

## Investment Advisory Committee (IAC) Quarterly Meeting

### Minutes of Meeting

#### Date

11/06/2019

#### Present members

Julius Pursaill (Chair)  
Colin Taylor  
Ewan Smith  
Piers Hillier  
Candia Kingston  
JB Beckett  
Dr. James McCourt

#### In attendance

Lorna Blyth  
Euan Craig  
Trevor Greetham (RLAM)  
John Matthews  
Craig Inches

#### Apologies

Robert Whitehouse  
Niall Aitken

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#### Owner

1. **REVIEW OF PREVIOUS MINUTES**

The minutes of the 27 February 2019 meeting were approved.

All

2. **PROJECTS**

**RLP Absolute Return Government Bond**

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Fund performance has remained below the benchmark of 2.5-3% pa above SONIA over rolling 3yrs and a paper was presented to IAC from RLAM which proposed changes to address this. These include increasing exposure to cash and short dated corporate bond assets to add potential for increased returns, increasing duration to +/-3yrs to allow positions to run longer and an increase in the maximum leverage position. IAC were comfortable that RLAM have a good track record in cash and short dated bond assets but questioned the increase in leverage. RLAM confirmed that they don't expect to need the maximum leverage limit and it was set in the event of a repeat of 2007/2008 type event. IAC asked about risk measures and positions taken within the fund, specifically on the use of value at risk measures and requested further information from RLAM and Investment Office on this. IAC also asked how RLI intend to model the asset class in the upcoming SAA review. IAC were supportive in principle subject to the response from the business on these points.

LB

**Responsible Investing (RI)**



A paper was presented providing an update on the RI project and the impact on the investment solutions offered through RLI. Details of the new RI policy, climate change framework and expectations for asset managers, including RLAM were shared. IAC asked for more detail around investment beliefs and asked about RLAM's ability to embed this across all asset classes. Piers responded that RLAM integrate ESG factors across some, but not all and this project will help to formalise current processes and ensure integration across all. As part of this RLAM will vote on all shares as currently overseas passives are excluded. IAC were happy with the direction of travel and consider ESG to be relevant for long term investment strategies and customer outcomes. A specific question was asked for the business to clarify the process and responsibility for oversight of ESG for external funds.

LB

### **IAC Effectiveness Review**

A paper was presented to IAC summarising responses from the effectiveness review. IAC were keen to gain more clarity on the interaction with Investment Performance Committee (IPC), Independent Governance Committee (IGC) and demonstrating value for money as well as clarity on what aspects of RI should fall under its remit. The following actions were agreed :

- Clarify interaction between IAC, IGC and IPC.
- Consider what information on ESG/RI is relevant for IAC.
- Include a specific aim in the Terms of Reference to reduce the overall median charge of the matrix fund range.
- Invite Mike Clarkson, RLAM to future IAC meetings to provide direct comment following his fund manager meetings.
- Review content of strategic pack and performance pack to allow IAC to answer the "so what" question. Include a summary of minutes from IPC where relevant.
- Consider adding information on funds which are tracking green on performance but have had a change to process.
- RLI to ask for an external company to review Committee structure and effectiveness at the next scheduled effectiveness review given that minutes are published externally.
- Request Co-Sec support for future IACs.

LB

### **Morningstar update**

IAC were supportive of the new reporting agreed with Morningstar. This now includes fund scorecards and access to Morningstar analysts on a regular basis and IAC were comfortable that this will ensure IAC are better informed. It was felt this provides a useful second opinion in addition to the analysis and commentary provided through Mike Clarkson's role.

LB

### **RLP Rathbone Global Alpha**

This fund outperformed in Q1 2019 but continues to underperform benchmark over 1, 3 and 5 years. In addition this fund is one of the most expensive on our range. At the February meeting Rathbone proposed a change of structure which IAC were not

comfortable with and asked RLI for clear next steps. The fund is a multi-manager fund and is currently positioned alongside a passive global equity fund from Blackrock and a lower cost active global equity fund from RLAM to offer choice to advisers and customers. The two key concerns to address are costs and performance and a proposal to consider moving the assets to sit under an internal multi-manager remit was presented. This would reduce costs significantly and provide greater transparency allowing IAC to challenge more effectively. IAC specifically asked about why a multi-manager fund structure continues to be appropriate, costs of transition and that any proposal is taken through our conflicts of interest policy. We will present further details on the proposal at the next IAC meeting.

EC

## **Performance Pack**

All data is at end March 2019.

### RLI Governed Range

All Governed Portfolios outperformed their benchmarks over the quarter with only Governed Portfolio 7 behind benchmark over 1 year. Governed Portfolios 2, 3, 6 and 9 are ahead of benchmark over 3 years to end of March 2019. Governed Portfolios 2, 3, 5, 6 and 9 are ahead of benchmark over 5 years to end of March 2019.

All five GRIPs are above benchmark over the quarter. They continue to outperform over 1, 3 and 5 years and also since launch, with all portfolios ahead of benchmark over all time periods.

### Global Managed

The fund is in line with benchmark over the quarter and slightly behind over one, three and five years.

This fund invests c. 80% in RLP unit linked funds which have underperformed their respective benchmarks. RLP American, European, Pacific and UK Equity have all experienced underperformance across 1, 3 and 5 years. Stock selection has largely been attributed to the underperformance which can be seen in the active European funds and in the UK Opportunities fund. Overseas equity can also be attributed to this underperformance, with exposure to North America the largest detractor. Given that this allocation is entirely passive, this was due to negative timing and FX effects as a result of market and FX movements after the funds valuation point.

IAC noted that the team has received more detailed performance attribution from RLAM and this will be presented at the next meeting in order to understand in more detail the impacts of valuation points.

### Property

The fund has outperformed benchmark over 1, 3 and 5 years to end of March 2019.

As at the end of March 2019, RLPPF cash holding was 14.2%. There are a number of purchases/developments in the works which would reduce this position if all were to be completed in the coming months. IAC expressed a specific desire to make cash in the fund work harder when it's not invested in property and have asked for further details on

how cash in the fund is managed. While there are a number of purchases in the pipeline, the cash inflows are currently running ahead of property purchases and the cash holding is trending upwards.

### Commodity

The Fund is underperforming over the quarter but is ahead of benchmark over 1 year to the end of March 2019. The fund was launched in June 2016 and as such lacks a longer term track record.

### Sterling Extra Yield

The fund is outperforming over 1, 3 and 5 years and finished the quarter just below benchmark.

### Global High Yield Bond

The fund is underperforming over 1, 3 and 5 years to the end of March 2019, but the RLAM OEIC is outperforming its benchmark over 1 and 5 years. The OEIC benchmark is not available on Lipper so a similar benchmark has been selected on the advice of the fund manager. Over Q1 the fund underperformed the benchmark with exposures to energy attributed to the negative relative performance.. The fund continues to retain a shorter duration than the index and has a preference for B and BB rated issues.

### Externally Managed Matrix Funds

#### Rathbone Global Alpha

The fund finished ahead of benchmark over Q1 2019, however was still behind benchmark over 1, 3 and 5 years to the end of March 2019.

Positive contributors over the year include the funds positioning in US equity markets with the Brown Advisory US Equity Growth and Edgewood Select US Select Growth funds performing particularly strongly. Contribution from the UK was also positive over the year with the Lindsell Train UK Equity fund being a particular highlight. However, both Japan and Emerging Markets positioning detracted from performance over the year. Over the longer term, the Rathbone Investment Committee is already aware of the drag on performance from the fallout from the UK referendum, and the difficulties in reducing our small and midcap exposures in the UK within a fund of funds structure. This continues to affect both the 3 and 5 year numbers.

#### Artemis UK Special Situations

Performance over the quarter has been poor, largely driven by management's value orientated stock selection, with the key detractors coming from the consumer cyclical, industrials and financials sectors. Restaurant Group and NCC Group were the main detractors, with Restaurant Group's CEO resigning suddenly and NCC suffering a number of profit warnings.

Due to the significant period and level of underperformance, IAC asked that a potential replacement fund proposal is brought to September's IAC.

### *Invesco Japan*

In recent years, the fund has had a valuation-driven approach which has resulted in overweight positions in sectors such as Auto manufacturers, Mega Banks, Real Estate and Energy. This has not been a successful strategy but mostly because there has been a significant de-rating of these sectors against any given level of fundamentals.

Due to the significant period and high level of long-term underperformance, IAC asked that a potential replacement fund proposal is brought to September's IAC.

### *Schroder Tokyo*

The fund has underperformed the benchmark year-to-date. There has been a small negative from sector allocation but most of the underperformance has been generated by stock selection. The fund's value bias has also underperformed over the year-to-date, while the overweight position in small caps also contributed to below benchmark performance.

Due to the prolonged period of underperformance, IAC asked that a potential replacement fund proposal is brought to September's IAC.

### *Schroder UK Alpha Plus*

Key individual positive contributors included underweight in British American Tobacco, emerging markets investment manager Ashmore and Vodafone. On the negative side, the main detractors included packaging business DS Smith, oil services company Wood Group. Lack of investment in AstraZeneca compared to benchmark was the biggest detractor.

Due to the period of underperformance, IAC asked that a potential replacement fund proposal is brought to September's IAC.

### *Invesco UK Growth*

Over the twelve-month period to 31 March 2019, fund performance was impacted by holdings across a range of sectors. The largest negative contribution was provided by Vodafone, which traded weakly throughout the year. The telecommunications sector was broadly weak, but Vodafone's share price was further impacted by investor concerns around the affordability of the company's guided dividend. The fund's largest overweight position, Oil & Gas, continued to support both relative and absolute performance. BP, Royal Dutch Shell and Total continued to provide strong positive returns against a backdrop of rising oil prices and supportive corporate results. The fund's holdings in Mining, notably gold miners, also supported returns over the year.

Due to the level of long-term underperformance, IAC asked that a potential replacement fund proposal is brought to September's IAC.

### *Stewart Investors Global Emerging Market Leaders*

One of the main negative contributors over the last twelve months has been Tiger Brands (South Africa: Consumer Staples) which was hit by a listeria outbreak traced to two of its manufacturing facilities. We remain confident that management and the Chairman are taking the necessary steps to address this issue and rebuild trust. Aspen Pharmacare

(South Africa: Health Care) declined as delays to the sale of Aspen's infant formula business led to subdued cashflow and higher-than-expected debt levels. The fund benefitted from strong performance by Indian tech company Tata Consultancy Services which rose on good results, rupee weakness and positive management changes across the Tata Group. Uni-President Enterprises (Taiwan: Consumer Staples) gained as it continued to show improvements in its Chinese business.

Although the fund is only triggering red for one quarter, it previously triggered at 7 of the previous 8 periods. The fund is soft closed and no longer sits in the Emerging Markets IA sector due to a 20% investment in Developed Markets. For these reasons IAC asked that a potential replacement fund proposal is brought to September's IAC.

## **Strategic Pack**

### *Governed Portfolios & Managed Strategies*

No changes were recommended to the Governed Portfolios and Managed Strategy strategic asset allocations this quarter.

All portfolios are within their target ranges for real volatility with the exception of GP3 and the Cautious Long Term Managed Strategy which remain below the lower limit. Due to the upcoming strategic asset allocation review there were no further actions proposed to the portfolios.

### *Governed Retirement Income Portfolios (GRIPs)*

No changes are recommended to the GRIPs strategic benchmark this quarter.

All portfolios remained within their target ranges on both the income risk metric and the fund risk metric. Sustainability scores have decreased marginally since last quarter, while the maximum 1yr loss numbers have increased very slightly.

### *Lifestyle Strategy Analysis*

Annuity income and real fund values for drawdown lifestyles have decreased since last quarter.

## **Tactical Analysis**

### *GPs, Managed Strategies and GRIPs*

All portfolios remain within their tactical risk budgets.

There have been three tactical changes made by the RLAM in the last quarter and the commentary below reflects their views:

- In January, we believed that equity markets had priced in a recession prematurely given strong labour market data and low real interest rates. At the same time investment sentiment indicator remained oversold. We were of the view that the recovery in stock prices had further to run and as such purchased equities, increasing our above benchmark allocation, funded out of commodities. We did this with the

outlook to sell into rallies, as strong economic activity in 2019 would probably spur a resumption of US rate hikes, ending the current business cycle.

- In February, investor sentiment returned to normal levels, rebounding from very depressed readings recorded in Q4 2018. Having purchased in market weakness at the end of 2018, we reduced our equity exposure following rallies through January, taking profits. The proceeds of which were moved into government bonds, commodities and short duration global high yield debt. We looked to see evidence of Chinese stimulus measures and a pause in the US rate hikes boosting growth before moving more positive on equities again.
- In March, investor sentiment seemed very optimistic. We continued to monitor Chinese stimulus measures and its effect on growth. As such, we continued to take profits from equity purchases made during market weakness early in the year and moved the proceeds into high yield bonds and cash.

The overall position as at end March, was overweight Equities, High Yield and Corporate Bonds; underweight Absolute Return Strategies (inc. cash), Gilts and Commodities. Neutral positions were maintained across Property and Index Linked Bonds.

#### Short Term Tactical View of the Chief Investment Officer

#### **Positioning & Activity**

- We started the quarter firmly overweight in equities, having bought equities through weakness in the last quarter, and benefitted from the sharp recovery in sentiment as investors shifted again to a 'risk on' attitude this year. This was driven by more benign interest rate rhetoric from leading central banks, including the Federal Reserve (Fed), which indicated the next hike in US interest rates could be delayed until 2020; and more positive expectations of the US-China trade talks. Having benefitted from the rebound in equity markets, we scaled back our equity holdings and took profits, but remain moderately overweight as there are early signs of growth stabilising in China.
- Within equities, the overweight holding of US equities was increased as economic growth there remains reasonably strong and the Fed's more dovish approach will help the expansion to be sustained. Our exposure to the UK ended the period close just above neutral as we believe there will ultimately be a positive resolution to Brexit. In the meantime, however, Brexit uncertainty continues to affect business investment and is now weighing on consumer confidence. We are now underweight in Japan and slightly underweight Pacific ex Japan, as these economies are struggling with the slowdown in Chinese growth. We remain overweight in emerging markets – these markets were impacted negatively by the stronger US dollar, but have performed better since the Fed's more benign interest rate guidance limited the currency's appreciation.
- We have overweight holdings of sterling investment grade corporate debt and short

duration global high yield bonds, with corresponding below benchmark allocations to UK government bonds. Interest rate hikes have been postponed because of slower global growth and, in the US, the impact of previous increases feeding through. Government bonds have adjusted to this new more dovish environment with bond yields falling. Over the coming quarters, however, we believe investment grade and high yield corporate debt are likely to outperform government bonds on a risk-adjusted basis. Fixed income exposure has a short duration bias to reduce interest rate risk.

- We have a small underweight exposure to UK property. While the positive supply/demand backdrop and rental yield cushion make the asset class relatively resilient, we feel the impact of Brexit-related uncertainty poses risks to the sector, particularly from the decrease in business investment.
- We are modestly underweight in commodities, although we reduced the scale of this underweight position as commodities started to recover with signs that global economic growth is stabilising.

### **Market Background**

- Equities rebounded as fears of slowing global growth receded; US-China trade talks seemed to progress more positively, although there is still no sign of a deal; and the US Federal Reserve (Fed) shifted its stance on interest rates, becoming far more dovish in tone and outlook. At the end of the quarter, there were early signs that the package of stimulus measures introduced by the Chinese authorities may be helping to stabilise the country's economic growth rate.
- Meanwhile, government bonds had a strong first quarter as the European Central Bank (ECB) joined the Fed in moving towards more accommodative policy, softening its guidance and surprising markets by announcing the rollover of its TLTRO bank refinancing programme. US 10-year treasury yields ended the quarter 28 basis points (bps) lower at 2.41% and German 10-year bond yields fell back into negative territory.
- The price of Brent crude oil rebounded sharply to over \$68 a barrel. Prices are still below their 2018 highs, however, so this is still effectively a 'tax cut' for consumers. Copper rose 13%, its first increase in four quarters, as commodity prices generally rose. Gold, which is traditionally regarded as a 'safe haven', rose only 1.2%.
- Sterling gained over the quarter while the uncertainty around Brexit continued, the scheduled date for the UK to leave the EU at the end of March 2019 was delayed and investors concluded that a 'no deal' Brexit was less likely.

### **TAA Performance**

- Asset allocation added to performance in Q1. We entered the quarter with a strong overweight in global equities, which rebounded sharply over the quarter, following a



supportive shift from central banks and perceived progress in the US-China trade talks. Slight underweight in commodities dampened the quarter's tactical allocation return at the margin.

- Within Fixed Income, the preference for sterling investment grade corporate bonds at the expense of conventional gilts added to performance over the quarter, as spreads narrowed.
- Muted performance contribution from the regional equity decisions in Q1 as positives from the bias towards US was offset by relative positions on Europe and Japan.

## **Outlook & Views**

- Stock markets have recovered but global economic activity remains weak. We expect China's stimulus programme to boost the world economy later in the year and this should be positive for stocks. However, investors may be too complacent in the short term and we wouldn't rule out a relapse if economic data disappoints.
- The world avoided a recession in early 2019 but risks remain for 2020. The interest rate sensitive US housing market is slowing, trade tensions remain elevated and the US yield curve is close to inverting.
- Volatility is a feature of the late stages of the business cycle. The greatest opportunities may come from being a contrarian investor, buying during panics and selling into rallies.

### *RLP Global Managed cash holdings*

IAC were pleased to see full cash look through on this fund, including the cash held within the underlying OEICs. It was noted that the data is based on economic exposures and didn't reflect cash held back for derivative positions and IAC asked to see this at the next meeting.

### *Review of customers in workplace default*

IAC receive information each quarter on the number of customers moving into drawdown, taking cash or purchasing an annuity. This quarter IAC asked if the data could be split into those under age 55 and those over age 55.

## **AOB**

IAC discussed the issues with the Woodford fund. It was noted that RLI have a strong fund due diligence process which captures information about permitted links, largest holdings and liquidity risks. It was noted RLI has no Woodford funds on its range.

IAC recognised that Colin Taylor would be leaving the Committee at the end of June and

presented him with a gift in recognition of his eight years of service. IAC thanked Colin for his attendance and input over the years and wished him all the best in the future.

## **IMPORTANT INFORMATION**

Past performance is not a guide to the future. Prices can go down as well as up. Investment returns may fluctuate and are not guaranteed so you could get back less than the amount paid in.

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June 2019

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