PORTFOLIO POSITIONING UPDATE JANUARY 2021

13 January 2021

momentum
global investment management

Performance

For the month of December, the Fintax International Balanced fund was up 3.5% in dollar terms and the Fintax International Growth Fund was up 3.8%.

Market Commentary

December was another positive month for risk assets with global equities building on strong momentum from last month. After much wrangling, President Trump signed a new $900bn stimulus package into law, prompting some weakness in the dollar and a modest rise in Treasury yields. Global Emerging Markets outperformed, capping their outperformance for the year as a whole as EM assets benefited from a weaker dollar and a rally in hard commodities such as iron ore and crude oil. The continued rally in markets was at odds with depressing developments in terms of the Coronavirus, as a new more infectious strain was discovered in the UK, prompting stricter lockdown measures both in the UK and elsewhere in Europe.

Country positioning – how much to allocate to China?

A big theme of 2020 was the outperformance of Chinese equities given the relative success of their lockdown efforts and stimulus measures. Given that China still represents a small portion of most investors' portfolios, this raises questions about the appropriateness of investor positioning. **The Chinese economy is now set to become the largest in the world by 2028 (according to the UK-based Centre for Economics and Business Research), yet it represents a mere 5.2% of the MSCI AC World Index versus the US at 57.3%.**

International benchmarks do not represent the full size of the Chinese stock markets, as can be seen from chart 1 below. China and Hong Kong now make up 17% of global market capitalisation, up from 5% in 2003, yet **the historic lack of access to the vast onshore market has made it difficult for major index providers to upweight China meaningfully**. This has changed in recent years with A shares being included in MSCI indices since 2018, but recent steps taken by the US to ban investment in Chinese companies may now be setting that process into reverse.

A lack of international buyers is part of the reason that the Chinese stock market is only 51% of its total GDP, a ratio that is well below many developed economies, particularly the US where that figure is 160% (see chart 2). **These figures show the growth potential of the Chinese public equity market to increase beyond GDP in the years to come it if continues to liberalise its capital markets.** It is notable that, while the US is putting up barriers to trade with China, the picture is not the same globally, as the EU and China concluded a Comprehensive Agreement on Investment during the month.

The current positioning of our equity funds reflects the growth potential of Asia, while recognising the current dominance of US companies in international benchmarks. The equity portion of the Fintax International Growth Fund has 55.6% invested in US domiciled companies, 23.0% in Europe and the UK, 9.6% in the Developed Pacific region, 8.2% in Emerging Asia and 1.1% in other Emerging Markets. **As Chinese equity markets continue to mature, we will look to increase our strategic allocation to this part of the world,** while remaining cognisant of tactical considerations, governance and other ESG issues, and the tendency that the offshore China market has had towards speculative bubbles in recent years.

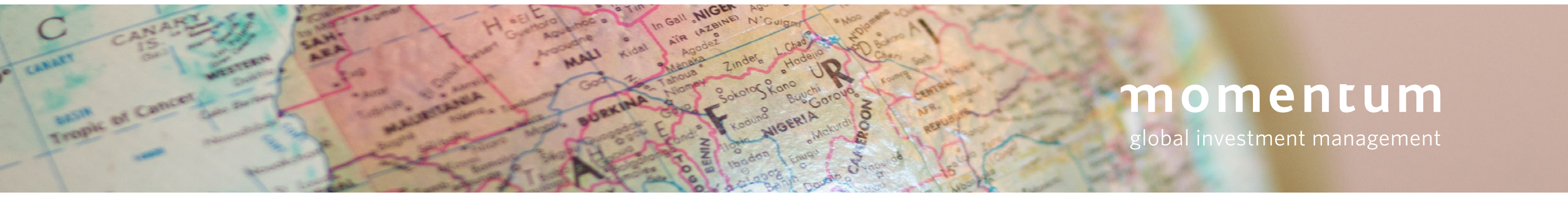


Chart 1:

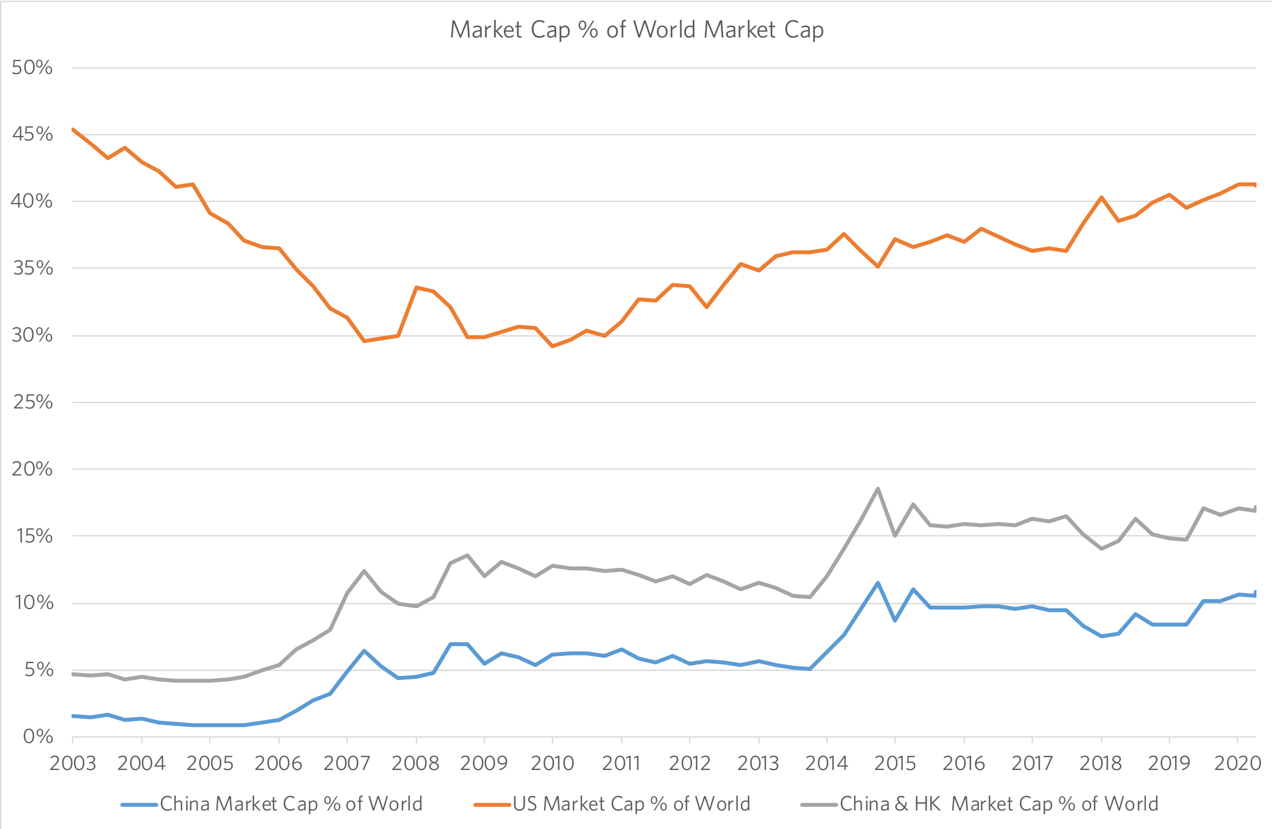
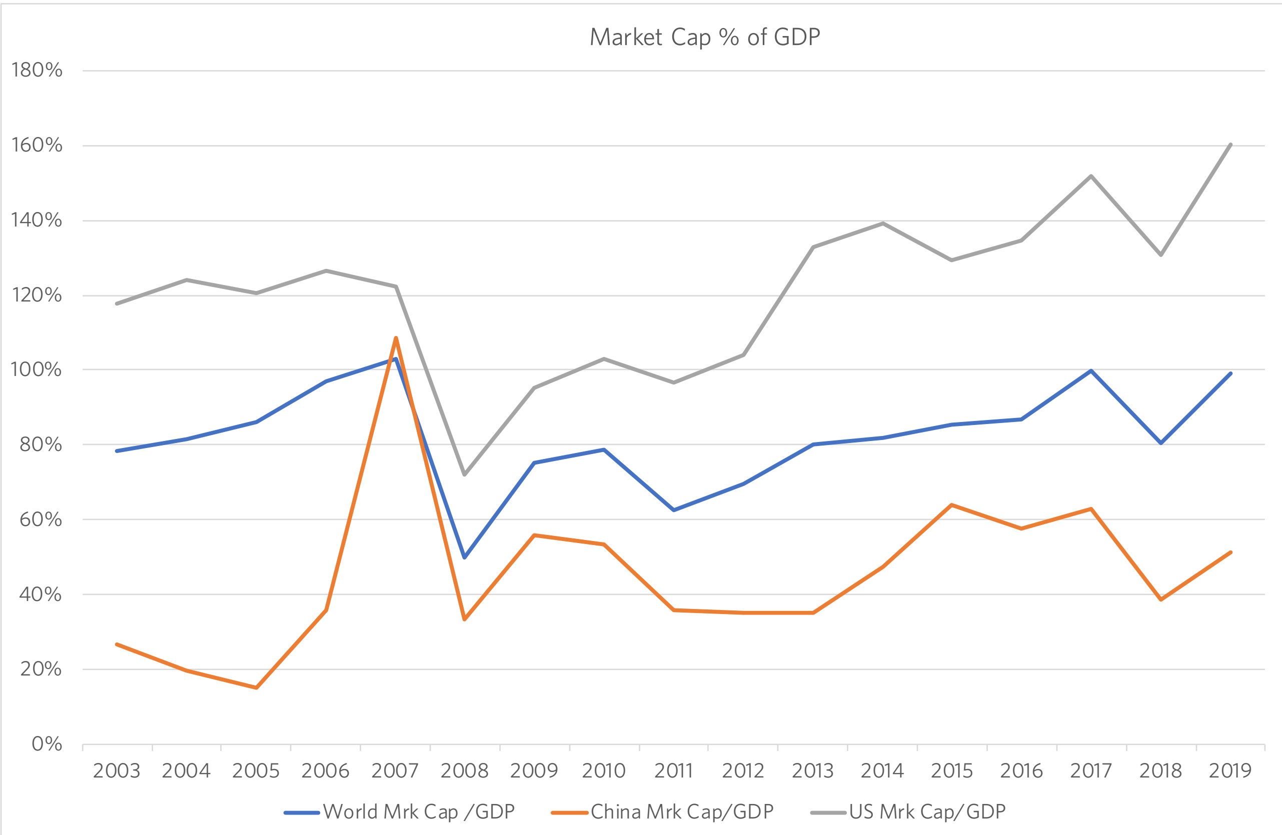
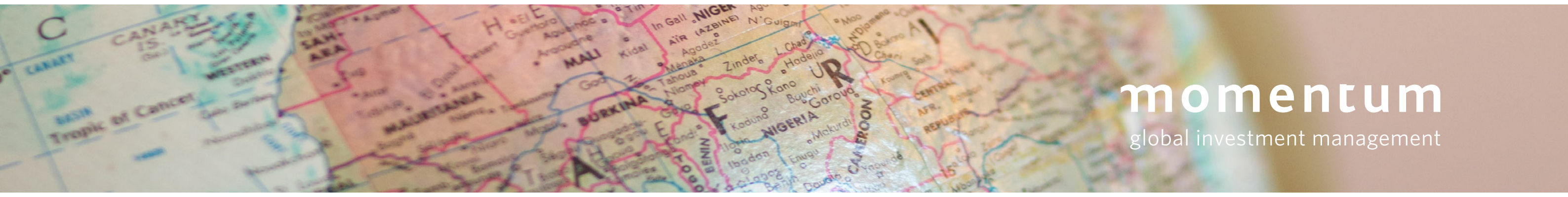


Chart 2:





Outlook

While the outlook for 2021 still looks strong given last month's positive vaccine developments, the first quarter of 2021 is shaping up to be challenging for the powerhouse economies of the northern hemisphere. **Seasonal factors combined with new virus strains means that infection rates look likely to get worse until the vaccine is rolled out in large enough numbers to reverse the tide. Thereafter the beginnings of a return to near-normality should be underway and the conditions are set for a strong recovery:** release of pent-up consumer demand, renewed business investment, refocus of fiscal spending on stimulus and growth rather than support for businesses and people most damaged by the pandemic, and continuing ultra-loose monetary policy. Biden's success is likely to result in greater fiscal packages to promote growth, however questions over international relations and tech company regulation remain pertinent. Overall we see good returns still on offer from equities over the medium term, especially in relation to areas of fixed income which remain vulnerable to increasing inflation expectations.