
# Quarterly Report

November 2019

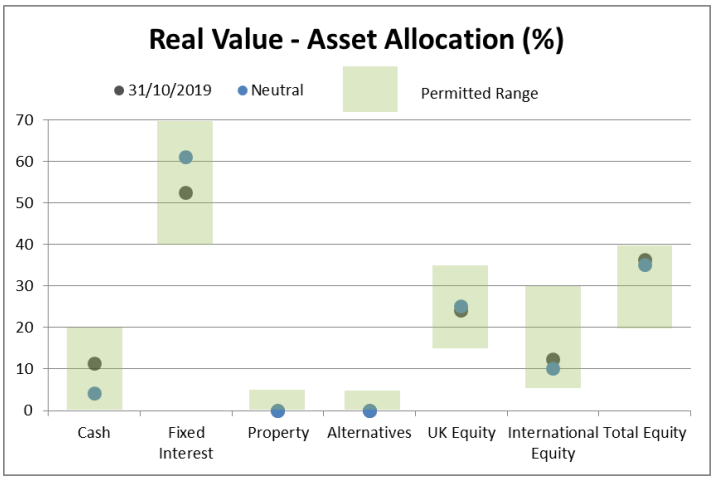
The Future Money strategies are run with the aim of providing investors with carefully risk managed investment solutions.

This report is designed to provide an insight into how the four strategies have been managed, along with the thought processes behind the investment decisions made by the fund managers.

## Quarterly Report

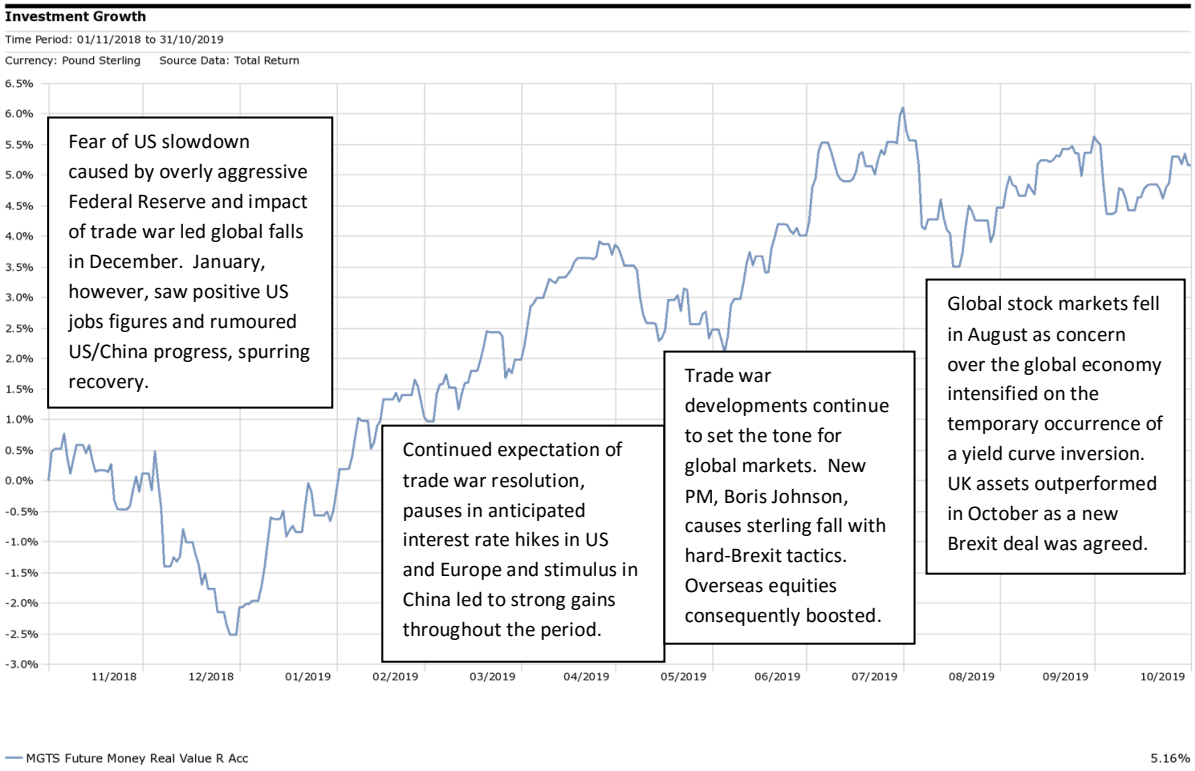
31 July 2019 to 31 October 2019

### MGTS Future Money Real Value




The Schroder European Alpha Income fund was removed from Real Value during the quarter and replaced with Fidelity European. Given the Fidelity fund's more balanced investment style we believe it more likely to perform well across a range of market environments and hence consider it to be preferable, as the only European holding in the portfolio. At less than 3%, we have a relatively small exposure to European equities. While we believe the European economy will benefit from positive global growth, we doubt that Europe can be a leader in this trend and therefore do not expect it to thrive as an investment region.

Our preference for short dated bonds proved a drag on performance overall on the reporting period given a strong performance in August, but this trend showed a significant reversal in October as long dated bonds fell in value as progress was seemingly made in Brexit negotiations, creating confidence in the domestic UK economy, lessening the appeal of the fixed returns of bonds.




Past performance is no guarantee of future performance. The value of investments can fall as well as rise and investors may not get back their original investment.

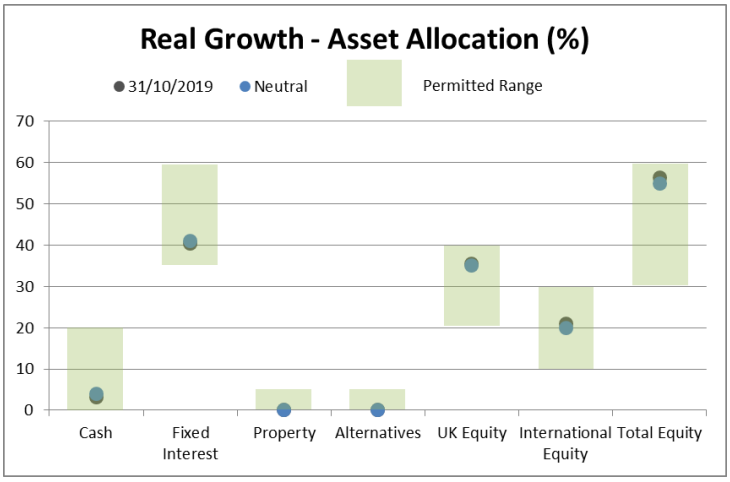
Source: Morningstar Direct

## Quarterly Report

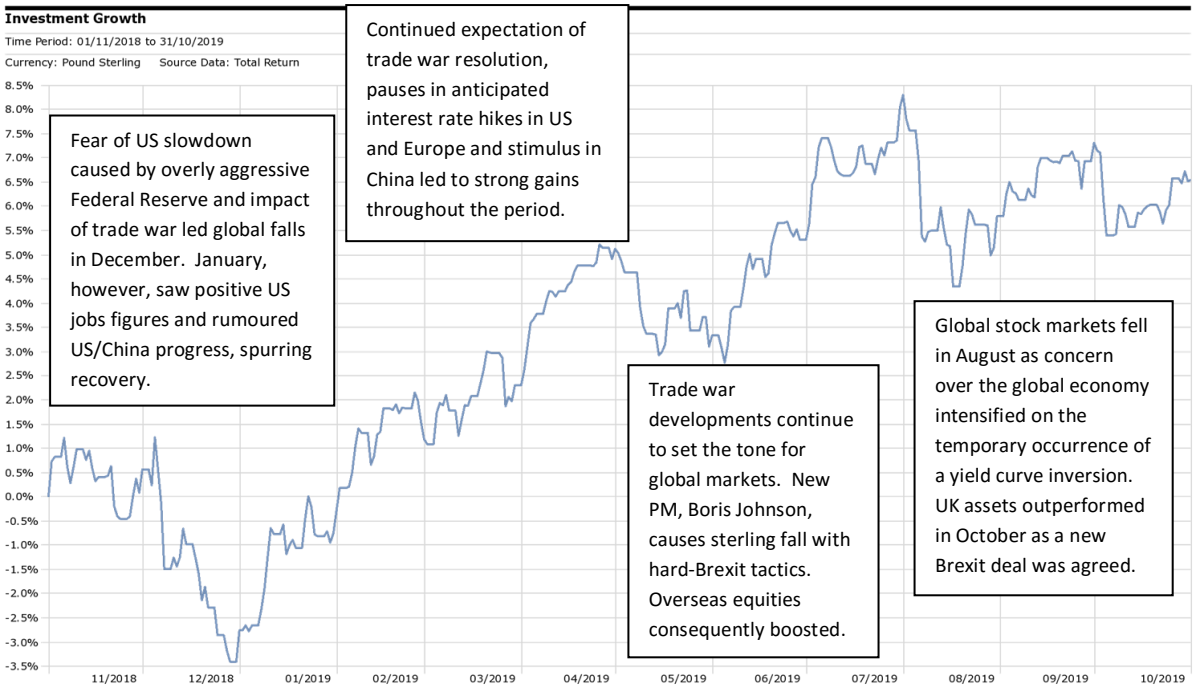
31 July 2019 to 31 October 2019

### MGTS Future Money Real Growth

The Schroder European Alpha Plus fund was removed from Real Growth during the quarter and replaced with Fidelity European. Given the Fidelity fund's more balanced investment style we believe it more likely to perform well across a range of market environments and hence consider it to be preferable as the only European holding in the portfolio.




The British pound rose significantly in October, giving strong gains for the quarter overall. This helped drive the outperformance of UK equities against their international counterparts. The pound has experienced significant weakness since the EU referendum of 2016 as overseas investors have been underweight to UK assets. With momentum towards a relatively amicable split from the EU, this trend has weakened somewhat, and a continued path towards a negotiated departure (as opposed to no-deal) will continue to provide support for the pound, in our opinion, and as such could lead to relatively strong performance of UK assets.

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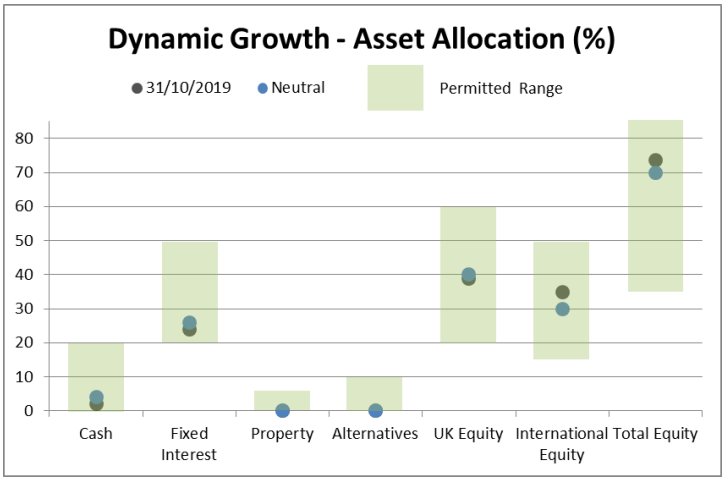
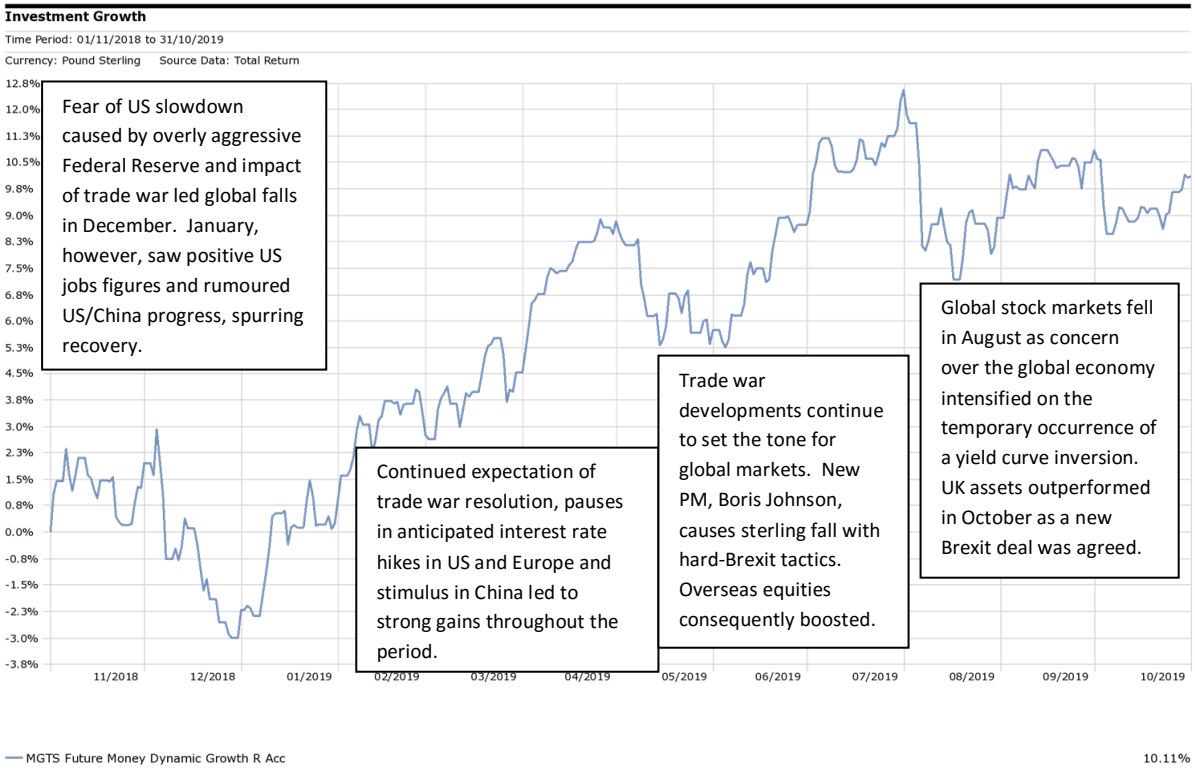
Source: Morningstar Direct

## MGTS Future Money Dynamic Growth




As in Real Value and Real Growth, Fidelity European was added to the Dynamic Growth portfolio given a belief in the balanced nature of the fund and expected relative consistency in performance. BMO Select European was sold to make way for the Fidelity purchase. BMO had undergone a transition in style in recent times, becoming more concentrated. We considered this to create an increase in the risk profile and while the performance had been strong, it had come with relatively high levels of volatility and so we felt it was right to move away from the holding.

No further changes are currently being considered for Dynamic Growth, with the fund selection performing well in the current environment. This is particularly the case in the Asian and Emerging Market areas where each of the funds held outperformed their respective peer group over the three months in what have been relatively difficult market conditions.

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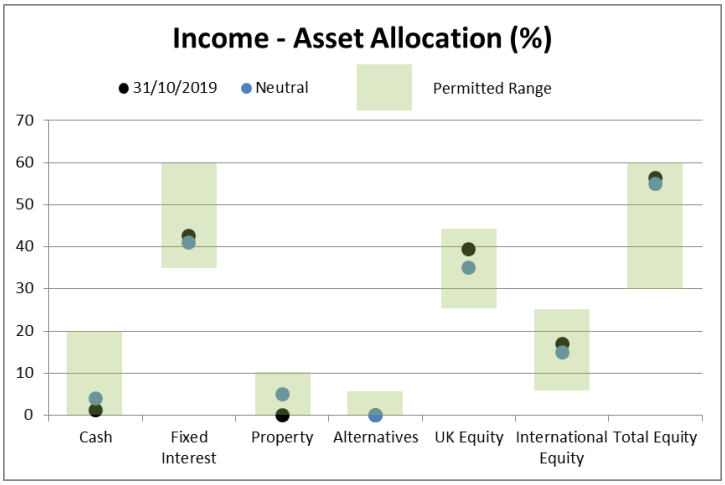
Source: Morningstar Direct

## Quarterly Report

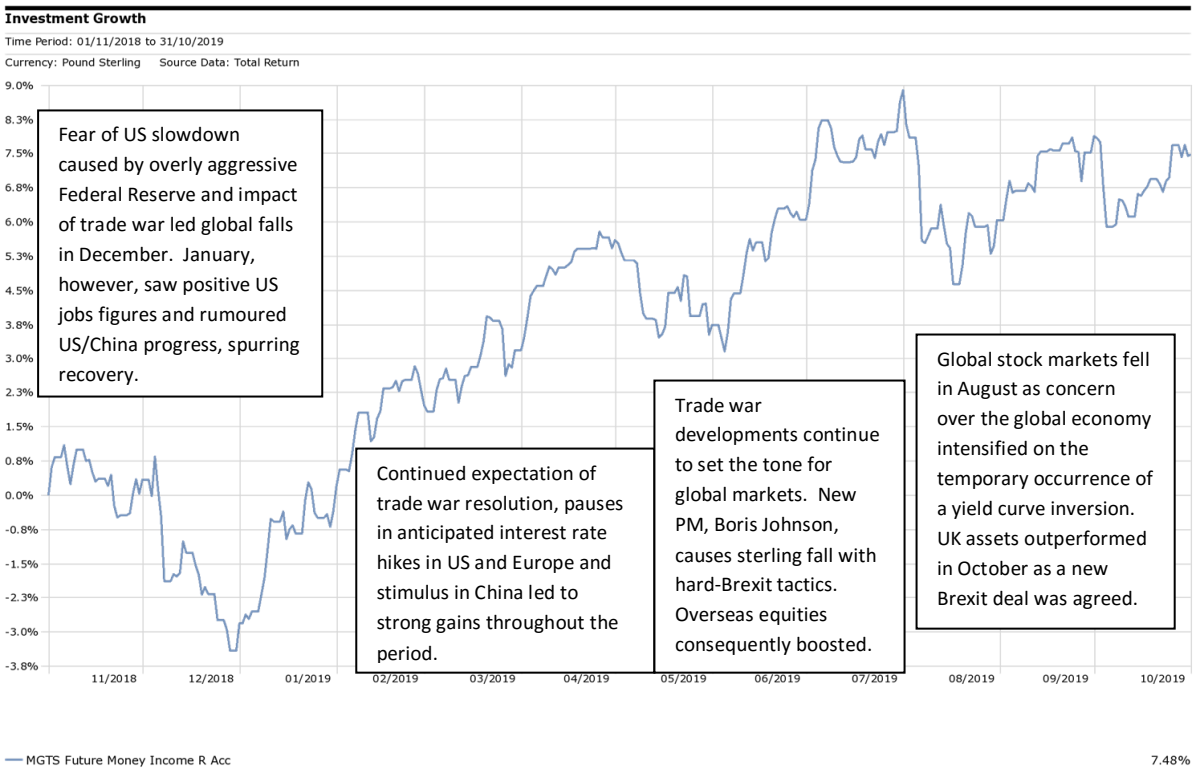
31 July 2019 to 31 October 2019

### MGTS Future Money Income

As discussed in last quarter's report, we hold the sterling hedged version of the M&G Emerging Markets Bond fund. Over this reporting period, sterling has experienced gains and consequently the M&G fund has delivered a strong performance relative to its non-hedged peers. While this trend will likely fluctuate we believe that the pound remains undervalued and therefore we continue to like the hedge in place.




In Future Money Income, the BlackRock Continental European Income is held and we remain happy with this holding. The yield provided by this fund is high relative to many of its peers and while this is created by a focus on high dividend payers, the reliability of the dividend is key, rather than simply the level. In addition, not all stocks in the portfolio have to be high yielders, meaning there is room for higher growth rate companies as well, which, in turn, allows the portfolio to deliver attractive total returns (the combination of both income *and* capital returns).

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Source: Morningstar Direct

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## Quarterly Report

31 July 2019 to 31 October 2019

### Performance

| | Year to Month End | 1yr | 3yr | 5yr |
|---|---|---|---|---|
| | 01/01/2019 31/10/2019 | 01/11/2018 31/10/2019 | 01/11/2016 31/10/2019 | 01/11/2014 31/10/2019 |
| MGTS Future Money Income R Acc | 10.58 | 7.48 | 12.32 | 28.39 |
| MGTS Future Money Real Value R Acc | 7.38 | 5.16 | 8.40 | 19.70 |
| MGTS Future Money Real Growth R Acc | 9.56 | 6.55 | 12.18 | 27.79 |
| MGTS Future Money Dynamic Growth R Acc | 12.60 | 10.11 | 16.09 | 37.48 |

| | 2018 | 2017 | 2016 | 2015 | 2014 |
|---|---|---|---|---|---|
| MGTS Future Money Income R Acc | -5.84 | 7.30 | 9.21 | 2.60 | 4.59 |
| MGTS Future Money Real Value R Acc | -3.87 | 4.61 | 7.28 | 1.10 | 4.87 |
| MGTS Future Money Real Growth R Acc | -4.84 | 6.66 | 9.61 | 1.76 | 4.60 |
| MGTS Future Money Dynamic Growth R Acc | -7.45 | 10.36 | 13.88 | 1.45 | 3.11 |

Source: Morningstar Direct. Currency: Pound Sterling. Total return. Past performance is no guarantee of future performance. The value of investments can fall as well as rise and investors may not get back their original investment.

### Economic and Market Commentary

*All figures sourced from Morningstar Direct unless otherwise stated.*

31 July 2019 – 31 October 2019

This reporting period witnessed falls in major equity markets in sterling terms, whilst fixed interest markets rose in value. Despite the recent falls, all major asset classes have recorded strong gains so far in 2019.

Looking at the notable IA (Investment Association) sectors over this quarter, North America provided the lowest return of -5.34%, Global Emerging Markets returned -4.91% and Asia Pacific (ex-Japan) returned -4.27%. These returns were significantly influenced by the c.6% rise in sterling during the period, reducing the value of dollar assets.

The UK All Companies sector was one of the strongest performing equity sectors, returning -0.97%, followed by Europe (excluding UK) returning -2.85%. The Sterling Corporate Bonds and UK Gilts sectors returned 1.32% and 2.16% respectively.

Brexit continues to dominate domestic politics and this reporting period has seen further developments. Boris Johnson was not able to meet his deadline of 31st October for the UK to leave the EU (which he had promised on a 'do or die' basis) as Parliament passed a law, referred to as the Benn act, compelling the Prime Minster to seek an extension if a deal had not been agreed. This prevented the UK from leaving without a deal and, given no deal could be agreed in time, the extension was requested and granted to 31st January 2020.

However, markets were surprised by the announcement that the withdrawal agreement had been reopened and a replacement to the Northern Ireland back-stop arrangements agreed despite the EU

previously insisting it would not renegotiate. The back-stop had been cited as the reason for Parliament rejecting the deal under Theresa May's leadership and the recent development gave hope that Parliament may now be able to support a deal.

Parliament did vote in favour of the bill at the second reading, but would not support an accelerated timetable, thereby ensuring the opportunity for amendments to be proposed. Boris Johnson felt the bill would not successfully pass the third and final reading due to the likely amendments which would, in his view, not sustain a majority. Therefore, he stated that Parliament was, in effect, broken and an election was necessary for the people to decide which party or parties should manage Brexit going forward. Boris eventually forced Parliament to agree to an election with the date set for 12th December.

This election is now being cast as a second referendum, with the main parties all taking a clear but different stance on Brexit. The Conservatives are promising to complete Brexit with a deal ready to be executed immediately. Labour have stated that they would re-negotiate the deal to be 'softer', include a customs union and a confirmatory referendum on this new deal. The Liberal Democrats would reverse Brexit altogether and have entered an alliance with the Green Party, SNP and Plaid Cymru to maximise the votes for 'remain' candidates.

This will not be a normal election as the parties' natural support will be conflicted with their Brexit approach. Many traditional Conservative seats voted remain in the referendum, so will these seats be lost? Labour also have many 'leave' seats in the north, so might they be tempted to vote for the Brexit Party or even the Conservatives? The polls show the Conservatives in front, but this will look familiar to observers of the 2017 election which swung towards Labour as the campaigns progressed leading to a hung Parliament.

We expect that the current polls do reflect the likely outcome as Boris Johnson is a strong campaigner, unlike his predecessor. The Conservative message of getting Brexit done will also appeal to many floating voters who are frustrated with the Brexit impasse and want greater certainty. Nevertheless, the outcome will impact portfolio performance and we will monitor the polls closely in case a change in strategy is required.

The performance of the various market indices during this reporting period gives an important indication how markets may react in each of the various Brexit outcomes. As news broke that a new deal had been reached, sterling appreciated in value, reducing the value of overseas assets, while UK stocks rose in value, particularly domestically focussed businesses, with the FTSE 250 index rising by more than 4% in one day.

In the event of a Conservative majority we expect a similar market reaction as UK equities have been avoided by many international investors due to uncertainty. A clear path for Brexit would encourage more investment into both sterling and UK stocks in our view. A Labour majority would also remove

the option of a no-deal Brexit; however, investors may be concerned by some of the policies announced by Labour such as nationalisation of key industries from private investors.

This is essentially a Christmas election and the main parties have fully embraced the festive season with huge infrastructure spending promises. This is a topic we have discussed in previous commentaries and another sign of the austerity imposed in the wake of the credit crisis coming to an end. In the case of the UK, the availability of cheap credit that can be borrowed over an extended period is breath-taking. For example, the UK can borrow for 50 years at a cost of 1.2% per annum despite the Bank of England aiming for a 2% inflation target.

This position is reflected across many developed economies and it will be very tempting for governments to promise spending increases which will be popular with voters. Mario Draghi, who recently stepped down as president of the European Central Bank, told European governments to increase spending as the limits of monetary policy to provide stimulus have been exhausted. He felt governments should now spend, taking advantage of low-cost debt, in order to transmit the effects of low interest rates into real economies.

Throughout this reporting period, and 2019 generally, the sustainability of global economic growth has been an area of increasing concern. Manufacturing surveys, which act as a leading indicator, began to point to a slowdown, and this has now been reflected in falling GDP growth. China's GDP growth has fallen from 6.8% in Jan 2017 to 6% more recently, whilst the US economy has slowed to 1.9% from over 3% in 2018.

The main shadow over the global economy has been the escalation in trade tensions between the US and China which has led to several waves of tariffs being applied to the goods traded between the world's two largest economies. This has caused a reduction in trade and confidence, explaining the drop in global growth, and although a resolution of these trade tensions has looked tantalisingly close on several occasions, the breakthrough has not yet occurred.

Political risk is difficult to manage and frustrating, especially in the current environment, where important news is often communicated directly through social media. As we move towards the next US election in 2020, there will be growing pressure on President Trump to provide good news, especially given the emerging impeachment investigation. Therefore, on balance, we expect a trade deal will be reached which would boost sentiment.

Looking forward, the combined global effect of increased government spending and a reduction in trade tensions should support future returns from equity markets. Although we have felt that fixed interest markets have been unattractive for some time, our view remains unchanged. If governments issue more debt, whilst increasing spending, this will push yields up due to the increased supply of debt and this could be compounded by the secondary inflationary effects caused by the spending increase.

We have also been considering the effects of debt issuance on the duration of fixed interest markets. As yield curves are both low and flat, debt issuers have been targeting longer-dated debt which, over time, is increasing the duration of fixed interest markets. Duration is a measure of the sensitivity of the price of a bond to a change in interest rates and therefore the higher the duration, the higher the capital loss if yields increase. This is particularly relevant to index trackers, where new longer-dated debt issuance is increasing the market sensitivity of an index during a period of all-time low yields. If yields do rise as we expect, the performance on the way down will be significantly greater than the profits made on the way up for the same change in yield.

During this reporting period, the performance of UK stocks has improved significantly, especially when compared to the global stock market in sterling terms. Part of this can be attributed to the rise in value of sterling, however we have also noted some rotation from growth stocks into value stocks. Although definitions vary, growth stocks are generally valued for their future expected performance whilst value stocks tend to be mature business models with less growth potential, but a higher degree of certainty.

The stretch between value and growth stocks has reached historic highs with growth stocks, particularly in the US, making large returns with a significant emphasis on disruptive business models such as Netflix, Uber and Amazon. During this reporting period, the trend has reversed as some growth models are being called into question. An example is Netflix, itself a disruptive business model, being disrupted by Apple and Disney moving into the streaming sector. This is starting to question the risk of disruptive business models and their ability to profit in the long term. We are concerned that businesses that are not profitable and require continual financial support may underperform in the future as the cost of borrowing rises, with the US market being the most exposed.

**Strategy**

We continue to see opportunities for equity markets to provide investment returns which are above both cash returns and inflation. Within equity allocations, we prefer value bias styles which we believe to be less exposed to downside risk with a higher upside potential. Therefore, we have a reduced allocation to the US and retain significant allocations to the UK, Asia and Emerging Markets.

We expect a negative real yield from investment grade debt and therefore have an underweight position. The flat shape of the yield curve currently presents the same opportunity at the short end as at the long end and therefore we continue to believe that duration risk is unattractive, preferring weightings in shorter maturity assets.

If the Conservatives secure a majority in the election on 12th December, we expect the current strategy to outperform due to UK mid-cap exposure and reduced US allocations, which would lose

value if sterling appreciates. Whilst this is our central view, and is supported by the most recent election polls, the outcome is not certain and voting intentions can change quickly.

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31 July 2019 to 31 October 2019

## Asset Class Review

### Investment Returns (%)

As of Date: 31/10/2019 Currency: Pound Sterling Source Data: Total Return

| | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | YTD |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Best | UK Small Cap 63.4 | UK Mid Cap 28.4 | Gilts 15.6 | UK Small Cap 35.0 | UK Small Cap 44.2 | North America 19.6 | Japan 17.6 | Emerging Markets 35.4 | Asia ex Japan 23.4 | Property 2.9 | North America 21.3 |
| | Emerging Markets 62.5 | Asia ex Japan 23.9 | Corporate Bonds 4.3 | UK Mid Cap 28.7 | UK Mid Cap 34.9 | Gilts 13.9 | UK Small Cap 13.6 | North America 34.1 | Emerging Markets 21.1 | North America 0.8 | World ex UK 18.9 |
| | Asia ex Japan 55.5 | Emerging Markets 23.6 | Property 2.9 | High Yield 18.9 | North America 28.3 | World ex UK 12.3 | UK Mid Cap 12.0 | World ex UK 30.4 | UK Mid Cap 18.2 | Cash 0.6 | UK Mid Cap 18.4 |
| | UK Mid Cap 52.8 | North America 19.1 | North America 1.2 | Asia ex Japan 17.5 | Japan 24.9 | Property 11.8 | Property 7.3 | Asia ex Japan 28.7 | Europe ex UK 16.9 | Gilts 0.6 | Europe ex UK 18.2 |
| | High Yield 47.9 | Japan 19.0 | Cash 0.5 | Europe ex UK 17.4 | Europe ex UK 24.0 | Asia ex Japan 10.0 | Europe ex UK 5.5 | Japan 22.7 | UK Small Cap 16.3 | Corporate Bonds -2.2 | Japan 14.4 |
| | UK Large Cap 27.3 | UK Small Cap 17.5 | FM Real Value -0.5 | Corporate Bonds 13.3 | World ex UK 22.7 | Corporate Bonds 9.8 | North America 5.3 | Europe ex UK 21.2 | Japan 14.4 | World ex UK -2.7 | FM Dynamic Growth 12.6 |
| | Europe ex UK 21.8 | World ex UK 16.7 | FM Income -1.9 | Emerging Markets 12.8 | UK Large Cap 18.7 | Emerging Markets 7.9 | World ex UK 4.8 | UK Large Cap 19.1 | World ex UK 13.5 | High Yield -3.6 | UK Large Cap 12.1 |
| | World ex UK 18.9 | FM Dynamic Growth 15.9 | UK Large Cap -2.2 | FM Dynamic Growth 12.8 | FM Dynamic Growth 16.9 | FM Real Value 4.9 | FM Income 2.6 | FM Dynamic Growth 13.9 | UK Large Cap 11.9 | FM Real Value -3.9 | Emerging Markets 10.6 |
| | FM Dynamic Growth 15.0 | UK Large Cap 12.6 | High Yield -3.1 | FM Income 12.2 | FM Income 13.0 | FM Real Growth 4.6 | FM Real Growth 1.8 | UK Small Cap 12.7 | North America 11.3 | FM Real Growth -4.8 | FM Income 10.6 |
| | North America 14.8 | High Yield 12.1 | FM Real Growth -3.9 | World ex UK 11.9 | FM Real Growth 11.4 | FM Income 4.6 | FM Dynamic Growth 1.5 | High Yield 10.1 | FM Dynamic Growth 10.4 | FM Income -5.8 | Asia ex Japan 10.3 |
| | Corporate Bonds 14.7 | FM Real Growth 11.0 | World ex UK -6.1 | North America 10.7 | FM Real Value 8.6 | FM Dynamic Growth 3.1 | FM Real Value 1.1 | Gilts 10.1 | Property 7.6 | FM Dynamic Growth -7.4 | FM Real Growth 9.6 |
| | FM Real Growth 14.4 | FM Income 9.2 | FM Dynamic Growth -8.7 | FM Real Growth 10.3 | Property 7.6 | UK Mid Cap 2.8 | Gilts 0.6 | FM Real Growth 9.6 | FM Income 7.3 | Japan -7.6 | Corporate Bonds 9.4 |
| | FM Income 13.8 | Property 8.4 | UK Mid Cap -10.3 | UK Large Cap 10.0 | High Yield 6.9 | Japan 2.7 | Cash 0.5 | FM Income 9.2 | FM Real Growth 6.7 | Emerging Markets -7.6 | High Yield 9.2 |
| | FM Real Value 9.0 | FM Real Value 7.8 | Japan -12.9 | FM Real Value 8.4 | Asia ex Japan 1.3 | High Yield 1.0 | Corporate Bonds -0.4 | Corporate Bonds 9.0 | High Yield 6.1 | Asia ex Japan -8.5 | Gilts 9.2 |
| | Property 8.3 | Corporate Bonds 7.7 | Asia ex Japan -14.8 | Japan 3.3 | Corporate Bonds 0.6 | UK Large Cap 0.7 | High Yield -0.9 | FM Real Value 7.3 | Corporate Bonds 5.1 | UK Large Cap -8.7 | FM Real Value 7.4 |
| Worst | Cash 0.6 | Gilts 7.2 | Europe ex UK -15.0 | Gilts 2.7 | Cash 0.5 | Cash 0.5 | UK Large Cap -1.3 | UK Mid Cap 5.1 | FM Real Value 4.6 | Europe ex UK -9.1 | UK Small Cap 4.4 |
| | Gilts -1.2 | Europe ex UK 6.6 | UK Small Cap -15.3 | Property 1.2 | Gilts -3.9 | Europe ex UK -1.4 | Asia ex Japan -3.5 | Cash 0.4 | Gilts 1.8 | UK Small Cap -13.5 | Cash 0.6 |
| | Japan -5.8 | Cash 0.5 | Emerging Markets -18.4 | Cash 0.5 | Emerging Markets -5.3 | UK Small Cap -1.7 | Emerging Markets -10.3 | Property -2.0 | Cash 0.3 | UK Mid Cap -15.2 | Property -0.3 |

Past performance is no guarantee of future performance. The value of investments can fall as well as rise and investors may not get back their original investment.

Source: Morningstar Direct

The table overleaf shows the performance of the major asset classes. This highlights the range of returns delivered over time and shows the risks in trying to predict individual winners.

Diversified portfolios, such as the four Future Money funds, can deliver attractive investment returns whilst reducing the effects of large swings in performance. Via such a structure, investors can own a professionally managed portfolio with exposure actively positioned across asset classes.

**Year to Date**

North American equities have been the top performing asset class of the year so far. Having been amongst the biggest losers of the market falls of late 2018 they bounced back strongly on the jump in sentiment of 2019 to date. With strong jobs creation numbers and a more accommodative stance on interest rates from the Federal Reserve, the economic picture has looked significantly brighter than late last year and therefore a strong relief rally has been experienced.

The index of world stocks excluding those listed in the UK has been the second best performer of the year to date. This is boosted by the strong US performance, with American companies accounting for nearly 60% of the index, but is also a broader reflection on the success of equities from across different regions.

In a 'risk-on' environment, such as we have experienced overall on the year to date, all major asset classes have made money, leaving cash and property as the least productive. Cash returns may be low, but it is important to note that any positive return is a major asset at times of stress and therefore this defensive characteristic can be very useful as a portfolio diversifier. Investors holding cash during 2018 for instance would have been very pleased with their non-negative returns.

Property has been the worst performing asset class of 2019 so far. While the property market will have benefitted from the general mood of increased confidence across markets, the illiquidity in the sector means that prices are very slow to react changes in market dynamic. As such, during the market falls of 2018, property looked like a very strong asset class in relative terms, yet had investors attempted to withdraw large amounts from the property sector at this time, then it is likely that difficulties may have been achieved in securing expected prices. The underperformance of property this year is therefore likely an unwinding of this divergence between published price and achievable value, i.e. prices in property markets have stayed relatively static this year, while underlying valuations have caught up.

**Important Information**

Please note that the contents are based on the author's opinion and are not intended as investment advice. This information is aimed at professional advisers and should not be relied upon by any other persons.

Any research is for information only, does not constitute financial advice or necessarily reflect the views of the author and is subject to change.

It remains the responsibility of the financial adviser to verify the accuracy of the information and assess whether the fund is suitable and appropriate for their customer.

Past performance is not a reliable indicator of future performance. The value of investments and the income derived from them can fall as well as rise and investors may get back less than they invested.

Important information about the funds can be found in the Supplementary Information Document and NURS-KII Document which are available on our website or on request.

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