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The Federation of European Independent Financial Advisers

Post–game analysis

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Words cost money and may even cost you clients

By Edden Kift from the PortfolioMetrix business development team.

It is not difficult to quantify the cost of producing a document such as a financial plan or a client review template. The cost of creating regular and relevant client communication is similarly quantifiable. In contrast, it is near impossible to calculate the cost of people not reading what you produce. If not done correctly it may create more questions than answers or, perhaps even worse, it may alienate the audience it aims to address. No business can afford to waste valuable resources producing documents that are dense, difficult to read or irrelevant. Consider too that the language used is of significant importance and value: plain language builds trust and contributes positively to a brand.

It is highly likely that people today read more but digest less. The challenge is being able to cope with the amount and frequency of information that reaches us via our inboxes, smartphones and various other forms of media. We consume information faster and demand easy to read text in bite-sized chunks. Being fussy about content means we are likely to skip to something new very quickly. Financial advisers are competing for the attention of their clients. Considering how they communicate may very well increase their chances of being heard and keeping clients happy.

Plain language is communication an audience can understand the first time they read it or hear it. Below is a simple way of testing whether a financial plan or a newsletter or even an email conforms to being written in plain language:

P	Is the **point** of the document / communication clear?
L	**Layer** and group similar content and use headings.
A	Use **accessible** language that is easy to read for the consumer.
I	Make it **interesting** by using charts and diagrams to explain complex concepts.
N	Ensure the document / communication is set out in a way that is easy to **navigate**.

The use of plain language in practice is perhaps best illustrated by way of an example. Below is an extract from an insurance contract:

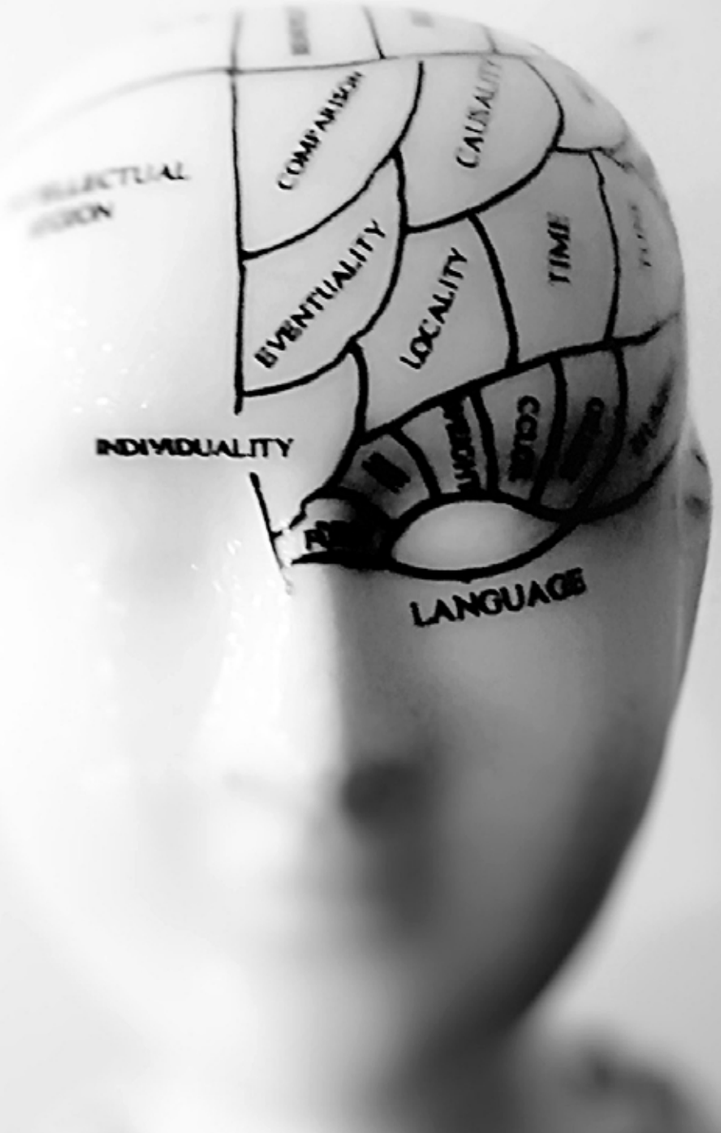
If you fail to comply with your duty of disclosure and we would not have entered into the contract on any terms if the failure had not occurred, we may void the contract within three years of entering into it. If your non- disclosure is fraudulent, we may void the contract at any time. Where we are entitled to void a contract of life insurance we may, within three years of entering into it, elect not to void it but to reduce the sum that you have been insured for in accordance with a formula that takes into account the premium that would have been payable if you had disclosed all relevant matters to us.

The identical message could perhaps have been more simply communicated as follows:

If you don't tell us about something that would have meant we would not have given you insurance, we may, within three years:

1. *cancel the contract or*
2. *reduce the sum for which you have been insured*

If what you don't disclose is fraudulent, we may cancel the contract at any time.



Communicating in plain language is an effective way to enable clients to find what they need to or what you want them to read, understand what they find and act appropriately on that understanding.

Arguably the highest measure of success is what a client may or may not do as a result of what was communicated. Furthermore, a Princeton University study conducted in 2005 concluded that writers who use long words needlessly and choose complicated font styles are seen as less intelligent than those who use basic vocabulary and plain text.

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Editorial Comment

Avoiding the B word!

Yes, I am now officially fed up with being asked about Brexit! Understandably, it is a subject that pervades much of life in the UK, particularly in London.

Outside of the major economic issues that arise from the UK/EU split, the most pertinent ones for our industry tend to revolve around the loss of passporting – and, specifically for the advisory sector, the loss of a simple means to keep advising clients "cross-border".

The FCA's TPR has potentially solved the immediate problem for EU-based advisers who want to continue operating in the UK.

The EU has not reciprocated – but we believe that we have a couple of solutions for UK advisers. We are doing the final "road testing" on these and will let you know ASAP if they are workable.

Regards

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Post-game analysis: Multi-Asset Core Income part 1

Nick Watson, Fund Manager for the UK-based multi-asset team, provides his 'match report' for Janus Henderson's Multi-Asset Core Income range in 2018. In this article, he looks at the divergent market forces that drove performance.

2018: a game of two halves

We entered 2018 with building concerns about markets. The irresistible influence of quantitative easing and a multi-year period of 'Goldilocks' economic conditions had pushed returns, markets, valuations and investor levels of bullishness to very elevated levels.

This translated into an outlook for lower returns and more volatility as markets came to terms with the fact that the tidal wave of quantitative easing was finite and due to end in December 2018, while politics and global trade also offered a potentially bumpy ride.

So how did 2018 actually play out? Well, to continue the already stretched sporting cliché, 2018 was very much a game of two halves.

First half: a choppy start but beta stars

January and February started off in volatile fashion as markets sharply corrected following a parabolic rally at the end of 2017 and a deluge of retail money chasing returns at its end. Positive inflation data in the US spooked bond and equity markets as investors feared a sharp acceleration in the pace of interest rate rises.

However, this fear of rising prices did not persist and markets swiftly resumed their steady march upwards. Nowhere demonstrated this better than the US equity market, which itself was led by an increasingly narrow and expensive sample of technology companies.

High-quality companies with steady earnings streams and a history of distributing profits to shareholders were completely ignored in favour of high growth startup companies. Income and diversification were sidelined, and while they delivered positive risk-adjusted returns, were ignored in favour of expensive and volatile 'rocket fuel' stocks.

So our expectation of lower returns and more volatility was hinted at by the market in January, but then fell by the wayside following the resurgence in US equity beta.

Second half: the market strikes back

Global equity markets peaked quickly in September, followed by a sharp reversal from all-time highs. An eruption in protectionist rhetoric from US President Trump spooked growth fears, while economic data broadly began to soften and the impact of pro-cyclical fiscal expansion in the US wore off.

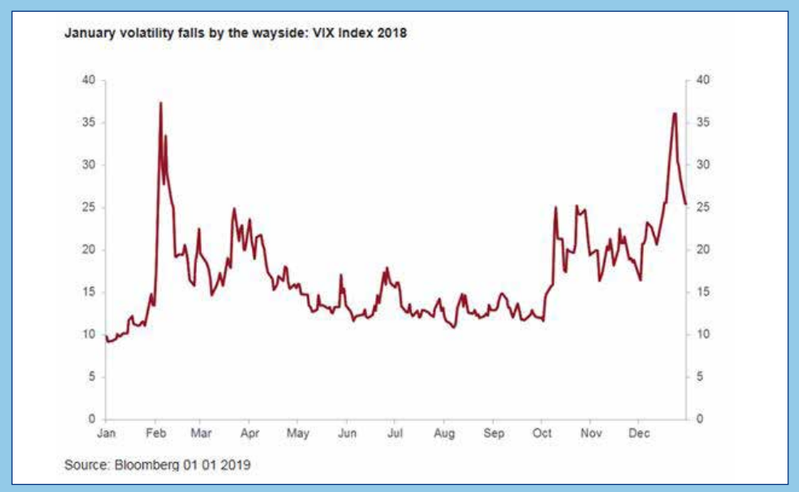
This market dynamic was the polar opposite of the first half of the year, as the market leaders reversed direction and gave back much of their gains before accelerating into negative territory amid the worst December for US equities since 1931.

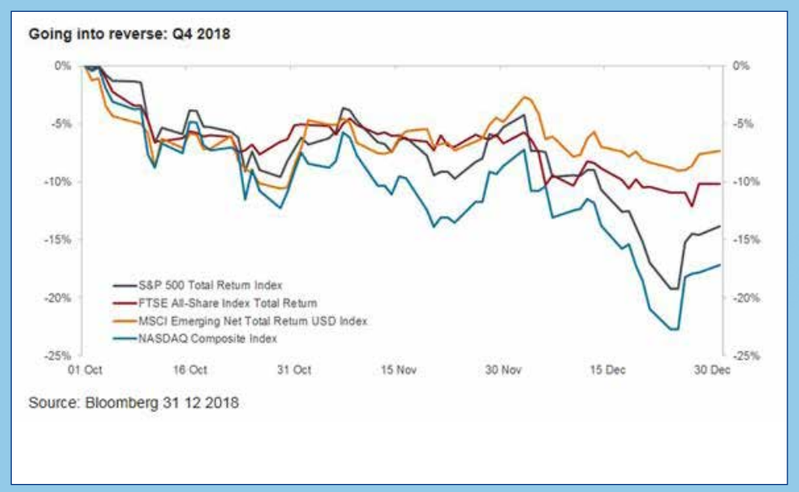
In this environment, high quality income-paying companies offered some protection against these drawdowns, with some well-known companies, such as Unilever, delivering a positive absolute performance.

Corporate bonds sold off after a fabulous multi-year period of falling yields and tightening spreads. More defensive active strategies held up well while government bonds protected through this 'risk off' turbulence.

Diversification worked, in contrast to the first half of the year, when the benefits of improved risk-adjusted returns were ignored in favour of chasing beta. The natural blend of equities and fixed income dampened volatility and reduced drawdowns while alternative asset classes, such as infrastructure and property, delivered relatively good, uncorrelated returns and income streams as markets weakened around them.

For information on our Multi-Asset Core Income range contact **Richard Turner – Richard.Turner@JanusHenderson.com** or tel: **+44 (0)207 818 5735**.





Platforms spreading to Europe

The thoughts of Novia Global.

Platforms have become an integral part of the UK advisory space with nearly all Independent Financial Advisory (IFA) firms using at least one or more platforms to facilitate their client's investments. Platforms have led, amongst many other things, to increased choice for advisers, reduced cost for clients and scalability for IFA firms looking to grow their client base.

The UK has taken its lead from the Australian market where platforms have been around for 20 or so years and the market has undergone a period of consolidation, primarily involving insurance companies with all the independent brands still going strong. What is then perhaps surprising is the relatively slow pace to date which platforms have emerged in the European space.

It is quite evident that a fragmented, commission driven environment seems to be the 'norm', with clients regularly experiencing up front commissions extending to around and upwards of 5% in many cases, which coupled with product kick-backs from certain bank traded products, and exit fees, can sometimes cause the clients portfolio performance overall to become trivial – not the desired outcome for a pension pot!

With European regulation such as MIFID II driving change and pushing hard for transparency and client protection across all its European members, the anticipation is that IFA firms using offshore bond providers or insurance companies to invest client's monies will eventually become a thing of the past. The expectation is that more financial products are likely to soon come into scope and under the scrutiny of the EU regulation as practices detrimental to the client become exposed.

Clearly, in some segments, the European financial advisory environment outside of the UK is not currently working in the interests of its consumers, contrary to what MIFID regulation is aiming to achieve. What is evident however is that a number of firms are anticipating that their business models need to adapt from product fee commission driven business, to ongoing client charging.

The UK regulatory environment banned advisory remuneration from product providers to advisers with the introduction and evolution of the Retail Distribution Review (RDR) in late 2012. This has led to a much more competitive space where clients have ultimately benefitted from a much more price sensitive, transparent market place where clients can have the confidence the system is not 'playing them' – it is playing for them. The expectation and view is that European firms are beginning to follow the UK's lead, anticipating MIFID II clamping down on previous commission heavy practices. This is where platforms come in.

Platforms offer a transparent way in which clients' money can be easily invested into the market, offering IFA firms the option to charge ongoing fees for the services they provide their clients. Firms such as Novia Global offer European and Global IFA's access to an FCA regulated platform, coupled with market-leading Australian technology and custody provided by a large blue chip bank.

In addition to this a paperless application process with the ability to invest in a range of currency options (GBP, USD, EUR, CHF, AUD, HKD) and the ability to FX clients' money for an institutional cost of 0.07% at the click of a button. These options along with access to over 5000+ assets gives rise to a compelling proposition for IFA's. For the IFA's clients, the benefits are greater. Access to online, real-time valuations available 24/7 allows uninterrupted access for clients globally, where previously it may have been unavailable to them without requesting directly from the provider. Platforms seem to be the future of the adviser led European space – a case of watch this space!

For further information contact **Chris Skelhorn – Chris.Skelhorn@novia-global.com** or tel: **+44 (0)7525 767 290**.

New Malta pension rules for personal retirement schemes

Following much consultation, Malta has released its new pension rules issued on 7th January 2019. The new rules pick up many industry concerns and help Malta move some way further from an occupational to a personal pensions framework and in particular for the member to appoint a DFM or other adviser with the requisite permissions.

Schemes are administered by Retirement Scheme Administrators (RSAs) and can either appoint a discretionary manager for the whole scheme (*non-member directed*) or can be established solely as a *member directed* scheme. Schemes cannot be both. There is a welcome general focus on transparency and fee disclosure and a clarification on many points which had previously caused concern. In particular the removal of the requirement of the mandatory separation of custody and investment management functions at member level is very useful for users of platforms/insurers.

This article only deals with 'member directed' schemes.

For advisers, the key changes are:

- Schemes can be 'member directed'. This means that a member can either appoint an investment adviser to advise the member on the choice of investments, and/or a discretionary investment manager. There is also an ability for a member to be classified as a 'professional member', though for most clients the bar is too high (two of (i) works or has worked in the financial services sector for at least three years in the last ten in a professional position which requires *knowledge of the transactions envisaged* [i.e. the specific transactions], (ii) the member's account exceeds €500,000 (iii) has carried out transactions, in significant size, on the relevant market at an *average frequency of 10 per quarter over the previous four quarters).*
- Investment restrictions (diversification requirements) are now only applicable at the member level and the investment policy of the Scheme is to be applied at the level of the member account, taking into account the risk profile of the member (there is transitional relief so that the restrictions only apply once there is a movement within the member's pension account or if any new investments are entered into).
- The member is required to receive full disclosure of all costs payable under the terms of any investment and any commissions payable to any investment adviser.
- All assets are to be ring-fenced from the assets of other members
- Unless a member requests to be classified as a 'professional member', a member may only invest in investments which can be classified as suitable for a retail member.
- The responsibility of the RSA in assessing the investments chosen is limited to carrying out due diligence on the proposed investment to satisfy itself on reasonable grounds that the investment can be classified as suitable for a retail member.
- The RSA must provide the member annually with at least the following information: underlying investments and their value, contributions received and benefits paid, name of investment manager or investment adviser, all applicable charges, commissions and fees incurred by the member and the availability, if any, of online access.
- Allow the member a 30 day 'cooling off' period.

For the RSA, as regards the appointment of IFAs, the RSA must:

- Carry out due diligence on each adviser and approve each one.
- Ensure that the IFA is appropriately licensed to provide investment or insurance advice in the EU or in an equivalent jurisdiction, and to monitor on an ongoing basis.
- Enter into an agreement with the investment adviser on behalf of the member setting out the roles/responsibilities of the persons.
- Ensure member receives a Fee Disclosure Sheet.

QROPS

In respect of the transfer of UK tax relieved funds, Members can take benefits 'in a manner consistent with those provided for under UK Rules provided for under UK Authorised Member payments for pension income under UK legislation'. Thus flexi-access is available to Malta QROPS in respect of tax-relieved transfer funds. If flexi-access is taken, our understanding is that under Maltese law, the first 30% is treated as a tax free lump sum with any balance being treated as a pension income payment and therefore subject to Maltese withholding tax @ 35% subject to any DTA relief.

For further information contact **Simon Ferbrache – Simon.Ferbrache@Bourse-Malta.com** or tel: **+356 2732 9208**.

How a widely used industrial metal takes the global economy's pulse

Julian Chillingworth, Chief Investment Officer, Rathbones.

Want to measure the pulse of the global economy? Ask Dr Copper, or so the adage goes. Copper is all around us. You need it to build a house, a car and a hairdryer. The red metal is even one of the most intensively used raw materials in the green energy revolution — more electrical motors, more battery packs (but fewer internal combustion engines) means more copper wiring. So demand for copper ebbs and flows with the ups and downs of the business cycle.

An expanding economy means people are building more houses, exporting new cars, buying more hairdryers, and therefore using more copper. In fact, as a crucial, core component of many products, it is often ordered by manufacturers well before the final product comes out of the assembly line. That's why a decrease in the demand for copper can provide an early indication of weakness in global activity.

A more timely prognosis?

Data confirming economic activity is generally only available with a considerable time lag. It can take at least six weeks for the first, error-prone estimate of quarterly global domestic product (GDP). Copper is bought and sold so often that its price changes by the second. This instantaneous pricing in response to changes in supply and demand is thought to give a much timelier prognosis on the health of the global economy.

What is Dr Copper telling us at the moment? And is he really qualified, or something of a "quack"?

The price of copper fell by about 15% in 2018. However, the plunge occurred entirely between June and August. It rose by about 5% over the final three months of the year, despite fears about slowing global growth riling most financial assets, and it is still 4% higher than it was 18 months ago. Copper prices are volatile and using a simple statistic, such as the annual change, would give many false signals of a contraction in economic activity. Copper prices also respond to factors other than demand and supply.

A recent study by the Bank of England found that a predictive model based on quarterly changes in industrial metals prices and the previous quarter's GDP growth did a better job at predicting next quarter's GDP growth than a model that used last quarter's GDP growth alone. But only just. That said, metal prices did predict the surprise increase in global GDP growth in early 2016. Few forecasters at the time expected a rise in global growth.

Ask Copper Yi sheng

Back then, forecasters' pessimism in part focused on China, which accounts for 50% of global copper demand. In 2017, China completed 77 of the world's 144 new supertall buildings (over 200 metres high). By comparison, there are only 113 buildings in New York City's current skyline in that league. Dr Copper is arguably more Copper Yi sheng.

In fact, we note a very strong correlation between the price of copper and our 'nowcast' of Chinese GDP growth over the past few years. Our 'nowcast' uses data less susceptible to error and manipulation to calibrate a more accurate gauge of activity than the official GDP numbers.

It currently suggests growth is actually close to the official figures, although that certainly wasn't the case in 2015 and 2016. Interestingly, we find the strongest correlation when we 'lag' our activity indicator by six months. In other words, the price of copper seems to respond to Chinese growth with a six-month delay.

Perhaps we shouldn't rely too much on Dr Copper's reputation for giving us an early diagnosis. High inventories are weighing on industrial output, and export growth has lost momentum, but the latest set of figures reported a modest improvement in spending elsewhere. Tension between America and China had started to thaw as 2018 drew to a close, but we don't believe the trade war is over and remain vigilant.

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Definitely interesting

GWMS are delighted to partner with Levendi Investment Management in the distribution of Levendi Thornbridge Defined Return Fund.

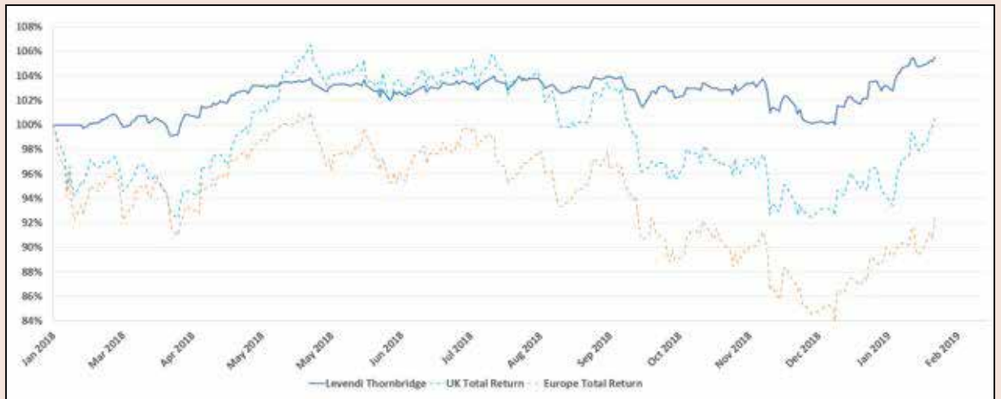
The Levendi Thornbridge Defined Return Fund offer the prospect of good returns with a degree of protection for lower risk clients. It was one of only a few funds to end 2018 in positive territory and has added more than 5% this year. David Stuff of Levendi Investment Management looks back on the way that the fund has performed and looks forward to explain why this is a strategy that should continue to offer an attractive risk/return profile.

2018 was a train-wreck in terms of performance for most funds. Equities performed horribly. Bond funds turned down as they started to feel the impact of higher yields. Most of the alternative/absolute return funds were below water despite offering the prospect of positive returns in most market conditions. Amongst this carnage, there were a few funds that stood out by offering a positive return. The Levendi Thornbridge Defined Return Fund was one of these.

What's particularly remarkable about this is that this is a fund that offers investors defensive equity exposure rather than a fund that invests in a niche market or one that aims to profit when markets fall. This is a daily traded retail UCITS fund that has exposure to broad equity market indices and which has been designed to be a core holding for lower risk clients.

The fund aims to generate a return of about 6% and to keep volatility below 10%. On a day to day basis the fund has some, about 30%, exposure to equity markets, so will go up and down as markets move. However, one promise that has been born out immediately is that it expects to be able to generate a positive return even when markets are flat or falling. The management team did not expect this to be tested so quickly, but are happy to be able to demonstrate the defensive benefits of the fund.

The chart above shows the performance of the fund since it was launched at the end of January 2018 to the middle of February this year against the total return of both the FTSE 100 and Eurostoxx 50 indices. The defensive benefits are clearly visible in the way that the fund held onto value through the fourth quarter to end the year just about unchanged while markets suffered double digit falls. Since then, the value of the fund has jumped with the market and is now over 5% up. Through this period the volatility of the fund has been below 6% and drawdowns have been minimal.



Source; Levendi, Bloomberg

	Levendi	UK Total Return	Europe Total Return
Since Inception	5.48%	0.46%	-7.61%
Last Month	3.28%	5.3%	5.86%

So what's the secret source of this fund? The fund invests in equity linked securities or defined return investments. These are an institutional form of structured product. They offer a potential return of between 7% and 9% but where there is a risk both to the return and to the maturity value. The sort of investment held by the fund are very defensive. Typically, the return will be paid out even if the level of the underlying markets falls by up to 40% and there would need to be a fall of more than 50% before the maturity value of any of the assets was reduced. To put this in context, this would take the FTSE and Eurostoxx below the lows of the financial crisis and the dot-com crash.

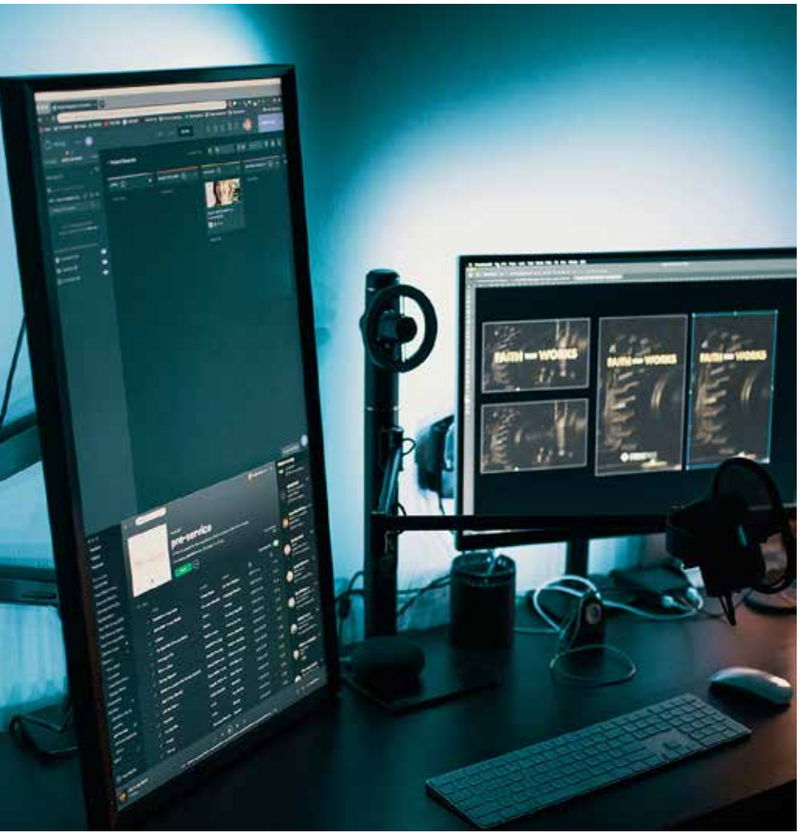
The retail form of defined return investments, structured products, have come in for a lot of bad press recently. This is not surprising. These retail products have been weighed down with excessive fees and have had to take on significant risks to offer the prospects of high enough returns to lure investors. It's important to realise that there is a massive gulf between the sort of assets held by the fund and retail structured products that are offered through advisers.

The fund deals directly with the issuing banks, there are no fees and charges. The investments are designed to be very cautious, to maximise the chance of a positive return and to minimise the chance and scale of losses. The team at Levendi come from top tier investment banks (J.P. Morgan, Morgan Stanley, Barclays) and know this business inside out.

Looking forward, the team at Levendi think that the fund is an attractive asset for lower risk clients. The management team have put their money where their mouth is and are both fully invested in the fund themselves. As David Stuff says, "Equity markets look fully valued as the global economy starts to slow down, bonds are unattractive given that yields are probably set to increase, and absolute return funds have largely failed to deliver.

The Levendi Fund uses a simple, transparent strategy that has every prospect of continuing to deliver the returns we expect. 2018 was a tough year to launch, but we were immediately able to demonstrate the defensive nature of the fund. The key for us is to keep things simple, focus on preserving value, strip out costs and expenses and try to maximise the chance of a positive return"

For more information on the Levendi Thornbridge Defined Return Fund, please contact your GWMS Regional Sales Partner or call their **Head Office** on tel: **+44 (0)1525 861 983**.



Quality over quantity

In an environment where asset classes and markets don't always behave as they should, active management becomes more important than ever. Danny Knight, head of investment directors at Quilter Investors, a sister company of Old Mutual International explains the benefits of active asset allocation and why choosing to take action in volatile markets can deliver greater benefits.

Since the start of the financial crisis in 2008 investors have been experiencing a 'new normal' of investing. The unprecedented quantitative easing that was unleashed by central banks around the world has seen previous investment correlations falter as most asset prices rose in unison, with equity markets such as the US S&P 500 index, racing towards a record bull run.

But as central banks have started tightening policy and interest rates rise, it is clear the environment will continue to change as we move further through the cycle, and investors need to be prepared to adapt to these changes.

Research from Deutsche Bank shows that 2018 was one of the worst years on record with roughly 90% of a broad spectrum of assets having delivered a negative total return in US dollar terms.

As volatility increases and markets struggle, there is a clear case that active management and broader diversification can be beneficial for investors.

The theory of diversification is clearly sound – holding a spread of assets so if one falls, the others offset the losses – but an issue some investors have with these types of solutions, is the cost, especially compared with the much cheaper passive option. But this is comparing apples with oranges.

Passive funds have their place, and many are used within multi-asset portfolios to provide certain types of exposure, but the cost is low because there is no control over what they invest in. There is no conscious decision-making about the underlying value of stocks or where new opportunities might arise. They track whatever index they are meant to, and follow that path no matter the direction meaning that investors are effectively on 'auto-pilot'. Meanwhile, with an active, multi-asset solution, the most important benefit is the management of a portfolio by an experienced manager.

Active managers have a vast opportunity set outside of the large-cap stocks that tend to dominate traditional passive investments. These index trackers are exposed to an 'obesity problem', where for example in the US the top 10 companies in the S&P 500 index account for 21% of the total, while the top 10 stocks in the FTSE All-Share account for 37.08% of the total on a market cap weighted basis. Active management can help mitigate this structural bias and prevent investor outcomes being dependent on a small number of positions.

Therefore focusing purely on the cost of investment management is not necessarily the most effective method of attaining the best value. Passive will always appear better on headline fees by themselves, but active management represents the potential added value that is contributed by managers – value that clients would not receive if they sit and hold an index.

That value is also provided over an extended period, and not merely a quarterly basis. Over a longer period, active management can take advantage of opportunities as they arise, such as adding risk following a drawdown, or providing downside defence in a period of strong growth. Passively holding an index negates this opportunity.

However, an active, multi-asset portfolio is very much a sum of its parts, and the behind the scenes work that creates the high quality end product should not be discounted. There are numerous components that are integral to the end strategy, this includes the time taken to source the best managers and asset classes in different areas, including in-depth research on the management style, costs, portfolios, due diligence, investment process and philosophy to name just a few.

Markets don't always go up, and when they slip they often present opportunities to exploit. That's why active management can be a sensible method of guiding investors through all scenarios in an increasingly complex financial world.

The views expressed in this article are those of our sister company, Quilter Investors and not of Old Mutual Isle of Man or Old Mutual International Ireland, and are subject to change without notice.

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Why time is the new currency

In a world in which fees are under ever more scrutiny, both advisers and fund platforms are increasingly looking at ways to lower costs. Managing Director of Praemium Asia, Dylan Navra, says one way of doing this is by taking your business fully digital.

In a recent poll which asked what clients really value from their financial advisers, one of the leading answers, by some distance, was relationship management. Navra believes in almost all cases, the administrative work to onboard and service a client is what takes up the bulk of an adviser's time.

This is because many advisers across the globe, still operate paper-based review and implementation processes.

"The job of the adviser is absolutely the relationship with clients, delivering a good and efficient service, but the administrative and compliance burden is a long process of ensuring that suitable advice is delivered in a coherent and transparent way. All the application forms and AML requirements are collated, photocopied, stored online, which is thereafter sent to the platforms and fund providers, who in turn have to manually input all these things into their systems," he says.

The problem with such a process, says Navra, is that it can lead to unintentional human errors, which he says a digital process would remove.

"The major benefit with going digital is what I call the 'input once, input nonce' concept," he says. "This basically means you only ever input something once, to the point where the data transfers from the investor to the adviser, to the back office, and then to the providers, without there being a need for administrators to re-enter the same data twice. This also lowers the risk to create mistakes."

In addition to streamlining the entire process, Navra says the end result would be the delivery of a much better experience for everyone involved; namely the investor, the adviser and the provider.

"At Praemium our argument is that time is the new currency," he says. "If you have more time as an adviser; then you can spend that time with your clients, delivering the service that matters and lowering costs. Less effort of manual work with fewer mistakes in a process means less time spent correcting those mistakes.

"We know that in both the advice and platform market there is a squeeze on fees, and if we are going to lower fees we have to lower our costs. The way to lower all of our administrative costs is to be digital and paperless."

In addition to increasing efficiency, Navra says going digital is also positive from a compliance perspective.

"In a digital workflow you are ensuring the work is done in a very specific way, which ensures people don't accidentally do the wrong thing," he says. "No-one goes out of their way to do the wrong thing, but when you are doing it digitally you are following a robust, compliance-approved process and it is very hard to step off the correct path.

"In addition to delivering a good experience, it means you are creating a strong audit trail. So, in terms of preventing human errors, embracing digital working practices is very much about ensuring people don't enter the wrong things which can cause delays and/or potential financial risk."

With this in mind, Navra says much of what Praemium aims to deliver in 2019 is a fully paperless process, from the first engagement of a prospect, all the way through to the digital opening of accounts on platform. "This process will be in the form of digital fact-finds, the online storage and sharing of documents and the pre-population of forms", he adds.

"The idea of living in a digital world is one which strongly resonates within our industry," he says. "The amount of administrative paperwork that goes into engaging with clients is consistently one of the top bug-bears for advisers across the globe, so we are looking at doing the heavy-lifting for advisers so that they carry out the whole advice process in a more scalable and progressive way."

For further information contact **Ben Lester – ben.lester@praemium.com** or tel: **+44 (0) 207 562 2475**.

2019: the year of sustainable investing?

Olivia Woodhead, LGT Vestra.

Every investment has an 'impact'. Many of us have been guilty of ignoring the repercussions of where we have chosen to invest and focused on financial return. However, what if your investments could generate competitive financial returns and improve the health of our planet and wellbeing of the global community?

Once synonymous with negatively screening for 'sins stocks' i.e. tobacco, alcohol, adult entertainment, armaments and gambling, investing with an awareness of global challenges is gaining newfound popularity. Sustainable investing now allows investors to align their investments with personal values and prioritise environmental, social and governance (ESG) factors and achieve a financial return that is comparable to traditional investments. The sustainable investment market is almost $23 trillion globally with around half of all assets managed in Europe and a third in the US. Staggeringly, the growth of ESG assets in the US is up over 200% over the past decade.[1]

The growing consensus is that a strong performance across ESG metrics can be a representation of operational excellence and enhanced business performance. Companies that actively tackle issues such as resource waste and working conditions for employees, have translated these ESG returns into financial ones. During recessions, an ESG focus can enhance performance as good governance can result in lower corporate risk. When one compares traditional equity indices to the MSCI ESG-focused alternatives since 2012, annualised returns for ESG indices have matched or indeed exceeded their counterparts.[2] Sustainable investing can give investors an edge to mitigate risk and in some cases deliver outstanding long-term returns.[3]

Responsible and sustainable investing is not a new phenomenon, but it has traditionally been a niche part of the market; 2019 may be the year where that changes. Last year, the UK Government published the report 'Growing a Culture of Social Impact Investing in the UK'.[4] The report outlines key recommendations to help encourage investing that has a positive impact on society. Whilst the report focuses on a small aspect of the sustainable market, it signifies the wider change in public attitudes to investments and shows the Government's commitment to supporting the market.[5]

Fixed Income ESG product innovation is also prevalent. Bloomberg has reported that it expects the issuance of Green Bonds in 2018 to increase more than 60% on 2017 from $155 billion to $250 billion. When compared to the world's total bond market of nearly $100 trillion this seems inconsequential, but issuance growth in 2017 across all categories remains encouraging.[6]

Long-term thinking is a critical part of ESG and sustainable investing. The United Nations Sustainable Development Goals (SDGs) provide a useful framework for investments that aim to make a positive impact whilst delivering financial returns.[7] The 17 SDGs were adopted in 2016 by all 193 U.N. member states and comprehensively detail targets and tangible indicators of impact.[8] They address global challenges such as climate change, education and healthcare. The U.N. estimates that it will require between $5 trillion and $7 trillion a year to achieve the goals by 2030.[9] In developing countries alone, the annual investment gap in major SDG sectors is estimated at $2.5 trillion. With current levels of private sector participation, there will be a shortfall of $1.6 trillion to be covered by the public sector.[10]

Clearly, a significant acceleration of private investment in SDG sectors is required to aid the U.N. in meeting its targets. The long-term framework that the SDGs provide has encouraged us at LGT Vestra to engage with investments in our Sustainable Model Portfolio Service, that not only have a deeply engrained ESG ethos or impact initiative, but that also encourage progress by supporting companies that show a measurable engagement with the SDGs.

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Why now is a good time to be invested

Ben Seager-Scott, Chief Investment Strategist at Tilney, discusses why now may be as good a time as any to be invested in the stock market.

Many people are understandably panicking about their investments at the moment. Political uncertainty and stock market volatility have both hit headlines consistently over the last few years, and we have heard from many clients who are concerned about committing their hard-earned money to the stock market at the moment. However, at Tilney we believe now is as good a time as any to be invested in the stock market. In this article we explain why.

Investing is for the long term

During periods of volatility it's important to remember that investing is for the long term. Generally the riskier the investment the longer you should be prepared to leave your money untouched, but as a rule of thumb it is a good idea to only invest money that you can leave for at least five years.

Here at Tilney a key part of our investment philosophy is to let time do the heavy lifting for us when it comes to generating investment returns. We base our investment decisions on the fundamentals rather than trying to time the markets or second-guess rises and falls.

Markets have a tendency to rise over time

Over time both stock markets and wider economies have a tendency to rise. This applies to everything from share prices and earnings to wages and the price of household goods.

Of course, there are ups and downs along the way. With long-term investing we can expect cycles – periods of falling prices followed by a recovery. And volatility is actually a sign of a healthy stock market – an unusually calm stock market can be a sign of complacency and problems on the horizon. We believe that a key to successful investing is being comfortable knowing that there will be falls as well as rises in the market.

Is this just a blip?

There have been many crashes and periods of extreme volatility over the past decades – from Black Monday to the dot com bubble bursting and the global financial crisis. Many of these events were terrible at the time, and yet when we look at the big picture we see that the stock market has recovered each time. Those who stayed invested for the long term eventually returned to profitability.

But of course, it can be difficult to keep this in perspective with today's 24-hour newsflow and sensationalist headlines. We also need to bear in mind that past performance isn't a reliable indicator of future performance.

Sentiment versus fundamentals

We should also consider the reasons behind the recent stock market volatility. Much of this can be attributed to sentiment – in other words, the general outlook and attitude of investors towards a particular country or stock market. The UK and emerging stock markets in particular have suffered from negative sentiment over the past few years – with Brexit uncertainty, the possibility of a Corbyn-led UK government and the US-China trade spat making investors feel uneasy.

It's important to bear in mind that changes in sentiment are one of the key drivers of short-term returns. However, short-term changes are impossible to forecast consistently, and trying to time the markets can lead to locking in losses and missing out on gains. This is why at Tilney we ignore market noise. Instead we focus on the fundamentals, particularly earnings growth, valuations and the impact of monetary and fiscal policy. These are the key drivers of long-term returns and they are possible to forecast with a degree of accuracy.

In conclusion

Although markets have been volatile and the future looks uncertain, we see no reason not to be invested in the stock market at the moment. We remain confident that good returns can be found for people who are comfortable investing for the long-term and riding out the ups and downs along the way.

It's important to remember that any time spent out of the stock markets is a period of time potentially missing out on returns. As we have seen, these periods of strong performance tend to provide a positive overall return over the long term, even if it's sometimes a bumpy ride along the way.

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