KING & SHAXSON
ethical investing

Fund Managers Report
Q4 2018

Fund Managers Report 30th September 2018 to 31st December 2018

We concluded our last report stating we had adopted a more cautious investment stance with a view to be opportunistic into any weakness. Over that quarter major global equity indices fell over 10% (as did most ethical funds) and fixed income lost much less at about 1%.

By far the biggest factor in this decline was a significant change in perception for global growth. The further deterioration in the US political narrative (including a partial Federal Government shutdown) and the growing global trade tensions led to widespread fear that the U.S. Federal Reserve had raised interest rates too fast, putting the US growth story in danger. The change in sentiment was swift and led to aggressive selling and these fears we further ignited when the global consumer behemoths of Apple and Samsung lowered expectations. Likewise US airlines (not an area we would invest in, but a good macro-economic barometer to watch) have been downgrading their expectations. As a reaction to this uncertainty the US Federal Reserve has softened its tone and fewer interest rate rises are expected in 2019.

What made matters harder for markets were the fact that there is no real sign of recovery anywhere else in the world. In China, the world's second largest economy, the transition towards a mature economy continues to hit bumps (both internal and trade related) and concerns over high debt levels and the economic slowdown continues to tax investor's minds. Japan, the world's third largest economy, continues its 30 year limp.

The political civil war over Brexit continues to crimp growth in the UK, the world's fifth largest economy. As matters reach a head we expect the noise to increase but little to happen until the end of March. Recent headlines celebrated the Eurozone's unemployment falling below a still staggering 8% for the first time since 2008! Meanwhile the ECB have finally ended their QE programme at a time when the economic outlook has declined. What is of more concern to the markets though are the increasingly weak forward looking data, and in particular the sharp slowdown in Germany, the only fully functioning major economy in Europe and the world's fourth largest. The riots in Paris, political turmoil in Italy and stalemate in Germany leave an unsettled picture both sides of the Channel and few options for risk sensitive growth investors.

Market Outlook

Concerns about the US economy have made the outlook more uncertain than it was at the end of September. Likewise the rapidly approaching deadlines for both Brexit (March) and

US-China trade talks (Feb) have added a sense of urgency. The key difference between now and the end of September is that a great deal more of this uncertainty has been priced in as the markets have already reacted to the uncertainty.

Whether the markets have not just reacted, but over- reacted is now the question we face as we enter 2019. The key variance being that there will be some kind of resolution for the issues by the end of the quarter. The US and China will either be talking or not, and instead of a stream of headlines and nonsense we will have some kind of answer on Brexit; hard, soft or even chewy. Either way, it's the uncertainty that markets do not like and whatever the outcomes, markets will adapt and with the current level of low expectations we see marginally more chances of a recovery. Whilst we remain very cautious, we used the uncertainty in the last quarter to opportunistically add to equity investments at points of weakness and will adopt the same nimble approach for the coming quarter.

Also from an ethical perspective, the oil price has remained volatile in line with the markets and this has a significant influence on stock markets. Add to this the highly valued FAANG stocks (Facebook, Amazon, Netflix et al) in the US have been more vulnerable to the global growth scares as well as increased political scrutiny.

At the same time we have seen increasing use of renewable energy around the world and some technologies continue to mature. With property investments that are focussed away from troubled retail we have seen some a little more stability.

Portfolio Changes

(These are major changes and may or may not apply to your portfolio)

In bonds we sold the Yorkshire Water Index linked bond in many portfolios. We have been pleased with the investment which we added in 2014 but having added some floating rate notes earlier in the year, we decided to take profit on this index linked investment.

The Triple Point Social Housing REIT raised more funds with a rights issue in which we participated, increasing portfolio exposure to this very important sector a little.

In UK equities we sold SSE as the investment outlook for this company continued to deteriorate and we continue to favour Orsted. We trimmed Unilever as the investment was relatively stable during the recent turmoil and we wanted to add some new investments making this a useful source of funds.

We added back to National Express in the market turmoil and also two new investments (depending on objective and holdings), Severn Trent Water in late November as an income investment, and Johnson Matthey as a growth investment. We also added to FirstGroup in the market weakness.

In Europe we added to Orsted after selling SSE, we see strong prospects for the world's leading offshore wind generator; we trimmed Vestas Wind Systems after a strong rally in the share price. We sold Fresenius after a series of unexpected profit warnings meant we lost confidence in the management.

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