PORTFOLIO POSITIONING UPDATE FEBRUARY 2021

11 February 2021

momentum
global investment management

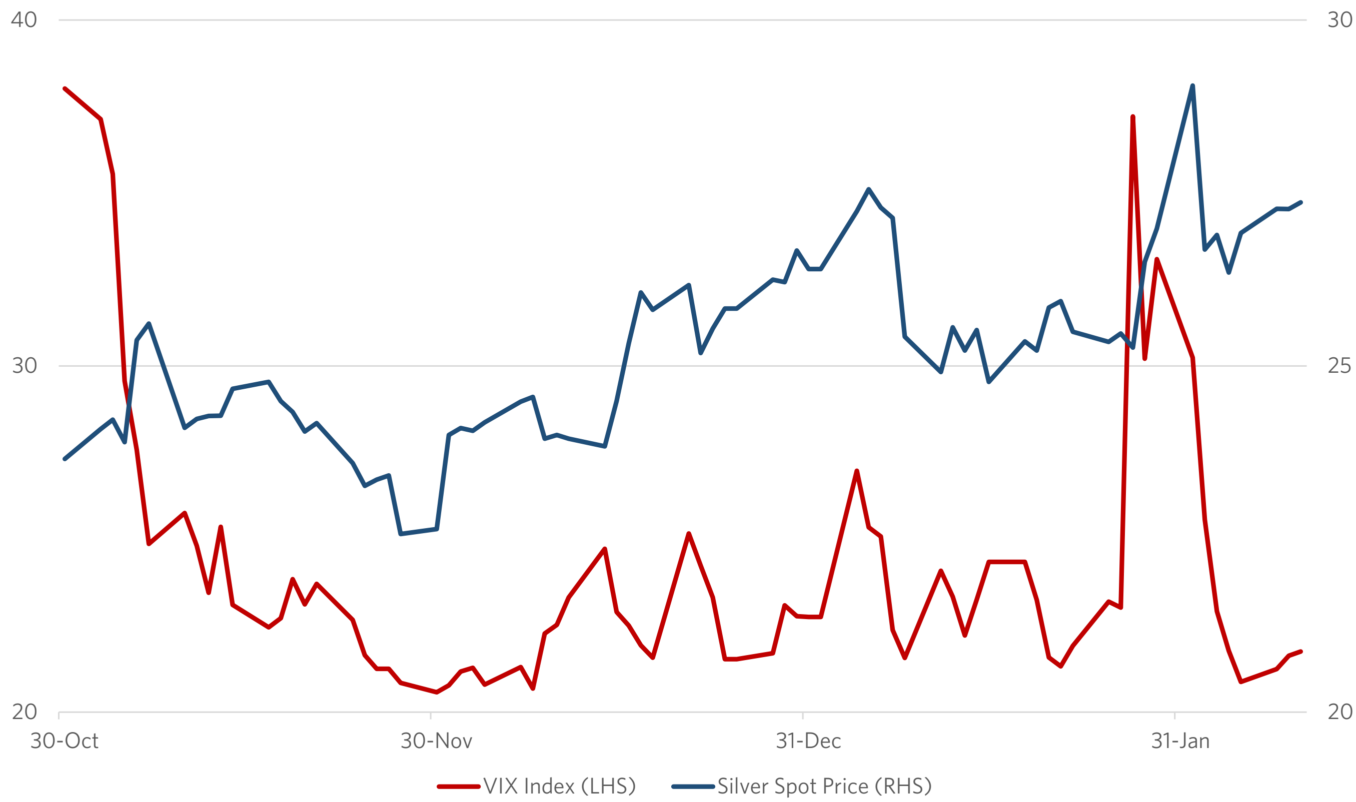
Performance

The Fintax Balanced and Growth Funds produced marginally positive returns in January, 0.1% and 0.3% respectively, a month when global equity markets (MSCI World) fell by 1% and government bonds (JPMorgan Global GBI) returned -1.3%.

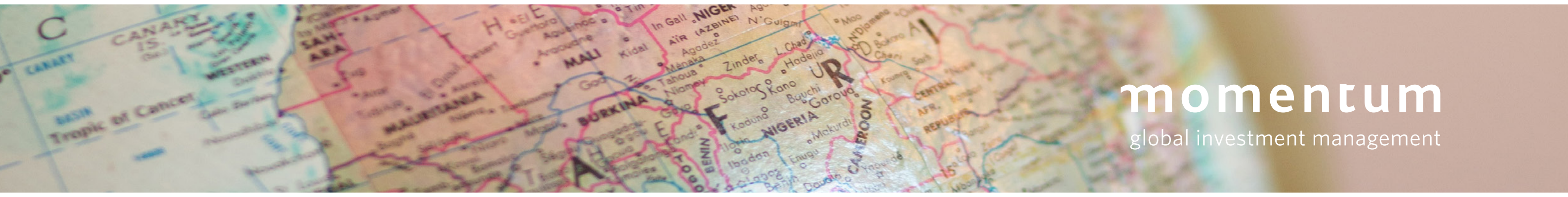
Portfolio changes

A new position was taken for the Growth Fund in the Evenlode Global Income fund; the manager specialises in equity income investing, focussing on real dividend growth in the long term, balancing present income with the opportunity for growth. The fund aims to outperform global developed world equities with less volatility and downside risk, investing in high quality, cash generative companies with diverse revenue streams. The addition of this quality income strategy complements the existing equity managers in the Growth Fund.

A sudden sharp spike in the silver price late in the month gave the opportunity to sell the position in the Growth Fund, where the precious metals component will be focussed on gold, a more recognised and less volatile store of long term value, and halve the position in the Balanced Fund. Capital gains of some 65% were realised since purchase in early 2020.



Source: Bloomberg, Momentum Global Investmnet Management



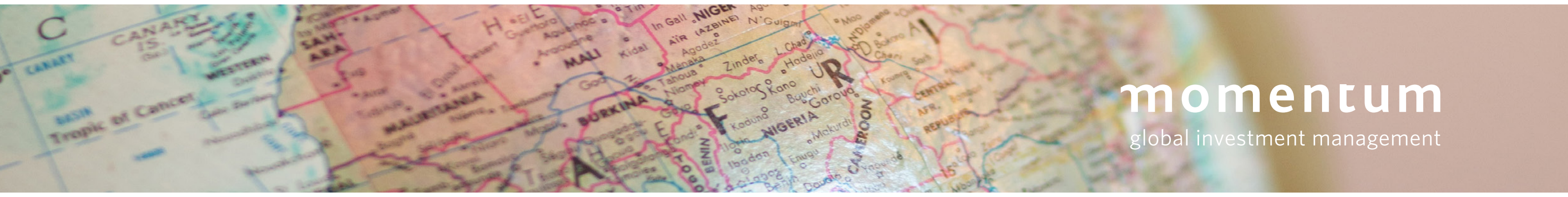
Main Street vs Wall Street?

Markets were gripped in January by a retail trading frenzy unleashed on Wall Street, with small investors operating en masse via social media, targeting hedge funds engaged in short selling of stocks. The power of the network effect, via online forum WallStreetBets, ease of trading at low cost and availability of leverage, using retail trading platforms such as Robinhood, fired on by pandemic stimulus cheques, combined to produce extraordinary share price movements. Retail investors bought into the most shorted stocks in massive volumes to squeeze the short sellers; GameStop, a bricks and mortar video games retailer struggling in a digital world, was the stock of choice (although by no means the only one), with its share price soaring twenty-fold in January amidst frenetic trading, triggering a huge short squeeze as short sellers were forced to buy back stock to limit losses. Most prominent among those losers was hedge fund Melvin Capital, which took a $7bn loss and booked a return of -53% in January. Hedge funds were forced into selling their favoured long positions to cover losses on their short books. Such was the scale of the trading that the Vix index of volatility spiked in a few days from the low 20's to a high of 37. These same retail investors also took on the silver market, pushing its price up by 15% to its highest level in 8 years in a matter of days, but found this an altogether different market to capture, being deep and liquid with a much lower proportion of short positions.

By month end, some of the speculative froth was coming out of the market, leaving many hedge funds and day-traders bruised and battered, and question marks around most of the players: hedge funds short selling, retail investors taking on inappropriate and little understood risks, trading platforms forced to suspend trading briefly to ensure capital adequacy, and the role of regulators, now in the process of scrutinising events.

Taking the long view, this is largely 'market noise', not systemically destabilising and unlikely to have a lasting broad-based impact. The Fintax funds have no exposure to short selling and were unaffected by the damage inflicted on hedge funds. However, by illustrating the power of networks in moving share prices dramatically this is unlikely to be the last time such extraordinary volatility is triggered. It raises questions about the appropriateness of small-scale investors, in an increasingly 'DIY' world, exposing themselves to such high risk, and the size, transparency and suitability of short selling. **It should also serve as a warning to investors: excess liquidity on the scale we have today can give rise to irrational behaviour and bubbles; this type of speculative exuberance with no regard to underlying fundamentals plainly happens only when markets have enjoyed a long bull run. It is not a bell ringing for a market top, more a warning shot and the need for careful diversification in portfolios.** For long term investors, it highlights the critical importance of sticking to fundamentals and valuation, avoiding high risk and speculative short term position taking, ensuring transparency and liquidity, and not being thrown off strategic course by sudden market-moving events with no meaningful implications for underlying economic conditions. Finally, the volatility and mis-pricing it creates gives rise to opportunities shorter term to take advantage of sudden spikes, either up or down, where these are unjustified by fundamentals.

Buffet perhaps put it best with his line **'the less prudence with which others conduct their affairs, the greater the prudence with which we should conduct our affairs'**.



Outlook

As the second wave of the pandemic and worries about mutations continue to damage confidence, disrupt activity and result in extended lockdowns, the first quarter of the year will be tough for many economies. However, **recovery has been delayed, not cancelled, and the roll-out of vaccines will soon result in eased restrictions and a gradual return to near-normality.** While some sectors will face longer term headwinds, much of economic activity will recover rapidly, boosted by huge pent-up demand and policy support measures. Corporate profits are set to recover substantially over the next 18 months. This provides **a strong backdrop for equity markets in 2021, driven by earnings gains rather than higher valuations.** While periods of volatility are inevitable, especially given the moves over the past few months and the high valuations in some asset classes and sectors, and risks around inflation and possible central bank policy shifts call for diversification of portfolios, we believe opportunities in risk assets are good for the year ahead.
