Watson Moore
INDEPENDENT FINANCIAL ADVISERS LIMITED

Monthly Investment Update
December 2020

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Performance Update

Global stock markets had their best month since 1987 following the news of the Coronavirus vaccine. The FTSE 100 and S&P 500 rose 12.69% and 7.45% respectively, though Gilts and Gold fell. With equities rising, our portfolios also rose between 3.49% and 9.02%.

The release of news that three vaccines have produced excellent test results, has ensured that our return to 'normal' lives will be sooner than expected. Global stock markets reacted with one of their best ever months as they anticipated a significant increase in companies' profits next year.

In addition, it is assumed that Janet Yellen will become the new US Treasury Secretary and as a result, will deliver the additional stimulus that the US economy needs. She is seen as the 'safe pair of hands' and someone who will continue the same policies as before. For stock markets, the more money that is in the economy, the better.

The vaccine news coincided with Biden winning the US presidential election (although one person doesn't agree!). While Biden is expected to raise taxes for companies, stock markets appear to be unconcerned as the potential increase in taxes will be offset by removing an unpredictable President.

Every major stock market rose significantly in November and they are all now in upward trends. This coincides with a seasonal period where stock markets generally perform well, in what is termed the 'Santa Rally'. Our trend following portfolios increased exposure to equities last month as a result.

While equity markets have moved higher, some bond asset classes and gold have had a difficult month and have fallen below trend. Long-term we could see bonds continue to move lower.

Finally, Brexit negotiations are going down to the wire as expected. This could cause some volatility in Sterling.

The performance of the portfolios over the last month, 6 months and 1 year is shown below:

Portfolio	Performance % 1 month	Performance % 6 months	Performance % 1 year
Foundation	3.49	3.95	2.55
Cautious	4.50	4.44	1.08
Balanced	5.55	5.99	1.10
Adventurous	6.73	6.25	1.47
Dynamic Equity	6.53	9.42	8.80
Income Generating	9.02	7.93	-5.37
Fourth Industrial Revolution	8.83	17.29	33.68
Retirement Investment Solution 1	4.45	5.39	2.69
Retirement Investment Solution 2	4.78	5.98	3.50
Retirement Investment Solution 3	5.09	6.53	4.24

Please note that these figures do not include the platform or Watson Moore's fees.*All figures are sourced from Financial Express to 31.10.2020.

Trend Following Signals

The table below shows whether the asset class is either in a positive trend (✓) or a negative trend (x). The portfolios will have more exposure to those asset classes in a positive trend and less (if any) to those in a negative trend. These are the main asset classes we monitor:

Asset Class	Trend Signal		Trend Signal
Global Equity	✓	Emerging Market Equity	✓
UK Equity	✓	Commodities	✓
Europe ex UK Equity	✓	UK Corporate Bonds	✓
US Equity	✓	UK Corporate Bonds (Short dated)	✓
Japan Equity	✓	UK Index Linked Bonds	x
Pacific Equity	✓	Global Bonds	✓
Gold	x	UK Gilts	x
Global Property	✓	Emerging Market Bonds	✓
Global Infrastructure	✓	Overseas Corporate Bonds	✓

Every equity market is now above trend. Gold and some bonds are now below trend.

Cautious, Balanced and Adventurous portfolios

Every equity market is now above trend and exposure increased to Pacific, European, UK, property and infrastructure equities within the Cautious and Balanced portfolio. The Adventurous portfolio already had maximum exposure to equities, but with Gold falling below trend, exposure to Gold has been removed from the Cautious and Balanced portfolios and Gold mining companies have been removed from the Adventurous portfolios. Exposure to bonds has also been reduced in the Cautious and Balanced portfolios.

Dynamic Equity portfolio

The momentum philosophy that forms the core of this portfolio attempts to invest more money in those stock markets that are experiencing the strongest growth (or the lowest losses). There were no changes made and we remain overweight US equities, gold miners, healthcare and technology. Gold miners have moved below trend, but the asset class still remains high up on the momentum scale as it has performed extremely well despite these recent losses.

Foundation portfolio

Every equity market is now above trend and exposure increased to Pacific, European, UK, property and infrastructure equities within the portfolio. Exposure was reduced to Gold, UK Gilts and Inflation linked bonds as they all fell below trend. The portfolio currently has the lowest exposure to equities out of all our portfolios and therefore is rising the slowest, albeit with a return of 3.49% last month. This portfolio will always be extremely well diversified.

Income Generating portfolio

Last month we wrote:

"There have been signs that some of the companies that were forced to cut or suspend dividend payments during the initial part of the pandemic are now ready to recommence paying them. In March, the regulator asked UK banks to suspend dividends until the end of this year. This caused a sell off in the banking sector but there are now rumours that they will be allowed to pay dividends again from the start of 2021. This has helped the banking sector to move higher. We believe that as we move into 2021 the companies that were hit the hardest due to the uncertainty surrounding their dividends, could move significantly higher as we begin to see the path towards a more normal economic future."

November saw the portfolio grow significantly and it was indeed our best performing portfolio.

Fourth Industrial Revolution portfolio

The Herald Investment Trust (invests in small UK technology companies) and the iShares Automation & Robotics fund were once again our best performing funds growing 10.07% and 11.93% respectively. We increased exposure to the Herald Investment Trust to 7.5% and initiated a new position in the iShares Global Clean Energy fund. We want to build up our position in clean energy due to the fact that Biden has signalled his intention to increase the amount of solar and wind power generated in the US. This is a major change away from Trump's policies. Surprisingly, despite the good news surrounding the vaccines, healthcare and biotech were somewhat laggards in the portfolio.

Retirement Investment Solutions

Exposure to equities was increased to the maximum amount and this benefitted the Retirement Investment Solutions as all 3 grew significantly. Exposure to Gold and bonds has been reduced somewhat though. The Retirement Investment Solutions all have exposure to the Dynamic Equity portfolio, and this has helped boost returns.

Summary of Portfolios

Stock markets surged higher in November on news that the vaccine trials have been much better than expected. Delivering a vaccine within ten months is an incredible achievement. The roll out will take place next year and stock markets moved higher due to the fact that they are not only expecting the global economy to open up, but for there to be a release of the pent-up demand from consumers who have had to save money due to the fact that they couldn't spend it. This is so different to a normal recession in which consumers do not have the money to spend. The economic growth rate in 2021 could therefore be extremely high.

The good news was compounded by probably the best US election result possible. Trump and his unpredictability has been removed, but the Republicans have not lost the Senate. This means that Biden will find it difficult to enact any radical changes and therefore the status quo of a more business friendly environment will remain. However, global trade relations will almost certainly improve under Biden, which can only be good for stock markets.

As a result of this, our portfolios benefitted significantly, and the trend following portfolios now have the maximum amount invested in equities. They will hopefully benefit from a possible Santa Rally.

Asset Class Review

This section will give you an insight into our current thinking and we have included some charts that we believe look interesting. The good news about the potential vaccine has ensured that every main stock market we monitor is above trend. This month we look at a few stock markets that have jumped higher on the news.

FTSE 250 – was moving sideways since June but jumped higher on the news

In addition to everything else going on, Brexit has been weighing heavily on the performance of UK stock markets, especially for the smaller companies that make up the FTSE 250 index. You can clearly see that the November jump has broken the sideways range which is very positive:

Europe – a downtrend has just been reversed

The Euro Stoxx 50 had actually started to fall again quite significantly. The vaccine news clearly has reasserted a new upward trend:

Japan – a big jump higher

Japan had recovered most of the losses seen in February and March but became stuck below 24,000. You can clearly see how well the vaccine news has been taken by companies in Japan:

Emerging Markets - continuing the upward trend

Emerging markets had been on a strong upward trend since the end of March, but again had failed to break above the levels seen earlier in the year. The market has now jumped above this level and reasserted a strong upward trend:

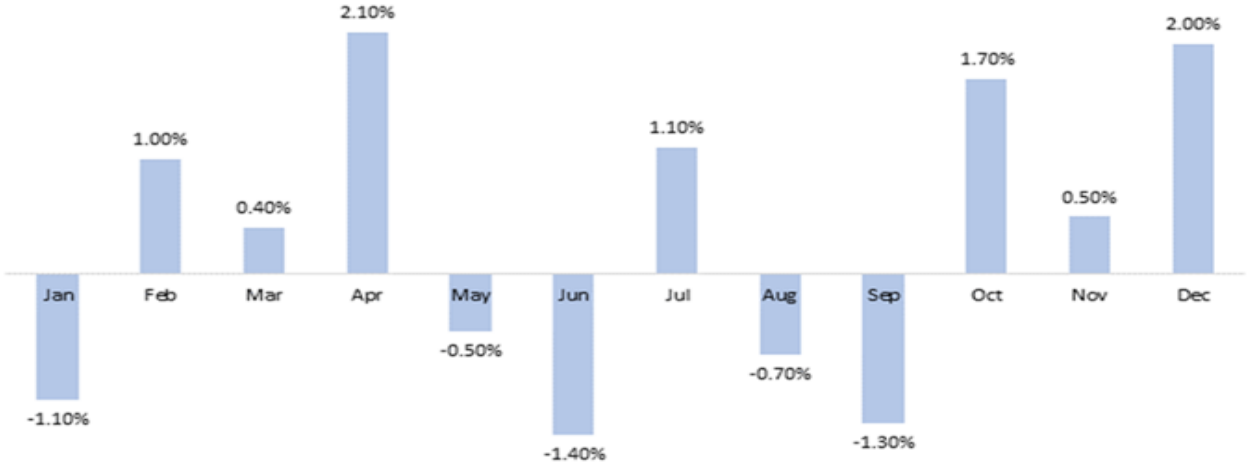
In Summary

The news that the vaccines being developed are showing great results has been taken extremely well by stock markets. They believe that the global economy will open up much sooner than anticipated and with all the new money that has been printed, will result in a very strong recovery. They have momentum behind them as we go into what is usually a strong period for stock markets and the 'Santa Rally'.

The Santa Rally

As the name implies, the 'Santa Rally' is the term for when stock markets post positive results in the run up to Christmas and the New Year. UK investors, for instance, have come to expect the FTSE 100 to achieve a good return in December. Over the last 20 years, the FTSE made an average gain of 2.0% in the last month of the year and has only fallen 3 times. The chart below shows the average monthly return for each calendar month from the FTSE 100, and you can see the effects of the Santa Rally:

The Average Calendar Month returns of the FTSE 100 over the last 20 years



Quite why this phenomenon should occur is unclear and in truth, there are probably several factors behind each individual rally. But a few of the major theories on why markets rally in December include:

- Seasonal goodwill among investors, who are more willing to buy around Christmas.
- Markets rising on lower volumes over the holiday period.
- Fund managers rebalancing their portfolios before the end of the year.
- People investing their Christmas bonuses.

It isn't just the FTSE 100 that has benefited from a Santa Rally, as most global stock markets have similar seasonal statistics. Interestingly, there is no agreement about when the Santa Rally period really starts, with different sources offering conflicting answers. Does it last the whole of December? Or just the week before Christmas? Or something in between? One source, however, found that the biggest rises in indices typically occur from the 14th – 16th December.

While you can get a broad idea of when a Santa rally might start by looking at historical data, each year's Santa Rally will be different. It might start early, it might start late, or it might not start at all. You can only know for sure if a Santa Rally has taken place once it is already over. This year we have seen stock markets break higher in November and post some of their strongest gains. If the momentum continues then December could be a good end to a turbulent year.

Conversely, if you look at the returns between May and September you can see that they are mainly negative and this leads to the adage 'sell in May, come back St Ledgers day'.

Whatever the reason, and whenever it occurs, we know that historically December is a great time for investing money and it just leaves us to say 'Happy Christmas!'.

Final Comment

The main reasons why stock markets are rising are:

- Removing Trump from power, but having the Republicans remain in control of the Senate is the best US election result possible. It means the unpredictability of Trump is no longer a risk and the business unfriendly ideas that Biden would enact should be watered down.
- A roll-out of vaccinations should begin shortly and this will help reopen the global economy.
- We are likely to see the continuation of monetary stimulus in the US with the forthcoming appointment of Janet Yellen as Treasury Secretary.
- The savings rate has been extremely high during lockdown for those that have remained employed, so there is a catalyst for a surge in spending in the economy.
- Those companies that have survived this year are likely to have implemented cost savings and may find less competition due to some companies not surviving. Therefore, profitability for some companies may increase significantly.
- Interest rates are likely to remain low for a long time in order to help try and increase inflation a little.

All of the above have helped move every main global stock market above trend and this momentum looks set to continue.

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