# Current Focus

September 2019

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

INTELLIGENT INTUITIVE INVESTING


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### Summary

- Investment markets remain calm despite rising global poltical uncertainty
- US dollar weakness, real interest rates, demand and supply determine gold prices
- Recently interest rates and investor demand, not dollar weakness have boosted gold
- Further increase is limited but diversification benefits of gold continue to be attractive
- At current valuations gold remains attractive compared to many Enhancer assets



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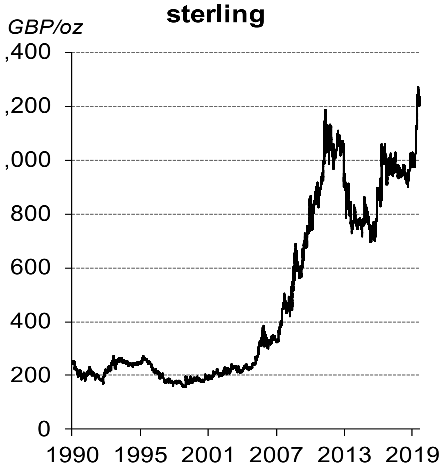
## Market Comment

Considering the political uncertainty around the world, investment markets were a picture of calm in September. Politics was centre stage with an unlawful prorogation of Parliament adding to Brexit uncertainty in the UK, initiation of impeachment proceeding against President Trump, escalating unrest in Hong Kong and an attack on Saudi Arabia's biggest oil facility. We do hope this political situation calms but believe its influence over investment markets, especially the global investment markets we look at, can easily be overestimated. For that reason, this month we want to focus on what historically has been the most political, but is now the most apolitical, asset class of all; Gold. Gold is held as a diversifier in all the portfolios we manage, it reached a 5-year high in August before falling nearly 5% in September. Despite the pullback, it remains among the best performing investments year to date and remains a safe haven. We explain what factors we think drive the return to gold, why we continue to allocate to gold despite the constraints on many of those factors, and what may prompt our next allocation change to this unique asset class.

Gold is probably the oldest asset class of all. Gold is scarce, it is almost impossible to make, or for that matter destroy, and as a result has been seen both as a store of wealth, or tool for barter, for millennia. Its mass, anonymity and beauty add to its charm but apart from making pretty jewellery, it has few practical uses. Its characteristics as a currency are well known, especially as a currency that no central bank can print. It is universally recognised, which is why, from a practical perspective, no crypto currency can yet replace it. Gold's universality sets it apart from all alternatives but with no yield and the cost of storage, the only real motivation for holding it as an investment is a belief that the gold price will increase. The ultimate 'greater fool' asset perhaps but as a Diversifier rarely has there been a period when a holding in gold hasn't improved the risk adjusted return of a portfolio. Having held Gold and benefited from its sharp rise in recent months we must consider what has driven that gain, whether it is likely to continue, and what changes to our allocation make sense as a result.

The price of gold is primarily driven by four factors. First is the strength of the US dollar.

**Gold spot price in pound sterling**




Source: Reuters Datastream, LBMA, World

As gold is internationally traded in US dollars the nominal 'value' of gold goes up when, all other things being equal' the value of the dollar decreases. This effect is true for all internationally traded assets which are priced in dollars but it is exaggerated for Gold which is seen as an alternative store of capital. The second factor is US interest rates to which Gold is considered inversely correlated. When interest rates fall, especially if they fall below inflation, creating negative 'real' rates, gold becomes attractive as an alternative store of wealth. Third is really just demand, not so much the demand for pretty jewellery (although population growth and global wealth does continue to grow that) but the speculative trading demand driven by the sentiment of investors. Fourth is supply. This is related to gold miners and overall investment in mines, as you cannot 'make' gold you have to find it, or sell gold that has already been found. As with everything else when demand exceeds supply, we can expect prices to rise. One characteristic of gold is that demand can change very quickly while supply tends not to.

So far this year, it has been investor demand and falling interest rates that have driven gold prices. The value of US dollars hasn't changed much, the DXY index, against a basket of global currencies, has increased a little. In such a short time there cannot have been any material changes in supply. Looking forward, interest rates could continue to fall, and demand rise further, but not at the rate, nor the magnitude seen recently. Global economic indicators continue to point to slower growth and the Federal Reserve may well lower interest rates, but a lot of this expectation is already in the price. In the US the 10-year interest rate is already close to all-time lows, and below the rate of inflation. Any room for further decline is limited. A fall in the Dollar could coincide with falling rates but given the slowdown is most likely to be global we think this is unlikely. The US dollar, given its status as the world's reserve currency, will likely appreciate if a global slowdown accelerates.

With benchmark interest rates unable to fall much further and the US Dollar unlikely to depreciate, the only driver to continued appreciation in the gold price is investor demand. If uncertainty, be it political or economic, continues to escalate that rising demand is likely. That said should economic data continue to deteriorate we would expect a more significant decline in Enhancer valuations, than has been experienced recently. Enhancer asset valuations, in our opinion, remain high. This can be sustained for some time. For as long as this continues, we prefer Diversifier and Anchor assets on a relative basis, specifically on this basis Gold remains an attractive alternative. If, and when, Enhancer valuations improve we will increase risk and lower the Diversifier and Anchor allocations back to a more neutral allocation. This will likely include lowering the gold allocation, especially if speculative demand for Gold continues to rise. On balance however the current allocation remains appropriate.

| Market Returns (£) - 30th Sept 2019 | 1 Month | 3 Month | YTD | 1 Year | 3 Year | S/I* |
|---|---|---|---|---|---|---|
| **Anchors** | | | | | | |
| Cash + 1% | 0.2% | 0.5% | 1.4% | 1.9% | 4.9% | 5.3% |
| Inflation Linked UK Bonds | -1.9% | 5.1% | 11.7% | 13.4% | 12.3% | 19.2% |
| Gilts | 0.5% | 6.6% | 11.8% | 14.2% | 10.6% | 13.3% |
| Global Government Bonds (hedged) | -0.7% | 2.5% | 7.2% | 9.2% | 6.5% | 6.3% |
| **Enhancers** | | | | | | |
| Global Corporate Bonds (hedged) | -0.6% | 2.3% | 10.1% | 9.7% | 9.4% | 11.3% |
| Global High Yield (hedged) | 0.5% | -0.3% | 8.3% | 4.4% | 11.7% | 17.5% |
| Emerging Market Bonds (hedged) | -0.1% | 2.3% | 11.6% | 17.1% | 17.1% | 23.3% |
| FTSE 350 TR Index | 3.0% | 1.4% | 14.6% | 2.9% | 21.7% | 31.0% |
| FTSE UK All-Small Cap | 1.9% | -0.9% | 7.7% | -3.4% | 20.5% | 35.2% |
| Global Equity (MSCI) | 0.8% | 3.7% | 21.4% | 7.6% | 40.9% | 52.1% |
| European Equity (MSCI) | 1.5% | 1.4% | 17.7% | 5.4% | 28.1% | 38.9% |
| US Equity (S&P) | 0.6% | 4.9% | 24.0% | 9.7% | 50.9% | 61.1% |
| Japan Equity (Topix) | 2.9% | 6.5% | 14.4% | -0.3% | 26.9% | 41.7% |
| Pacific Ex Japan Equity (MSCI) | 0.3% | -1.3% | 9.7% | 1.3% | 26.7% | 44.2% |
| Emerging Market Equity (MSCI) | 0.7% | -1.1% | 9.5% | 3.7% | 25.5% | 40.8% |
| Chinese Equity (Hang Sang) | 0.6% | -4.8% | 7.7% | 2.8% | 30.3% | 51.3% |
| Indian Equity (Nifty) | 1.9% | -2.1% | 5.6% | 10.8% | 27.4% | 38.9% |
| **Diversifiers** | | | | | | |
| Commodity Index | 0.1% | 1.3% | 8.1% | 0.1% | 12.0% | 12.4% |
| Gold | -4.7% | 7.2% | 18.0% | 29.6% | 15.2% | 17.7% |
| Silver | -8.3% | 14.1% | 12.1% | 21.0% | -10.1% | -5.0% |
| Brent Oil | -0.5% | -6.0% | 17.5% | -20.6% | 31.1% | 33.1% |
| UK Property | 0.2% | 0.2% | 0.9% | 1.0% | 14.7% | 13.4% |
| Global Property Shares | 6.9% | 6.4% | 16.1% | 5.3% | 14.4% | 20.1% |
| **Rivers Model Portfolios** | | | | | | |
| *Rivers Preservation Portfolio* | *-0.2%* | *1.6%* | *5.5%* | *4.0%* | *8.7%* | 13.6% |
| *Rivers Cautious Portfolio* | *-0.2%* | *2.2%* | *9.4%* | *5.6%* | *16.4%* | 23.4% |
| *Rivers Balanced Portfolio* | *0.2%* | *2.3%* | *11.1%* | *6.3%* | *20.7%* | 29.5% |
| *Rivers Adventurous Portfolio* | *0.2%* | *2.1%* | *12.0%* | *6.7%* | *22.5%* | 32.2% |
| *Rivers Aggressive Portfolio* | *0.4%* | *1.7%* | *13.6%* | *6.0%* | *26.9%* | 37.9% |
| *Rivers Cautious Income Portfolio* | *0.5%* | *1.6%* | *8.7%* | *4.9%* | *10.0%* | 13.9% |
| *Rivers Balanced Income Portfolio* | *0.5%* | *1.7%* | *9.7%* | *5.1%* | *14.2%* | 20.9% |

Source: Financial Express in GBP (unhedged unless stated) as at 30th September 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.**