

Current Focus

September 2019

A monthly market comment from Rivers Capital Management. Views expressed here are subject to change and for professional advisors only



Market Comment

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Summary

- Market volatility has been a result of increased justified concerns regarding growth
- Manufacturing production is declining in most regions as trade and demand falls
- Bond market warning signals are not being reflected in equity valuations
- Strong returns from Anchors and Enhancers have boosted portfolio returns
- BMi portfolios remain positioned to opportunistically add risk at better valuations

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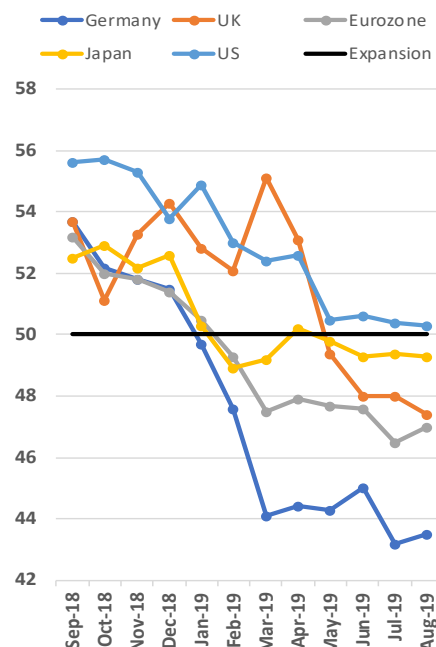
Concern over economic growth, trade and Brexit rose sharply during August. Global growth is slowing down, protectionism is on the rise and Brexit has become the political equivalent of an oubliette with parliament unable to implement an ambiguous 'will of the people'. How Brexit turns out is, literally, anybody's guess now but given the extensive coverage in all news services, we will concentrate on global growth, and specifically slowing manufacturing, in this month's Focus. The portfolios we manage are allocated globally and notwithstanding the direct impact on the value of sterling, which we can moderate through currency hedging, the impact of Brexit on the portfolios is likely to be modest, whatever the outcome domestically.

The one survey that has been flashing red warning signs for the last few months is the Purchasing Managers Survey for Manufacturing (PMI). The data for the index is collected through a survey of purchasing managers in the manufacturing sector in each country. An index reading of 50.0 means that the variable is unchanged, a number over 50.0 indicates an improvement, while anything below 50.0 suggests a decline. As shown in the graph the recent decline has been universal. While the falls have been most significant in Europe and the UK, probably heightened by Brexit uncertainty, the global impact, at a time when borrowing costs remain low, is clear. There is some evidence that the falls in the euro-zone index might be bottoming out, but it is currently at a level consistent with ongoing industrial recession.

In the US, the survey for manufacturing does remain just above the 50 level but currently points to the weakest pace of expansion in the manufacturing sector there since September 2009. The imposition of tariffs by China is affecting production as new export orders fell at the quickest pace since August 2009. In the same survey business confidence dropped to a new low. Less export orientated surveys, for non-manufacturing, remain above 50 for the US but have fallen consistently since last year.

Manufacturing growth continues to improve in emerging economies, but the rate of growth has slowed sharply as falling export demand and rising tariffs have taken their toll. During July the only countries with increased manufacturing were India, Brazil and China. The increase in China, to

Falling Manufacturing PMIs



Source: River Capital Management

a 5-month high in July, reflected an boost in domestic activity from stronger public spending on infrastructure, rather than any let up in tariffs, or demand, from the US.

With almost all countries' manufacturing employment indices now pointing to falls in employment, the effect on the rest of the economy is unlikely to be positive. This indicator, among others, provides some explanation for the worrisome inverted yield curve (the yield on government 10 Year debt being lower than that for 2 year) which has been widely reported recently. The fact that 'long-term' money provides a lower return than 'short-term' money has been an accurate warning sign for recession for many years. Bonds yields are very low and are indicating that economic difficulties lie ahead. As discussed, the forward-looking PMI manufacturing surveys provide further evidence that investors need to be cautious. Given these economic warning signs, we continue to be surprised by the high level of valuations that have been sustained in equities.

With the exception of the UK, which arguably remains at a discount due to Brexit, global equity indices remain high on a valuation basis. As a result, we have been recommending a relatively

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Portfolio is not suitable for all types of investor and investor accounts may only be attached to it by the instruction of a professional Financial Adviser. Past performance is not necessarily a guide to the future performance. Market movements may cause the value of investments and the income from them to fall as well as rise. Unless otherwise

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underweight allocation to equity related, Enhancer, assets since April. Partly due to falling interest rates, which tend to boost Anchors, and high returns in uncorrelated assets, Diversifiers, the portfolios we manage have performed positively while being less affected by the recent volatility from Equities. At this time last year, we recommended a similar portfolio tactical allocation, which provided some protection during the volatile final quarter of 2018. This allowed the opportunity to add risk, by increasing Enhancer and lowering Anchor allocations, at lower equity valuations in November and December. Thereby

benefiting from the strong equity returns as investor confidence returned in the first half of 2019. The main driver to this return in confidence was not economic growth but a belief that Central Bank intervention will be able to stimulate sufficient demand, we agreed with this initially but concluded in April that it had been overdone. Looking forward, while our global economic outlook is more cautious for 2020 than it was for 2019, we will again take the opportunity to increase Enhancer exposure, at better valuations when they become available, and move to a more neutral stance in the next few months. Unless the economic

outlook is incorrect and growth improves, causing rates to rise and corporate profits to soar, current Enhancer valuations are difficult to justify at current levels.

Market Returns (£) - 31 st August 2019	1 Month	3 Month	YTD	1 Year	3 Year	S/I*
Anchors						
Cash + 1%	0.1%	0.4%	1.2%	1.8%	4.8%	5.1%
Inflation Linked UK Bonds	2.9%	7.7%	13.8%	14.3%	15.5%	21.5%
Gilts	3.7%	6.2%	11.3%	11.8%	7.3%	12.7%
Global Government Bonds (hedged)	2.5%	4.4%	8.0%	9.4%	7.1%	7.0%
Enhancers						
Global Corporate Bonds (hedged)	2.2%	5.0%	10.8%	9.9%	9.8%	12.0%
Global High Yield (hedged)	-1.5%	1.9%	7.8%	5.3%	11.8%	16.9%
Emerging Market Bonds (hedged)	-2.5%	6.9%	11.7%	20.1%	20.2%	23.5%
FTSE 350 TR Index	-3.6%	2.1%	11.3%	0.6%	20.2%	27.2%
FTSE UK All-Small Cap	-2.7%	-2.3%	5.7%	-5.3%	20.5%	32.6%
Global Equity (MSCI)	-1.5%	8.6%	20.4%	6.5%	41.0%	50.9%
European Equity (MSCI)	-2.1%	5.6%	15.9%	3.6%	27.8%	36.8%
US Equity (S&P)	-1.1%	10.4%	23.3%	9.2%	51.2%	60.1%
Japan Equity (Topix)	-0.6%	6.1%	11.2%	-0.5%	27.4%	37.7%
Pacific Ex Japan Equity (MSCI)	-4.0%	4.7%	9.4%	-1.2%	28.1%	43.8%
Emerging Market Equity (MSCI)	-4.4%	3.3%	8.7%	0.4%	25.1%	39.8%
Chinese Equity (Hang Sang)	-6.6%	0.4%	7.0%	2.2%	32.9%	50.4%
Indian Equity (Nifty)	-2.4%	-5.0%	3.6%	-3.1%	22.9%	36.4%
Diversifiers						
Commodity Index	-1.8%	3.1%	6.6%	0.9%	5.2%	-0.3%
Gold	7.1%	20.3%	23.8%	34.5%	22.4%	23.5%
Silver	11.7%	29.3%	22.2%	33.0%	1.6%	3.6%
Brent Oil	-6.0%	-3.6%	18.1%	-16.8%	38.9%	33.8%
UK Property	0.0%	0.0%	0.7%	0.8%	16.1%	13.1%
Global Property Shares	2.3%	-0.1%	8.7%	-3.9%	5.2%	12.4%
Rivers Model Portfolios						
Rivers Preservation Portfolio	0.8%	2.7%	5.6%	3.8%	9.6%	13.7%
Rivers Cautious Portfolio	0.5%	4.3%	9.6%	5.4%	17.4%	23.6%
Rivers Balanced Portfolio	0.0%	4.6%	10.9%	5.1%	21.4%	29.3%
Rivers Adventurous Portfolio	-0.3%	4.8%	11.8%	5.2%	23.1%	32.0%
Rivers Aggressive Portfolio	-1.4%	5.3%	13.1%	4.2%	27.3%	37.3%
Rivers Cautious Income Portfolio	-0.1%	2.7%	8.2%	4.0%	9.7%	13.3%
Rivers Balanced Income Portfolio	-0.4%	3.1%	9.1%	4.1%	14.6%	20.2%

Source: Financial Express in GBP (unhedged unless stated) as at 31st August 2019. *Rivers Portfolios since launch June 30th 2016

Model Performance is indicative only and is net of Rivers Capital Management Charge and Underlying Fund charge but not advisor or platform costs.

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