighter monetary policy. Expectations for monetary policy then shifted over Q2, notably so in the US where the market began to speculate that the Fed could cut interest rates.

The Fed subsequently cut base rates in July, the first reduction since 2008. This also had the effect of spurring other central banks to loosen monetary policy. Latest GDP data confirms that growth in the world's major economies has decelerated in 2019, with both the UK and German economies contracting in Q2. Meanwhile, forward-looking indicators pointed to a further softening in the economic and inflation outlook, with the prognosis for manufacturing particularly weak. Brexit and domestic political uncertainty remained elevated as Boris Johnson took over as the UK's new prime minister on a "do or die" pledge to depart the EU by the revised exit date of 31 October.

Outlook

The global nature of UK equities has resulted in international developments setting the tone for the market. Recent global economic data increasingly points to deteriorating fundamentals. This has caused central banks to again loosen monetary policy in order to try and keep economies stable.

One particular market distortion resulting from the loose monetary policy of the last decade has been the outperformance of growth companies versus value stocks. Growth has become an increasingly sought after commodity and these companies have

been valued off the back of very low bond yields (which have declined further over the course of the period), a dangerous yardstick to use.

In addition to the global trends influencing UK equities, Brexit continues to dominate sentiment, creating considerable uncertainty for the UK economy and political environment. As a result, we are presented with a compelling valuation opportunity in some good quality, soundly-financed domestic companies taking a long-term perspective. We continue to be very selective in the types of business model and financial characteristics we choose to invest in. We are wary of companies whose business models are particularly susceptible to disruption, such as areas of general retail. In addition, we place a large emphasis on balance sheets and accounting, as a weak balance sheet can hamper the ability of a company to invest in its operations or respond to changing market conditions.

. . . .

Robert Talbut, chairman of Shires Income:

Market background

The first half of the financial year saw stock markets continue to move higher and, on the surface, the economy continues to perform reasonably well at both a UK and global level. Low levels of unemployment, some wage growth and low interest rates mean the consumer continues to have more disposable income. However, that headline assessment hides what has been a general weakening in economic growth indicators and a growing concern about the strength and duration of the economic cycle.

Over the six month period, the global economic outlook continued to be dominated by a number of controversies. These have affected both corporate and investor confidence, witnessed by a slowing in business investment and more skittish investor behaviour. On a global basis, the ongoing trade dispute between the US and China has been the prime driver of market sentiment. Any worsening of relations has seen global growth questioned and a selling of equities. However, more recently, progress and optimism appears to have returned, at least until the next change in direction. It would appear that, even if some sort of deal with China is secured relations are likely to remain fragile, and the US is likely to move onto a further tariff war with the EU and uncertainty is unlikely to dissipate.

The other main driver of economies has been interest rate movements, with the last six months seeing a sustained reduction in rate expectations as the US Federal Reserve has reversed direction and begun to cut rates while the European Central Bank has implemented even more negative interest rates. This reflects a lack of confidence in the underlying strength of the economy. Indeed, Global Purchasing managers' Indices (PMI) surveys suggest that the manufacturing sector is already enduring a mild recession. In August, for the first time since 2012, surveys in China, Europe and the US were below the 50 level, indicating a synchronised industrial contraction in activity. Although the larger services sector has been more resilient it is still trending downwards, and signals that extremely accommodative monetary policy is likely to remain in place.

In general, the environment of low interest rates and increased political and economic uncertainty has led to investors continuing to favour what are perceived to be lower-risk growth stocks. While this has been the trend for much of the last ten years, it was notable in September that a small move higher in bond yields triggered a sharp rally in value assets. More consistent positive economic data is required for this to be sustained, but the potential remains for value, and therefore more cyclical stocks to return to investor favour.

In the UK, the process of our exit from the EU continues to dominate even these global macro trends. Over recent weeks there has at least been some progress, with a revised

deal proposed and the prospect of a no-deal exit made more unlikely by Parliament. UK domestic assets have rebounded in response, but remain cheap compared to international companies. Steps towards clarity over Brexit have also seen a number of UK companies acquired or bid for by foreign buyers, highlighting the attractiveness of valuations. The UK equity market remains historically cheap and out of favour from international investors, both of which provide the potential for upside in returns.

Outlook

As highlighted above, the market outlook is balanced. While there are legitimate concerns around the strength of growth we also expect to see stimulus in China and EU and the persistence of very low interest rates in the US and around the world. These should be supportive of equity valuations in the UK which are currently far from high by historic standards. Investor positioning has been clearly defensive, with cash positions at the highest level since 2008, but the manager believes there is scope for the UK stock market to move higher from here.

From the perspective of the UK Equity Income sector, this is the case even more so. Dividend yields are high and the gap between equity yields and bond yields remains at very high levels.

In the short term we continue to see UK economic data remaining uninspiring and, as long as this continues, a rise in bond yields and a full shift in market positioning looks unlikely. The under-performance of value / yield has thrown up many attractive yield opportunities in companies that should prove resilient in a downturn. Overall, the UK equity market remains very out of favour with many investors which we feel provides the potential for outperformance were this to change.

. . . .

Manager's report for Troy Income & Growth:

Review

The 12 months to 30 September 2019 had an inauspicious start with volatility elevated and equities experiencing steep declines globally. The unwinding of Quantitative Easing, a deteriorating global trade environment and weakening economic data applied downward pressure on most developed equity markets. Despite widespread concerns of a prolonged period of weakness, it would appear that central bankers remain preoccupied with mitigating the deflationary impact of falling asset prices. Statements from the Federal Reserve indicated a sharp reversal of policy stance with rate hikes that had previously been in market forecasts for 2019 rapidly being unwound. Robust corporate earnings and what appeared to be a period of détente in the US-China trade disputes fuelled a sharp first calendar quarter rebound.

Equity markets continued to make steady gains through the second calendar quarter but by August the equity market rally had faltered. Bond yields also plunged in response to new salvos in the US-China trade war, with both parties announcing new tariffs from September 2019. Investor concerns led to the US and UK yield curves inverting(1) in the month, a phenomenon last seen in the UK in 2008 and often deemed to presage a recession. In the weeks that followed, the US Federal Reserve announced a 25bp rate cut but crucially failed to guide towards further monetary easing in 2019. This stance prompted a short but sharp rotation into 'value' investments and out of 'quality', which limited the portfolio's participation in what was a strong final month for markets.

Despite the predominance of international companies amongst its constituents, the returns from the FTSE All-Share Index remain inextricably linked to the performance of the UK economy, its currency, and by extension, the progress of Brexit negotiations. During the early months of 2019, the UK equity market moved increasingly to price in

a relatively benign Brexit outcome. Domestically focussed equities, including many UK banks and retailers, rose strongly and sterling hit a nine-month high of 1.33 to the dollar. However, following the failure by Mrs May to gain approval for her deal and the subsequent appointment of Mr Johnson as Prime Minister, the probability of a harder Brexit was again resurgent and during July the pound slid to 1.21 against the US dollar, levels not seen since early 2017. Meanwhile, the Bank of England Monetary Policy Committee voted unanimously to hold the base rate at 0.75%, maintaining the potential for a future interest rate cut if the UK leaves the EU without a deal.

Outlook

A year ago, we lamented in this report a lack of resolution or a clear path forward on both Brexit and US-China relations. Both topics continue to dominate headlines and move markets. UK confusion is now compounded by the decision to hold a pre-Christmas election. While PM Boris Johnson hopes this could lead to Tory success and an end to the parliamentary deadlock, a resounding result is far from certain. In the US, the tone on negotiations with China currently points to positive signals, however, we are cognisant we have been here before.

Over a longer time, scale, much discussion continues around the 'unconventional' monetary policy of the past decade. The US has attempted 'normalisation' by raising interest rates in recent years. However, three rate cuts in 2019 serve as admission that supposed normality is not yet achievable. With the ECB and the US both restarting their bond-buying programmes in recent weeks, so-called quantitative easing no longer seems so unusual! The US claims their new programme is 'in no way' the same as post-crisis QE, citing the extraordinary continuing strength of the US economy. The S&P 500 is reaching new highs as we write this report, despite lingering concerns of weak global economic data points and a mature bull market. Confusion on what the year ahead holds is not just for investors - Mario Draghi went against the ECB's monetary committee in restarting their purchase programme, demonstrating central banks themselves are at odds with how to read the global outlook.

. . . .

Patrick Harrington, manager of Value and Income:

Outlook

Globally, economic growth is slowing, particularly in Europe. President Trump’s trade policies have raised the risks in the world economy, with particular anxiety about the impact of his proposed tariffs on Chinese and European goods, though so far these have not been too extensive. GDP growth in America has moderated to an annual rate of 2% as the impact of the 2018 tax cuts has evaporated, but the Federal Reserve has reacted by cutting interest rates and signalled that further cuts are likely and that it will resume Quantitative Easing (QE). The ECB has also restarted its programme of bond buying in an effort to boost flagging Eurozone growth. Despite all the uncertainty surrounding Brexit, the UK economy has continued to grow at a reasonable pace. Whilst the reported annual growth to the end of June of 1.3% is below the long-term average it shows the UK economy is some way from a recession.

The labour markets in both the USA and the UK have continued to tighten, with unemployment in both areas at the lowest levels for more than 40 years. This has led to a rebound in the rate of wage growth in the UK, which has now reached 4%. This is well ahead of inflation and should provide significant support to consumer spending. Despite all the difficulties and threats to world stability, forecasts for global growth in 2019 remain at around 3% with a slight acceleration expected in 2020. In the UK, economic growth is slowing but not as fast as many economists have predicted. The ongoing Brexit saga is clearly affecting confidence in some areas and current UK growth expectations for 2019 as a whole remain fairly subdued at 1.3%. The Bank of

England has not changed interest rates for over a year after increasing them once in 2017 and once in 2018. Given the cuts elsewhere in the world, pressure is clearly growing on the Bank to reduce rates, especially given the uncertainty surrounding Brexit. Unfortunately, Brexit remains the predominant topic of politics and the UK Parliament is currently paralysed as a result, although the forthcoming General Election may resolve this. At the time of writing, the Prime Minister has sought an extension to the Article 50 process which has been granted and which will delay the country's departure once more. This may be advantageous from an economic perspective, but the General Election adds new uncertainties. The likelihood of a hard-left Labour administration appears to be diminishing, in part due to the Labour Party's equivocation over Brexit.

The valuation of the UK equity market at the end of VIT's half year of 12.7x earnings for the current 2019 year, falling to 11.8x for 2020 (source: Bloomberg) looks attractive and is below the long-term average. Furthermore, the average yield of 4.2% looks compelling, especially when compared with gilt yields and cash returns, which remain well below the current rate of inflation. To the overseas investor the UK looks good value compared to overseas markets, with the pound trading at a severely reduced exchange rate since the EU Referendum in June 2016. As a consequence of this we have seen a number of bids for UK companies. Until the shape of Brexit is determined, much uncertainly will overhang our market but we do believe that investors will take advantage of the low valuation once the future of our relationship with Europe has been resolved.

. . . .

Europe

(compare Europe funds **here**)

R M Curling, chairman of Montanaro European Smaller:

The last six months have seen a further deterioration of global economic growth indicators alongside rising geopolitical tensions. No-one knows if this will continue and how Central Banks and Governments will react should it do so. Brexit remains a source of ongoing uncertainty.

. . . .

Japan

(compare Japan funds **here**)

Karen Brade, chair of Aberdeen Japan:

The Japanese stock market will continue to face the same litany of risks that it has done over the past half year. At the forefront is the protracted trade negotiations between the world's two largest economies and the unpredictability of the messages on these and other issues emerging from the US President. Also affecting share prices are the geopolitical uncertainties that compel investors to flood into the yen as a safe haven each time volatility spikes. Japan/China relations have however improved (although Japan/Korea relations have deteriorated) and prospects for a resolution of US/Japan trade tensions (and perhaps also those between US and China), and the possibility that the forthcoming UK general election may bring some clarity on the way forward on Brexit, may help to calm market uncertainty. The slowdown in China in 2019, however, has had a consequential impact on the Japanese manufacturing and service sectors.

Against this backdrop, the manager feels that many Japanese companies, particularly those held by the company, are now well-positioned. At the company level, many are still expanding, investing for the future. Their efforts are augmented by the strength of the yen, which is encouraging some to invest abroad. The manager (and other asset management companies) are also watching closely and liaising with Japanese officials on proposed changes to Japanese law to reduce the threshold at which foreign investors are required, for reasons of national security, to file pre-acquisition notifications.

. . . .

Nick AC Bannerman, chairman of Baillie Gifford Japan:

Outlook

A significant boost to the country's morale was felt in May when Crown Prince Naruhito acceded to the throne on the abdication of His Majesty Emperor Akihito, ushering in the new Reiwa era, meaning beauty and harmony. The onset of the new era is expected to encourage a fresh focus on innovation and revitalisation of the economy.

As was the case in my last report, there remain some political tensions in the region. The deterioration in US-China trade relations has increased US pressure on its trade relations with Japan, and a downturn in Japan-South Korea relations is straining US-Japan-South Korea cooperation over East Asian security issues. Ongoing missile testing by North Korea is adding to tensions.

. . . .

Eiji Saito, Naohiro Ozawa and Michiko Sakai, managers of JPMorgan Japan Smaller:

Review

The Japanese stock market experienced a volatile six months and ended the period with a flat return. A major source of this volatility was elevated uncertainty driven by US-China trade friction and associated concerns about the outlook for global economic growth. During the same period, the Japanese yen strengthened against the US dollar and sterling.

Investment themes

Smaller companies in Japan comprise a diverse sector with strong growth potential, serving both local and global market needs. While our decisions are based on company-specific factors, there are also structural, long-term trends and themes that underlie much of our stock selection. These include:

- Changing demographics: Japan's population is ageing, providing opportunities for innovative smaller companies that are working to improve quality of life for seniors as well as for those businesses whose focus is on labour productivity in the workplace.
- Technological innovation: many companies are embracing the productivity opportunities that technology offers. Despite Japan being an advanced industrial economy, certain areas such as financial services and payments lag other markets in terms of technological sophistication. Japanese manufacturing is world class and the country is a leading supplier of factory automation equipment, robots, and electronics parts and materials.
- Improving corporate governance standards across Japanese companies: this has resulted in increasing numbers of independent, external directors serving on company boards, as well as improving governance policies overall, including shareholders returns, internal controls and disclosure. The market is likely to

reward companies that improve their governance standards and we maintain a constructive dialogue with companies on this broad theme.

- Overseas growth: businesses operating beyond Japan's shores are in a very strong position to capture the benefits of the dynamic economic growth across Asia which is creating new customers for high quality Japanese goods, services and brands.
- Government policy reforms that improve labour productivity: the record numbers of Japanese women in employment is testament to this. The stable political environment has also led to the adoption of policies to reform labour laws and corporate governance and to encourage inbound tourism.

Review

Although many economies around the world have seen steady growth over recent years, there has been an undeniably marked slowdown this year, notably in China. The outlook for global markets remains uncertain, with the fallout from the US/China trade tensions continuing to cast a shadow.

In Japan, cyclical sectors have experienced sluggish earnings growth. And there could be uncertain times ahead, leaving companies reliant on export business potentially vulnerable. Japanese companies are sensitive to economic cycles in overseas markets and, although we do not expect a recession, a failure to achieve a positive outcome for the current range of trade issues would pose a headwind.

In the midst of widespread caution, it is important to highlight that valuations of Japanese companies remain reasonable, lower than historical averages and below those of most major markets. The fundamental long-term outlook for Japanese smaller companies remains positive, in our view, and we see no shortage of exciting investment opportunities.

As symbolised by the new Imperial era named Reiwa (meaning 'beautiful harmony') which began on 1st May, Japan is seeking to achieve sustainable and broadly-based growth thanks to progress in corporate governance, free trade, international relations and tourism. Japan's key structural challenge, the declining size of its population, presents significant opportunities, especially for smaller companies.

The company maintains its focus on investing in businesses with leading market positions, strong cash generation and solid balance sheets, across a diverse range of industries.

China

(compare country specialist: Asia Pacific ex Japan funds here)

Dale Nicholls, manager of Fidelity China Special Situations:

US-China trade conflict

The trade conflict between the US and China which has resulted in higher tariffs has clearly dominated market sentiment since early 2018, and we are still awaiting the phase 1 trade agreement. It is quite evident that the China-US dynamics have meaningfully shifted away from the status quo that had prevailed up until the trade issue assumed centre stage. Chinese companies directly impacted by tariffs have already begun to factor in the impact of the tariffs both in their earnings as well as their capital expenditure plans. Having said that, Chinese exports to the US as a percentage of their total exports globally has been trending downwards as China has expanded its global reach and trading partners. The greater concern is how the uncertainty impacts

business and consumer sentiment and thus capital expenditure and consumption decisions.

China's economic outlook

We have seen a clear slowdown in Chinese economic activity. While trade war uncertainty has clearly weighed on business sentiment, tighter credit conditions, especially around some of the so-called "shadow banking" sectors has played a part in my view. The government is now more clearly on the front foot with increased actions to improve liquidity and support domestic demand. It is also key to reiterate that, even at this slower pace, the relative rate of growth we see in China remains significant when compared to the West. China is also maintaining the momentum in its plans of opening up its capital markets and the recent removal of the Qualified Foreign Institutional Investor quotas (QFII quotas) in September reflects this intention. There also remains considerable policy headroom in the economy to stimulate growth, and we have seen several approaches taken to lower borrowing costs in the economy.

While the pace of growth is tapering, structural changes continue to unfold in China. Thus, even at a milder pace of activity, there remains room for expansion with the shifts in demand patterns. China continues to provide a diverse opportunity set where the growth rate is not homogenous across the board and where research resources on the ground can help identify winners that are yet overlooked by the broader market.

Outlook continued

It is widely known that China is a volatile market, where sentiment can swing sharply. Given the unenthusiastic news surrounding China in recent months, the fact that worst case scenarios (such as the potential for full tariffs on all China exports to the US) are widely discussed gives comfort as an investor that potential downside is significantly factored into market valuations. Whilst I remain optimistic on prospects for a trade deal to be reached, as highlighted in this and previous reports, the portfolio's holdings are predominantly domestic focused. Chinese growth prospects remain attractive relative to its global peers in the West, and the policy impetus continues to favour domestic consumption drivers. The ongoing A-share inclusion in global equity indices is also supportive of investor interest towards Chinese stock markets.

We continue to highlight the significant valuation gap between large and small cap segments of the China market.

Looking across valuations within the portfolio overall, we are back to levels last seen after the sharp A-share driven correction in 2015, which was an opportune entry point for investors. I continue to see significant opportunities in well-managed companies growing strongly on the back of the structural shifts discussed above, unfairly penalised by macro and trade concerns that will have little impact on the ability of these companies to continue growing earnings over the mid-term.

Global emerging markets

(compare global emerging markets funds here)

Chetan Sehgal, manager of Templeton Emerging Markets:

Market overview

Emerging markets weathered increased volatility over the 6-month period driven primarily by ongoing US-China trade-related events, central bank monetary policies and concerns of slowing global economic growth.

US-China trade tensions escalated in May with the two countries increasing tariffs on imports of each other's goods. Market hopes of an agreement in the near future, following a truce in the summer, were short-lived with several rounds of retaliatory actions following in the latter part of the reporting period. The United States also formally labelled China as a currency manipulator in August after the Chinese renminbi depreciated to above a symbolic ¥7 per US dollar for the first time since 2009. These events sparked a broad sell-off in Chinese equities as well as global stock markets. Conciliatory moves, however, were made in September along with a decision to resume trade talks in October. The US and China reached a partial agreement on the first phase of a deal between the two countries, which included the US suspending the scheduled October tariff increase and China increasing agricultural purchases. The agreement is also believed to cover intellectual property, financial services and currency measures.

Emerging markets received some good news in July when the US Federal Reserve cut its key interest rate for the first time since 2008. A second interest rate cut was subsequently made in September and another after our reporting period in late October. The rate cuts should alleviate upward pressure on US dollar exchange rates, helping emerging market currencies while also facilitating greater flexibility in emerging market monetary policy with several markets including South Korea, Brazil, Indonesia, and Thailand already reducing interest rates. History has shown that over the last four Fed rate cycles, emerging markets have tended to outperform the US market in the 2-3 year period following the first rate cut. The only exception to this was in the run up to the Asian financial crisis in the late 1990s.

Chinese stocks fell over the reporting period as investors focused on the US-China trade conflict and slowing growth in China. However, we believe that China's economy may be better able to absorb the trade issues than the market fears. It is important to note that China's growth is now less dependent on exports than it was a decade ago. China's trade balance with the United States has also narrowed. China's economy has been re-balancing with domestic consumption the key driver of economic growth. In addition to targeted stimulus measures, the government lifted restrictions on foreign investment in China as part of efforts to increase access to its financial markets. The People's Bank of China also implemented an interest-rate reform in August, designating the loan prime rate as the new benchmark for household and business loans, effectively lowering interest rates in August and September. China's second-quarter GDP growth slowed to 6.2%, although the figure was in line with market expectations. We expect the government to continue to focus on economic restructuring and sustainable long-term growth.

South Korea: the South Korean market started the period on a positive note on better-than-expected first-quarter earnings results and a change in the Bank of Korea's monetary policy guidance from a defensively hawkish to a more neutral monetary policy. Escalation in the US-China trade dispute, growing trade tensions between South Korea and Japan, and North Korea's missile launches fuelled investor caution. South Korea's trade feud with Japan heightened as both countries decided to end preferential trade treatment for each other, driving the market down. The central bank cut its key interest rate in July, reversing the rate hike from November 2018 in view of raising growth concerns and a downward inflation outlook. Markets staged a recovery late in the period on the back of the government's record expansionary 2020 budget which was intended to stimulate the economy and cushion the impact of the trade feud with Japan. Improving sentiment in the computer memory sector further supported market sentiment and resulted in equity prices ending the reporting period virtually unchanged. While domestic economic indicators have been weak, expectations for a recovery in the Korean economy are rising on encouraging signs in major industries including semiconductors, shipbuilding and automobile.

Taiwan: Recovery in the technology sector favoured the Taiwanese market where technology-related stocks account for a substantial portion.

Optimism surrounding the government's economic agenda, including the key social security reform, has resulted in a more favourable climate in **Brazil**. While the country's economic recovery has been slower than expected, with the government forecasting the GDP to grow by only 0.85% in 2019, government and central bank efforts could improve the country's longer-term GDP growth potential. Inflation has also remained under control, allowing the central bank to lower interest rates to record-low levels to stimulate the economy. We believe that the approval of pension system reform is key to stimulating investment and credit, which should help improve economic activity, as well as helping significantly to reduce Brazil's fiscal deficit. A major privatisation plan has also been announced, and we expect tax and other reforms that could improve the ease of doing business to follow. Despite the strong market performance over the last 12 months, we remain positive on the outlook for Brazil's market.

Russia was the best performing market in the MSCI Emerging Markets Index over the six-month period and remains one of the most undervalued markets globally, despite its strong performance. Many international investors have avoided this market because of economic sanctions against the country. However, we believe that Russia's fairly self-sustained economy has limited the impact of sanctions. While the economy has proven to be resilient, we have seen many companies take steps to adapt and flourish in the current environment. Moreover, corporate governance in many Russian companies has improved significantly. For example, many companies have increased dividend pay-outs, while others have undertaken share buybacks to improve shareholder value. Overall, we believe that Russia continues to offer interesting opportunities and that exposure to select well-established companies in the financials, energy, materials and communication services sectors should continue to serve TEMIT well.

Indian equity markets experienced some volatility in the earlier part of the reporting period, impacted by uncertainty around the outcome of the national elections, weaker economic growth and global macro uncertainty. While sentiment did turn positive following Prime Minister Narendra Modi's victory with an outright majority for his party, weaker economic growth this year has continued to impact overall investor sentiment. The government surprised investors with a meaningful reduction in India's corporate tax rates to spur investment and boost economic growth. Overall this is positive, with the level of impact differing from sector to sector. For instance, banking would be a key beneficiary as it is a full-tax paying industry. Most consumer companies also benefit from the corporate tax cuts. Overall, the case for investing in India remains strong as fundamentals remain intact. Indian equities are also expected to show resilience to global trade concerns due to less export dependence. We continue to favour companies that can benefit from secular growth drivers such as favourable demographics, infrastructure investment, urban and rural consumption growth and increasing income levels.

The **Argentine** market tumbled during the reporting period amidst increased political and economic uncertainty as the government imposed capital controls and extended the maturities of its debt. We note, however, that market volatility has been largely contained within the country.

Outlook

Emerging markets have been resilient in the face of negative macro events over the last six months but continue to trade at a wide discount to developed markets. We are of the opinion that the underlying fundamentals in emerging markets do not justify these valuations over the longer term, especially since we believe that the long-term structural drivers of emerging markets remain intact.

Emerging markets continue to demonstrate strong economic potential, with undervalued currencies, high foreign exchange reserves and more favourable debt levels than their developed-market peers. Emerging market fundamentals and corporate governance have also been improving. Emerging market cash flows have increased significantly, especially in the last three years, allowing companies to reduce debt ratios, making more yield available to shareholders.

We believe that 2020 could be another strong year for earnings in emerging markets because, based on what we are seeing, a lot of cyclical recoveries have started to emerge, and they should fully materialise in 2020. These conditions, when paired with improving corporate governance that includes dividend pay-outs and buybacks, present an increasingly attractive long-term buying opportunity for investors and contribute to our optimism in the asset class.

Although the US-China trade conflict has been dominating headlines, it should be stressed that the impact of the conflict has not been limited to China; rather we have seen global implications. While the United States and China reached a verbal agreement in October, de-escalating tensions in the short term, we remain cautious and expect continued market volatility until a more comprehensive deal is finalised.

Slowing economic growth expectations, declining inflationary pressures and easing monetary policies in developed markets have generally led emerging market central banks to turn to more expansionary monetary policies to stimulate their economies. In addition to providing a more conducive operating environment for companies, we expect a low-interest rate environment to lead to greater inflows into higher-yielding assets including emerging market equities.

In this environment, we continue to seek companies that demonstrate sustainable earnings power and potential resilience against market uncertainty. Amongst the portfolio's top holdings are technology and consumer-related companies that are highly competitive and appear well-positioned to gain market share even in the face of macroeconomic challenges.

Many emerging market companies are world leaders in the areas of financials, technology and in the production of consumer goods. We are confident that technology will remain a primary driver in emerging markets, whether manifested through world-leading semiconductor manufacturing, e-commerce or other areas. The growing adoption of technology and growth of digital platforms have also helped to create new goods and services for consumers across emerging markets, while at the same time creating growth opportunities for many emerging market companies and investors.

We are of the opinion that consumerism in emerging markets should help to drive growth in many regions. Growing middle-class populations and increasing affluence continue to spur demand for high-end products in emerging markets. In our view, companies with superior products and services should experience sustainable growth in the years to come.

. . . .

John Rennocks, chairman of Utilico Emerging Markets:

We continue to expect populism to rise and influence global agendas. This is likely to result in ongoing volatility in investment markets as political positions harden or in some cases, change sharply. The outcome of the US/China trade talks is now enmeshed in a deeper conflict around technology and security. This heightens the risk of sharp divisions and outcomes are likely to be more volatile. Against this, the world's Central Banks are, for the most part, looking to soften their stance, which should help to moderate the political impact of the populist governments.

. . . .

Asia ex Japan

(compare Asia Pacific funds **here**)

James Will, chairman of Asia Dragon:

Outlook

Sentiment will likely remain subdued as the risks confronting Asian equities remain heightened. The most obvious is the US/China conflict over trade and technology. Signals that both sides are battening down the hatches suggest that an immediate resolution is unlikely. Other geopolitical hotspots are emerging, such as the Hong Kong protests, the Japan-Korea dispute arising from Japan's curbs on semiconductor related exports to Korea, as well as rising tensions in the Middle East. These geopolitical anxieties could further hinder the global economy. Near term prospects for both output and investment are softening.

That said, the fundamentals of most Asian economies are resilient, and policymakers have acted to support growth and liquidity. Central banks' tightening measures in 2018 now appear prescient as it enables them to lower rates as and when required from a higher base. Further easing seems likely given the deteriorating outlook for growth over the months ahead.

In these uncertain times, staying disciplined is crucial. This means looking past the noise and maintaining a focus on quality companies that offer good value.

. . . .

Michael Kerley, manager of Henderson Far East Income:

Overview

Asia Pacific markets recorded a modest gain of 1.7% in Sterling terms over the twelve months to the end of August 2019 as measured by the All-World Asia Pacific ex Japan Index. This return was boosted by the strength of Asian currencies compared to Sterling as markets actually fell by 2.5% in local currency returns over the period. Considering the uncertainty both within the region and globally surrounding politics, trade wars, social unrest, slowing global growth and declining corporate earnings momentum equity markets have proved to be quite resilient. Supportive policies from central banks have helped underpin sentiment but only time will tell as to whether these measures will have the desired effect of reviving economic growth.

In the manager's report last year, I wrote about the trade dispute between China and the US and summarised the escalation as bad for both economies and hoped that pragmatism would reign and a sensible agreement would be reached. Sadly, a year on, the relationship hasn't improved and, despite a series of delays to tariffs being implemented and the odd conciliatory word, the antagonism between the two sides continues to ratchet up. With economic performance in both economies showing signs of trade related deterioration the need for a deal is intensifying, but with both Xi and Trump requiring a 'win' to appease domestic audiences the path to progress is unclear.

It is fair to say that politics has dominated world news in the last twelve months. While the continuing debacle surrounding Brexit has kept UK based investors' attention there have been developments in Asia both positive and negative. On the positive side the re-election of Narendra Modi in India with an increased majority was taken well by the market and reinforces the path of reform that was embarked upon under his first term. In Indonesia the re-election of Joko Widodo, also under a reform agenda, was well received despite some protests from supporters of chief rival and former general Prabowo who disputed the result. The surprise re-election of the ruling liberal party in

Australia also had a positive impact on markets as the expected success of the populist labour party was thwarted at the polls. On the negative side the situation in Hong Kong is cause for concern. The protests, following the attempt by the Hong Kong government to pass an extradition bill to allow suspected criminals to be tried on the mainland, started in June 2019 and are showing no signs of abating. Although the bill has now been officially withdrawn the protests continue with increased vigour as the focus turns toward protecting Hong Kong's freedoms and the fear of greater influence from Beijing. The impact on the Hong Kong economy has been marked with retail sales falling by 23% year-on-year in August which was the worst monthly decline since records began in 1981.

With global and regional growth slowing the outlook for corporate earnings has deteriorated. Earnings growth in Asia Pacific ex Japan is now expected to be low to mid-single digit for 2019, down from solid double digits at the start of the calendar year. The expectations for 2020 have also been revised lower but analysts are still expecting greater than 10% growth - this is likely to come under pressure if economic momentum doesn't improve. The companies most exposed to global trade have been the hardest hit with South Korea and Taiwan showing the greatest earnings deterioration. Ironically China, which is at the centre of the trade dispute, has been more resilient as government measures to increase liquidity and promote consumption have partially offset declines elsewhere.

The best performing market was Indonesia which benefited from the positive election result but also from a 10.0% increase in the currency against Sterling as high real interest rates attracted positive foreign flows. Other ASEAN markets benefited from this trend with Thailand and the Philippines also seeing double digit currency appreciation. The Australian dollar was the only currency which weakened against Sterling over the period as the Reserve Bank of Australia embarked on a series of interest rate cuts to revive the slowing economy, but the unexpected election result plus positive revisions for the mining sector, ensured a better than average return. The worst performing market was South Korea which took the brunt of the slowdown in global trade but also suffered as a spat with Japan, overcompensation derived from the Japanese occupation, resulted in further trade restrictions.

The returns at the sector level were more predictable with a clear divide between the best and worst performers. Export sectors and those exposed to global manufacturing were weak while domestic sectors were more resilient. Oil and gas, materials, industrials and technology all posted negative returns while telecommunications, utilities and consumer staples ended in positive territory.

Outlook

We remain cautiously optimistic on the outlook for Asia Pacific markets. Valuations remain attractive, especially compared to other world markets, and underlying economic growth should prove more resilient than other regions. The weakness in earnings is a concern and a degree of stabilisation is required before becoming more positive on the region as a whole.

The economic performance of China is key to the region's prospects. The world's second largest economy has responded to the challenges of the trade dispute with a pragmatic and proportionate response focused on alleviating the impact of slowing trade without losing sight of the long-term goal to transition from a manufacturing to service based economy. We feel China offers the best combination of growth, value and dividend yield in the region and remains the largest part of the portfolio.

Elsewhere our focus remains on domestic orientated areas which are exposed to the improving spending power of the consumer across the region and away from the export orientated and manufacturing based sectors which are exposed to a slowdown in global growth and an increase in protectionism. Our preference at the sector level is for

consumer related areas, property and telecommunications while avoiding commercial banks and high-priced technology.

Despite slowing earnings, the outlook for dividends in Asia Pacific is still the most compelling story. Asian companies have low levels of debt, a pragmatic view on capital expenditure and strong cash flow generation which should allow dividend pay-out ratios to rise in the years ahead.

. . . .

Manager's report for Schroder Oriental Income:

Review

Although regional markets ended the financial year in positive territory, this was thanks to the weakness of sterling in the last four months of the year amid rising speculation over a no deal UK exit from the European Union. The underlying reality is better represented by performance in US dollar terms in the chart above. Regional markets staged a strong rally early in 2019 from the depressed levels of December, spurred by a more accommodative stance from the US Federal Reserve. Since then, they have lacked more tangible sources of support. Outside the United States, global economic expectations continued to soften, global trade stagnated and corporate earnings revisions remained in negative territory across the region.

Politics also weighed on sentiment. The China-US disagreements have dominated the headlines, with concomitant impact on corporate confidence and investment. The varying perceptions of trade progress (or lack of it) caused significant market volatility through the period. In addition, the street protests in Hong Kong have materially impacted the domestic economy with retail sales and tourist arrivals falling sharply as the summer progressed. Less prominently but not helpful, Korea/Japanese relations have cooled due to a dispute over culpability for World War II atrocities.

With the notable exception of Malaysia, emerging ASEAN markets were leading performers, with the markets seen as less sensitive to trade and benefitting from increased scope to ease monetary conditions given quiescent inflation and relatively high real interest rates. Australia and New Zealand also performed well given their defensive characteristics and high yield stocks were notably strong at a time of interest rate cuts by their central banks. Korea suffered as its key exports fell sharply and the administration has pursued a populist agenda. Malaysia suffered as initial optimism surrounding the end of five decades of United Malays National Organisation leadership faded.

Outlook

It is difficult to regard recent global macro and political developments as having been supportive of either equity markets or investor sentiment. Global political developments have dominated the front pages in Asia, but have scarcely been absent closer to home. The broad threads to these tensions could be viewed as the nexus between populism and resentment at perceived widening of wealth disparities. Whether related or not, economic trends have softened, with retracement in global sentiment indices, soft private capital spending in a number of countries, and slowing global trade growth.

The growth scare has been given further credence by the flattening/inversion of yield curves worldwide. The historic evidence linking this to inevitable recession is ambivalent, but increasingly desperate measures from central banks (at least outside the US) to support growth smack of panic that may do more harm than good. Albeit circumspectly, we do not sit in the recession camp, and indeed are inclined to feel that many cyclical growth sectors and stocks offer the most attractive medium-term prospects. In contrast, defensives and bond proxies seem inordinately rewarded for income generation and their perceived stability.

Softening global sentiment indices, sluggish trade volumes, and supply chain disruption are obvious impediments for Asian markets. Aside from the political noise, it would also be true to say that more domestic stimulus attempts have been pretty half hearted. China remains notably disciplined despite excitements surrounding the recent National People's Congress meetings, and activity elsewhere is far short (mercifully?) of European-style policy panic. Short term growth numbers are undoubtedly being distorted by inventory build ups/drawdowns surrounding tariff increases (and indeed cancellation/deferment thereof). It is also undoubtedly affecting investment decisions; bad news short term, but this suggests that there is strong pent-up demand in industrial investment and related areas.

The situation in Hong Kong is obviously of concern as it remains a substantial exposure for the company, with real estate and financials particularly vulnerable should confidence in stability be permanently impaired. While respecting the political motivations behind the protests, there is also an economic backdrop as the squeezed middle classes articulate their dissatisfaction. The local administration has considerable fiscal fire power should they elect to use it, while strong corporate balance sheets should provide some re-assurance as to shareholder returns.

As we have said before, we believe current dividend payment levels in Asia are generally well supported given strong cash flows, conservative capital spending intentions and strong balance sheets. More doubt surrounds the likely level of growth we can expect. Markets have, probably correctly, written off hope for much earnings growth in calendar 2019, but expectations look too sanguine for 2020, and this will feed through to dividend outturns. Many pieces of the jigsaw for recovery might fall into place (trade truce, recovery in Western economies, re-stocking, a return of corporate confidence) but these are not our central expectation.

. . . .

Latin America

(compare Latin American funds here)

Richard Prosser, chairman of Aberdeen Latin American Income:

Overview

Latin American markets delivered strong returns during the year under review. Equities were volatile yet ended as one of the best performing emerging markets over the period, while bond markets had comparable returns. Despite global uncertainties and trade worries, domestic events played a larger role in shaping the trajectory of the markets in the region. Most notably, the Brazilian equity market single-handedly pulled the region into positive territory. This was largely due to the positive election outcome and policy developments. Conversely, the Mexican market fell on deteriorating economic activity and Argentina suffered a late decline after unexpected primary election results which gave left-wing candidate Alberto Fernandez a stronger chance of winning the presidential race.

A few key themes stood out over the past year, none more so than elections. Two of Latin America's largest economies, Brazil and Mexico, elected new presidents. In Brazil, stocks rebounded on Jair Bolsonaro's win in October, and maintained its upward momentum on encouraging prospects that the proposed pension reforms will be approved. Mexico's President Andrés Manuel López Obrador's (AMLO) win brought uncertainty around policy making and economic growth. The new government's controversial decisions on key infrastructure projects, based on unconventional public referenda and its interference in banking policies hampered sentiment.

The US-China trade war unsettled markets and, in Mexico, uncertainties over the US-Mexico-Canada Agreement (USMCA) kept investors guessing. Tensions with the US rose as Washington DC threatened to close the border with Mexico over illegal migration issues. However, negotiations are underway to resolve this and ratify their trade agreement.

Monetary policy also played a major role during the review period, as initial tightening was replaced by the US Federal Reserve's (the "Fed") easing amid global growth concerns. The Fed lowered rates in July; Mexico followed with its first interest rate cut in five years and the government planned to inject US$25.5bn in stimulus via infrastructure projects and the private-sector. Brazil, Peru and Chile also cut rates amid benign inflation, to boost their weakening economies.

Outlook

I remain optimistic about the outlook for Latin American equities amid encouraging regional developments.

Mexico was the first country to ratify the USMCA trade agreement - its final approval by the US and Canada could boost sentiment. Moreover, investors remain optimistic that Brazil's pension reform bill will be approved. President Jair Bolsonaro's administration has shown resolve in pushing for fiscal and structural changes. Such reforms, along with lower interest rates, are expected to attract investments and create jobs, which should fuel the economy.

However, there is some room for caution amid weak global economic conditions and the ongoing trade war. As such, lower demand globally could also result in a further decline in commodity prices. In Mexico, investors remain watchful over political developments with particular focus on the current administration's economic policies, and its stance towards the private sector. Meanwhile, Argentina's outlook remains uncertain as it focuses on stabilising the exchange rate and reducing inflation, while restructuring its debt.

India

(compare country specialist: Asia Pacific ex Japan funds here)

Manager's report for Aberdeen New India:

Overview

Indian equities were flat in the six months under review. Nevertheless, compared to the wider Asia Pacific ex Japan region, which fell against a backdrop of a slowing global economy and heightened trade tensions, they proved resilient.

The re-election of the Bharatiya Janata Party with a larger than expected majority initially lifted the market as it signalled continuity of government policies. However, surprise tax hike proposals announced during the Federal Budget, together with a lack of any stimulus package to boost consumption, rattled investors and pared back these early gains. Throughout this period the financial storm in the shadow banking sector continued to rumble on, dampening the performance of financial stocks, as credit growth moderated and liquidity tightened. In particular, the default by non-banking financial company ('NBFC') Dewan Housing Finance Corporation and then fraud allegations against small lender Punjab and Maharashtra Co-operative Bank, renewed investor concerns.

In response, the Reserve Bank of India cut rates five times and proposed stricter regulations for NBFCs. The government unveiled measures to support investor and

consumer sentiment including the consolidation of public-sector banks. To combat a slowdown in auto sales, it also deferred the increase in new registration fees and encouraged the scrapping of old vehicles. Near the end of the review period, stocks clawed back some losses, as the government slashed corporate tax rates. The stimulus measures propelled consumer staples stocks to put them among the biggest gains for the year while healthcare equities lagged the most.

Outlook

In the near term, concerns over the liquidity and solvency of the shadow banking sector, as well as slowing domestic growth and global macroeconomic uncertainty, will continue to affect the market. These factors were reflected in the cautious note struck by many of the company's holdings for the short term in the most recent earnings reporting season. On a brighter note, above-average monsoon rains will likely boost rural incomes and, along with the recent Diwali festival, bode well for consumer spending. Recent corporate tax cuts have made valuations more attractive, and will help support a recovery, particularly in the financials and consumer staples sectors.

Notwithstanding its present challenges, India still has many structural drivers of long-term growth. It maintains a big domestic economy and an entrepreneurial culture. Furthermore, it stands to benefit from still-low oil prices and multinationals looking to relocate their factories out of China to avoid US trade tariffs. Its prowess in computer engineering makes it an increasingly important force as industries, ranging from automotive to finance, embrace digitalisation.

. . . .

Flexible investment

(compare flexible investment funds **here**)

Manager's report for Caledonia Investments:

Investors have witnessed ongoing pricing volatility over the past year in both fixed interest and equity markets. These swings are often instigated by the pronouncements of central bankers who, in the US, raised interest rates and then dropped them again, whilst the European Central Bank has continued to pump huge amounts of liquidity into markets in an attempt to stimulate life into a moribund economy. Prices remain at extended levels and great care needs to be taken when purchasing assets, especially in competition with those with seemingly bottomless pockets. When one reads reports of fixed interest investments being purchased at a price that guarantees a loss of capital at redemption, no further evidence of the misallocation of capital is required.

. . . .

Alexander Barr, James de Bunsen and Peter Webster, managers of Henderson Alternative Strategies:

The continued deterioration in key global economic indicators remains a concern, and unsurprisingly recessionary fears are at their highest for many years. Added to these are concerns over increasing debt levels, ongoing uncertainty over China / US trade and from a UK domestic perspective, deep unease on the impact that the ongoing Brexit impasse has had on investment and confidence. We do not intend to add further to the debate, in what remains a rapidly changing situation, however we believe that any negative economic impact from a potential 2020 Brexit on our global alternatives portfolio should be contained.

That is not to say the portfolio is immune from unexpected events, for example a surprise UK election win for Labour.

Public equity market performance continues to be exceptionally strong and year-to-date the S&P 500 is up 22.9%, the EuroStoxx 50 up 17.4%, and China's Shanghai Shenzen CSI 300 up 24.8%[6]. Even the All-Share is up 10.9%. Much of this has been driven by the availability of cheap money and by the rise of government spending to compensate for economic softness. At some stage though, such support has to slow or come to an end. This team's central expectation is that growth continues to soften and equity volatility increases and we believe the portfolio to be well positioned to weather such a change in conditions.

Areas which look attractive to us currently include secondary portfolios in private equity (and which can often be purchased at discounts to fair market value), certain private debt opportunities and also the increasing number of ways in which royalties from intellectual property can be accessed. Many of these opportunities come in both listed and private form.

. . . .

Sebastian Lyon, manager of Personal Assets:

Despite the modest fall in the FTSE, the environment has been relatively supportive amid falling bond yields and a resilient US stock market. Sterling's rally from its early September lows has been a headwind, although most of our US dollar exposure is hedged back into sterling.

We have had a longstanding preference for medical device companies over pharmaceuticals for their consistency of returns and lack of exposure to patent expiries. Demand for medical interventions such as stents and heart valves has grown steadily as populations in developed countries get older and emerging markets modernise healthcare provision.

Since the end of August there has been a resurgence in structurally challenged or cyclical 'value' stocks, including those confronted by ongoing technological change and the erosion of pricing power. An upturn in the global economy could support a more sustained period of positive performance for such businesses, but as yet we see few signs of it. We have experienced these bouts of stock market rotation before, most recently in late 2016 and early 2017. Such snap-backs usually throw up opportunities for us in our favoured sectors and enable us to increase the company's equity allocation.

As regards specific political events such as Brexit, the UK general election or the US 2020 presidential election, short-term tactical decision-making is likely to fail.

. . . .

Debt

(compare debt funds **here**)

Manager's report for Alcentra European Floating Rate Income:

Outlook

Credit markets performed strongly in the first nine months of 2019 as prices rebounded from the Q4 2018 weakness. The more volatile credit markets performed particularly well after trading lower in Q4 2018, with US loans up 6.39% and Euro High Yield, which also benefited from a change in rate expectations, up 9.22%. The Credit Suisse Western European Leveraged Loan Index (CS WELLI) (hedged to EUR) returned 3.81% for the same period.

We continue to expect solid issuance for the full year at €70bn to €80bn, albeit lower than the €96bn level seen in 2018 due to the quieter start to the year. Issuance is expected to remain robust given private equity sponsors still have excess capital to put to work, however we do not expect as many jumbo deals as were seen in 2018.

On the demand side we expect appetite for European loans to remain solid. We expect the CLO market, a large part of the European investor base, to see continued robust issuance, aided by the recent tightening of the cost of leverage (particularly AAA spreads).

We continue to expect low default rates and we would anticipate 1.5%-2.0% over the medium term. There remains some scope for volatility with Brexit, trade negotiations, global growth concerns, QE and political developments all likely to feature in the headlines.

However, we would still expect the core European Loan market to continue to be relatively well insulated in comparison to other asset classes. New CLOs, unlevered loan funds and to a lesser extent banks, will all continue to drive demand and the underlying, senior secured borrowers are more resilient to the macro factors mentioned above.

. . . .

Manager's report for TwentyFour Income:

Market Commentary

The key themes that have driven wider market sentiment year-to-date, continued throughout the period, with central bank policy and the trade tariff dispute dominating the markets; while Brexit uncertainty remained heightened.

Sentiment in the European ABS market continued to improve throughout the month, with the Brexit extension adding to the support and following the successful refinancing of the large legacy Northern Rock mortgage portfolio transaction in March. The strong technical support remained due in part to a fairly limited issuance in Q1, which was not focused in any particular sector but spread across a diverse array of credits. The UK market also saw its first Prime STS RMBS deal from Nationwide, which drew very strong demand. The deal was also notable as it was the first publicly placed deal in the market referencing Sonia as the index, as opposed to Libor. The transition of UK issuers who migrated to the Sonia index increased during the period, which had been expected, as the Bank of England encouraged and continues to encourage a move away from fixing to Libor; which is due to be phased out at the end of 2021.

May saw fairly light supply in primary issuance at the beginning of the month, with spreads continuing to grind tighter across most asset classes; albeit at a slower pace. As the month progressed, the market saw multiple new issues being announced, culminating in what was the busiest two weeks of the year in ABS markets. Throughout the month the tone of the market was positive despite the "risk-off" tone in wider credit markets, and although there was more supply, the levels of oversubscription and pricing being at the tighter end of the range suggested that the supply was not sufficient to fill investor demand. Secondary activity remained fairly quiet at the start of the month with fairly balanced flows, and spread levels remained broadly unchanged. However, supply picked up steadily as the month progressed and we started to see a little weakness seep into the ABS market, as broader volatility and wider Crossover and Main index spreads started to feed into dealer pricing at the end of the month. Primary CLO issuance was slower over the month compared to April, and although CLO spreads continued to lag the credit and loan markets, overall year-to-date performance, particularly in the AAA and mezzanine space, remained positive. Some of the focus on primary deals was at the shorter end, as we saw a pick-up in CLO refinancing deals

and continued to see a steeper tiering on a spread basis develop between manager, maturity and tranche rating.

Markets rallied across the board in June, with both “risk-off” and “risk-on” assets posting positive returns, as the Fed seemed to pacify the markets’ call for lower rates, and the rhetoric relating to the US-China trade standoff eased during the month. As a result, 10-year US Treasury yields dipped below 2% for the first time since 2016, and European government bonds hit record low yield levels, while all major equity indices were up on the month. The key event in Europe was the ECB meeting where outgoing president Mario Draghi delivered a particularly dovish speech, stating that the ECB stood ready to act with additional stimulus if the outlook in Europe did not improve. This naturally led to a strong rally in both European government bonds and credit.

The positive macro sentiment filtered through to the European ABS market throughout June, although a combination of heavy secondary offerings and consistent primary issuance at the end of May and early June weighed on spreads, and volatility remained elevated. Secondary flow was respectable with decent liquidity provided by dealers, and once the broader macro picture recovered in wider markets, we saw more balanced flows in the ABS space, with buyers returning to the secondary market as the month progressed; leading to a compression in spreads. CLO secondary market supply was also quite heavy in the first part of the month, which was mainly attributable to rotation into primary, profit taking from Q1 and realisation of CLO outperformance in May. Again a lot of the liquidity was provided by dealers, but this still led to a dispersion in clearing levels of around 5-10 bp in mezzanine bonds on ‘tier one’ managers and slightly wider for ‘tier two’. In the latter part of the month there was a better tone with a strong pick-up in two-way flows leading to a compression in spreads, particularly in mezzanine bonds.

The momentum of primary ABS issuance continued unabated throughout July against a fairly benign macro market backdrop. With low levels of volatility, most deals were placed at the tighter end of guidance with decent levels of oversubscription in mezzanine bonds in particular. One or two deals found the going a little tougher – typically those from less vanilla asset classes, but were fully placed once the pricing terms were adjusted to more attractive clearing levels. The pace of issuance in CLOs led to spreads being a little weaker in the mezzanine tranches, which was understandable given the amount of supply. This was in contrast to AAA CLO spreads, which contracted by around 5bp over the month, highlighting the compelling relative value of the asset class versus other investment grade credit, particularly once the heightened value of the Euribor floor is taken into account following the movement in the swap curve; also reflecting the attraction for yen and US dollar based investors. The deeper mezzanine spreads have been driven more by the manager and the quality of the underlying portfolio. Secondary spreads in the wider ABS market generally held in well over the month, trending sideways as opposed to widening in the face of heightened primary supply.

At a macro level, August was far from the subdued market activity normally associated with this time of year. Escalating trade wars, geopolitical events and deteriorating economic data combined to create a more vulnerable backdrop to risk markets and a relentless rally in government bonds, resulting in all developed economy government bond markets ending the month sharply tighter. As is often the case when broader markets are volatile, and particularly given the summer recess, the European ABS market was typically very quiet with virtually no primary public issuance. As a consequence, spread movement over the month in the UK market was a little mixed, widening in sympathy with broader markets in the first part of the month, negligibly in the case of AAAs but a little more in mezzanine bonds. Some modest tightening occurred in the latter part of the month on the back of improved sentiment and falling yields in rates markets; albeit, based on very low traded volumes. In contrast euro

denominated ABS spreads held in better as some sectors saw modest tightening, and this was reflective of lower supply, the ongoing impact of the falling euro swap curve and a more stable geopolitical backdrop.

Following the typical summer lull for ABS primary issuance, the market bounced back in September with a wide range of deals priced. Issuance over the month grossed around €9bn, a cumulative total of around €71bn year-to-date, which is at this point, almost at the same level as this time, last year. Another positive factor was an increase in the amount of mezzanine bonds available in new issues, giving more opportunity to add incremental yield. Subscription levels were very strong across all transactions, particularly in mezzanine bonds, and all tranches were priced at the tighter end of initial guidance.

Outlook

Geopolitical events, central bank policy and Brexit remain in the background and will continue to play a part in the ongoing spikes in volatility as and when they are imported to the ABS market, to varying degrees.

A large post-summer primary ABS pipeline has been absorbed by the market, with relative ease, confirming that investor sentiment remains strong with a large amount of cash being available on the side-lines. We expect to see further supply over the final quarter of the year and the backdrop suggests this will continue to be well received subject to structure and pricing.

Current elevated spreads in the UK ABS market will likely be an effective defensive holding against the deep uncertainty around the Brexit outcome, and could ultimately also offer some spread upside, given the high level of fundamental credit protection within the structures.

Leasing

(compare leasing funds **here**)

Manager's report for Doric Nimrod Three:

Market Overview

According to the International Air Transport Association (IATA), industry-wide passenger traffic, measured in global revenue passenger kilometres (RPKs), grew at a rate of 4.7% between January and July 2019 against the same period in the year before. Growth in RPK has been running below the long-term average rate of 5.5% and IATA expects an annual growth of 5.0% for this year, largely due to declining growth in the Asia Pacific region. IATA notes that this slower growth trend is likely to continue against the backdrop of weaker growth in several large economies and a pick-up in global risks.

Industry-wide capacity, measured in available seat kilometres (ASKs), increased by 4.1% between January and July 2019 versus the first seven months of the previous year, resulting in a 0.5 percentage point increase in the worldwide passenger load factor (PLF) to 82.6%. So far in 2019, all regions have recorded modest capacity growth and high load factors with July's PLF of 85.7%, a new all-time high for any month of the year.

Passenger traffic in the Middle East increased by 1.5% between January and July 2019 against the same period in the previous year. Capacity grew by 0.7%, which resulted in a 0.7 percentage point increase in PLF to 76.0%. IATA's seasonally-adjusted data show a clear levelling off in passenger traffic volumes since the first half of 2018. This

is attributable to the weakness in global trade, volatile oil prices and heightened geopolitical tensions.

European-based operators continue to be the top performers in overall market demand so far in 2019, as RPKs increased by 5.6% compared to the same period in the previous year. Latin America ranked second once again with 5.2% followed closely by the Asia Pacific region with 5.1%. Africa experienced an increase of 4.9% while North America saw positive growth at 4.0%.

Lessee - Emirates Key Financials

In the 2018/19 financial year ending on 31 March 2019, Emirates increased revenue by 6% to AED 98bn (USD 26.7bn) compared to the previous financial year. However, as operating costs rose by 8%, Emirates' net profit fell nearly 70% compared to last year to AED 871m (USD 237.3m). The decrease in profit was attributed to higher fuel prices, strong competition, and unfavourable foreign exchange effects.

Emirates overall passenger traffic grew marginally during the 2018/19 financial year with the airline carrying 58.6m passengers. Passenger traffic, measured in RPKs, increased by 2.7%, while capacity, measured in ASKs, grew by 3.6%. This resulted in a passenger load factor of 76.8% compared to last year's 77.5%.

The rise in total operating costs was largely due to increasing fuel prices, which grew 22% over the financial year. This came on top of the 15% increase in fuel prices during the previous year. Fuel continued to be the largest cost component, making up 32% of the airline's total operating costs. Additionally, Emirates saw an AED 572m (USD 155.9m) negative impact on its financial results due to the strengthening of the US Dollar against many revenue generating currencies.

As of 31 March 2019, Emirates' balance sheet amounted to AED 127.4bn (USD 34.7bn), largely flat compared to the end of the previous financial year. Total equity increased marginally by 1.9% to AED 37.7bn (USD 10.3bn). The equity ratio remained stable at 29.6%. The airline's cash balance amounted to AED 17.0bn (USD 4.6bn) at the end of the financial year, down by AED 3.4bn (USD 921.8m) compared to the end of the previous financial year.

In the 2018/19 financial year, Emirates received 13 new aircraft - seven A380s and six Boeing 777-300ERs - and retired 11 older aircraft, bringing its fleet total to 270 as of 31 March 2019, including 12 freighters. The fleet roll-over resulted in an average fleet age of 6.1 years. In February 2019, Emirates signed a heads of agreement with Airbus to order 40 A330neos and 30 A350-900s to be delivered from 2021 and 2024 respectively. At the same time, it adjusted its A380 order book position and will receive 14 more A380s from 2019 until the end of 2021, taking the total number of A380s delivered to Emirates to 123 aircraft. Emirates' latest report, however, omitted the USD 15bn agreement for 40 Boeing 787-10 from the 2017 Dubai Air Show, which had previously been included in its 2017/18 financial report.

Emirates' half-year results for 2019/20 are expected to be released in November 2019. According to Tim Clark, the airline's president, uncertainty over the status of key widebody programmes is preventing Emirates from revamping its orders with Airbus and Boeing. Delays in Boeing's 777X programme with Emirates as launch customer have prevented the airline from entering into discussions around contract adjustments or introducing new aircraft to existing

deals. Additionally, Emirates has delayed the firming up of its deal for A330neos and A350s, both of which are exclusively powered by Rolls-Royce, due to concerns about the engines' ability to meet its specific performance requirements. Setbacks in Rolls-Royce's programmes have led Emirates to demand definitive guarantees for trouble-free performance "from day one" before the airline will commit to any further orders.

Weeks before Emirates concluded the first six months of its 2019/20 financial year ending on 30 September 2019 Tim Clark provided some guidance on the expected financial results: "I'm pleased with our performance to date." At the same time, he sees "difficulties" on multiple fronts including demand issues in South America with the collapsing peso in Argentina, challenges in Asia with the unrest in Hong Kong and the Brexit discussions in Europe. Emirates had also to manage the closure of one of its two runways at the airline's Dubai hub due to maintenance for a period of six weeks. Clark was in particular pleased with the operation to London, Emirates strongest A380 destination outside its Dubai hub, reporting a 93% load factor on the nine daily A380 flights the airline runs out of London Heathrow and London Gatwick. The latter airport is serviced by A380s with a 615 seat high-density configuration.

Aircraft - A380

As of mid-September 2019, Emirates operated a fleet of 108 A380s, which currently serve 52 destinations within its global network via its hub in Dubai. A380 destinations include: Amsterdam, Athens, Auckland, Bangkok, Barcelona, Beijing, Birmingham, Brisbane, Casablanca, Christchurch, Copenhagen, Dusseldorf, Frankfurt, Guangzhou, Hamburg, Hong Kong, Houston, Johannesburg, Kuala Lumpur, Kuwait, London Gatwick, London Heathrow, Los Angeles, Madrid, Manchester, Mauritius, Melbourne, Milan, Moscow, Mumbai, Munich, Muscat, New York JFK, Nice, Osaka, Paris, Perth, Prague, Riyadh, Rome, San Francisco, Sao Paulo, Seoul, Shanghai, Singapore, Sydney, Taipei, Tokyo Narita, Toronto, Vienna, Washington, and Zurich.

Also, as of mid-September 2019, the global A380 fleet consisted of 231 planes in commercial service. The fourteen operators are Emirates (108), Singapore Airlines (19), Deutsche Lufthansa (14), Qantas (12), British Airways (12), Korean Air Lines (10), Etihad Airways (10), Air France (10), Qatar Airways (10), Malaysia Airlines (6), Thai Airways (6), Asiana Airlines (6), China Southern Airlines (5), All Nippon Airways (2) and Hi Fly (1). Another six aircraft are listed as in storage, including four from Emirates, which were parked at Dubai-World Central International airport.

During the period under review the first two A380 part-outs have been initiated by Dr Peters Group, which estimates USD 45m in revenue per aircraft from component sales alone due to the demand for parts from existing A380 operators preparing for upcoming maintenance events. Dr Peters estimates a total revenue as high as USD 80m per aircraft. The engines are currently leased to Rolls-Royce through 2020, after which Dr Peters intends to sell the engines. The aircraft owned by the company have Engine Alliance (EA) manufactured engines. In the event that these aircraft are parted out, it is not certain that the engines can be leased and the parts will be subject to market prices at that time.

Since 1 July, Emirates has been operating its shortest A380 route at just 340km (184nm). Twice-daily flights between Dubai and Oman's capital Muscat with A380s replacing the Boeing 777-300ERs, which served the route before. The announcement came a month after the launch of A380s operations on another short route between Dubai and the Saudi Arabian capital Riyadh (870km, 470nm). Emirates' shortest regular route for the A380 was previously Dubai-Kuwait, which covers a distance of roughly 850km (460nm). Emirates stated, "The new A380 services to Muscat demonstrate the airline's agile approach to fleet deployment and its commitment to providing an enhanced on-board experience for its passengers".

In July, Air France announced that it intends to retire its entire Airbus A380 fleet by 2022 and is studying options to replace the double-deck type with twinjets. The airline had previously announced plans to retire at least three of its 10 A380s, but has now approved "in principle" the retirement of the remaining aircraft. Five of the aircraft are owned by Air France, while the rest are on operating leases.

At the end of July, Flynas announced that it operated its first Haj pilgrims flight on A380s wet-leased from Malaysia Airlines. The Saudi carrier anticipates transporting 200,000 pilgrims from 17 countries.

In September, the Portuguese wet-lease operator Hi Fly confirmed its plans to acquire additional second-hand A380 aircraft. Chief executive Paulo Mirpuri stated, "as more A380s become available, we will be taking more aircraft", further adding that the market would "say how many". The operator's current A380 has mainly been used for transatlantic flights, but has also been deployed on routes to South America, Indian Ocean destinations and during Operation Matterhorn involving the repatriation of Thomas Cook holiday makers back to the UK.

Also, in September, Emirates' president Tim Clark stated that the airline is conducting a review of its fleet and network structure as it plans to start a gradual retirement of the A380 from its fleet. Noting that "this aircraft will still be flying in Emirates in 2035" Clark expects Emirates' A380 fleet to peak shortly and then stabilize at around 115 aircraft, before declining to about 90-100 by the mid-2020s. Two Emirates-owned A380s are earmarked to be withdrawn from service shortly and will serve as a spares source to meet upcoming overhaul requirements for its operational fleet. According to Tim Clark, the A380 will remain a pillar of Emirates' fleet mix for the next 15 years. However, Emirates has dropped plans to install new first class suites on its A380 aircraft, but will introduce new premium economy seats on its A380s towards the end of next year.

. . . .

Biotech and healthcare

(compare biotech and healthcare funds **here**)

Geoff Hsu and Richard Klemm, managers of Biotech Growth:

Market review

The biotechnology sector underperformed the broader market during the review period. We attribute sector weakness to general macro concerns about the economic outlook and concerns about the potential for drug pricing regulation, particularly in light of the upcoming 2020 U.S. presidential election. These concerns resulted in a net outflow of approximately U.S.$7.5bn from biotechnology/healthcare funds during the review period. Much of the underperformance was concentrated in small and mid-capitalisation biotechnology companies, which previously had performed strongly. We view this more as profit-taking rather than a deterioration in fundamentals.

The broader economic backdrop has become more uncertain as U.S. investors have become increasingly concerned about a potential recession in the U.S. These concerns have increased as the retaliatory tariff war between the US and China has escalated, which has slowed the pace of economic growth. Although the biotechnology sector has low direct exposure to trade flows, the resulting economic uncertainty has weighed on shares as we saw a general shift in funds from growth to more defensive sectors in the latter part of the review period. Biotechnology, which is considered a growth sector, fell in tandem with this broader market shift.

More specific to the biotechnology sector, concerns over the direction of healthcare policy in the U.S. have created some investor caution. Policies have been proposed by both the Trump administration and Congress that could adversely affect drug pricing, such as implementing international reference pricing for Medicare drugs, permitting drug reimportation, instituting inflation-based price caps on drugs, and allowing Medicare to negotiate prices directly with biopharmaceutical companies. Thus far,

these proposals have not been implemented. We believe that the current Congress is unlikely to act in a meaningful way. Nevertheless, drug pricing rhetoric from both President Trump and the Democratic presidential nominees continues to be an overhang for the sector. As of the time of this writing, Elizabeth Warren, one of the more progressive Democratic presidential candidates, has been gaining in the polls for the Democratic nomination versus former Vice President Joe Biden, who is regarded as more centrist in his outlook. Warren is viewed as more antagonistic to the drug industry compared to Biden, and her ascendance in the polls led to increased share weakness in biotechnology towards the end of the review period. Our view on the political situation remains the same. We do not expect any dramatic changes to drug pricing policy even if a Democrat is elected President in 2020 because we expect a split Congress, with Republicans controlling the Senate and Democrats controlling the House. This would effectively prevent any extreme legislation from passing after 2020. We view Medicare for All, an idea espoused by Warren which would create a single-payer government-run health system with no private insurance, to have virtually zero chance of being enacted even in the case of a Democratic sweep in the 2020 election. Even moderate Democrats would likely oppose such a disruptive proposal, not to mention the significant opposition it would face from Republicans and industry stakeholders and the formidable political barriers to raising the necessary taxes to pay for it. Ultimately, we expect any new reform to be manageable for the industry, but the uncertainty during the election season may continue to weigh on sentiment.

Notably, from a valuation perspective, the major biotechnology companies continue to trade at historically low price to earnings ratios, many in the single digits, with share prices already discounting fears over the macro drug pricing environment. In previous instances when political headlines and rhetoric about drug pricing have depressed share prices for the biotechnology sector (e.g. Hillary Clinton's tweet on drug prices in the fall of 2015, and debates over Obamacare), the sector has staged a relief rally when the episode has passed, and no material change to drug pricing policy has taken place. We expect the same recovery once the current spate of drug pricing rhetoric passes as well.

Re-emergence of Targeted Therapy

Despite the headline noise from the US election campaign, the fundamentals of the biotechnology industry remain strong. The regulatory stance at the U.S. Food and Drug Administration (FDA) remains proactive with regards to expediting new drug approvals, even after the transition from former FDA head Scott Gottlieb to acting head Ned Sharpless earlier this year. Innovation remains strong, and new technologies such as gene therapy, cell therapy, RNA-based therapeutics, and bispecific antibodies are still in the early stages of reaching their full potential. These technologies are resulting in marketed products that could unlock multi-billion-dollar revenue opportunities.

One area of innovation we would like to highlight is the re-emergence of targeted therapies for cancer as a focus area for biotechnology investors. This precision medicine approach aims to personalise cancer therapy to treat patients based on specific genes or pathways that are mutated. First-generation tyrosine kinase inhibitors (TKIs) have produced dramatic clinical results across a variety of tumour types in subsets of patients defined by the genetics found in their tumours, though broadening the applicability of such targeted approaches to additional patients has remained dependent on a better understanding of tumour biology and the development of specific drugs. Improvements in genetic sequencing capabilities over the past decade has enabled better identification of the mutations driving cancer growth, and genetic information for a patient's specific cancer is now becoming better integrated into patient care. This has led to a profound improvement in patient outcomes, which we expect to continue to advance in the coming years.

We see the targeted therapies for cancer as a clear success for precision medicine approaches and believe that this field will continue to generate therapies that are increasingly personalised and tailored to the specific disease characteristics of the patient. Large pharmaceutical companies continue to be interested in this field, as evidenced by the recent acquisition of targeted therapy company Array Biopharma by Pfizer.

Outlook

As we have previously highlighted, the biotechnology industry is at an important inflection point as new platform technologies spur innovation and make more diseases amenable to treatment. Although the backdrop of election year politics may continue to hurt sentiment for biotechnology and healthcare stocks in general, we believe over the longer term, the fundamental strength of the biotechnology industry will drive strong returns.

. . . .

Manager's report for Syncona:

We see a rich pipeline of opportunities around to found new companies with the ambition of taking products to market, including across areas such as gene therapy, cell therapy, small molecules and biologics.

. . . .

Sven H. Borho and Trevor M. Polischuk, managers of Worldwide Healthcare:

Sector developments:

Overwhelmingly so, the overall fundamentals of the healthcare industry remain positive. The secular tailwind is as strong as ever, from more people (from global population demographics), more innovation (from unparalleled technological advancements), more drugs (from record number of approvals), and more money (from increasing gross domestic spend on healthcare). Simply put, the demand for healthcare continues to rise on a global basis.

Undeniably, we remain at a peak era of innovation in the biopharma industry. The genomic revolution at the turn of the century is now ripe enough to be producing more treatable targets than ever before. Drug development is more sophisticated and has resulted in less attrition in later stages than previously seen, and the number of platform technologies continues to expand. Gene therapy, cell therapy, next generation targeted therapy, immunotherapy, antibody drug conjugates, bispecific antibodies, and novel small molecule receptor/ligand science are just some of ways in which unmet medical needs are being satisfied using today's modern medicine.

The U.S. Food and Drug Administration (FDA) has just had another record year for new drug approvals. 2018 marked the second consecutive year in which the Agency has approved a record number of new molecular (or biological) entities, with 59, smashing the 2017 record of 46. Also of note, the Agency approved a record number of generic drugs in 2018, eclipsing the newly set record in 2017. As of the end of September 2019, the run rate for expected approvals in 2019 was 47 (source: Washington Analysis). Whilst a third straight record setting year seems unlikely, it is clear that new product flow in the industry is at unprecedented levels.

The unexpected resignation of FDA Commissioner Scott Gottlieb in early 2019 was disappointing. Health and Human Services named Ned Sharpless, head of the National Cancer Institute, the acting Commissioner in April 2019. Already an appointee of President Trump and vetted by Congress, we believed Dr. Sharpless was the leading candidate to become the next head of the FDA. However, news reports out of Washington D.C. in early October 2019 suggested that President Trump may nominate

oncologist Dr. Stephen Hahn, who currently serves as the chief medical executive at MD Anderson Cancer Center in Houston, Texas. Regardless, the FDA has established unprecedented levels of efficiency, modernisation, and collaboration and has never been more aligned with the bio-pharma industry to get new drugs approved. We expect the career staffers to carry on this current culture of achievement, regardless of who may become the next commissioner.

M&A remains a constant theme for healthcare stocks. Whilst the exact pace may ebb and flow due to a variety of factors, the continued take-out of small and mid-capitalisation biotechnology stocks by their large capitalisation bio-pharmaceutical peers continued in 2019. Whilst the IPO and secondary market has been "hot" in 2018 and 2019, we have continued to see these deals. Most recently, 2019 has been witness to the return of the "mega merger", with the close of Takeda Pharmaceutical's acquisition of Shire and the announcements of the Bristol-Myers Squibb merger with Celgene and Abbvie's similar announcement with Allergan.

The main and perhaps the only headwind in the sector today has been purely political in nature. President Trump's unexpected U.S. Presidential election victory in November 2016 temporarily muted the rhetoric around U.S. drug price reform, originally catalysed by Democratic Presidential nominee, Hillary Clinton, in a September 2015 tweet about drug "price gouging". Rather, the President initially focused on continued motivation to increase competition to lower drug prices via market forces, through innovation (a positive surprise) and more drug approvals. But after an 18-month respite, President Trump has resumed the drug price rhetoric and 2019 has brought an inflection point around the topic as yet another Presidential election cycle is upon us some 12 months ahead of the November 2020 vote.

Whilst a host of proposals have been tabled on how to curtail out-of-pocket expenses for seniors in America, including those that may dramatically impact how drugs are priced in the U.S., we do not expect any legislation to be passed ahead of the next election. Timelines and partisan politics will almost surely scuttle any notable legislation. In fact, given the powerful PhRMA lobby and the likelihood of a continued split Congress post the election, we expect the status-quo even post-election.

Strategy review:

The company's objective remains unchanged: to achieve a high level of capital growth through investment worldwide in a diversified portfolio of shares in pharmaceutical and biotechnology companies and related securities in the healthcare sector. As productivity and innovation rise, the number of investable ideas also rises, but the scrutiny and diligence required to isolate them becomes more complex.

Biotechnology

Sentiment regarding major biotechnology has remained tepid throughout the six-months ended 30 September 2019 as expectations for slowing growth and the perceived competitive challenges to the companies' core franchises have persisted. Concerns over future competition from biosimilars as well as other innovative drugs continue to weigh on share prices, as there is significant uncertainty about how some of the competitive markets will unfold.

Layered on top of the slowing growth outlook for large capitalisation biotechnology has been the overhang of drug pricing rhetoric during the U.S. Presidential election campaign season. Both President Trump and the Democratic Presidential nominee candidates have talked publicly about wanting to reduce drug prices in the U.S., and the rhetoric continues to cast a cloud over the sector. As of the time of this writing, Elizabeth Warren, one of the more progressive Democratic Presidential candidates, has been gaining in the polls for the Democratic nomination versus former Vice President Joe Biden, who is regarded as more centrist in his outlook. Warren is viewed as more antagonistic to the drug industry compared to Biden, and her ascendance in

the polls led to increased share weakness in the biotechnology sector towards the end of the review period. From a valuation perspective, major biotechnology companies continue to trade at historically low price to earnings ratios, many in the single digits, with share prices already discounting most of the fears over slowing growth, competition, and the future macro drug pricing outlook.

Our view continues to be that no matter which Presidential candidate is elected, a split Congress post-2020 with the Republicans maintaining control of the Senate and Democrats maintaining control of the House, will effectively prevent any egregious drug pricing legislation from passing. There remains some chance that President Trump and Congress will manage to enact an incremental drug pricing bill prior to the election, which would hopefully clear the drug pricing overhang for the sector. Historically, when political overhangs on drug pricing have cleared, the sector has re-rated upwards in a "relief rally."

While it's commonly acknowledged that major biotechnology will need to engage in M&A to improve their growth prospects, the amount of M&A consummated during the period has been disappointing. Possible reasons for the relative lack of M&A include continued uncertainty about the drug pricing environment in the U.S., inability to reliably predict future cash flows for assets in competitive disease areas, and a healthy financing environment for smaller biotechnology companies, which diminishes their need to sell to larger companies. We continue to believe that M&A activity by large capitalisation biotechnology companies, either as acquirors or as targets, should lead to an upward inflection in share prices from the current depressed levels.

As the global leaders in innovation, the fundamentals of the emerging biotechnology sector remain positive, yet recent stock performance has been weak, which we attribute to political uncertainty in the drug price debate. In particular, investor interest has been high for novel targeted therapies for cancer. These new drugs seek to target molecular pathways which are dysregulated in cancer and are personalised based on mutations identified in patients' tumours. The recent acquisitions of targeted therapy companies, Array Biopharma and Loxo Oncology, at significant premiums also show that large capitalisation pharmaceutical companies recognise a significant opportunity for this therapeutic class. We expect targeted therapies to continue to transform cancer treatment as more mutations driving cancer growth are identified and biotechnology and pharmaceutical companies generate drugs that specifically block these novel targets.

Pharmaceuticals

Like their larger biotechnology brethren above, large capitalisation pharmaceutical stocks were impacted by the political rhetoric around healthcare reform and U.S. drug pricing. However, that is where the similarities end, and divergence begins.

Performance for U.S.-based versus E.U.-based pharmaceuticals has been disparate in 2019. For the most part, the American domiciled companies have all traded down in the calendar year. Meanwhile in Europe, double-digit share price gains have been the norm. Investors have sought refuge in these stocks in a classic defence strategy from several issues, including (1) Brexit uncertainty, (2) risk-off mentality, (3) lowering interest rate environment, (4) growing fears of recession, and (5) U.S. drug pricing risk.

Overall, we regard the sector as being on solid footing as we remain at or near the high end of the current innovation cycle. New product flow and pipelines are generally strong. But the cradle of innovation does not rest within large capitalisation pharmaceutical companies. That is still the domain of emerging biotechnology companies domiciled mainly in the United States. Hence, M&A must be a key mandate for these companies going forward, creating a partial air of uncertainty about the state of business development within large conglomerates and their ability to adjudicate

about "the next big thing" within an environment that does not reward risk taking. Hence, we remain selective in the large capitalisation pharmaceutical space.

Elsewhere in pharmaceuticals, the performance of U.S.-focused specialty and generic pharmaceutical stocks was mixed during the period with significant disparity between winners and losers. In general, specialty pharmaceutical stocks outperformed generic pharmaceutical stocks, as the former group benefited from notable new product launches, favourable pipeline disclosures and lower financial leverage. The outlook for many specialty pharmaceutical stocks is quite bright, and we believe new launch cycles and impactful business development will keep investors' interest elevated and potentially drive multiple expansion for the group over time.

In stark contrast, generic pharmaceutical stocks remain plagued by significant legal overhangs, including opioid and pricing collusion litigation, that have significantly hampered performance. These issues, combined with relatively high debt burdens, have shaped our view that many stocks in the generic pharmaceutical group are effectively "uninvestable," at least in the near-term. That said, with such severely depressed valuations, we recognise the potential for volatile stock re?ratings for certain names in response to positive news flow, so we continue to monitor this group closely.

Medical Technology and Devices

Fundamentals overall in the medical technology and devices sector have remained favourable, in keeping with a trend that has persisted for the past five plus years and one we see continuing in the near- to intermediate-term, if not longer. The sector continues to benefit from favourable macroeconomic dynamics in the United States as evidenced by elevated consumer confidence levels and depressed unemployment levels, ongoing strong investment in research and development pipelines, and a more accommodative FDA. Moreover, medical device companies have been largely insulated from many of the political issues facing other healthcare sectors, such as drug pricing debates and "Medicare for All" rhetoric from several Democratic Presidential primary race candidates.

From a valuation perspective, we recognise that the group currently trades toward the higher end of its historical ranges, both on an absolute basis and relative to the S&P 500 index. Nevertheless, we believe that the valuation is warranted given the consistent mid- to high-single digit organic sales growth rates and low to mid-teens earnings per share growth rates posted by the large capitalisation medical device companies. This represents the best growth the sector has seen in more than a decade, and is very favourable when compared to other companies across the S&P 500 index.

Turning to stock selection, our favourite areas of innovation and growth are in the cardiology and diabetes markets. In cardiology, we are keenly focused on the transcatheter aortic heart valve market where strong data from several companies in the space have served to drive a reacceleration in overall market penetration rates. We see this trend continuing. In diabetes, we expect several exciting new product launches to fuel elevated growth rates for years to come. Other areas of interest include surgical robotics, single use endoscopes and transcatheter mitral heart valves where we see the potential for robust innovation to drive changes in treatment paradigms in very large existing markets.

Life Science Tools and Services

The share price performance of the life science tools and services sector has been strong year-to-date as the group has shown relatively stable, albeit moderating, top-line growth and insulation to several key policy debates across the healthcare landscape such as drug pricing and "Medicare for All". Even still, puts and takes around moderating macro indicators and China tariffs have been key overhangs to navigate. To that end, after a largely uneventful first quarter, second quarter earnings were more difficult as organic growth slowed against increasingly difficult comparisons from 2018,

stoking concerns that the softer economy and China trade rhetoric is beginning to have an impact on fundamentals.

Whilst valuations are still towards the high end of the historical band, we believe the sector is in the midst of a "proving out" period that results can be more insulated to macro dynamics than years past. Therefore, we believe the main question moving forward is whether organic growth and profitability can remain sustainably more resilient in the face of a macroeconomic deceleration and China trade rhetoricirca While the inflection in organic growth in 2018 is likely to prove a "high-water-mark," we believe companies across the sector have line of sight to sustained mid-single-digit growth.

To be clear, we believe there is still an element of cyclicality to the business. However, the sector is broadly less sensitive to capital equipment spending and more reliant on higher visibility ongoing services/consumables revenue streams than in years past. From an exposure perspective, there has been a broad-based effort to allocate resources towards secular growth opportunities, most notably supporting the robust innovation and activity in the biopharmaceutical space, which we view as the most durable and defensible end market. With regard to China, growth in the region has remained strong despite trade and tariff concerns as these stocks benefit from having differentiated solutions from secular investments by the government in biopharmaceutical research and development (R&D) as well as air, water, and food quality.

Healthcare Services

The environment for healthcare services companies has remained incredibly volatile as the spectre of the 2020 U.S. Presidential election weighs heavily over the sector, with anxiety building to the point where a simple "round of applause" at a Bernie Sanders town hall event on Fox News precipitated a 20% selloff in managed care stocks in April.

More recently, the perception has grown that managed care performance has become inversely correlated with Elizabeth Warren's rise in the Democratic primary polls, and the perceived increased risk of "Medicare For All" legislation that would eliminate the private insurance industry in the United States, making the investing environment for managed care quite difficult.

Worse, fundamentals in managed care showed signs of weakness in the second quarter of 2019, with many companies showing higher benefit costs. Other areas of healthcare services offer little reprieve from controversy, with hospitals demonstrating strangely uneven performance, distributors mired in opioid litigation, and pharmacies showing little signs of improvement in combating reimbursement and retail headwinds.

Looking ahead to the remainder of 2019 and 2020, we remain underweight healthcare services, acknowledging the difficult environment for the sector. We believe managed care stocks are materially undervalued, with a view that the eventual winner of the 2020 election will not eliminate private insurance, and instead may expand health insurance coverage or otherwise improve access to coverage, which would be positive for the industry.

We see many theoretical opportunities for the sector to re-rate higher, including: Joe Biden winning the Democratic primary, Elizabeth Warren shifting to support less disruptive healthcare policies after winning the Democratic primary, a Trump re-election, or the election of any Democratic candidate without a Democratic majority in both chambers of Congress. We believe concerns over heightened benefit costs are overblown and expect sentiment to improve off of its current low. However, we acknowledge that many investors will remain fearful until "Medicare For All" uncertainties are definitively resolved and take a long-term view.

Whilst we see election risk excessively priced into managed care, we believe election risk is underappreciated in hospitals, where a shift to lower Medicare reimbursement rates would be problematic, and are also not optimistic on fundamentals. In the supply chain, distributors lack visibility into timing and magnitude of resolution of opioid litigation, and pharmacies face headwinds that will take years to resolve. Additionally, possible legislation or administrative action on drug pricing reform could have negative implications for both sectors.

Emerging Markets

Whilst volatility was the hallmark of the Chinese pharmaceutical sector in 2018, it has rebounded very well year-to-date. It has taken some time and education, but the market has come to realise that the new government-led group drug purchasing programme has had variable impacts on different companies. For example, the impact on the larger pharmaceutical players with innovative pipelines and strong commercialisation is not a negative and is perhaps even a positive. These leading companies will continue to gain market share from small-and-medium sized companies.

The healthcare services sector in China has also performed well, owing to the increased R&D expenditure on innovative drugs and rising domestic demands for private healthcare services in the region.

In addition, we have been active in newly allowed biotechnology initial-public-offerings in Hong Kong. In our due diligence, we assign significant value to the quality of management and conduct comprehensive analysis on clinical pipelines. We believe there will be an increasing number of pre-revenue companies seeking an IPO in Hong Kong and mainland China.

Also in the period, Beijing officially launched its new technology innovation board. The "STAR Market" board is widely regarded as China's own "NASDAQ". The notion is to encourage investment in domestic technology innovators, ensuring these companies have resources to develop and have an incentive to list on an onshore market.

In India, we prefer companies where the new generic launch momentum can mitigate the pricing erosion seen in the U.S. generics markets. We focus on the compliance history of a company and any upcoming major FDA inspections when evaluating an investment decision. We also prefer revenue diversity, especially from domestic (India) markets and other emerging markets, that adds to earnings stability and growth. We see increasing challenges faced by Indian generic companies on their U.S. business and selectively hold a negative view on those stocks. A few such challenges include regulatory issues related to FDA inspections, and declining profitability in U.S. business led by higher generic competition, increasing expenditure in R&D and rising cost of compliance.

We also look at investing in domestic (Indian) healthcare companies such as leading pan-India private hospitals chains having scalable and profitable business models. We continue to keep a keen eye on changing pricing dynamics, cost efficiencies, leverage and are intensely focused on the cash generating abilities of our portfolio companies.

Geographically speaking, we would highlight an important increase in our exposure to emerging markets on a year-over-year basis, with nearly a doubling of exposure there, particularly in China. The reasons for the increase are a result of an accumulation of factors. First, we note that the regulatory environment for new drug approvals in China has shifted to a more stringent, "Western" style approach with new rigorous clinical testing requirements. This favours the more highly innovative companies, both foreign and domestic, that we prefer to own. Second, the regulatory requirements for new equity listings has also changed, with companies no longer needing specific revenue and profit requirements before being eligible for IPO's. This has allowed for an increasing number of biotechnology IPOs there, in a number of which we have participated. Third, given the uncertain U.S. political backdrop, we felt it was appropriate

to decrease exposure to equities that may be more exposed, either real or perceived, to the volatility that may follow the headlines on U.S. drug pricing and/or changes to Medicare.

Outlook for 2020:

The fundamentals underpinning healthcare equities remain strong. Technology and innovation have never been more prevalent across sub-sectors, but especially in therapeutics, medical devices, and life science tools companies. With a strong secular tailwind with increases in population and patient demographics, demand for healthcare will continue to rise. Overall valuations remain reasonable and undemanding.

Global macroeconomic data remain in flux and recessionary fears are on the rise. Markets may turn defensive and global fixed income may gain a bid at the expense of equities. However, healthcare equities may offer a respite for those needing to maintain equity exposure. Of course, news flow on trade, especially between U.S. and China, could have an outsized impact on market sentiment.

2020 will bring another U.S. Presidential election. Current polling results make the outcome "too tough to call" currently but we are sanguine about the outcome. A re-election of President Trump most likely results in status quo from a drug pricing perspective as the tenor of his healthcare policy has become more patient-focused than industry bashing. A win for the Democratic nominee could also result in status-quo for federal healthcare policy. Former Vice President Joe Biden would certainly look to maintain and bolster the Affordable Care Act, a signature piece of legislation he and President Obama passed in 2010. More left-leaning Democratic candidates such as Elizabeth Warren and Bernie Sanders would have a very difficult, if not impossible, time in trying to pass legislation that would result in a material change to U.S. drug pricing without the full support of both divisions of Congress, which we would not expect. Overall, we would welcome any legislation that reduces out-of-pocket expenses for patients and increase their access to prescription medicines at the same time while protecting the innovation that stems from a free market system.

Lastly, innovation-driven growth remains at the forefront of our bullish view of the healthcare sector. The current new product cycle across the industry is clearly the best we have witnessed, with approvals of new medicines at all-time highs. And the medicines of today are clearly superior to those of the past, with new standards of care being approved across a wide range of therapeutic categories. Overall, we expect many alpha generating opportunities to exist as this golden age of innovation continues.

....

Infrastructure

(compare infrastructure funds **here**)

Manager's report for HICL Infrastructure:

The market for core infrastructure investments continues to be very competitive, characterised by high levels of demand from unlisted investors for good quality infrastructure assets.

Despite the challenging market dynamics, the pipeline remains healthy, [*this*] include[*s*] PPPs in Northern Europe and North America and regulated assets in selected geographies, including additional OFTOs. Selectively, the investment manager also continues to consider assets with corporate offtake counterparties, such as rolling stock or metering businesses.

....

Manager's report for Sequoia Economic Infrastructure Income:

Market review

The company has operated in a relatively calm environment over the last six months with tightening lending margins and bond spreads since the volatility of the corporate bond and loan markets in the fourth quarter of 2018. The stability of the private and public debt markets during the first half of this financial year has contributed to a steady stream of infrastructure debt opportunities that the investment manager was able to acquire at attractive prices

Primary market issuance in the infrastructure loan markets has been exceptionally strong, with deal volumes of US$ 264bn over the last six months, split approximately 30% in the North America, 36% in EMEA, 15% in Asia3, and 19% in the rest of the world. In addition, there were significant amounts of infrastructure debt issued in the bond markets, and through bilateral loans and private placements that are not always captured in the market data. The opportunity for the company to deploy capital, therefore, is exceedingly large.

Sequoia has developed a very strong pipeline of mostly private debt infrastructure lending opportunities, which are expected to become executable mostly over the next three to nine months. Pricing on these opportunities is consistent with the company generating a gross return in excess of 8%. The potential investments are widely spread across a range of sectors and jurisdictions. Sequoia is especially excited about potential investments in the transport assets, accommodation and renewables sectors where the current portfolio is arguably underweight, lending opportunities are often attractive and additional investments into these sectors would be desirable.

Sequoia expects project finance senior lending margins, especially in the UK and Europe and for "core" infrastructure projects and availability-based PFI/PPP projects to remain tight, driven by sustained commercial bank appetite for these types of assets and by increasing demand from institutional investors such as continental European insurance companies. However, spreads in the mezzanine market, and for senior debt in the US and some asset classes in the UK and Europe, are expected to remain more attractive.

Overall, the opportunity for the company in economic infrastructure debt is strong and the asset class remains under-invested and attractive.

Renewable energy infrastructure

(compare renewable energy infrastructure funds **here**)

Manager's report for NextEnergy Solar:

Review

In the UK, the summer of 2019 was one of the hottest on record, with the highest ever UK temperature of 38.7 degrees Celsius recorded in Cambridge on 25 July. Whilst the extra irradiation drove a greater than expected level of generation, the Asset manager had to cope with the adverse effects of high temperatures on the technical performance of solar PV components, which perform optimally at temperatures below 25 degrees Celsius. In addition, certain plants suffered from grid curtailment, as generation peaks driven by exceptional irradiation levels exceeded, at times, the export capacity allocated by the grid authority to each plant.

In Italy, the weather pattern was not unusual during the period.

Current and Long-Term Power Prices

During the period, the Consultants revised their forecasts for the UK wholesale power price downwards in the short-term and the long-term. Short-term projections are mainly driven by the decrease in the commodity prices of gas and coal. In the long-term, wholesale prices are expected to move downwards as more low-cost generation is being deployed, notably offshore wind and solar PV.

The company's current long-term power price forecast implies an average growth rate of approximately +0.9% in real terms over the 20-year period and an average price of circa £53.8/MWh in today's terms. This represents a decrease of 4.6% compared to those used at the end of the previous financial year.

Compared to the previous interim period end, electricity day ahead prices in the UK decreased from circa £67/MWh in September 2018 to circa £36/MWh in September 2019.

Following a similar trend, the price of electricity in Italy decreased from circa €76/MWh in September 2018 to circa €51/MWh in September 2019.

Property - debt

(compare property debt funds **here**)

Ravi Stickney, manager of Real Estate Credit Investments:

State of the markets:

European Real Estate and Real Estate Debt Markets

Following a strong start to 2019, the first half of RECI's financial year has seen several negative macroeconomic influences, including US trade tensions, a leadership election for the UK's Conservative Party, continued Brexit uncertainty and southern European elections which are beginning to cause some concern in these markets. The UK and French markets remain lagging, in the case of the UK this is likely to continue for some time whilst Brexit moves from the current phase into the transition phase (or indeed a post 'hard' Brexit phase).

ABS issuance increased significantly in Q2 2019 compared with Q1. In particular, there were a significant number of new issuances in June, resulting in a quieter secondary market. UK spreads remained relatively stable, indicating that investors are continuing to participate in UK deals despite Brexit uncertainty. Whilst primary and secondary ABS markets were relatively busy at the start of July, they quietened in late July and August. Despite a volatile macro environment, the impact on the ABS market was muted due to the drop in trading activity in both the primary and secondary markets over the summer. Despite slightly more activity in September, activity remains muted by macro headlines dominating broader markets as we approach the Brexit deadline of 31 January 2020.

Brexit

Over the last three years the implications of Brexit on UK real estate prices have been accepted and priced by buyers and sellers. The UK real estate market is, and has been for some time now, a 'stressed' market. The borrowers we work with have pricing assumptions that assume significant downside scenarios and high yield expectations. The real estate lending market in the UK has been impacted by Brexit in that foreign lenders (US and European) have largely withdrawn from this market for most transitional/value-add/development lending. Local banks are still active, albeit only on

core/core+ income loans at very constrained LTV levels. Core income loans are assets that benefit from having long term income while core+ income loans are assets that benefit from having strong current income, but do require some measure of asset management to optimise its income profile and term. As such, the managing company has seen its origination volumes substantially increase, especially for senior loans in the value-add/transitional space. We have also seen our senior loan margins improve by 50-100 bps and have moved substantially to a lower risk profile in the UK as a result of Brexit. We are originating senior loans at LTVs in the region of 60%-70%, capable of withstanding further significant shifts in values in the event of a 'hard' Brexit.

Outlook:

The current environment continues to present an extremely challenging time for global capital markets. Most asset classes continue to suffer negative returns as key macroeconomic concerns remain.

. . . .

Property securities

(compare property securities funds **here**)

Marcus Phayre-Mudge, manager of TR Property:

Whilst the overall property indices travelled in a tight band over the period, at the sector and country level there were large dispersions of returns. The slow 'car crash' of retail property values continued to be evidenced in the interim results of companies such as Hammerson, Intu and Capital & Regional. Share prices have disconnected from underlying asset values given how hard it is to assess value accurately. The twin evils of too much leverage and weakening earnings continue to keep investors away.

German residential has been a mainstay of performance for many years. In the Annual Report, I highlighted the concerns around the risk of the State of Berlin seeking to impose (in contradiction of federal practice) rent freezes and aggressive restrictions on indexation. These new rules ('Mietendeckel') look likely to become law in November, although the devil is always in the detail. Investors also worry that there could be contagion of this type of legislation to other regions. We do not agree with that premise and have maintained our non-Berlin exposure.

Our loosely termed 'alternatives' group which includes student accommodation, self-storage and healthcare, all performed well. I have highlighted in the past our index-linked, long income exposure which overlaps with this group, particularly in healthcare and we saw strong returns there as these businesses benefited from the drop in the cost of long term financing.

This theme of 'lower for longer' debt cost resonated strongly in Sweden. Swedish property companies, with just one exception, have greater than average gearing coupled with higher proportions of short term debt. The combination of a falling cost of debt environment, coupled with rental growth at the asset level has led to very strong performances from many of these companies.

Switzerland, a market where we see little organic growth, benefited from being a safe haven in these volatile times. Swiss investors also sought exposure to their domestic currency and property names yielding 3% to 4% look attractive regardless of the medium term fundamentals.

The industrial and logistics overweight remains a key theme in the portfolio. Not only did we experience strong organic growth from all our companies (particularly those with development opportunities) but we benefited from corporate activity as well. In May,

Office markets across Europe continue to see rental growth. Our overweight to Paris and Stockholm added to performance but our underweight to Madrid and Barcelona proved costly.

Central London's solid performance remains a conundrum. Our overweight to decentralised South East offices versus our underweight to Central London proved a poor decision. However, I am confident that that has more to do with illiquidity in the smaller companies which provide us with that exposure than the health of the underlying markets.

Offices

The resilience of the London office market in terms of both rents and capital value stability continues to surprise us. Demand remains broad based, particularly across tech and media industries. Companies are happy to pay for quality and the premium rents achieved on Grade A (new and refurbished) space have persisted. In fact, the drought of new space has driven pre-lets (advance commitments) to record levels. Investment appetite is driven by expectations of sustainable rents with future growth prospects. As a consequence, investors remain active buyers. The difference between 2018 and 2019 has been the resurgence of domestic interest particularly in the City. However, the Brexit 'drag' has pulled investment volumes lower with Savills year to date estimates of £4.9bn in the City and £2.8bn in the West End both c50% below the five year average.

The rise of the flexible office provider remains a key topic, not least because of the travails of WeWork. Our view is that the flexible space market share (currently c5% of floorspace in Central London) will continue to grow. Tenants want the convenience and tenure flex and are prepared to pay for it. WeWork has led the space absorption charge, doubling its footprint each year since 2016. They are not alone and the difficulty for market observers is getting a handle on the underlying occupancy of these types of operators. WeWork et al will quickly cease acquiring space if they cannot fill or make money from their current estates. We remain cautious.

The picture across the largest cities in Continental Europe has been similar but with particular strength in Paris, Amsterdam, Madrid and Barcelona. Paris has year to date capital growth of 15% in core CBD and even higher figures in some peripheral markets. Underlying this is year on year rental growth of 5% to 7% across all the Paris sub-markets. In Spain, CBRE reported the fastest take up in Q3 for over 12 years. Vacancy has fallen a full percent to 8.7% in a year and prime rents reached €35.5 per sq m/per month (+7.6% year on year). Rents have been stable in the big six German cities with Berlin again reporting best in class growth.

Investment volumes in Paris have been lower than last year (but that period was buoyed by the Terreis €1.4bn transaction). Germany, Spain and Scandinavia all continue to attract global capital however the Netherlands (-34%) and Ireland (-17%) both saw falls in investment volumes between H1 2018 and H1 2019 according to CBRE.

Retail

Retail property of all types (with the exception of well let supermarkets) across Europe continue to suffer value degradation to varying degrees. Matters remain most acute in the UK. The period saw a number of high profile CVAs (company voluntary arrangements) including the long anticipated Debenhams and Arcadia. The CVAs provided a 'stay of execution' for both retailers with store closures and large rent reductions but neither retailer's future is assured. The twin headwinds of the online challenge and high property taxes (rates) continue to batter the profitability of all but best in class retailers. Overall, vacancy in UK retail reached 13%, the correction towards sustainable rental levels remains work in progress. With concerns over the quality and depth of cashflow, investors have not returned. Shopping centre transaction

volumes will be lower in 2019 than they were in 2018 which itself was a previous record. The largest transaction was the sale by Intu of its Derby centre. However, the buyer receives a priority income stream and, therefore, the vendor was left with significant capital risk if the rental income falls. A desperate transaction from the seller's point of view. We expect Intu will be forced to raise capital as its balance sheet deteriorates.

Whilst we have seen a number of retailer failures across Continental Europe, particularly in the Netherlands, compared to the UK numbers these have been modest. European retail rents are generally much closer to sustainable levels. Whilst we see weakness in headline rents, it is not on the scale of the UK. The market share of online purchases is currently far lower than the UK but investors expect the trend to online to accelerate as next day delivery becomes more standard. It is no surprise that retail investment has fallen 22% between H1 2018 and H1 2019 according to CBRE. Spain, which has seen strong employment and wage growth was the only country where investment volumes rose.

Distribution and Industrial

Occupier demand has remained robust in the UK even in the face of the supply chain uncertainty surrounding Brexit. The first nine months of 2019 saw take up reach 19.7m sq ft, just 10% down on last year. DTRE, predicts that full year lease up will match the five year average of 28m sq ft. Whilst this may only be matching the average, these are huge numbers and reflect the scale of growth in this key market. The supply response has been forthcoming and we predict little rental growth in certain regions such as the East Midlands where new supply is more than matching demand. Much hinges on the Brexit outcome for this type of real estate. We continue to favour the smaller, urban and suburban markets as opposed to the larger 'big boxes'. Yields have stopped falling for this latter group. However, the medium term outlook remains positive with the ONS reporting that online retail accounted for 18% of total retail sales in 2018. Forrester's (a research and consulting group) forecast that it will reach 25% by 2023.

Continental Europe is a different story with Western Europe averaging 10.2% but just 5% in Spain and Italy. With a relatively nascent big box market, yields have historically been much higher than the UK. We are confident that yield compression will remain an attractive feature of almost all these markets. CBRE estimate that €32bn of capital flowed into this subsector in the year to June 2019, a sum only just eclipsed by the same period a year earlier. This year will exceed the 10 year average and this figure excludes the largest single property transaction, Logicor, which alone accounts for €12.2bn of logistics assets across Europe. The money is following the rental growth. Spain saw prime logistics rents rise 4% in H1 2019. In Dublin, the figure was 5%. Vacancy stands at less than 5% in Germany, Sweden, Ireland and the Czech Republic.

Analysis by Savills assessed the attractiveness of 32 European countries across 23 different metrics. One of the conclusions identified was the tipping point for rapid growth in ecommerce logistics. Once online retail sales exceeded 11% of all sales, there was a step change in logistics demand.

Residential

The private rental sector continues to flourish with demand continuing to outstrip supply. The risk is not economic but political. As detailed earlier, Berlin is experiencing an extreme form of state intervention. Our view remains that the unique history of this city, coupled with the unusual political structure where the city and the state of Berlin are effectively one, makes the likelihood of contagion to other German residential markets low.

However, the speed of market driven rental growth and the social sensitivity of this particular sector means that we must have a constant eye on the risk of state intervention across Europe. We remain more attracted to markets where there are already state restrictions as this ensures that book values remain below rebuild cost.

The key is to ensure that the rent restrictions allow for indexation and this makes these income streams very attractive. We continue to favour Germany (ex-Berlin), Ireland and Sweden, although the Swedish residential names have become expensive and we have recently reduced exposure to those.

Debt and Equity Capital Markets

Refinancing and securing record low costs of debt remains a popular activity for CFOs across the listed property sector. EPRA recorded £12.6bn of debt raised in the period under review and £15.3bn in the calendar year to date. This is a slightly lower run rate than previous years but that is to be expected given how much debt has been refinanced at these very low levels over the last few years. We do continue to see record low costs of debt being secured. By way of example, in October, Unibail-Rodamco-Westfield priced a €750m 12-year bond at a fixed annual coupon of 0.875%.

There were no IPOs in the period, however, we saw £3.7bn of follow on capital raisings. These were dominated by businesses raising capital to make corporate acquisitions.

Property Shares

Property equity markets moved broadly sideways until late July when the background (rumbling) noise of the Brexit debacle once again rose in volume and pitch, driving investors away from UK domestic stocks. Property companies are a disproportionately large component of UK domestic 'baskets' due to their high level of GBP earnings. UK property names which had been weakening over the summer fell by 7.5% in the first two weeks of August. What was almost more surprising was the subsequent rally which ran from 15th August to 30th September adding 12.4% as investors changed their views entirely with the incoming Prime Minister appearing to be more determined than ever to drive matters to a conclusion, albeit an unknown one. Broader markets also saw a strong style rotation from 'growth' to 'value' and property names - seen as value plays - were a beneficiary.

Once again the central banks have played a leading role in investor behaviour. ECB President Draghi delivered his parting shot, another rate cut and a renewed bond buying programme. More QE saw the 10-year Bund yield fall to -0.6% at the end of September. Property values with their long duration income profiles benefit from these further falls in the cost of long-term financing.

Against this benign backdrop of positive macro policies, there was a broad dispersion of fundamental real estate factors driving performance at the sector and company level. The issues surrounding retail property require no introduction. I have highlighted in previous reports the differential in characteristics between UK retail property and its Continental counterparts. These differences particularly around greater affordability across Europe continue to dominate. The essence is that the UK has a triple whammy of higher rents, much higher property taxes (rates) and greater online penetration. This continued to be reflected in the performance of the respective retail landlords..

As mentioned in the summary, German residential has been a stalwart sector for many years, growing in importance through capital increases and M&A driven by excellent returns. The Berlin political situation - which remains unresolved - rocked investor confidence. There are three listed companies with high exposure to the Berlin residential market. The weak returns from these stalwarts, who own thousands of apartments across the whole of Germany, points to investors' concerns. Nevertheless, their relative outperformance of the Berlin names illustrates how investors see little chance of contagion from the Berlin political process.

Scandinavia and Sweden in particular were strong performers in the period. Almost all Nordic property companies operate with higher leverage and shorter duration debt structures than the average pan European property company. The consequence of the dovish response by the Riksbank (mirroring the ECB) was to supercharge earnings

expectations and total returns with the Swedish element of the benchmark returning 20.2% in the six months. Residential names performed particularly well. Not only have the underlying residential letting markets remained strong but corporate activity provided reinforcing datapoints.

The industrial/logistics markets across Europe remain top of investors shopping lists.

Swiss property stocks draw investors in volatile times. The uncertainty surrounding the global outlook as well as the ongoing local issues in Europe resulted in the Swiss property companies collectively returning +15% (in CHF) in the six months to September.

Outlook

The ongoing Brexit saga continues to dominate the outlook. However, the country does appear to be inching towards an outcome after three years of negotiation and Parliamentary stalemate. Clarity will result in the release of pent up investment decisions. This will aid property values as both tenants and investors commit to transactions. Beyond that potential short term bounce, we remain focused on the longer-term sector-focused dynamics which are broadly the same as they were six months or a year ago. Retail property (particularly in the UK) remains of deep concern. The flipside of that coin - logistics - the reverse. However, equity markets are now up with events with deep discounts applied to retail names and premiums for logistics businesses. The largest city office markets across Europe are set fair with few exhibiting over supply. The private residential sector is also robust with wage growth ensuring affordability, although the pace of rental growth is a growing concern and (further) direct intervention (as seen in Berlin), whilst unlikely, cannot be ruled out. The reality of the situation is the acute shortage of accommodation as these key cities grow and more rural areas depopulate.

Underpinning all this commentary at the sector level is the response of the central banks. Inflation expectations in the Eurozone, a metric closely watched by the ECB's governing council, fell to an all-time low in early October. The 'five-year, five year inflation forward' which measures how much annual inflation markets are pricing in starting in five years' time sank below 1.1%. With this low level of inflation expectation, interest rates will remain lower for longer and the hunt for income and yield is set to continue. Real assets remain a good source of that income. The key is in the assessment of that income quality.

. . . .

QuotedData

QuotedData is a trading name of Marten & Co, which is authorised and regulated by the Financial Conduct Authority
123a Kings Road, London SW3 4PL
0203 691 9430

www.quoteddata.com

Registered in England & Wales number 07981621,
2nd Floor Heathmans House
19 Heathmans Road, London SW6 4TJ

Edward Marten
(em@martenandco.com)

Alistair Harkness
(ah@martenandco.com)

David McFadyen
(dm@martenandco.com)

Nick Potts
(np@martenandco.com)

James Carthew
(jc@martenandco.com)

Matthew Read
(mr@martenandco.com)

Shonil Chande
(sc@martenandco.com)

Richard Williams
(rw@martenandco.com)

IMPORTANT INFORMATION

This note was prepared by Marten & Co (which is authorised and regulated by the Financial Conduct Authority).

This note is for information purposes only and is not intended to encourage the reader to deal in the security or securities mentioned within it.

Marten & Co is not authorised to give advice to retail clients. The analysis does not have regard to the specific investment objectives, financial situation and needs of any specific person who may receive it.

This note has been compiled from publicly available information. This note is not directed at any person in any jurisdiction where (by reason of that person's nationality, residence or otherwise) the publication or availability of this note is prohibited.

Accuracy of Content: Whilst Marten & Co uses reasonable efforts to obtain information from sources which we believe to be reliable and to ensure that the information in this note is up to date and accurate, we make no representation or warranty that the information contained in this note is accurate, reliable or complete. The information contained in this note is provided by Marten & Co for personal use and information purposes generally. You are solely liable for any use you may make of this information. The information is inherently subject to change without notice and may become outdated. You, therefore, should verify any information obtained from this note before you use it.

No Advice: Nothing contained in this note constitutes or should be construed to constitute investment, legal, tax or other advice.

No Representation or Warranty: No representation, warranty or guarantee of any kind, express or implied is given by Marten & Co in respect of any information contained on this note.

Exclusion of Liability: To the fullest extent allowed by law, Marten & Co shall not be liable for any direct or indirect losses, damages, costs or expenses incurred or suffered by you arising out or in connection with the access to, use of or reliance on any information contained on this note. In no circumstance shall Marten & Co and its employees have any liability for consequential or special damages.

Governing Law and Jurisdiction: These terms and conditions and all matters connected with them, are governed by the laws of England and Wales and shall be subject to the exclusive jurisdiction of the English courts. If you access this note from outside the UK, you are responsible for ensuring compliance with any local laws relating to access.

No information contained in this note shall form the basis of, or be relied upon in connection with, any offer or commitment whatsoever in any jurisdiction.

Investment Performance Information: Please remember that past performance is not necessarily a guide to the future and that the value of shares and the income from them can go down as well as up. Exchange rates may also cause the value of underlying overseas investments to go down as well as up. Marten & Co may write on companies that use gearing in a number of forms that can increase volatility and, in some cases, to a complete loss of an investment.