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Property and discounts drive February portfolio picks

Advice businesses have reacted to market changes and shifts in fund management by making strategic plays to get good deals for clients in February

IFAs across the UK have been making changes to their model portfolios in the first two months of the year. SG Wealth Management, which has a foothold in Norfolk and Suffolk, formally reviews its asset allocation on a quarterly basis to assess whether it wants to tactically tilt away from its long-term strategic targets.

'Over the last couple of years, the decision-making process has been interesting with the recessionary concerns that affected markets in 2018 being pushed out by the global central bank pivot back towards easy monetary policy through 2019,' says chief investment officer Henry Gaskin (pictured right), who is based in its Ipswich office.

Given the rally in risk assets in the early part of 2019, the firm decided to take some risk off the table. It reduced allocations to UK and overseas equities in August and moved back towards the lower end of its risk ranges, a position it has been happy to maintain since.

It aims to create all-weather portfolios. Recent changes to its models include the addition of real infrastructure with the inclusion of the FP Foresight Global Real Infrastructure fund at the start of the year.

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>
> Henry Gaskin
> SG Weatlh Management

'Valuations have done well recently but we feel the asset class could continue to perform thanks to supportive monetary and increasingly fiscal policy,' Gaskin says.

Another recent addition to help diversify risk is Rathbone Strategic Bond fund, managed by Citywire A-rated Bryn Jones and co-manager Noelle Cazalis, in February.

'This is a less volatile strategic bond fund with a capital preservation mindset and a good record of delivering attractive returns to accompany the risk control characteristics,' he says.

COMMERCIAL PROPERTY

One area that SG likes for its ability to diversify risk is commercial property, to which it has an 11% allocation for balanced clients. 'We regularly discuss our allocation to property and how to access this asset class either via listed or open-ended fund routes,' Gaskin explains.

'Currently, our bias is towards physical property, open-ended funds. Their lower volatility helps them function as a diversifier within our portfolios. We've been able to manage the liquidity challenges by using funds that have good track records of managing liquidity.'

These include BMO UK Property, Kames Property Income and L&G Property, which the firm likes for their limited exposure to the challenged traditional retail sector. It also uses Premier Pan European Property, a fund of UK and European real estate investment trusts, as more liquid ways of accessing the wider regional asset class.

SG is slightly lighter than neutral on developed market equities and is also modestly underweight emerging market equities. It envisages returning to a more neutral position when the current coronavirus situation stabilises and sentiment improves.

'We don't think investors' appetite for risk assets, particularly Chinese and other emerging markets equities, will improve until there's news that the virus is under control,' Gaskin predicts.

'The impact of the scale of the coronavirus outbreak and the US election later in the year are two areas we are considering at length. We are watching for any signs of building inflationary pressures, which could be the next inflection point for a further shift in our asset allocation.'

INSIDE THE NEXUS

Meanwhile, in Hampshire, Nexus Independent Financial Advisers has been cautious for a while. Recent developments have not changed the mind of its managing director Kerry Nelson.

She has been concerned about global risks, the mismatch between stock market valuations and the wider economic picture and the lateness of the cycle by historic standards for a couple of years now.

'We had already taken some risk out of all our portfolios months ago and were waiting for triggers that could undermine already anaemic global growth and which would finally be reflected in markets,' Nelson says.

'The coronavirus may be a strong candidate because of its damaging impact on the Chinese economy and its knock-on impact on the rest of the world. Even with trade wars, we would suggest the world is still learning about how the Chinese market and developed markets are interacting.'

She challenges anyone to start trying to time their approach to any of these events. That said, she is keeping a watchful eye on the US. It is gearing up for a presidential election, but that might not have the biggest impact on financial markets, in her opinion.

'Ultimately, when we review the past few years, it may be the US Federal Reserve [Fed] not the tweet-happy president that has had the biggest impact,' she says, pointing to the Fed's volte-face on interest rate hikes last year, when it made three cuts.

Nexus' approach has been to dial down clients' exposure to riskier funds and move away from emerging markets given that that stocks and bonds in these markets are, in different ways, dependent on events in China and the US.

It has, however, avoided the traditional shift from equities to bonds. 'Our move has been towards safer alternatives with a strong track record, a reasonable income-producing profile and which give our portfolios an overall bias towards capital preservation,' she says.

These tend to be total return type funds, which minimise exposure to traditional stock and bond markets and balance this with things such as cash, currencies, commodities, money market instruments, options and structured notes.

ASSET ALLOCATION

SG WEALTH MANAGEMENT	%
Overseas equities	33%
Fixed interest	20.5%
Alternatives	19.5%
UK equities	15%
Property	11%
Cash	1%

NEXUS IFA	%
Equities	44%
Alternatives	39%
Bonds/Cash	12%
Property	5%

PHILIP J MILTON & CO	%
Income investments	21%
International equities	21%
UK equities	20%
Defensive investments	16%
Smaller companies	14%
Cash	4%
Far East equities	2%
European equities	2%

'We have to be careful because some of these funds can be quite expensive, but they give our clients a good shelter and hedge against volatility,' she adds.

Funds currently used include Garraway Financial Trends, Merian Gold and Silver, MontLake Dunn WMA and SVS Church House Tenax Absolute Return Strategies.

'We are big fans of the Church House fund. We've used it for five years and it's in every single portfolio,' she says.

Nexus clients have not been exposed to property since 2008 because 'liquidity seems to be a recurring issue. Regardless of the size and expertise of the fund manager, gating should always be avoided', Nelson explains.

'Our view is that other assets and funds can give us a similar return profile without the liquidity risk,' she says.

WHEN, AND ONLY WHEN

North Devon-based Philip J Milton & Co changes its models only when managing director Philip Milton (pictured above) sees opportunities for strategic alterations. As a value investor, he often buys investment trusts trading at discounts. Investment trusts account for around three-quarters of the company's assets under management.

A recent interesting addition is Schroder UK Public Private Trust, formerly Woodford Patient Capital, which Milton added to portfolios before the trust's new manager was announced last October. Tim Creed and Ben Wicks have since taken over the running of the trust after Woodford was sacked.

'We started too soon with smaller nibbles, but have continued buying it since,' Milton says.

'It could easily double from present levels while the downside from here should be somewhat limited.'

Given its bias towards private equity, the trust is uncorrelated to ordinary equities. Clients of Philip J Milton & Co hold more than four million shares. That represents less than 1% of its assets.

'No client is over-exposed. We believe in a vast range of components so no holding represents a big proportion,' Milton explains. 'Pursuing small exposures in things that can produce a real kick means even smaller clients can have some – a £20,000 investor may have £300 in the trust.

'Brokerage costs are percentage-based with no minimal, so very cheap to buy and sell. It won't break the bank if it falls, but a doubling would add 1.5% to the total return with the other £19,700 doing its own thing.'

In January, Milton started selling Shires Income when its shares were trading at a small premium. He had owned it for years (predominantly at a discount) but started selling to raise capital to buy Aberdeen Diversified Income & Growth and Perpetual Income & Growth at what he calls decent discounts.

'The Aberdeen holding has been unpopular having missed its original target as an absolute return fund, something we never really pursued as a concept, but as people have been quitting a big discount has opened and it became compelling to us as a relatively low-risk diversified holding with a good yield,' Milton says.

'If nothing changes, it doesn't matter but if the discount [currently 9%] disappears our investors unlock an extra return for nothing.

'At Perpetual, [Invesco fund manager] Mark Barnett has been blighted by the Woodford debacle and the fact that he had many similar holdings. The market knows what he has and what he has had to sell in the unitised range – that has depressed the values of a number of the stocks he also holds in the investment trust. With a yield north of 4% and a potential 13% uplift to our investors from the current discount narrowing, it too is a compelling story.

'I like the UK concentration in the portfolio – the UK represents better value than many other markets.'

The chartered financial planner has also increased property exposure by adding BMO Commercial Property real estate investment trust at an 18% discount. It has £1.35 billion of assets so is liquid and yields 5.5%.

Typical cash weightings are small, with part of a 4% allocation coming from currency funds. 'I favour being pretty fully invested at present,' Milton adds. ■

JENNIFER HILL