CREDO WEALTH

How the Shippers Stole Christmas

In 'The Consolation of Philsophy', Boethius tells us that constancy is foreign to the character of Fortune; misfortune strikes indiscriminantly. Such sentiments, however, would provide little solace to the millions of consumers who went without last Christmas, as inclement weather and inadequate infrastructure caught UPS and FedEx off-guard. Their misfortune was the concurrence of an unusually late Thanksgiving and surging levels of online shopping, which overwhelmed shippers' distribution networks.

In its infancy, eBay built a new datacentre, many fold larger than their existing one, and called it "The Church". The name was apt given the synonymous construction requirements of the two. Like the wax and wane of religious fervour throughout the year, their new system had to be able to cope with peak traffic around the Christmas holiday, yet run at low cost for the remainder of the year where capacity utilisation would be below 50%. eBay executed this incredibly well and posted industry leading growth figures for the decade that followed. The question is, with shipments expected to grow by 11% this year can FedEx and UPS similarly capitalise on fast growing volumes, or will Fortune continue to stymie their efforts?

So far, UPS has spent $500m on automated sorting systems to rapidly identify ZIP codes and reroute packages in the event of bad weather. The new system, that identifies ZIP codes with colours, has cut the training time down from an intensive two-week programme, where employees memorised over 100 ZIP codes, to between two and three days. Given the army of some 85,000 temporary employees UPS will employ over the festive period, the impact is anything but neglible. Even now the number of packages processed has increased by up to 15% in some facilities, contributing to recent promising figures: on Monday 22nd December UPS delivered 34 million packages, an unprecedented figure.

As jet fuel prices fall, so too do the attached fuel surcharges. In the third quarter this year, jet fuel prices declined 30%, and as the couriers source their fuel under contracts, we can expect greater savings over the coming quarters. Add to this the stimulatory impact of lower gas prices on retail demand, we can expect buoyant air freight and ground volumes to persist into 2015. If FedEx and UPS have learned from last year's mistakes, where chaotic Christmas deliveries resulted in 2 million delayed express packages and landed UPS a 14% decline in Q4 earnings, the returns on their restructuring and infrastructure investments should be considerable. And the secular trend of increasing e-commerce as a share of consumer spending should enable them to continue to reap the rewards. This holiday period will be the test of their mettle.

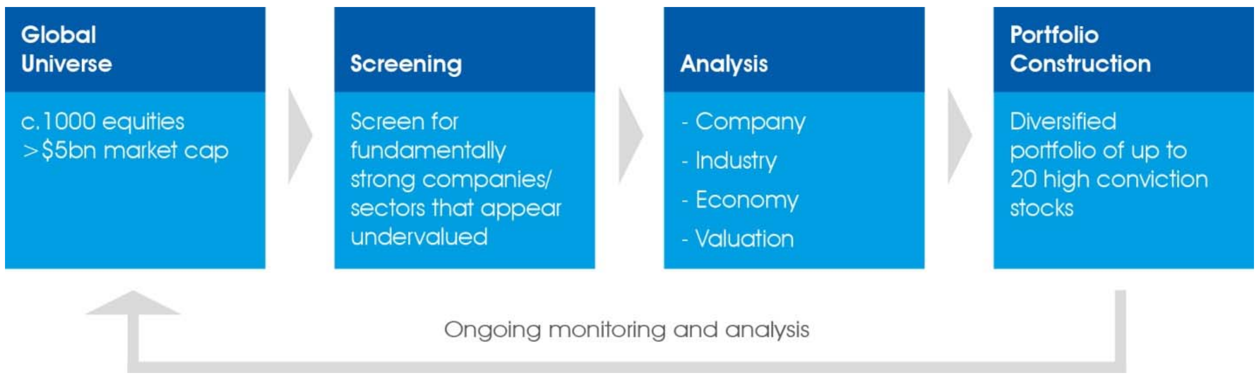
Already, some have been tried and found wanting. The collapse of City Link on New Year's Eve may seem prophetic for the industry as a whole: online consumers expect rapid, traceable, and convenient deliveries, but do not wish to pay much for the service. Accordingly, City Link's misfortune can be largely attributed to "sub-market pricing" in a bid to win business. UPS and FedEx, however, are largely insulated from such woes, offloading the back-end of their cheaper delivery options onto the USPS, a quasi-governmental agency.

However, just as inefficiency begets innovation, poor execution incentivises new entrants. Continued failure on the part of the large shippers will increasingly motivate large, cash-rich tech companies (i.e. Amazon) to enter and attempt to reshape the industry. There may come a time when the likes of Amazon will snap at the heels of the established shippers, but for now, with scale and momentum on their side, and fortune in the balance, UPS and FedEx can continue to deliver.

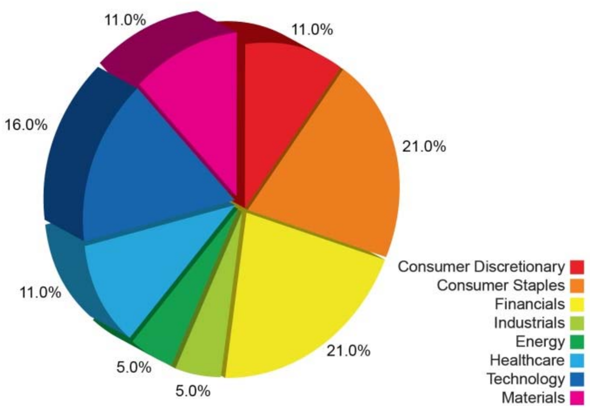
BESTIDEASPORTFOLIO

The Credo Best Ideas Portfolio is a diversified portfolio (not a fund) of global equities which we believe to be well-positioned to outperform the wider equity market over the longer term. The portfolio has a bias towards developed market, large capitalisation stocks. Our aim is to generate sustainable excess returns versus global market indices through careful stock selection.

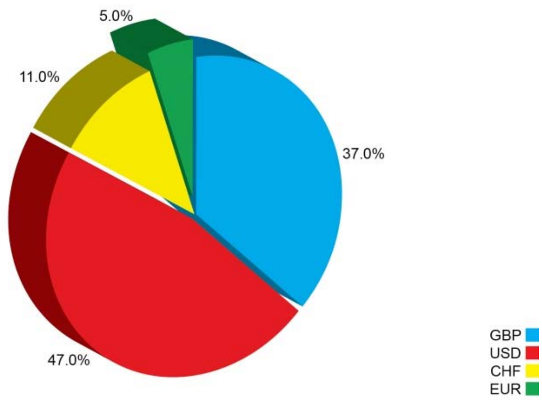
Investment Process



Sector Allocation



Currency Allocation



Performance / Stats[1]

	Trailing 12 Month P/E	12 Month Forward P/E	Dividend Yield	Return Since Inception (14/04/2011)[2]	Annualised Return Since Inception
Best Ideas Portfolio	14.7x	14.2x	3.0%	53.0%	12.1%
MSCI World Index	17.6x	15.8x	2.6%	44.4%	10.4%

(1) Source: Bloomberg pricing as of 31/12/2014 close.
(2) Performance figures are based on a notional portfolio, denominated in pound sterling, designed to track the holdings of the Credo Best Ideas Portfolio. Portfolio incorporates all additions and removals. Portfolio may not be fully invested at a point in time and therefore can hold a portion of assets in cash. Performance is calculated before any fees (which can vary depending on the level of service) but includes net dividends, reinvested. Following additions or removals, each holding is rebalanced to a 5% weighting.

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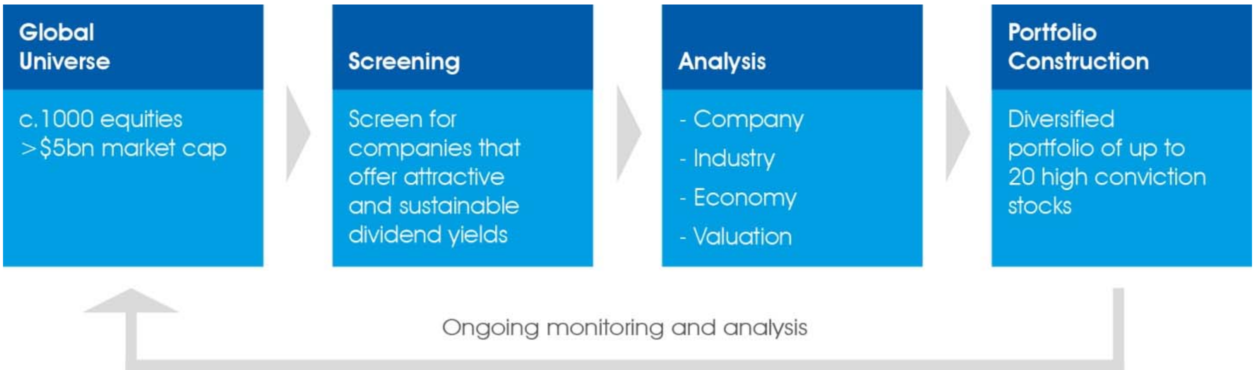
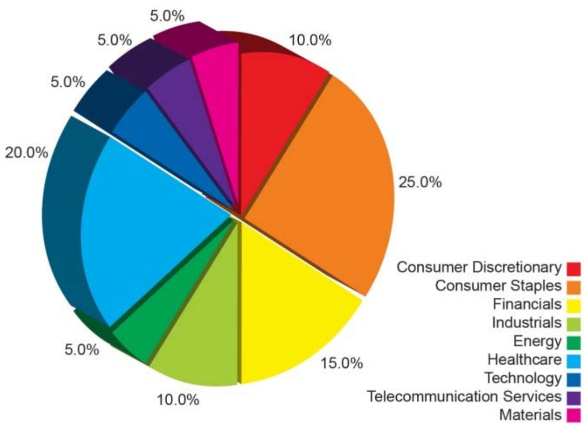
DIVIDEND GROWTH PORTFOLIO

The Credo Dividend Growth Portfolio is a diversified portfolio (not a fund) of global equities that has an objective to provide investors with a sustainable and growing income stream through dividends and share buybacks. We focus on companies that pay attractive dividend yields, with an ability to sustain and grow these over the long term. The portfolio has a bias towards developed market, large capitalisation stocks. Our aim is to generate a total return in excess of the MSCI World.

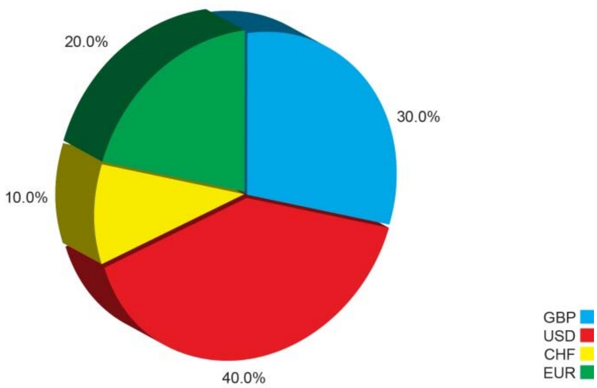
Investment Process



Sector Allocation



Currency Allocation



Performance / Stats[1]

	Trailing 12 Month P/E	12 Month Forward P/E	Dividend Yield	Return Since Inception (28/12/2012)[2]	Annualised Return Since Inception
Dividend Growth Portfolio	15.0x	14.0x	3.7%	33.8%	15.6%
MSCI World Index	17.6x	15.8x	2.6%	37.4%	17.1%

(1) Source: Bloomberg pricing as of 31/12/2014 close.

(2) Performance figures are based on a notional portfolio, denominated in pound sterling, designed to track the holdings of the Credo Dividend Growth Portfolio. Portfolio incorporates all additions and removals. Portfolio may not be fully invested at a point in time and therefore can hold a portion of assets in cash. Performance is calculated before any fees (which can vary depending on the level of service) but includes net dividends, reinvested. Following additions or removals, each holding is rebalanced to a 5% weighting.

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Update on Notional Portfolio Performance Calculations

Until now, the performance figures for each portfolio (which include total returns since inception and annualised returns since inception) have been displayed on the basis of a notional portfolio, at the launch of which it was assumed that an investor put a fixed amount of pound sterling into each stock recommendation and held until we recommended a sell. Of course, many of our clients have invested subsequent to the inception of our portfolios, and so we have decided that the methodology outlined above needs to be adjusted to account for this.

Going forward, we will report figures that more closely represent the investment team's model portfolios, using percentage weights as opposed to notional fixed amounts. Each portfolio was initially conceived as equally weighted; using percentage weights enables the portfolios to remain so, while also accounting for changes in the overall portfolio value. Importantly, these figures are based on a notional portfolio and, as such, the changes reflect no change to the actualised performance of any current client portfolio. However, these changes will provide a much fairer depiction of the typical investor's experience when investing in the Credo Best Ideas and Dividend Growth Portfolios.

Please contact your Relationship Manager if you have any queries or would like more detail on the specific changes to our methodology.

Important Notice