

THE MI HAWKSMOOR FUNDS

31st October 2018



FUND COMMENTARY

Is the Goldilocks' economy dead? Many investors seemingly fear it is, given October saw the some of the sharpest falls in share prices in a single month across global equity markets since the Global Financial Crisis a decade ago. For a long time bond and share prices have been supported by conditions characterised as the 'Goldilocks economy', in which economic growth has been neither too hot nor too cold (i.e. like baby bear's porridge). Investors have enjoyed a period in which economic growth has been sufficient to support a healthy level of corporate profitability, but not strong enough to cause the levels of interest rates and inflation to rise to levels that undermine the valuation support for bond and equity prices. However, in recent months not only have US government bond yields risen to levels that provide stiff competition to other assets, but the strong upward momentum in corporate profits that has fuelled the strong performance of US shares in particular during 2018 has faded, given a majority of analysts' forecasts for future profits are now being reduced. With the world's central banks only having just moved in aggregate to quantitative tightening from quantitative easing, it is too early to tell whether the upward pressure on bond yields will resume after their 'safe-haven' rally last month in reaction to the sell-off in equity markets. Much will depend on whether signs of building wage inflation persists, or if the slowdown in the US housing market heralds a broader deterioration in the US economy. As ever we are not positioning the Funds' portfolios for a particular outcome, but we continue to believe that the combination of a murky outlook and the high valuation afforded to many assets is an environment that warrants a cautious approach.

As would be expected the movements in our three funds reflected their risk profiles, with Vanbrugh being the most resilient during the sharp sell-off, and Global Opportunities most exposed. In the short term at least, the Global Opportunities Fund's launch date of 18th September 2018 has proved to be a challenging time for a fund catering to investors with a high-risk tolerance. The total returns of Vanbrugh, Distribution and Global Opportunities for October were -2.3%, -2.9% and -5.1% respectively. These results compared with those of their respective peer group averages which lost -3.0%, -4.6% and -5.1% (IA Mixed Investment 20-60% Shares Sector, IA Mixed Investment 40-85% Shares Sector and IA Flexible Sector). In a difficult month, it was encouraging to see a good contribution to performance from some of our

holdings providing exposure to specialist fixed interest, niche areas of real estate and some absolute return funds. These funds' contributions enabled Vanbrugh and Distribution to be more resilient than their IA Sectors in weak markets during October even though Vanbrugh and Distribution significantly outperformed their IA Sectors in recent years when most asset prices were rising.

Our Funds' performance would have been better in October had it not been for sharp mark-downs in share prices of some of our closed-ended holdings. We have talked frequently about the risk that closed-ended funds' share prices would be vulnerable in rapidly falling markets, and this duly proved to be the case for some of our holdings even though it is important to emphasise that we believe these losses will be temporary mark-downs rather than permanent losses of capital. It has certainly not helped closed-ended fund share prices that there has been a surfeit of new issuance. October saw the record-beating £822 million launch of Terry Smith's new investment trust, Smithson, and it is possible that we are getting close to a cyclical high for fund-raising in the closed-ended fund sector. The appearance of increasingly attractive discounts to net asset value on existing funds makes it harder to launch new ones. Therefore, in the short term there is a risk that closed-ended fund ratings may deteriorate further. However, in the medium to long-term we are optimistic about future returns given the scope for ratings to recover, and this should act as a tailwind for the performance of our Funds. With this in mind we added to closed-ended fund exposure in October. For example, we introduced a holding in Artemis Alpha at a c17% discount for Vanbrugh, while also adding to Global Opportunities' holding. We also increased both Funds' holdings in Henderson Alternative Strategies at close to a 20% discount and added to Global Opportunities' holding in Golden Prospect at discounts between 25% and 30%. We also further diversified all three Funds' portfolios by introducing holdings in Tufton Oceanic Assets, a closed-ended fund developing a good track record in delivering an attractive yield and capital growth from investment in shipping assets. Vanbrugh's holding in Janus Henderson UK Absolute Return was sold at the end of the month to provide liquidity for purchases including additions to positions in Polar Capital UK Value Opportunities and Artemis Alpha Trust.

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RISK WARNINGS AND OTHER INFORMATION

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