ISSUE 03

AUTUMN 2021

INVESTOR

HYDROGEN – MORE THAN HOT AIR

SPLASHING OUT: THE HISTORY OF WEALTH IN BATH

LOSS AVERSION

GOING FOR A SONG

AND AFTER ALL, YOU'RE MY WORRYWALL

HAWKSMOOR
INVESTMENT MANAGEMENT

WELCOME

When we published the Summer edition of our ***Investor*** newsletter, the Covid vaccination programme in the UK appeared to be offering a welcome light at the end of a long lockdown tunnel, and there was a great deal of industry discussion about how companies could get 'back to normal'.

Although the Great Unlock has turned out to be not quite so clear-cut, at Hawksmoor we are determined to embrace the opportunities of the 'new normal' in terms of wider choices for our working styles and communications options – driven by the desire to look after our staff and to provide you with the best possible service.

I hope this newsletter gives you a flavour of some of the broader elements that go into the business of managing your investments. In this edition, our CIO Private Clients & Head of Research Jim Wood-Smith touches on the distorting effect of bad news on financial markets – and I hope our 'Next Gen' article by Assistant Investment Manager Jason Hopton about the psychology of loss aversion adds some perspective on the importance of a long-term outlook when investing.

In addition, the spectre of rising inflation seems to be looming large in the financial news, and in our 'Dear Hawksmoor' section Senior Investment Manager Greg Sellers explains how we aim to make our clients' portfolios inflation-proof.

As always, if you have a question about any aspect of our service to you, please don't hesitate to contact your Investment Manager.

Sarah Soar
CEO

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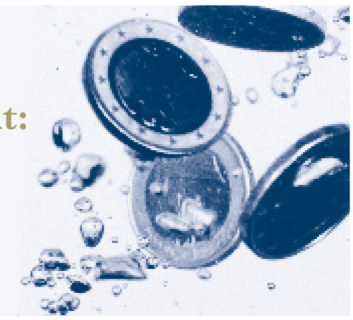

MARKET UPDATE

AND AFTER ALL, YOU'RE MY WORRYWALL

Jim Wood-Smith, *Chief Investment Officer, CIO Private Clients & Head of Research*

One of the first clichés taught to students of investment is that 'markets climb a wall of worry'. Occasionally they take the Humpty Dumpty approach and plummet off this wall, but it is undoubtedly true that profound, logical nervousness and good investment returns frequently go hand-in-hand. In this regard, at least, 2021 has been true to form.

It is also a truism that 'bad news sells'. When I was last studying psychology, the accepted understanding was that bad news affects us around two and half times more powerfully than an equivalent piece of happiness. With more media than ever scrambling to prove to their advertisers that they have our attention, it should be no surprise that the ongoing commentary surrounding financial markets should be unremittingly miserable. Nothing grabs one's attention quite like a scare story.

The first nine months of 2021 have played out almost entirely in keeping with this picture. The news – be it Covid, inflation, higher interest rates, China or Afghanistan – has been consistently miserable. Equity markets, especially in the United States, have gone from strength to strength. It is a formula born of the years.

The markets, of course, are not necessarily right to have ignored all that has been cast in their way. On inflation in particular, investors have placed all their bets on a single, benign outcome. Which brings us to the most inelegantly named 'spike theory'. The argument runs that we need not be concerned by inflation as what we are currently witnessing is caused by the coincidence of a series of one-off factors, which will work their way out of the calculations over the course of next year.

Doubtless there is a strong element of truth in this. The headline rate of Consumer Price Index inflation in the United States has reached a high point (so far) of 5.4%. That is quite something. This rate has been distorted upwards by last year's horrors, but that cannot disguise the possibilities that a) the actual rate is even higher and b) 2022 is not as benign as many appear to expect.

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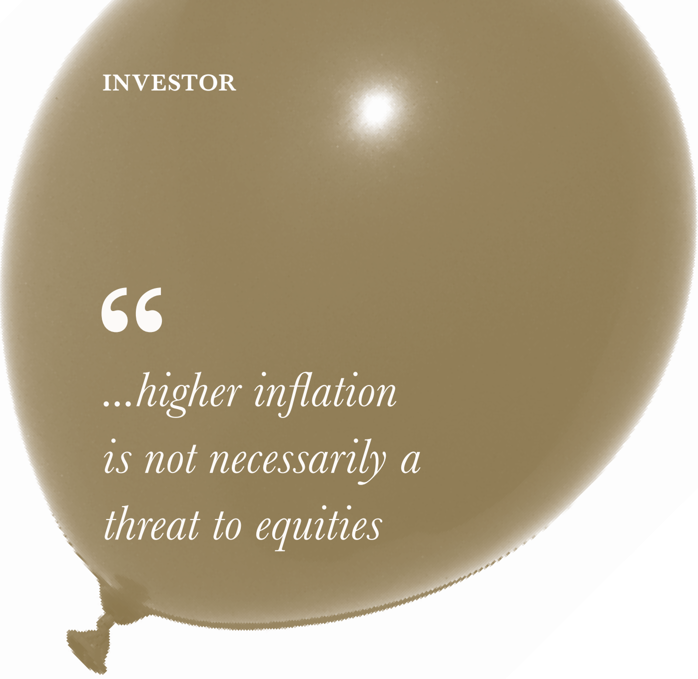
Nothing grabs one's attention quite like a scare story

This inflation is creating some challenging distortions in the markets. The yield on the US 10 year Treasury is (as I type) 1.34%. In round numbers, that is a negative real yield of 4%. No matter how this apple pie is sliced, that is terrible value. It is also a timely reminder of the fundamental difference in the returns offered by bonds and equities. Bonds, usually, pay a fixed rate of income. That is eroded over time by inflation. Equities pay dividends, which, over time, tend to rise with inflation. This patently obvious truism, however, was only brought into the investment mainstream in the 1950s, by George Ross Goobey at the Imperial Tobacco Pension Fund. Ross Goobey's far from complex line of reasoning was that the yield provided by bonds should be higher than that of equities to compensate for this risk of erosion of value by inflation. It was different times, but 70 years ago the thinking was revolutionary.

It appears to us that inflation brings a much greater threat to bonds than to equities. Indeed, for the latter, it may even be bearing opportunity. In a normal world, bond yields would already have risen very sharply. But that is not the planet that we currently inhabit. The Earth of 2021 is still turning to the beat of quantitative easing, the process which involves the Central Banks creating their own money in order to buy bonds. The reason that the yield on American sovereign bonds is a full 4% below inflation is that this is the price at which the Federal Reserve buys them. One may query the wisdom of printing endless amounts of money in order to buy assets that are insanely overpriced, but that is the Alice in Wonderland state of 21st century finance.



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...higher inflation is not necessarily a threat to equities

Our point, though, is that higher inflation is not necessarily a threat to equities. It will differentiate between companies with and without pricing power, but for those in the former camp, there is opportunity. We like high and sustainable margins, companies with limited competition and those able to forge ahead as the world transitions into low carbon. We have argued for a number of years now that there will be a wide gap between transition leaders and laggards. This holds true, but also extends to inflation.

There was a time earlier in the spring when our faith in the merits of leaders was being tested. The promise of vaccines, and the perception that the world may return to the good old days of 2019, saw a rush of money into the stocks that had been hit hardest during lockdown. It was short-lived. Whether it was the evolution of the Covid variants, or the realization that many businesses will never return to their pre-Covid modi operandi, or a combination of both matters little. Despite the protestations of many, 2021 has seen the leaders of 2020 continue to lead. And the UK has continued to lag.

Whilst we are discussing lagging, we should mention China, and Asia in general. We came into 2021 with high hopes that the then very low Covid infection rates across much of the continent would give Asian markets a considerable advantage. What we have failed to appreciate was the arrogance, or negligence, in many authorities that has resulted in them becoming the vaccination tail-end Charlies. In giving credit where it is due, as admitted by Matt Hancock, the UK's government studied the film Contagion (possibly in the belief that it was a documentary) and learned the importance of vaccination planning. It is something we got right, and much of Asia ignored. The result of inaction has been poorly performing economies and stock markets.

This situation has not been helped by the power battle in China between President Xi and a number of the most prominent, and successful, Chinese businessmen. It is an unfair contest and Xi has been highly successful in establishing who is top dog. He is also reining back on a number of areas of the economy where he feels the position of the Chinese Communist Party is challenged by the free market. One of the most notable areas has been education, where the ability of the wealthy to buy private education has fallen foul of collective doctrines. Investors have been thoroughly rattled by this and the summer months have seen very sharp moves in share prices – mostly downwards – in industries thought to be under threat of increased regulation by Beijing. Our view remains that the Chinese authorities are well aware of the virtues of access to international capital and that this will blow over in time. In the shorter term, however, the ride will remain rocky.

We should come back to inflation. Our suspicions are that 'higher for longer' is a strong possibility. We are not going to be drawn into the folly of forecasting, but merely feel that this is something that the markets may be treating unduly benignly. Our protections against higher inflation (and our assets to benefit from it) are high-quality, international businesses with proven pricing power. We are also attracted to various opportunities in Property & Infrastructure, where we are able to invest into a good number of funds where substantial portions of their income are index-linked.

The world of Covid and decarbonization will continue to provide opportunity and threat in equal measure. Markets have been exceptionally benign in the year so far, in the face of inflation, Covid variants, looming monetary tightening and Chinese interventionism. This winter may well bring even greater challenges. We are though convinced of the merits of investing internationally, seeking high quality businesses with pricing power and leadership in decarbonization. This is still a large pond in which to cast one's line.
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THEMATIC RESEARCH

HYDROGEN – MORE THAN HOT AIR

Ben Luck, *Investment Analyst*

Introduction

With an atomic number of just one, hydrogen sits at the top of the periodic table. It is the simplest element and is believed to account for roughly 74% of the visible universe. Its role as a source of clean fuel in an ever-changing world could be transformational. Hydrogen production is a fascinating and rapidly evolving technology which has great investment potential. As we discuss below, we believe the diversified structure of an Exchange-Traded Fund (ETF) is the best means of providing exposure within portfolios. But first, let us examine the merits of this so-called fuel of the future.

Colour spectrum

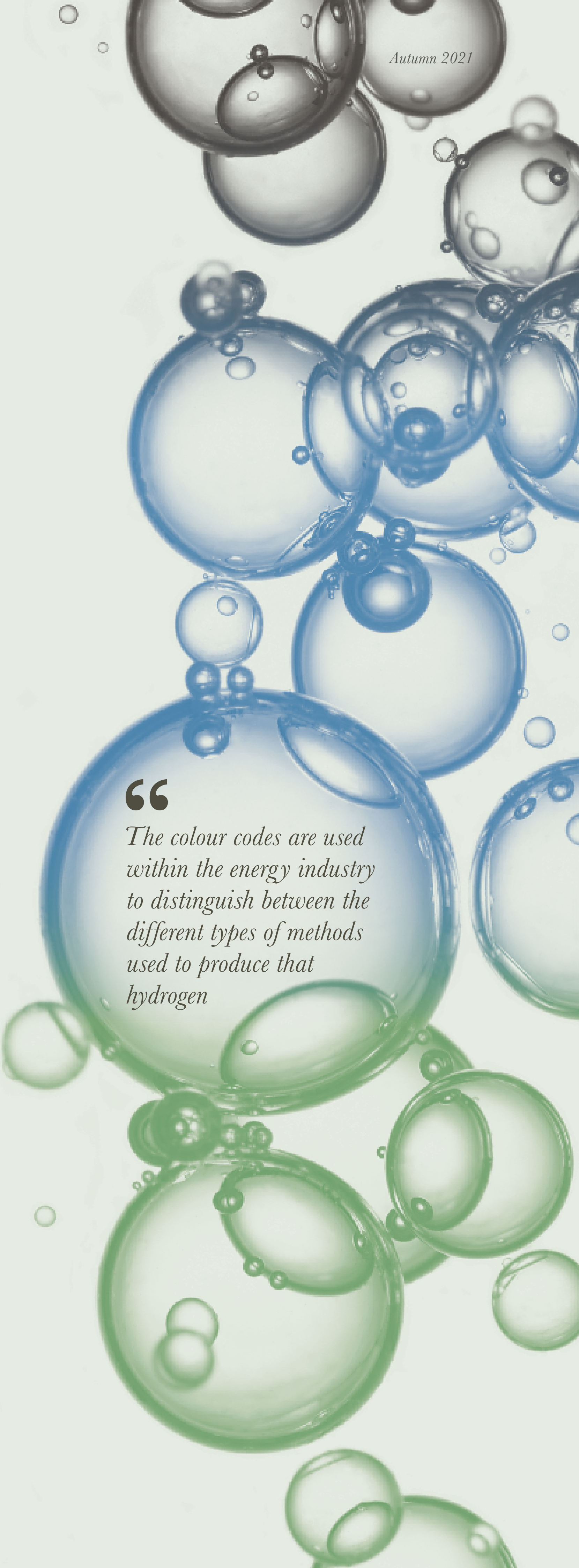
You may hear hydrogen being described as grey, blue or green. You are forgiven for being confused as to how an invisible gas can be referred to in such a multitude of colours. The colour codes are used within the energy industry to distinguish between the different types of methods used to produce that hydrogen.

There are four main sources of commercial hydrogen production: natural gas, oil, coal and electrolysis. A quick look at that list and it is easy to separate the fossil fuels.

Grey hydrogen is produced from natural gas, oil or coal; carbon dioxide (CO_2) is generated as a by-product and released into the atmosphere. This is by far the most common method of producing hydrogen.

Blue hydrogen uses the same production techniques as grey hydrogen but involves a carbon capture and storage process to keep emissions underground.

Green hydrogen is produced using electrolysis. A current is passed through an electrolyser that separates water into hydrogen and oxygen. Importantly, this process is powered by renewable energy and is therefore free of greenhouse gases, making it the cleanest method of production.



> *"The colour codes are used within the energy industry to distinguish between the different types of methods used to produce that hydrogen*

Uses of hydrogen

To combat climate change we need to increase the supply of renewable energy. Wind and solar play key roles and have scaled up significantly in recent years. However, they are still reliant on weather conditions and therefore may be underproducing or overproducing at any given time. A system of storing energy when a surplus is being produced is one way to smooth the imbalance. A hydrogen storage facility could store larger quantities and for longer than its battery counterpart. It has also proven its merits in the real world – Markham Energy Storage Facility (North America's first multi-megawatt power-to-gas facility) uses renewably sourced hydrogen to provide grid regulation services in Ontario, Canada.

In addition to its storage capabilities, hydrogen is a clean source of fuel. When used in a fuel cell it can generate power, producing only water and heat as by-products. Fuel cells work in a similar fashion to batteries but do not need to be periodically recharged; instead, they continue to produce electricity as long as a fuel source is provided. These qualities make them an attractive option for powering vehicles and portable power devices as well as heating homes.

Hydrogen is also being explored as a means to decarbonize traditionally 'dirty' industries. Currently, it is not practical to lower emissions in chemical and natural resources companies through electrification, so CO_2 emission levels have remained high. There are a number of companies across Europe working on hydrogen as a solution.

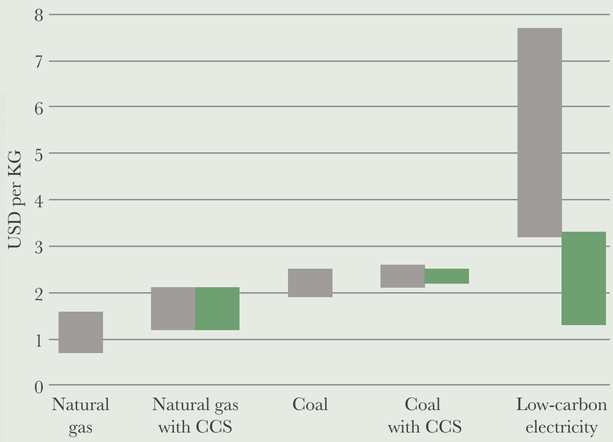
> *A hydrogen storage facility could store larger quantities and for longer than its battery counterpart*

Challenges to industry adoption of green hydrogen

Supplying hydrogen to industrial users is already a major business. The problem is that current methods are responsible for CO_2 emissions of around 830 million tonnes per year – equivalent to the CO_2 emissions of the United Kingdom and Indonesia combined, according to an International Energy Agency (IEA) report. Governments, industry, and investors will need to coordinate plans in the roll out of more climate-friendly hydrogen to scale up infrastructure development.

As with many technologies in the early stages of adoption, costs are higher than those of established production methods. Though the falling cost of renewable energy is making it cheaper to produce green hydrogen, the average cost of just over $5/kg is still significantly above that of grey hydrogen, which is roughly $1.5/kg. However, the Hydrogen Council forecasts that renewable hydrogen could break even with grey hydrogen before 2030 in optimal regions. This is down to increased utilization levels and falling capital expenditure requirements, although in less favourable areas the IEA suggests 2050 is a more reasonable target.

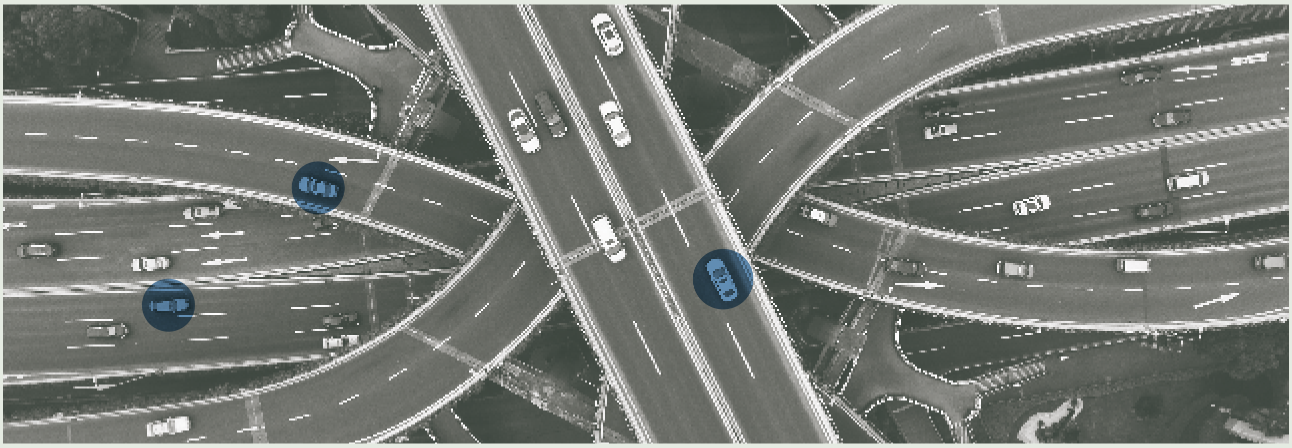
CHART 1: GLOBAL AVERAGE LEVELIZED COST OF HYDROGEN PRODUCTION BY ENERGY SOURCE AND TECHNOLOGY, 2019 (GREY) AND 2050 (GREEN)



CCS = Carbon Capture and Storage

Source: **IEA (2020) Energy Technology Perspectives.** www.iea.org/data-and-statistics/charts/global-average-levelised-cost-of-hydrogen-production-by-energy-source-and-technology-2019-and-2050.

The final and arguably most important challenge is increasing investor confidence. Without investment the industry will fail to grow. New projects stand at the riskiest point of the development curve. It is vital that governments and the private sector work together to eliminate any unnecessary regulatory barriers and support research and development. Not only will that involve the use of public funds but it will also attract private capital.



Hydrogen is undoubtedly a hot topic but this is not the first time

Government support

Governments will play a major role in getting the widespread adoption of clean hydrogen on the right path. Already we are seeing policies put in place in a bid to hit net zero targets. President Biden, for example, has released infrastructure plans that include $10bn for clean energy innovation. The European Union has plans for at least 40GW of renewable hydrogen electrolysers by 2030, whilst Australia is funding AU$370m for new hydrogen projects.

Green hydrogen is at the heart of energy transition plans. Closer to home, the UK government has recently launched a strategy to meet its goal of 5GW of low-carbon hydrogen production by 2030. Roughly £900m of funding will be made available to support hydrogen projects and it will consult on the design of a £240m Net Zero Hydrogen Fund to support the development of low-carbon hydrogen plants.

Another hydrogen bubble?

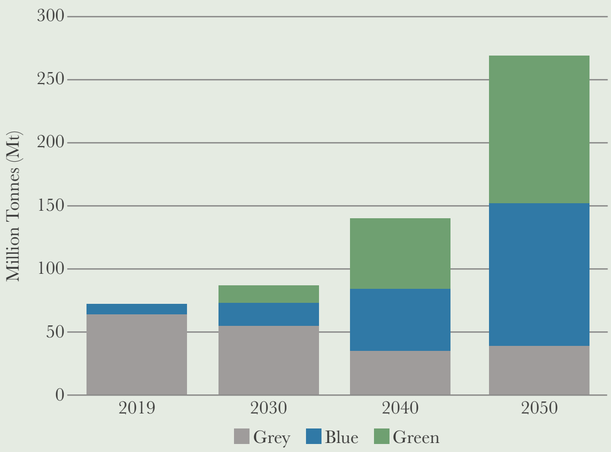
Hydrogen is undoubtedly a hot topic but this is not the first time. In 2003, President Bush announced a $1.2bn hydrogen fuel initiative with hopes of reversing America's growing dependence on foreign oil. The initiative included $720m in new funding to develop technologies and infrastructure to produce, store and distribute hydrogen for use in fuel cell vehicles and electricity generation.

Shortly before this hydrogen push, as the dotcom bubble burst, the share price of hydrogen stocks rocketed. In 2000, fuel cell stocks such as Plug Power, Ballard Power and Fuel Cell Energy saw tremendous share price appreciation only to see gains unwind in the subsequent years.

This time, hydrogen share price appreciation is being supported by three factors: policy decisions, industry disruption and green investment. Governments are putting hydrogen at the core of their clean energy plans. A report from the Hydrogen Council highlights that 75 countries representing over half of the world's GDP have net-zero carbon ambitions and more than 30 have hydrogen-specific strategies. In the private sector, pressure is intensifying on corporations to cut emissions. Companies from oil majors to media firms are making significant changes to current operations in a bid to reach net zero. BP and Royal Dutch Shell, for example, are funnelling millions of dollars into hydrogen projects as they seek to redefine themselves. Environmental and Social Governance has moved on from being a side-line act to the main event, and investors are willing to put their money behind it. That creates a huge opportunity for hydrogen companies to attract funding and, with rates so low, financing is at more affordable terms too.

Hydrogen is currently a relatively small contributor to the global energy mix, but research provider Bloomberg New Energy Finance projects that its share could increase from 2% in 2018 to 13–24% in 2050.

CHART 2: GLOBAL HYDROGEN PRODUCTION FORECAST, 2019-2050



Source: **IEA (2020) Energy Technology Perspectives.** www.iea.org/data-and-statistics/charts/global-hydrogen-production-in-the-sustainable-development-scenario-2019-2070.

> *BP and Royal Dutch Shell, for example, are funnelling millions of dollars into hydrogen projects as they seek to redefine themselves*

Hydrogen market

Hydrogen gas producers

Industrial gas businesses, such as Air Liquide and Linde, operate leading hydrogen ecosystems. They build, own and operate assets with a focus on production and distribution. In collaboration with partners, new hydrogen applications are developed. These companies help tackle some of hydrogen's biggest challenges – storage and transportation. Though seen as a high-growth opportunity, hydrogen tends to make up a small percentage of total revenue.

Storage and transportation

Storing hydrogen is complicated. It can be stored as either a liquid or a gas. As a gas it requires high-pressure tanks. As a liquid, it needs extremely low temperatures to keep it below its low boiling point. Hexagon Composites engage in storing and transporting hydrogen, though again, it is a small part of their business.

Fuel cell producers

As discussed earlier, hydrogen fuel cells are used to generate power. The development and manufacturing of fuel cells is very specialised. These businesses are crucial to the chances of hydrogen power taking off. Though still at early stages, fuel cell technology is being tested in the transportation sector and successful trials could lead to increased demand. Ceres Power is an example of a UK fuel cell producer.

Pure play hydrogen

Plug Power is a great example. It provides alternative energy technology with a primary focus on the development of hydrogen and fuel cell systems. It recently started working on its third green hydrogen plant, with its reach now covering the majority of the East Coast of the US. This is essential for enabling commercial vehicle fuel cell adoption. The group could be a beneficiary of a larger scale hydrogen roll out, though this is somewhat reflected in recent share price appreciation. Note too that the group is loss-making and burning through cash. While there are mitigating factors – losses are perhaps to be expected when in the early stages, and Plug Power is leading the hydrogen ecosystem scale up – the losses bring risks.

Conclusion

Hydrogen is an attractive theme for a number of reasons. It is a clean source of energy with the potential to decarbonize high CO_2-emitting industries, and it is being supported by government policies and backed by private investors alike. This creates a huge opportunity for market growth. However, picking an individual winner is difficult. Many pure play hydrogen stocks are currently loss making as the market still develops. Nevertheless, share prices enjoyed a good run through much of last year. Since peaking earlier this year they have moderated, creating a much better entry point. Other businesses with a vested interest in hydrogen tend to be less exposed to the theme. For industrial gas businesses, as an example, hydrogen is only a small part of the picture.

L&G Hydrogen Economy ETF

Our chosen way to gain exposure to the hydrogen theme is via an ETF. There are currently only two options within the market: L&G Hydrogen Economy ETF and VanEck Hydrogen Economy ETF. Our preference is for the L&G product, which is much bigger in size, offers a more diversified portfolio and has a less concentrated list of top ten holdings. That being said, this ETF slots into the upper end of the risk spectrum. Hydrogen is in the early stages of what could be the beginning of a super cycle. For those wanting to take that bet, this is a good option.

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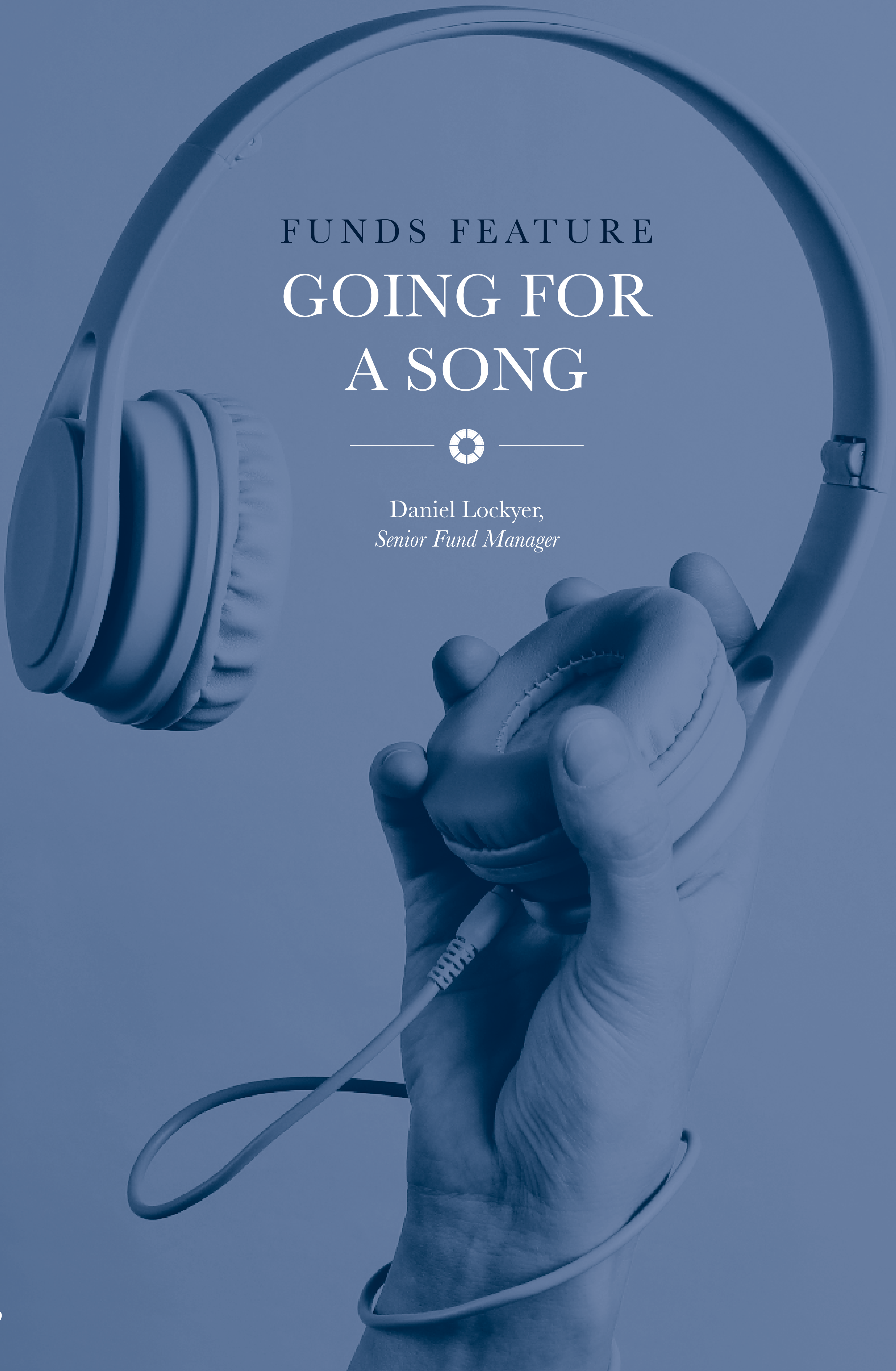

FUNDS FEATURE

GOING FOR A SONG

Daniel Lockyer,
Senior Fund Manager

How important is music in your life? Certain songs can take me back to key moments in my life such as the first record bought with my saved up pocket money, the first time I heard a particular artist having had a recommendation from a friend at college, or the song I 'danced' to at my wedding (no, I am not disclosing any of them but feel free to guess!).

Music seems central to our lives and today it is so easy to access with phones and connected devices such as smart speakers, cars and watches linked to streaming services or digital radio stations. We only have to ask Siri, Alexa or Google to play something and it is instantly in our ears.

I also remember spending hours putting together a mix tape (younger readers will have to ask Siri *et al*), recording songs from the radio or from my record player, pressing the pause button before the DJ started talking or the needle got to the end of the record. Now you just pick from an infinite list of songs on your phone and you have a bespoke playlist.

The reason for this trip down memory lane is to highlight that 'songs' is now an investable asset class as well as something to listen to, dance to, cry to, etc.

In the UK there are two publicly listed companies – Hipgnosis Songs and Round Hill Music – that have acquired, over the years, catalogues of songs belonging to artists, song writers and producers. Cash is handed to these individuals in return for their song royalties, which are then paid as dividends to shareholders in these companies.

> *Globally, there are 450 million subscribers to music streaming services, up from 280 million three years ago*

This is now possible largely because of the digitalisation of the industry, allowing revenue sources and rights to be much more transparent and easier to register. Twenty years ago nearly all the revenues from the $24 billion industry came from sales of physical music: CDs, cassettes and records. Today, after a trough in 2014 when annual revenues fell to just $13bn due to piracy and illegal downloads (which discouraged buying and therefore new investment in the industry), it is back to $23bn. This is made up of just $5bn coming from physical sales, with streaming now accounting for over $13bn a year. Downloads and synchronisation (when music is used in films or adverts) and performance rights (live music or music played in bars, restaurants, gyms, etc) make up the difference.

To illustrate the growth in streaming and how music is now viewed as a utility rather than a discretionary item, in the old days to achieve a platinum disc you needed to sell one million records. In the US (which has a population of 360 million people), that is 1 in every 360 people bothering to go to the shops and buy that record for $10. Today in the US there are over 100 million households with a subscription to a music streaming service (costing around $10 per month), meaning more than 1 in 3.6 people can now listen to a particular song.

> *When an asset class is hot, like 'songs' is at the moment, it is important to remember investment principles to ensure returns are not impacted by overpaying for the asset*

Globally, there are 450 million subscribers to music streaming services, up from 280 million three years ago. Currently, Spotify is the market leading platform with around 34% market share, followed by Apple Music, Amazon Music and Tencent Music. In addition, there are other platforms that have to pay royalties such as YouTube, Peloton and TikTok, which expand the sources of revenue for the owner of the songs. Although the amount per stream that is paid to the songwriter or artist is tiny (typically $0.007 per stream), the ability to reach a much bigger audience today is considerably greater and many have made their fortune from a billion-streamed song. Remember that the mix tape was free for me and the rest of the world who recorded it, but now I am paying a monthly fee.

At the moment when debt is free, money is plentiful and yields on bonds and equities are low, it is natural that capital is flowing to higher yielding assets. With a c.4% yield, a huge pool of assets to pick from and the longevity of the royalty rights (typically the lifetime of the last surviving artist/writer +70 years), it is not surprising that songs are on the radar of many investors including deep-pocketed private equity funds.

It is also unsurprising that many artists are considering selling their catalogues for a lump sum to avoid the hassle of managing all the various income streams and to ease the estate planning on death. It may also serve to replace the lost income from the lack of touring over the past year, which ruined their planned 'farewell' or 'reunion' tour.

When an asset class is hot, like 'songs' is at the moment, it is important to remember investment principles to ensure returns are not impacted by overpaying for the asset. In the case of Hipgnosis Songs and Round Hill Music, their average cost of acquiring catalogues of high-quality artists that span the eras and genres is around 16x revenues. This doesn't seem excessive to us, especially when compared with the valuations afforded to much larger peers, such as Universal Music Group or Warner Music Group.

When we listen to some of our favourite songs now, as shareholders in Hipgnosis Songs and Round Hill Music, we can help generate additional royalty income for them and us; although it may take a while to get through the 164,000 songs in the combined catalogues (about a year I reckon)!

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> ...you become poorer if inflation outstrips the rate of return from your assets

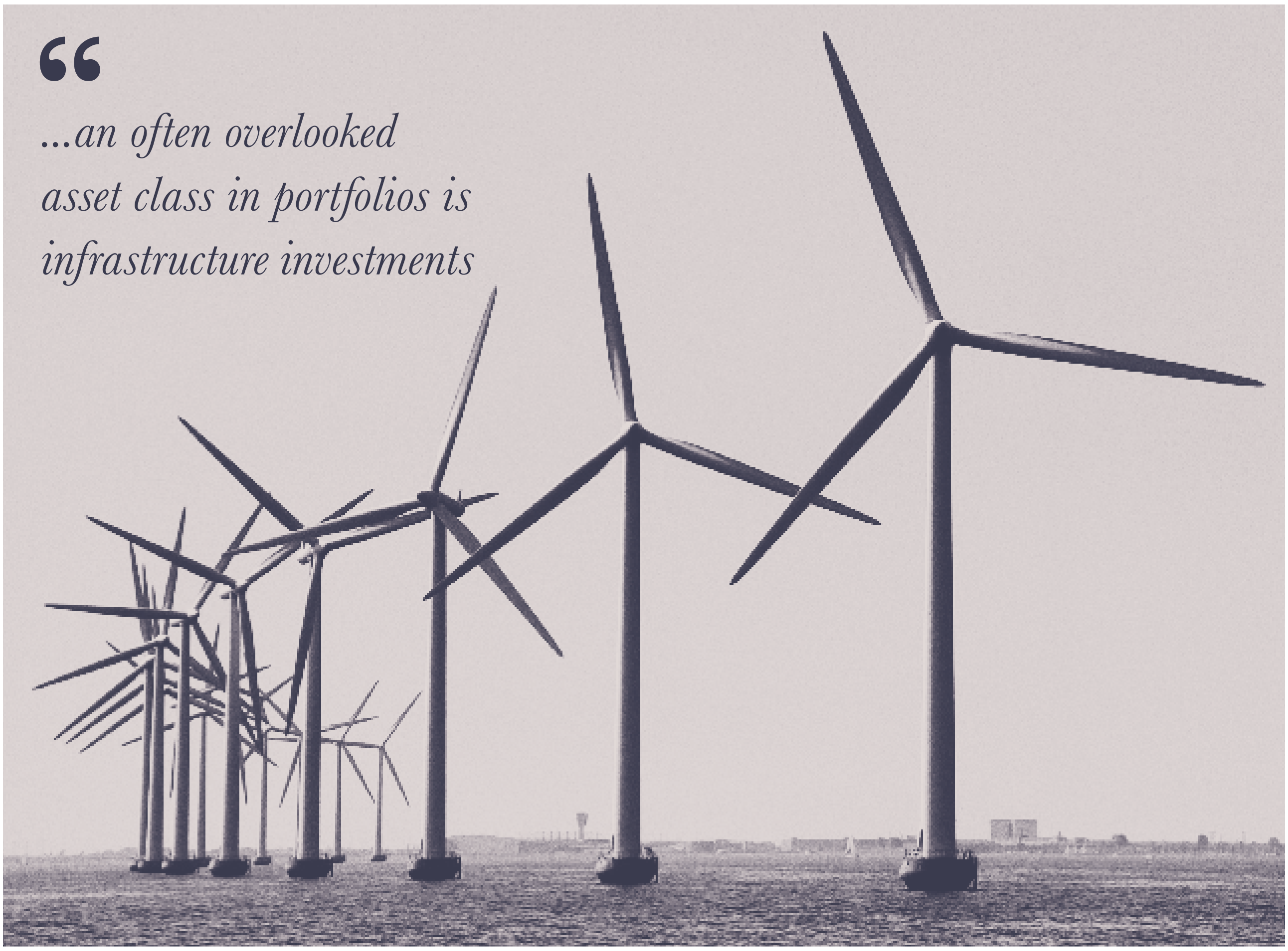
DEAR HAWKSMOOR...

The prospect of higher inflation seems to be dominating the financial press currently. How does Hawksmoor inflation-proof client portfolios?

This is a very pertinent question. One of the many unpleasant side effects of persistently high inflation is that it can rapidly reduce the purchasing power of your investments – in other words, you become poorer if inflation outstrips the rate of return from your assets. Even with modest inflation of 2%, £1,000 stuck under the mattress would only purchase the equivalent of just over £900 of goods in five years' time. Inflation has effectively made you £100 worse off. Cash is certainly not the solution.

Resurgent inflation (rising prices) such as we are witnessing now is unsurprising. The impact of both governments and central banks pouring money into the global economy since the beginning of the pandemic and the unleashing of pent-up demand were always likely to be inflationary. The figures are eye-popping; in the US, the M2 Money Supply (crudely a measure of how much extra money is sloshing about the economy) grew by more than 25% last year compared with the trend rate of 7% per year in the past decade. Labour and supply shortages (the latter partially caused by the Suez Canal blockage earlier in the year) coupled with surging demand has added to the inflationary pressures.

It is worth remembering that as a rate of change measure, the inflation rate was inevitably going to be higher this year compared with last – as an example, the oil price is now rising having tumbled last year with the onset of the pandemic. As Jim Wood-Smith eloquently explains in his article, the question which has been vexing economists and taking up plenty of column inches in the press is whether this higher inflation is temporary. At the time of writing, the Bank of England believes this will be an inflationary spike rather than a return to a permanent 1970s-style rate of inflation.



Whatever the true outcome, having some inflation-proofing in a portfolio is a sensible strategy. To return to the question, a textbook answer would give a number of options but many of them have flaws. Gold is often seen as a store of value during inflationary times, although it is far from being the perfect solution as other factors influence the gold price. For example, a booming US economy could lead to a strong dollar which in turn is often bad for the price of the yellow metal. Investing in commodities (raw materials) can, at times, defend a portfolio against inflation but they are highly volatile and, like gold, an imperfect defence. Booming commodity prices earlier in the year helped lift the mining shares, supporting this inflation-proofing thesis of commodity-backed investments. However, the recent collapse in the iron ore price thanks to curbs on steel production by China has seen the mining shares retreat. Another popular choice is inflation-linked (index-linked) government bonds. The income and the price of the bond will rise with the inflation rate over the lifetime of the index-linked bond. In theory, they should be the perfect solution. For brevity, I will not delve into the complexities of index-linked bonds, except to say that their popularity has meant they are very expensive such that they are already pricing in a good deal of inflation. Only if inflation surges much higher than the level these index-linked bonds are implying will you truly make an inflation-beating return. The shares of companies with pricing power and low levels of debt should do well with modest inflation and such shares should form part of any well-constructed portfolio.

However, as Jim briefly touches upon in his article, an often overlooked asset class in portfolios is infrastructure investments. These can be an especially good option for investors seeking an income that keeps pace with inflation. There is a wide range of infrastructure assets including renewable energy networks, ‘next day’ delivery warehousing, storage facilities, digital infrastructure such as deep sea internet cables and critical transport such as toll roads. The income from these assets may be derived from supply contracts, rents or customer demand. As physical, tangible assets, they are often a good way of providing a portfolio with a high degree of inflation protection as rents or valuations often rise at least in line with the general level of prices. The performance of such investments may differ. For example, property demand tends to be more vulnerable to the state of the general economy whereas, by its very nature, demand for essential infrastructure is more stable. There are plenty of options for investors to add infrastructure assets to their portfolio. At Hawksmoor, we tend to use specialist property and infrastructure investment trusts as a way of providing some inflation-proofing to a portfolio.

Greg Sellers, *Senior Investment Manager, Taunton Office.*

NEXT GEN

LOSS AVERSION

Do you respond more strongly to a financial loss than a gain? Assistant Investment Manager Jason Hopton looks at the psychology of investing.

Back in 2008 I was finding my feet in the adult world; I had just started my first job and was blissfully unaware that we were in the midst of the great financial crisis. The naivety of youth!

Why is this relevant? It meant that up until March 2020 I had never experienced a severe market crash as an investment professional, and based on my experiences, the markets always went up. Luckily, in the modern world we do not have to rely solely on our experiences and instead can read up on history in order to prepare ourselves for any potential extreme market events.

There is a lot of talk amongst the investing professionals about selecting good fund managers and picking good companies, but you rarely hear about the psychology of investing. We can select the best fund managers or the best companies, but if we sell all our investments during a general market crash then our skill at picking these funds and companies becomes irrelevant.

To add an extra layer, not only do we have to control our own psychology but we also need to make sure that you, as our clients, have the right psychology.

Loss aversion is one of the more common elements in investing psychology. In short, loss aversion means that we put a greater weighting on a loss than on an equivalent gain. For instance, we react much stronger to a loss of 10% on our portfolio than a gain of 10%.

To put this into a real-life context, the MSCI PIMFA Balanced Investor Index* gained 95% from the start of 2012 to the end of 2019 but lost 15% in the first three months of 2020. At the time of writing, this index was 10% higher than at the end of December 2019 and had recovered all of its coronavirus-induced losses by the end of 2020.

However, I imagine that the market crash at the start of 2020 remains more in your mind than the strong run leading up to this crash and the impressive returns achieved since.

At Hawksmoor, our method of controlling our psychology is to follow an asset allocation that diversifies the portfolio whilst allowing us to remain invested. Our role, as your investment manager, is to help guide you through your investing journey and build a trusting relationship.

With this trust in place, we can help manage your expectations through the market drops that occur from time to time and allow you to enjoy returns on your investments regardless of whether it is during a bear market or a bull market.

**the MSCI PIMFA Balanced Investor Index aims to represent the investment strategy of a client seeking a balanced approach between income and capital growth in their portfolio.*

SPLASHING OUT: THE HISTORY OF WEALTH IN BATH

As Hawksmoor's new Bath Office opens its doors, Senior Investment Manager and Head of Office Ian Bailey considers the city's historical association with wealth and investment.

Mention the City of Bath to people and the chances are they immediately think of the TV series Bridgerton! However sitting in Hawksmoor's newly opened Bath Office and looking out of the window at the Roman Baths and Bath Abbey, I am instantly reminded that the city has a long and eventful history. It seems UNESCO is in agreement as it made the whole city a World Heritage Site in 1987. Such "heritage" originally came from wealth (someone had to have the money to construct these buildings in the first place) so now seems like an opportune time to sit back and think about the history of wealth in Bath.

The city boasts its own Iron Age hill fort, but the first big development came with the Romans when they built the baths between 60 and 70 AD. These were actually built on a Celtic shrine based around a sacred spring – thus demonstrating one of the first great business principles of adapting success for a new age. Over the next 300 years the Romans developed the bathing complex, creating significant wealth in the city. A good example of this wealth is the hoard of 30,000 silver coins unearthed in an archaeological dig near the baths (proving that at least one Roman made the foolish decision not to invest, resulting in his capital failing to retain its real value against inflation!).

Of course, all things must eventually change and in the early 5th century AD the Romans departed, leaving behind strong Romano-Celtic communities. Like many investors throughout history, these communities tried to adhere to the old way of doing things. Sometimes they were successful (King Arthur is purported to have seen off Saxon invaders in a battle on Bathwick Hill) but the winds of change are irresistible and in 577 AD the last Celtic kingdoms fell to the Saxons in a battle at Dyrham, a few miles north of Bath.

As all good investors know, a period of change comes with both risks and opportunities and so it was with the coming of the Saxons. When not burning cakes (Mary Berry, herself born in Bath, would not have approved) or defeating Vikings, King Alfred found the time to lay out a new road structure for the city and in 973 AD King Edgar started building Bath Abbey. There would certainly have been lots of investment opportunities there – although investing in major public building contracts can be fraught with peril!

Moving past 1066 (and all that) Bath reinvented itself, prospering from its proximity to the flourishing wool trade of the Cotswolds, which was the Silicon Valley of its day. The area also gained political importance with the establishment of the Bishop of Bath and Wells. City status came in the reign of Queen Elizabeth I and the baths were improved to such an extent that Anne of Denmark paid royal visits in 1613 and 1615. The English Civil War saw the city divide between a Royalist mayor and strongly pro-Parliamentarian merchants, and one of the great battles of the war was fought on Lansdown Hill overlooking the city (close to what is now the Park and Ride).

The Georgian period saw the city re-inventing itself yet again following Thomas Guidott setting up a medical practice in the city that focussed on the restorative properties of the spa waters (a good 'Pharmaceutical'-style investment). Tourists began to flock to the city and in the early 18th century we see the first investments in this new source of wealth with the building of a theatre and the Pump Room. Indeed, the city fathers appointed Beau Nash, a celebrated dandy, as Master of Ceremonies (an early form of social influencer) and between 1705 and 1761 he introduced a code governing the city's social life. By 1801 the population was in excess of 40,000 and just after the Battle of Waterloo, Bath was described as being a "a seat of amusement and dissipation" where "scenes of extravagance in this receptacle of the wealthy and the idle, the weak and designing" were commonplace. Salacious stuff indeed! This was a time of great expansion, providing the city with the skyline and ambience we all know so well today. There was massive investment in the city, with the architect John Wood (and later, his son) laying out the new squares and street network and building extensively using the famous Bath stone. This was the era that saw the building of the Assembly Rooms and the architectural marvel that is the Royal Crescent. In addition to the investment in the leisure sector, there was scientific discovery happening elsewhere in the city. In 1781, William Herschel discovered the planet Uranus from his garden in New King Street and went on to become Court Astronomer to George III.

Everyone, it seemed, wanted to come to and be seen (and invest) in Bath…except for Queen Victoria. When a young Princess Victoria opened the Royal Victoria Park in 1830 it is said that a resident of Bath commented on the thickness of her ankles. When this was reported to the Princess it caused her to shun the city for the whole of her reign. It is alleged that she even used to request the curtains be drawn if a railway carriage she was in passed through Bath! Clearly she was "not amused."

So there you have it. An ever-changing city able to reinvent and adapt itself to the prevailing market conditions. A city with a distinct individuality and character. Whether you are Jane Austen, Mary Shelley or Mary Berry it is a place where you can let your creative juices flow. A city that is very much built on its legacy and history, but also one that is constantly looking to the future and a natural home for wealth. Above all, it is a natural home for our new office!

> *Bath reinvented itself, prospering from its proximity to the flourishing wool trade of the Cotswolds, which was the Silicon Valley of its day*

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IMPORTANT INFORMATION

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