CREDO NEWS

The market waits for no-one

Deon Gouws

Black's mirror

Ainsley To

Corporate bonds rally hard after ferocious falls
Rupert Silver

Managing equities through the turmoil
Jarrod Cahn

and more...

Issue 33 | June 2020

A WORLD IN LOCKDOWN

The Twenties, then and now:

decades of reset

"Hopefully with astute political and economic leadership and with the benefit of experience, the difference between the Twenties of then and now will be that as we recover from the great "Wall Street Crash of 2020", depression will be avoided, and the lessons of history will have been learnt."

I am writing this note as I sit in my study after four months of home working, something which was inconceivable a mere six months ago. However, Credo, like almost all other businesses in the UK, had no choice: **we were ordered by the government to go into lockdown!**

We thus had to urgently put in place untested contingency plans in order to continue operating and servicing all our clients.

I am extremely proud of the way my colleagues responded, and we are now operating efficiently from about 90 different locations as all the UK staff as well as many of the SA staff are still working from home. The initial 3-6 weeks of the lockdown were particularly stressful for the entire Credo family, as both client queries and transaction volumes were multiples of the usual numbers, and all this whilst going through the shortest and sharpest bear market in my lifetime. Deon's article provides further colour on the market's unusual behaviour, whilst Calvin writes about the risk versus reward trade-off as well as the increase in volatility that we have experienced.

Whilst we are considering plans of when we can get back to the office and embrace the "new normal", no definite arrangements have as yet been agreed. Obviously, our major consideration in preparing the return-to-work plans will be the health and safety of the whole Credo family: colleagues, clients, suppliers as well as people working for other businesses in our different office locations.

We have kept in touch with and responded to clients timeously and all of us at Credo continue to ensure that clients receive the same personal and efficient service that we have always prided ourselves upon.

See page 23, which has pictures of most of the Credo employees, in their lockdown attire and locations.

As we go through these surreal times, I thought it would be interesting to compare and perhaps contrast the 1920s with the 2020s.

The social and cultural features of the 1920s, known as the Roaring Twenties, began in leading metropolitan centres and spread widely in the aftermath of World War I.

It was a period of economic prosperity with a distinctive cultural edge in the United States and Europe, and particularly in major cities such as New York, Chicago, Los Angeles, London, Berlin, Paris and Sydney.

This period saw the large-scale development and use of automobiles, telephones, movies, radio and electrical appliances becoming a part of the lives of millions of Westerners. Aviation soon became a business. Nations saw rapid industrial and economic growth, accelerated consumer demand which introduced significantly new changes in lifestyle and culture. The media, funded by the new industry of mass-market advertising driving consumer demand, focused on celebrities, especially sports heroes and movie stars, as cities rooted for their home teams and filled the new palatial cinemas and gigantic sports stadiums.

Much of the above could perhaps have been written about and aptly describes the noughties, the 2010s and our entry into the 2020s, with a few minor changes, i.e. one could also have added numerous other cultural centres such as Beijing, Hong Kong, Seoul and Abu Dhabi, to name just a few, as well as easily substituted "..use of automobiles, telephones, movies, radio, and electrical appliances..", with battery-operated autonomous vehicles, smartphones, the internet, social media and reusable space rockets.

The spirit of the Roaring Twenties was marked by a general feeling of novelty associated with modernity and a break with tradition. Everything seemed to be feasible through modern technology. New technologies, especially automobiles, moving pictures, and radio, brought "modernity" to a large part of the population… a hundred years later this all sounds eerily familiar as well.

It appears that the more things change, the more they stay the same!

The Wall Street Crash of 1929 ended the era, as the Great Depression brought years of hardship worldwide. Hopefully with astute political and economic leadership and with the benefit of experience, the difference between the Twenties of then and now will be that as we recover from the great "Wall Street Crash of 2020", depression will be avoided, and the lessons of history will have been learnt.

Until we meet again, stay safe, stay well and please feel free to stay in touch. ■

Deon Gouws - *CIO* | @DeonGouws_Credo

The market waits for no-one

"…financial markets have been created to make the greatest number of people look like fools for most of the time."

It's always a conundrum when someone asks us about our view of the market: is this a good time to invest, yes or no?

The honest response will always be that no-one really knows… but unfortunately that's also the one answer that clients do not want to hear. Many people see it as our job to have a view in this regard – we are investment professionals, after all?

It is a truism to say that markets are volatile, and they often move more quickly (in either direction) than even the most astute strategist would be able to forecast with any sort of consistency. This is why we do not try to "time" the market at Credo (and also why we typically invest larger inflows in a number of periodic tranches).

Take the last few months for example: after the most dramatic collapse in stock prices ever (as measured both by the speed and the extent of the decline), we have now also seen the quickest recovery on record: from an all-time high in the third week of February, to levels more than 30% lower five weeks later, and nearly back to the previous highs less than three months after that.

Who would have ever expected such a rapid rise in share prices, given a global economy in effective shutdown, record job losses being reported on a weekly basis, and doomsday scenarios – related to both our physical health and financial wealth – being painted by most of the mainstream media?

We were only about ten days into this recovery in the first week of April when I responded to a tweet by an acquaintance in which he stated that the stock market had decoupled from reality. He also asked the question: **how long can it last?**

My answer at the time was that the two are never really coupled: ultimately, the stock market reflects consensus "guessing" about a future state of reality. Financial markets are discounting mechanisms after all, and share prices today are already taking into account expectations of a potential recovery in 2021 and beyond.

Moreover, the stock market is but a narrow representation of the real economy. Your local florist might not be able to reopen when the lockdown finishes, but it's probably not listed either. It's the largest and strongest businesses in the world that are members of stock exchanges, and whilst some of them may suffer for an extended period in a post-COVID-19 world, a company like Microsoft will get through this crisis with an even stronger business than before. And the Microsoft share price has been reflecting this: it was the only constituent of the Dow Jones Industrial Index not to fall in the first quarter, and at the time of writing, it's up approximately 25% for the calendar year to date.

Also bear in mind the impact of the US Federal Reserve which has been acting in financial markets as a buyer of last resort. How the role of this institution has evolved over time is probably a topic for another day, but suffice it to say that it has never been a good idea to fight the Fed.

Just as well then that we have not been trying to tactically allocate to the market, for if we had, chances are that we might have blinked near the March bottom (as many market participants did), trying to "keep powder dry" until there was more clarity about the pandemic playing out as well as its economic consequences. We are only human, after all, affected by the same psychology of greed and fear as other investors.

As ever, though, the market showed that it waits for no-one.

What next, you might ask. Whilst I have no view about how stocks might perform in the next quarter (or even the next year or two), I will always be optimistic about longer term prospects for equities. What does equity investing really mean, after all? Unless you're a day trader, buying shares on the stock market should never be seen as a "bet" on the likelihood that the price will go up over any short timeframe; as Warren Buffett famously teaches us, **we should always think about investing in terms of acquiring a piece of a business for the longer term**.

Think of it this way: stock markets enable you to invest alongside the founders of the greatest businesses in the world: if you buy into their companies, you effectively get the likes of Bill Gates and Steve Jobs and Elon Musk (as well as the teams reporting to them) to work for you on a 24/7 basis. You thus stand to benefit from all their creativity and foresight and hunger and drive and long hours and business acumen and management skills.

By investing in equities, you back the forces of human endeavour, animal spirits, free markets, and entrepreneurship. Over time, this powerful cocktail will always lead to economic growth and positive returns, even if some blips occur along the way.

And yes, you have to accept that some of these blips will come in the form of severe crashes and bear markets such as the one we've just experienced. Nobody said that it was meant to be easy.

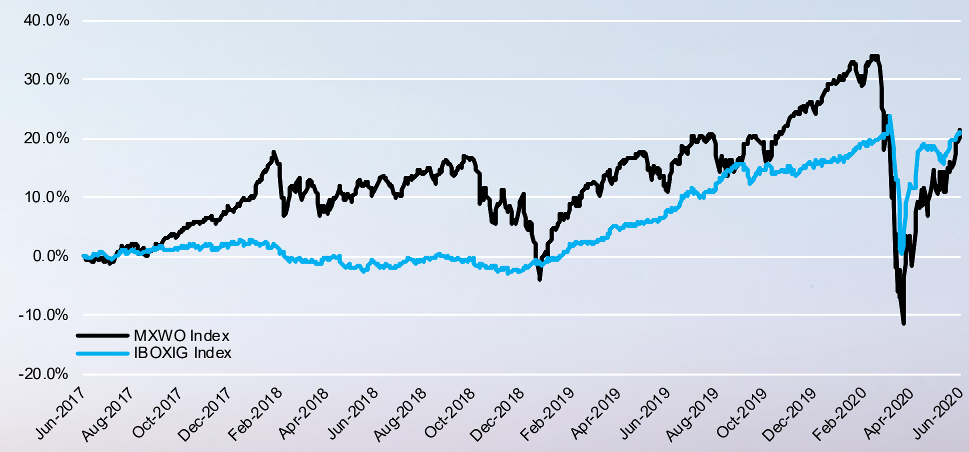
Veteran investment strategist Charles Gave once said that financial markets have been created to make the greatest number of people look like fools for most of the time; he also added that historically they have been very successful at this. Probably never more so than the last few months, one might add.

So, is this a good time to invest, I hear you ask once more?

With a view to the longer term, my answer is yes… just be prepared to look at least a little bit silly for some of the time.

Rupert Silver - *Director*

Corporate bonds rally hard after ferocious falls



The first quarter of 2020 was like no other that I've seen during my career in financial markets – specifically in fixed income. Whilst bond pricing didn't fall as much as it did during the credit crunch, the ferocity of the falls was still quite incredible as was the subsequent lack of liquidity that had been abundant only a few weeks before. With limited knowledge on how companies would cope during the COVID-19 crisis, it was no wonder that buyers held back. Most traders operated from home, thus communication was limited, and the market couldn't cope with the deluge of sell orders. In such a situation, selling begets more selling as stop losses are triggered and investors pull money from falling markets.

Only a couple of months on, the market looks very different as bonds have rallied hard alongside equity prices. The graph above plots investment-grade debt (blue line) alongside the MSCI World Index (black line) over the past three years. The correlation is quite striking, although, as one would expect, the magnitude of the recent fall was more muted in the case of bonds.

Of course, an index chart doesn't necessarily tell the whole picture and when we dig a little deeper, we note a significant divergence between those corporates caught in the eye of the storm and those that are broadly unaffected. As we saw with equities, the travel, hospitality, and non-food retail bonds lagged the market, with many companies struggling to survive and thus offering higher yields (some in the double digits). On the other hand, corporates with strong balance sheets, or those that suffered limited impact from the COVID-19 crisis (or even increased market share, like technology and pharmaceutical firms as well as food retailers), have gone on to touch new highs, resulting in yields not materially higher than government bonds presently.

With perfect hindsight, we would have "filled our boots" with bonds and stocks at the March lows. Unfortunately, very few people had the required 20/20 vision in this period. We know this not just anecdotally but by looking at investors' weighting to cash globally.

The obvious question now is: **have investors missed the boat and might debt markets plunge just as fast again should/when a second wave materialises?**

Whilst I hold no crystal ball, I'm fairly convinced that corporate bond markets are more likely to retest the highs than the lows for the following reasons:

1) Bond yields have become relatively more attractive as interest rates globally continue to fall. Lower rates look to be embedded for some time yet and zero is no longer the lower bound. We have seen negative interest rates in a number of countries. Although the Chairman of the US Federal Reserve has said that he is not considering negative interest rates at this time, the Bank of England is known to be considering such a move. Any further impact from COVID-19 is likely to see interest rates globally continue to fall.

2) Stimulus has been "off the charts". We have seen government loans, mortgage holidays, helicopter money, payments to stay home and the list goes on. Countries seem determined to pull out all the stops before it's too late. The US has made headlines for the biggest stimulus package by quantum to date, but that staggering sum is trumped by Japan relative to the size of its economy which stands at 21% compared to 13% in the US.

Whilst the stimulus has been most pertinent to equity markets, it also affects high-yield issuers that are more sensitive to the economy than to rates. The action that has had the biggest effect on the bond market as a whole, however, is the Federal Reserve's decision to buy a significant amount of debt of those companies that are now defined as high-yield from the impact of COVID-19. Whilst the EU hasn't yet dipped a toe into the high-yield arena, it has notably increased its buying programme only recently, illustrating that the stimulus we have seen to date is highly likely to continue if required.

3) The initial shock of the virus seems to have worn off somewhat and markets have subsequently adjusted. The technical impact of city workers being uprooted to setting up home offices is likely to have been a once-off phenomenon. As discussed previously, the market has differentiated clearly between those names that contain uncertainty and long-term winners. Whilst I don't profess to say the picture is totally clear now, it is notably less opaque than it has been.

With supportive governments, rate cuts, and a touch less uncertainty in the world, it is no surprise bond markets (as a whole) are returning to their pre-COVID-19 levels. **Working out how to play this is a little harder though, and very much depends on each client's own risk tolerance and investment timeframe.**

Whether you are a more cautious investor drawn towards a "bulletproof" portfolio or an adventurous one focussed on high-yields that have yet to recover, we look forward to helping you build a fixed income portfolio to best suit your circumstances. For more information, please contact your Relationship Manager. ■

Jarrod Cahn - *Director*

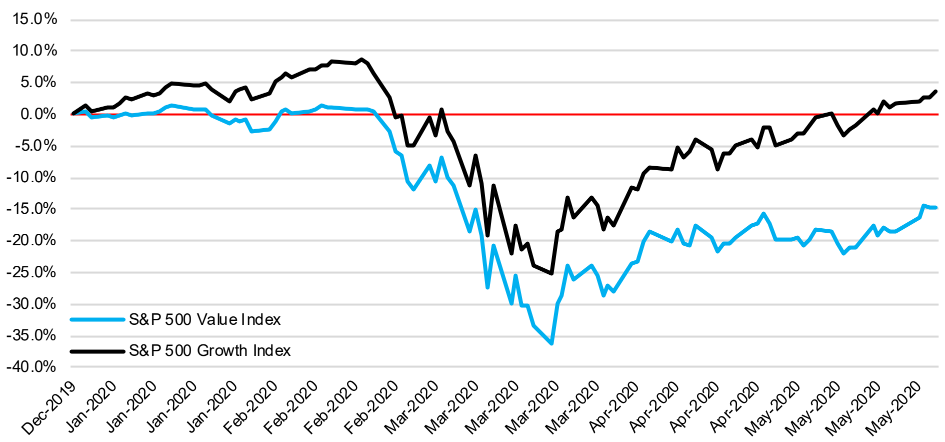
Managing equities through the turmoil

In the previous issue of CredoNews, published at the beginning of this year, we were able to reflect on a successful 2019 for Credo's managed equity products. A few months later, the picture looks a little different, and we'd like to use this opportunity to explain our performance as well as the resulting portfolio actions.

The coronavirus has essentially highlighted a few key themes during the first 6 months of 2020.

Firstly, the divergence in performance between growth and value strategies has reached some of the most extreme levels seen in the last 20 years. To put it in perspective, the S&P 500 Value index underperformed the Growth index by 18.4% in the first five months of the year.

This theme is of course not a new one and we've been grappling with it for the past decade. Over the last few months in particular, the rally in a narrow band of growth stocks has led to a significant divergence in performance. The list includes the likes of *Amazon*, *Netflix* and others that continue to screen expensively, based on which we would not consider them for inclusion in our value-based portfolios. This has clearly hampered our performance of late.



We remain true to our investment philosophy and continue to believe that an eventual rotation from Growth back into Value is likely to provide a strong tailwind to the performance of our portfolios. Indeed, since the beginning of June, there has been the first signs of such a rotation.

Secondly, the divergence in performance of various sectors has been extreme.

The Technology sector (in which we include *Amazon*) has significantly outperformed, whereas Financials & Insurance, Travel & Leisure, Oil, and Real Estate have all significantly underperformed.

During lockdown, the markets became fixated on asset light, cash rich, platform type businesses that were able to operate successfully over this period. Conversely, investors were very quick to sell any companies that were leveraged and may be structurally impaired over the short and longer term because of the coronavirus.

S&P 500 sector returns (Jan-May 2020)

Ticker	Sector Name	Return (%)
S5RETL	Retailing	14.8
S5SFTW	Software & Services	10.0
S5INFT	Information Technology	7.3
S5MEDA	Media & Entertainment	3.0
S5HLTH	Healthcare	1.6
S5TELS	Communications	0.2
S5FDSR	Food & Staples Retailing	-1.8
SPX	S&P 500	-5.0
S5UTILX	Utilities	-6.7
S5MATRX	Materials	-8.9
S5REAL	Real Estate	-9.9
S5DIVF	Diversified Financials	-12.7
S5TRAN	Transportation	-14.6
S5CPGS	Capital Goods	-18.4
S5INSU	Insurance	-19.6
S5BANKX	Banks	-34.4
S5ENRSX	Energy	-34.5

We entered 2020 cautiously positioned, holding 15% in cash in the Credo Dividend Growth Portfolio ("DGP") and 5% in cash in the Credo Best Ideas Portfolio ("BIP"). In January, while the virus was still only prevalent within China and parts of Asia, we took the decision to sell *Las Vegas Sands* from both portfolios, fearful of the consequences of a significant and prolonged lockdown in Macau. In retrospect this was a good sale. This however left the DGP portfolio 20% in cash, and BIP 10% in cash. In the middle of February, we decided to add *Progressive Corporation* (PGR) to the DGP portfolio. Early indications are that this has been a successful investment, as PGR has benefited from the coronavirus in that there has been less car traffic in the US, and therefore fewer insurance claims.

The sell-off in March was rapid and extreme, and caught most investors by surprise. Our first reaction was to try and identify stocks that we believed might possibly not survive longer term, particularly those that were starved of cash or exposed to industries in structural decline.

Thankfully, we identified only one such stock in our portfolios, namely *Meggitt*. Unfortunately, however, the price of this stock had dropped so much and so rapidly that we ended up taking the view that it was in fact not worth selling. As things stand, we continue to monitor the performance of *Meggitt* as a stock that we may want to exit at the appropriate time.

As the period progressed, the businesses that could operate under lockdown conditions have continued to benefit. 'Stay home' stocks like *Amazon*, *Netflix*, *Electronic Arts*, *Zoom*, *Microsoft*, *PayPal* come to mind. On the other hand, sectors that have either suffered short-term, operational issues or more long-term, structural issues have been severely marked down.

In terms of our portfolios, the stocks that have been negatively affected mostly fall in two categories, namely Financials and Travel & Leisure (as well as Aerospace – linked to the latter).

Financials

More than half of our underperformance relative to benchmark in the period to the end of May stems from financial holdings (*Wells Fargo*, *Arch*, *Chubb*, *Prudential*, and *AIA*).

These stocks have been hurt by lower interest rates, a worsening outlook for credit, business interruption insurance claims and softer equity markets. With that being said, we remain positive on the outlook for property and casualty insurers from here. ▶▶

"...we remain cautious on the substance behind the rally and will continue to be patient in our endeavours to add stocks to the portfolios."

Managing equities through the turmoil

Although we may not be equally optimistic on the outlook for banks, we continue to believe that a company like *Wells Fargo* is simply too cheap at these levels as it is extremely unloved by the market.

Something else that needs to be noted, is that a number of stocks that have historically been defensive, actually behaved quite differently during this pandemic: when government rules that all businesses except essential services shut down for months on end, the only ones that are able to escape relatively unscathed are those able to operate online, with a product where demand actually benefits from lockdown (e.g. increased demand for home entertainment). A historically defensive sector that has been impacted specifically, is insurance – this is generally not particularly correlated with the economic cycle, but the fear of large-scale business interruption claims has precipitated a big sell-off in these names.

As the lockdown unwinds, investors are getting more comfortable with the longer-term fundamentals of this sector, and with that we are starting to see a strong rotation into names such as this. We believe that we own some of the highest quality names in the sector, which are ultimately positioned to benefit from the disruption.

Travel & Leisure and Aerospace

These sectors are responsible for the bulk of the remaining underperformance (*Raytheon*, *Meggitt*, *Crown Resorts*, *Disney*, and *Madison Square Gardens*):

In the case of the leisure stocks, we believe that we own some of the best quality franchises in the world. The extent and length of the lockdown – and thus their ability to optimise capacity in order to operate profitably – are clearly key in the short term, but longer term, these stocks should be winners when the pandemic eventually ends.

Crown has managed to reduce its costs significantly while Australia has been in lockdown, but as the country now has an extremely low incidence of new cases, we envisage a relatively rapid recovery when casinos eventually reopen as gambling is essentially an addictive activity. Indeed, we have recently seen particularly strong demand in Las Vegas (which has already reopened). *Crown* has one of the best balance sheets in the sector and a unique portfolio of trophy properties. We also believe that it is a prime takeover candidate.

Disney has had to deal with the closure of its theme parks and delays in film production. However, as Asia and the US start moving out of lockdown, it would appear that business may in fact get back to a new normal sooner than anticipated. Although still a small part of the business, *Disney+* has enjoyed a massive acceleration of subscribers during the lockdown period.

Madison Square Gardens Sport and *Madison Square Gardens Entertainment* have now unbundled. It is unfortunate that the split took place during a time when markets happened to be in distress and with live sport and entertainment being shut, as significant value could have been unlocked otherwise. Notwithstanding this, we continue to believe that these two entities have some of the most unique and high-quality assets in their space and we thus remain confident that value will be recognised over the medium term when sport and live entertainment eventually resume.

Raytheon is another company that has seen a substantial fall in its share price, but after extensive work on the stock, we remain comfortable holding it. The reason being is that post the merger with *United Technologies* (our historic holding), the combined entity is actually more of a defence business as it generates approximately 60% of its income from this industry – which is not considered to be in decline since the onset of coronavirus. The remainder of *Raytheon's* business is civil aerospace and this does of course face challenges over the short to medium term; however, when one analyses the stock on a sum-of-the-parts basis, you are effectively paying very little for this segment of the company at the current share price and we are thus comfortable holding the stock.

Meggitt is of course our other civil aerospace exposure. The company does have balance sheet refinancing risk and although management has done well to mitigate costs, its longer-term prospects appear to be challenged. As mentioned above, we will look to sell *Meggitt* at the appropriate time.

During the market sell-off, we added one further position to the DGP portfolio, namely *Otis Worldwide Corporation*. *Otis* happened to be part of the spin-off from *United Technologies* when the *Raytheon* deal took place and is one of three companies that dominate the elevator and escalator world market. The stock trades at a discount to its two European competitors *Kone* and *Schneider Electric*, and has a very attractive recurring revenue model. As is often the case when stocks are unbundled from bigger groups, many investors tend to sell these stocks, either because they are under-researched, or the holdings simply become immaterial in their portfolios. We therefore saw this as an opportunity to buy a world-class, quality business at a good discount.

In the case of DGP, the current financial environment has led to a unique situation where companies have been forced to preserve capital and have either completely stopped paying dividends or significantly cut and rebased their dividend policy. Although we expect this to be a temporary measure, one must expect the yield on companies to be lower for the foreseeable future. It also means that the universe of stocks that we would look to own in this portfolio has shrunk.

Moving forward, as world equity indices are rebounding, we remain cautious on the substance behind the rally and will continue to be patient in our endeavours to add stocks to the portfolios. **As always, the key to successful portfolio management is diversification, and although technology appears to have been "the only game in town" over the last six months, it remains prudent to remain diversified.**

We anticipate that there will be a significant rotation back to good quality, value stocks over time; in fact, as of the first half of June, it appears that this rotation may have begun already, and with it we have started to see the first signs of improved performance of stocks that have lagged within our portfolios. Long may it last.

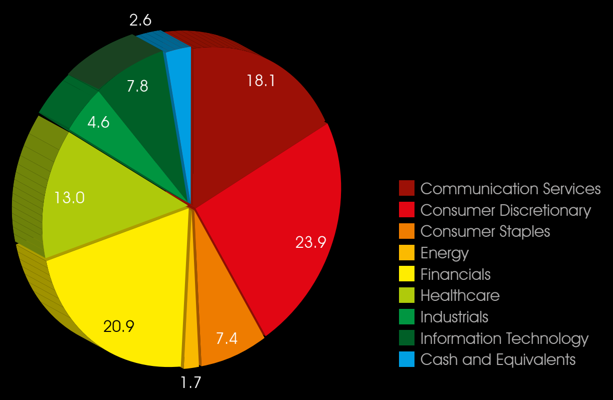
The Credo Funds

GLOBAL EQUITY FUND

Credo Global Equity Fund

Credo has a strong track record of managing long-only, value-based, direct equity portfolios with a bias towards developed market, large capitalisation stocks. The Credo Global Equity Fund (UCITS) is actively managed and follows this same investment philosophy. Our aim is to generate sustainable excess returns versus global market indices through careful stock selection.
On 3 February 2020, Credo launched the **BCI Credo Global Equity Feeder Fund**, giving South African investors direct access (in ZAR) to Credo's global equity investment offering.

Sector Allocation (%)



Currency Allocation (%)

GBP	18.3
USD	69.7
Other (AUD, EUR, HKD, MXN, ZAR)	12.0

Past Performance (%)

	Fund	Benchmark
1 Month*	5.0	7.1
3 Months*	1.2	4.5
1 Year*	6.4	9.5
S. Inception *(Cumulative)*	12.9	24.2
S. Inception *(Annualised)*	4.3	7.7

(*) Actual performance of the Credo Global Equity Fund (UCITS) A GBP retail
Inception: 03/07/2017. Benchmark: MSCI World Index Net Total Return (in GBP)
Highest: 27.0%, lowest: -6.1%

Top 10 Holdings (%)

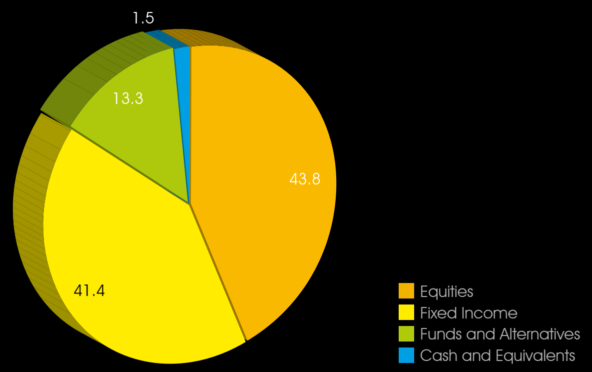
Facebook Inc	Communication Services	6.0
Microsoft Corp	Information Technology	5.3
Cigna Corp	Healthcare	5.2
Flutter Entertainment plc	Consumer Discretionary	5.1
Alibaba Group Holding Ltd	Consumer Discretionary	4.9
HCA Healthcare Inc	Healthcare	4.9
Crown Resorts Ltd	Consumer Discretionary	4.1
The Walt Disney Co	Communication Services	4.1
Becle SAB de CV	Consumer Staples	3.6
Madison Square Garden Sport	Communication Services	3.5

DYNAMIC FUND

Credo Dynamic Fund

The Credo Dynamic Fund (UCITS) utilises the long-term and successful investment strategy that has historically been employed within the traditional stockbroking arm of Credo and aims to achieve a balance of income and capital growth over the longer-term. The fund has flexibility to invest across asset classes depending on prevailing market conditions and has a bias to UK markets.

Asset Allocation (%)



Currency Allocation (%)

GBP	72.8
USD	23.7
Other (AUD, EUR)	3.5

Past Performance (%)

	Fund	Benchmark
1 Month*	3.6	3.8
3 Months*	-6.6	-0.8
1 Year*	-3.0	1.4
S. Inception *(Cumulative)*	5.2	6.5
S. Inception *(Annualised)*	1.8	2.2

(*) Actual performance of the Credo Dynamic Fund A GBP retail
Inception: 03/07/2017. Benchmark: IA Flexible Investment Sector
Highest: 15.5%, lowest: -4.9%

Top 10 Holdings (%)

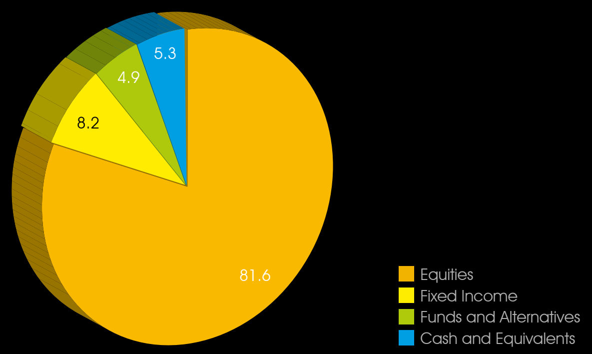
AQR Managed Futures UCITS	Open-End Fund	4.8
iShares Core S&P 500 UCITS	Exchange Traded Product	4.0
Co-operative Group Ltd 11 12/18/25	Corporate Bond	4.0
WisdomTree Physical Gold	Exchange Traded Product	2.8
SPDR MSCI World UCITS	Exchange Traded Product	2.6
Team17 Group plc	Communication Services	2.3
iShares NASDAQ 100 UCITS	Exchange Traded Product	2.3
Punch Taverns Finance 7 ¾ 12/30/25	Corporate Bond	2.2
VanEck Vectors Video Gaming & eSports	Exchange Traded Product	2.1
BB Healthcare Trust plc	Closed-End Fund	2.0

GROWTH FUND

Credo Growth Fund

The Credo Growth Fund (UCITS) is a reflection of the fund manager's (Roy Ettlinger) personal investment style and strategy which he has successfully adopted for clients in past years. The fund is globally diversified and follows a flexible investment strategy with a growth bias. It aims to provide attractive risk-adjusted returns to investors and has flexibility to invest across asset classes.

Asset Allocation (%)



Currency Allocation (%)

GBP	47.1
USD	51.0
EUR	1.9

Past Performance (%)

	Fund	Benchmark
1 Month*	7.3	6.4
3 Months*	2.5	-0.8
1 Year*	6.3	1.4
S. Inception *(Cumulative)*	14.9	6.5
S. Inception *(Annualised)*	4.9	2.2

(*) Actual performance of the Credo Growth Fund A GBP retail
Inception: 03/07/2017. Benchmark: IA Flexible Investment Sector
Highest: 20.7%, lowest: -8.4%

Top 10 Holdings (%)

Microsoft Corp	Information Technology	5.9
Alibaba Group Holding Ltd	Consumer Discretionary	4.8
PayPal Holdings Inc	Information Technology	4.4
Alphabet Inc	Communication Services	4.4
Costco Wholesale Corp	Consumer Staples	4.1
Primary Health Properties plc	Real Estate	4.0
Amazon.com	Consumer Discretionary	4.0
Scottish Mortgage Investment Trust	Closed-End Fund	3.8
J Sainsbury plc 6 ½ Perp	Corporate Bond	3.7
Ocado Group plc	Consumer Discretionary	2.3

Source: Société Générale Securities Services (Ireland) Limited, Bloomberg and FE Analytics. As at 31/05/2020. Performance is of the Class A (GBP) Retail share class for all UCITS funds and is measured using NAV to NAV dates, net of fees and with income reinvested. Individual investor performance may differ as a result of initial fees (if any), the actual investment date, the date of reinvestment and dividend withholding tax. Annualised performance shows longer term performance rescaled to a 1-year period. Annualised performance is the average return per year over the period. Actual annual figures are available to the investor on request. Highest and lowest are calendar year returns which are the actual annual figures. NAV is the net asset value and represents the assets of a fund less its liabilities.

A schedule of fees, charges and maximum commissions are available on request. Credo Growth Fund is weekly dealing. Credo Global Equity Fund and Credo Dynamic Fund are daily dealing. Full performance calculations are available from the Manager on request. The Manager of the UCITS funds is FundRock Management Company S.A. and is Boutique Collective Investments (RF) (Pty) Ltd for the Feeder Fund. Prescient Management Company (RF) (Pty) Ltd is the Representative Office in South Africa for the UCITS funds and is registered and approved under the Collective Investment Schemes Control Act (No.45 of 2002). For any additional information such as MDDs, prospectus and supplements, please visit www.credogroup.com.

Black's mirror

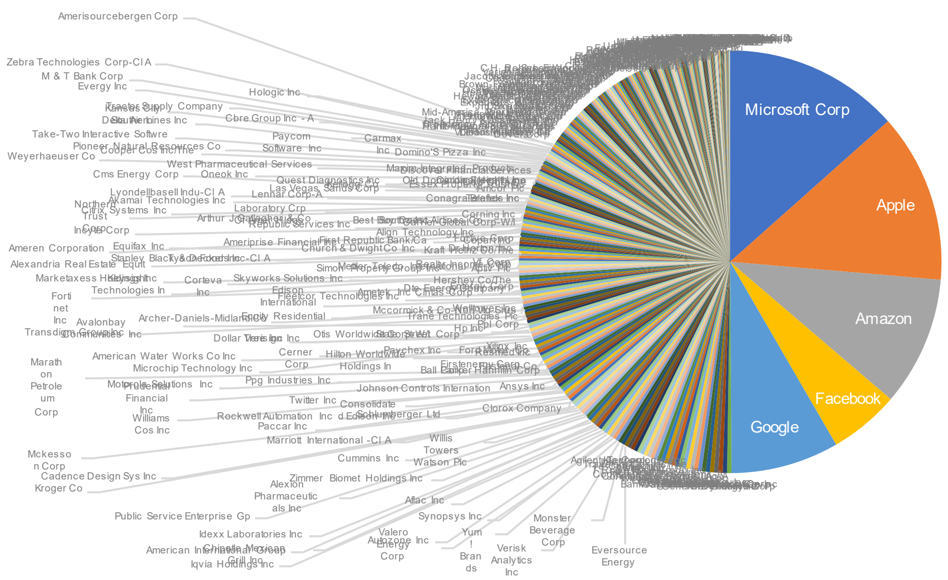
"…what would passive investors see were they to peer into Fischer Black's mirror?

The impact of lockdowns imposed in a number of countries during this extraordinary time has been softened by online connectivity, which has enabled many of us to continue to live and work remotely. Our continued reliance on technology has not gone unnoticed in market prices, with the five largest companies in the world having significantly outperformed so far this year and approaching $6 trillion in combined market cap: the nature of this crisis has resulted in an incredible wealth transfer from small businesses to some of these tech giants.

Though an index is typically broad in terms of its number of members, this can mask the concentrated positions it takes in terms of its largest constituents – Chart 1 shows how an investor in the S&P 500 is betting as much on the big five technology names as they are on the bottom 350 companies combined. The stellar outperformance of these giants has propelled the S&P 500 in the first half of this year - one cannot help but ponder whether the index may in fact be higher today than it would have been had the pandemic (and the subsequent stimulus) never happened.

With the events of this year further accelerating our reliance on technology giants, it is hard to imagine a future in which they do not dominate every facet of modern life. One can only hope that our dependence has not set us down the dark path to a dystopian future as imagined in Charlie Brooker's eerily prescient series Black Mirror, in which technology manipulates and controls most aspects of human behaviour – though we began as masters of these technological tools, the series portrays a not too distant future in which we eventually become slaves (the irony is not lost on me that the show is only available through *Netflix*).

Chart 1: Market Cap of Top 5 vs Bottom 350



For any investors underweight these largest companies during the crisis, they may have come to believe that they are already living in an episode of Black Mirror, where market cap weighted indices are the dark financial technology which we are all now slaves to.

There are many virtues to indexing and to passive investing, but concentration into a small number of stocks and risk factors are not amongst them.

The phrase "**Black Mirror**" references the appearance of a blank video screen – what you see when you look into a TV, a laptop, or a smartphone when it is switched off. For most advocates of passive investing, this is what they believe they see when looking at a cap weighted index, that their portfolio is not making any forecasts, and investment decisions are effectively switched off.

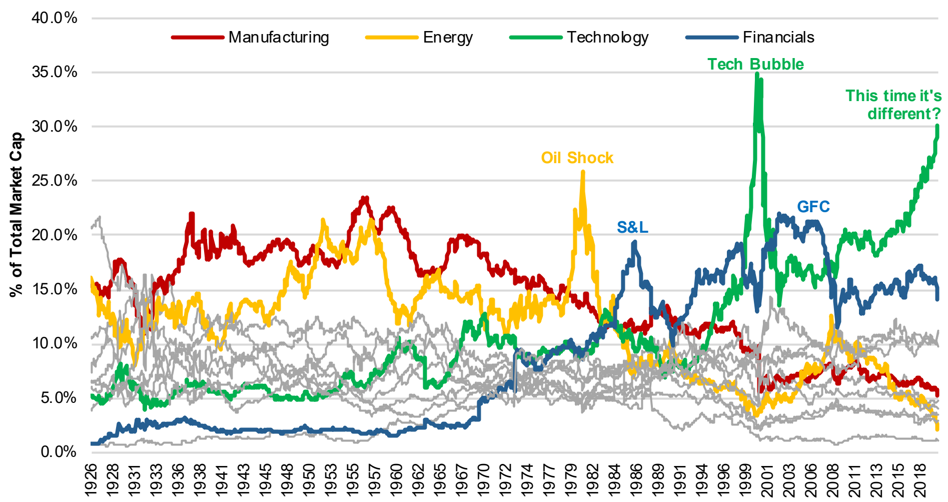
But as illustrated with the big five, **market cap weighting is not unbiased at the stock level, and certainly not at the sector level**. Chart 2 shows the sector weights in the US equity market over the last century, highlighting the largest sectors historically. Once far and away the largest sectors, Manufacturing and Energy have since given way to the Financial and Technology sectors, which came from nothing to become the giants of the modern era. The last century has seen spectacular bubbles across various parts of the economy.

Upon learning the definition of a "Black Mirror", I was reminded of the work of a finance legend of the same name. A decade after publishing the Black-Scholes formula, Fischer Black spent some time at *Goldman Sachs* where he co-developed the **Black-Litterman** model. Though its main function was integrating subjective market views into asset allocation, another unique feature of the model is that it could be used in reverse – with one's portfolio, the model could reveal to an investor the implied forecasts they were making in their portfolio holdings.

The size of a position in an investor's portfolio should be proportional to the expected benefit from owning that position.

So, what would passive investors have seen were they to peer into Fischer Black's mirror during these sector bubbles? Implied return forecasts for Energy stocks were at their highest in the 1980s oil shock, just before their collapse. Expectations for Financials were greatest just before the Savings & Loans collapse in the mid-80s, and again on the brink of the Global Financial Crisis, with banks at the epicentre. The market's all-time highest forecasts in history were for Technology stocks at the peak of the Tech Bubble, just in time for their breath-taking collapse. Today, a cap weighted investor needs to look into Black's mirror and ask themselves whether they truly believe their forecast that the largest five companies are going to produce 70 times the returns of the bottom 350.

Chart 2: The Market's Great Expectations



One grave concern with the rise of automation is that our algorithms are encoding the human biases & prejudices embedded in the data they are trained on. Yet in finance, cap weighted indices are designed to do precisely this, by reflecting the biases of everyone else in the market - passive investing is not passive in terms of its bets. This isn't an issue for investors in these indices if these bets also reflect their own views about the future. But for those who think they are simply getting an unbiased exposure to an asset class, they might need to think harder about what is in their own portfolios and pay less attention to what is in the portfolios of everyone else. ■

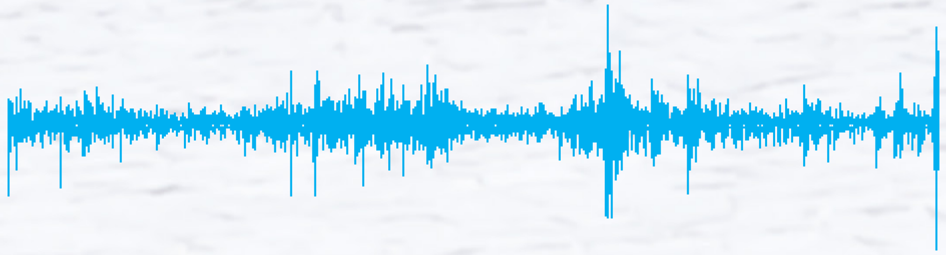
Calvin McLean - *Investment Analyst*

Ladies and Gentlemen, we're experiencing some turbulence

As the world went into lockdown a few months ago and financial markets were put through the wringer once again, the result was further evidence of the lack of normalcy in investment returns and the major impact tail events have on investors' portfolios. Such events, even if on a somewhat smaller scale than we've recently experienced, can see risk within a portfolio increase not slightly but in multiples. This is because, when constructing a portfolio according to traditional methods, there is an assumption that an asset's average risk is the best estimator of risk throughout time, and that returns are independent. This, however, has not empirically been the case.

Looking at Chart 1, which shows a typical equity daily return time series, it is clear that the largest returns (positive or negative) are not randomly scattered throughout the chart (as would be expected if returns were independent) but tend to be close to other outsized returns - this is known as volatility clustering. This phenomenon was first noted by the mathematician, Benoit Mandelbrot (1963), who characterised these periods as market "turbulence" because of their chaotic vagaries as investors are driven by fear and greed.

Chart 1: Typical Equity Daily Returns Chart



This has an important implication: knowing the current market volatility could help guide expectations for volatility in the immediate future. Could one thus use this insight to improve the investment decision process? An approach that looks to take advantage of this, is Risk Targeting. With this approach, the exposure to the asset is varied as the risk changes to maintain a steadier level of risk through time (this is done by scaling back during those high-volatility periods and leveraging during the low-volatility periods).

The result is that drawdowns are generally reduced and return / risk metrics are higher. This can be seen in the Table 1, which compares a buy-and-hold S&P 500 investment to an S&P 500 investment whose exposure was adjusted to target 1-month annualised volatility of 12.2% (this level was chosen so that the realised median 1-month volatility of the two investments were the same i.e. an investor would typically have felt the same riskiness in the two during "normal" times).

Table 1

	Buy -and -hold	12.2% Volatility Target
Return *(annualised)*	10.4%	10.4%
Volatility *(annualised)*	17.7%	13.5%
Return / Risk	0.59	0.77
Max Drawdown	55.3%	42.2%

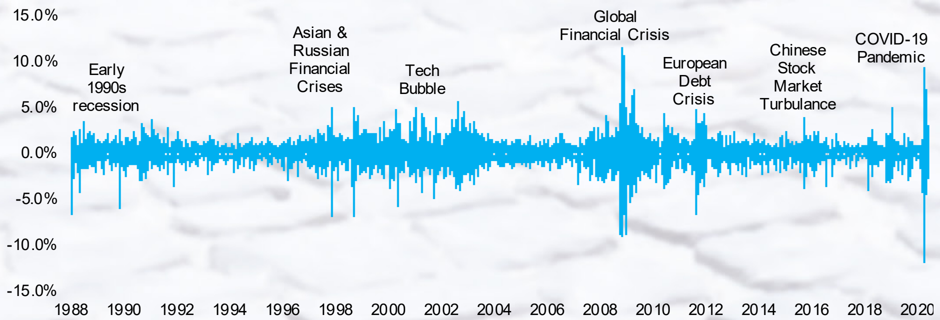
Performance summary of strategies between February 1988 and May 2020

There are two key aspects that contribute to this outcome:
(1) Risk Targeting experiences a fewer number of extreme returns, and
(2) volatility and returns have a weak negative relationship.

The first point follows directly from volatility clustering (extreme price movements happen close to each other) and helps explain why overall volatility (13.5% for volatility target vs 17.7% for buy-and hold) is much lower despite the strategy being optimised so that the median volatility of the two strategies matched.

The second point is more nuanced. Volatility has no directional bias, so there is nothing fundamental which requires volatility and return to be negatively correlated, and given the strategy takes an agnostic view of future returns (a good thing given they are notoriously difficult to forecast), it also does not differentiate between "good" or "bad" volatility. However, if we look at Chart 2 (which provides context to Chart 1), we perhaps can gain some insight. What it shows is that **periods where volatility has been at its highest have often been times of panic, not euphoria**. The relationship is weak though, as panics often create opportunity and lead to some of the biggest gains, so investors shouldn't always expect such an approach to come out on top.

Chart 2: S&P 500 Daily Returns



An additional consideration for investors is the implementation of this approach. This article demonstrated the approach when applied to a single asset, however this can be easily extended to an investor's whole portfolio and in fact this improves the approach as it begins to leverage that vital investment principle of diversification. Also, while this approach is simple in theory, it can be costly with the amount of trading required, so really requires a manager with exceptional trading capabilities.

Risk and reward are often compared to two sides of the same coin, and one can't help but wonder during times like these whether investors have been focused on the wrong side. Risk Targeting is an attempt to offer a viable alternative. With its non-reliance on return forecasts, it offers a break from more traditional approaches, which investors have been all too poignantly reminded, can be caught up in the brutal winds of change.

Jack Carbutt - *Relationship Manager*

Diversified equity portfolios

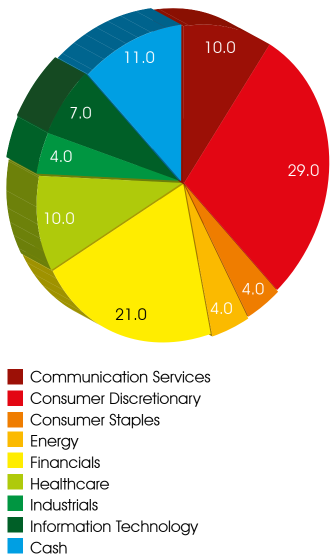
The Credo Best Ideas and Dividend Growth portfolios are diversified global equity portfolios, which we believe to be well positioned to outperform the wider equity market over the longer term. The portfolios have a bias towards developed market, large capitalisation stocks.

BEST IDEAS PORTFOLIO

Performance (%)

Return	
YTD	-11.3
1 Month	2.9
3 Months	-3.5
1 Year	0.2
Annualised Return	
3 Years	5.3
5 Years	8.8
Since Inception	10.6

Sector Allocation (%)

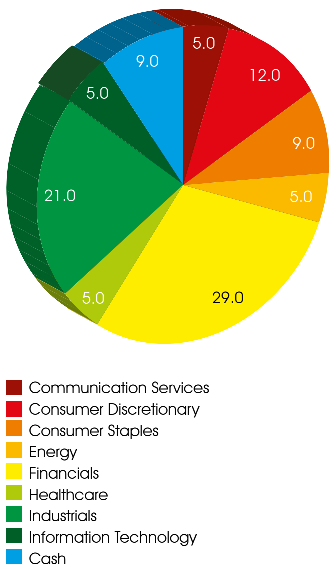


DIVIDEND GROWTH PORTFOLIO

Performance (%)

Return	
YTD	-9.1
1 Month	0.8
3 Months	-1.2
1 Year	3.1
Annualised Return	
3 Years	4.2
5 Years	9.7
Since Inception	11.8

Sector Allocation (%)



Value orientated investment philosophy

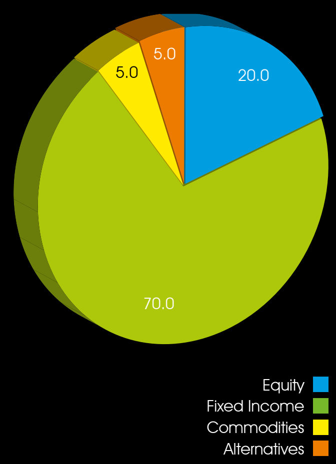
The Credo Multi-Asset Portfolios (MAPs) invest in regulated funds and exchange traded funds (ETFs) on a global basis, with a focus on diversification across a broad range of asset classes using liquid securities. The funds and ETFs are selected using Credo's in-house selection process. The MAPs are offered as four solutions targeting varying levels of equity exposure and are available in both GBP and USD.

MULTI-ASSET PORTFOLIO 20/80

Performance (%)

Return	
YTD	-0.9
1 Month	1.7
3 Months	-0.1
1 Year	3.0
Annualised Return	
3 Years	3.15
Since Inception	5.4

Strategic Asset Allocation (%)

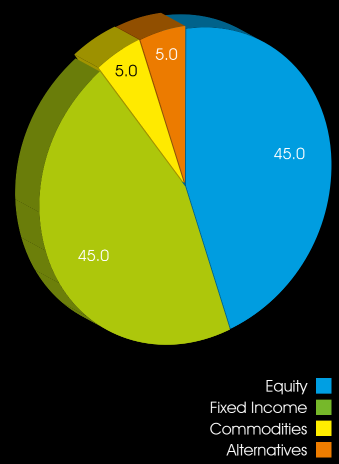


MULTI-ASSET PORTFOLIO 45/55

Performance (%)

Return	
YTD	-3.2
1 Month	2.9
3 Months	0.4
1 Year	2.3
Annualised Return	
3 Years	3.17
Since Inception	6.4

Strategic Asset Allocation (%)

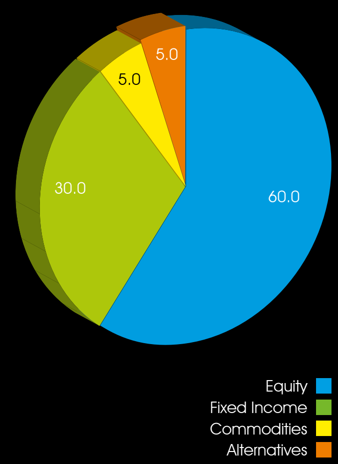


MULTI-ASSET PORTFOLIO 60/40

Performance (%)

Return	
YTD	-4.6
1 Month	3.7
3 Months	0.6
1 Year	1.9
Annualised Return	
3 Years	3.20
Since Inception	7.0

Strategic Asset Allocation (%)

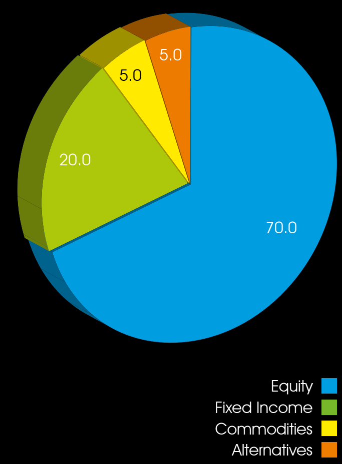


MULTI-ASSET PORTFOLIO 70/30

Performance (%)

Return	
YTD	-5.5
1 Month	4.3
3 Months	0.8
1 Year	1.6
Annualised Return	
3 Years	3.22
Since Inception	7.3

Strategic Asset Allocation (%)



Performance figures are based on a notional portfolio, denominated in pound sterling, designed to track the holdings of the Credo Best Ideas, Dividend Growth and Multi-Asset portfolios. Portfolios incorporate all additions and removals. Portfolios 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 the model weighting. Source: Bloomberg pricing as of 31/05/2020 close. All portfolio performance is calculated using Bloomberg PORT, rounded to 1 decimal place. Inception dates: Best Ideas Portfolio 14/11/2011, Dividend Growth Portfolio 28/12/2012 and Multi-Asset Portfolios 02/07/2014.

Jack Carbutt - *Relationship Manager*

A new offering for the next generation

One area Credo is particularly proud of is its diverse client base. Credo has a wealth of clients, whether they be trusts, companies or individuals, from a range of countries and backgrounds. In addition to catering for a varied client base, we are also able to provide investment solutions for a number of different and unique investment requirements.

However, when it comes to average client age, the demographic is a bit more skewed. This is hardly surprising, given that younger individuals haven't had the time to accumulate excess cash with which to invest in the capital markets. This has, invariably, resulted in the demographic of our client base being rather "top heavy".

In our main boardroom at our Marylebone office, we have a quote imprinted on the wall that reads ***'the best time to plant a tree was 20 years ago; the next best time is now.'*** This refers to the fact that the earlier one gets invested in the stock market, the better. But for us to truly believe in this, we need to cater for younger individuals with more modest investment amounts so that they can invest their hard-earned money at the earliest possible opportunity.

Against this background, Credo is launching the Credo Multi-Asset Portfolio (MAP) Select portfolios (**MAP Select**); a new offering targeting younger investors who want to start their investment journey.

With regards to the investments, individuals will have a choice of two portfolios which are adaptations of the successful Credo Multi-Asset Portfolios, as explained on pages 18 and 19. The MAP Select portfolios follow the same investment philosophy, methodology and process as the standard MAPs, with a focus on rigorous research and evidence-based, long-term investing. The only difference to the standard MAPs is that the MAP Select universe is restricted to mutual funds only and due to the lower initial investments amount, will also have fewer funds in the portfolio.

There are also a number of synergies to be had with the recently launched business, Credo Wealth Planning (**CWP**). Alongside the investment management, CWP can support our younger clients' financial journey in a variety of ways and provide advice relating to mortgages, life cover and other protection products, tax efficient savings and pension planning.

> The MAP Select portfolios provide the perfect solution for those who may have felt that their initial investment amount was too small but who now wish to start their investment journey.

The best possible time to plant your tree is now… and there's no better place to let it grow than with Credo.

If you would like to find out more, please contact your Relationship Manager or Jack Carbutt, jcarbutt@credogroup.com. ■

Alan Noik - *MD* | @AlanNoik_Credo

Phone a friend

We have seen enormous volatility in the markets since the COVID-19 pandemic outbreak in February and equity markets began to tumble by as much as 35%, reaching their lowest points on 23 March.

> It's at times like this that clients need to be able to pick up the phone and speak to their wealth manager. We are here for you.

A Credo wealth manager has a holistic understanding of their client's unique personal needs and significant experience of the patterns of equity markets. We have been through the 2000 dot-com boom and bust and more recently the 2008/09 global financial crisis, and whilst this pandemic is unprecedented in our lifetimes, we have seen the long-term pattern and movements of the markets repeat over time. Therefore, short-term, reactive decisions may not be beneficial in the long term as equity markets have historically shown that they will eventually recover.

At Credo we had several panicked clients calling us, wanting to throw in the towel on their investments and move into cash. At that juncture it was important to reassess two things. Firstly, the client's existing asset allocation and whether it still fitted into their medium to long-term objectives and secondly their true appetite for risk. Clients who had previously thought they had a far higher appetite for risk (in a rising bull market) now found themselves reconsidering whether they did, in fact, have that same appetite in a highly volatile environment.

There is no right or wrong answer as these reactions are highly personal to each client. Our role, as experienced wealth managers, is to have that conversation with our clients, unpack the various scenarios and guide our clients to the decision that is best for each individual. ■

Fireside chats

Over the past few months, Credo Wealth arranged two "Fireside Chats" in the form of live webcasts, consisting of a question and answer session hosted by Chief Investment Officer, Deon Gouws. The events were both very successful, and we had a total of approximately 1,000 registrations for the two combined. ***On Wednesday 8 July, we'll be hosting the next one – more details below.***

In the first event at the end of April, our guest was **Max du Preez**, well known South African writer and columnist. Max was the founding editor of Vrye Weekblad, and between 1982 and 1988, he was a political correspondent for various publications including Beeld, Financial Mail, Sunday Times and Business Day. He won the Nat Nakasa Award for fearless reporting in 2008.

Max gave some insightful and incisive commentary on the situation in South Africa – ranging from the government's response to COVID-19 to his thoughts on the long-term future for the country.

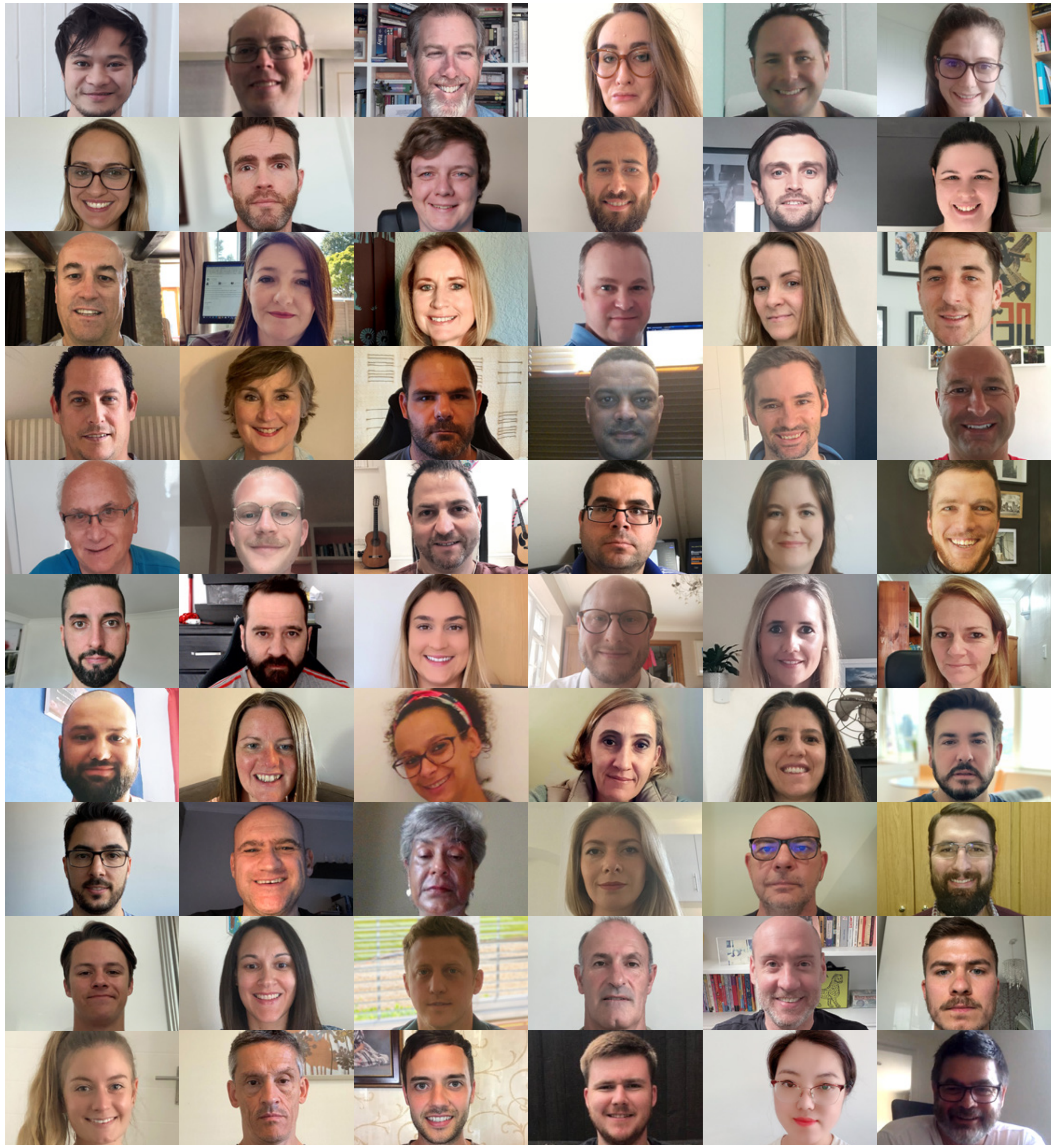
In the second event at the beginning of June, our guest was **Stephen King**, senior economic adviser at HSBC Holdings, where he was chief economist from 1998 to July 2015. Stephen also works as a journalist and consultant, and was a specialist adviser to the House of Commons Treasury Committee until 2017.

Stephen shared his views on a world moving away from globalization, a trend which he wrote about in his last book and one that he sees accelerating as a result of the coronavirus. Stephen is also a distinguished piano player, and he entertained us with a few minutes of Schubert at the end.

The third event is scheduled to take place on Wednesday 8 July at 16:30 (UK time). Our special guest on this occasion will be **Dawid Krige**, co-founder and Chief Investment Officer of Cederberg Capital. Cederberg manages US$2bn in Chinese equities from London and Shanghai on behalf of institutions, families and individuals. Since its inception in 2011, the Cederberg Greater China Equity Fund has generated +17% p.a. returns (US$, net of fees), placing it in the top percentile of its peer group.

Please email events@credogroup.com if you'd like to attend this event but haven't received an invitation.

Some of the Credo family in lockdown



credogroup.com

CREDO
WEALTH