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# THE TRADE PRESS

The Federation of European Independent Financial Advisers

## Life transitions and the value of advice

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# Platforms – a profitable process rather than just another product

**By Paul Forman, Novia Global.**

Like most businesses, adviser firms are focussed on making profits and one way that they can streamline the business is by using an investment platform to automate their day to day processes and remove the manual tasks usually associated with international financial services.

As client data is held securely online then advisers can use the platform to access this in order to deliver a range of functionality (portfolio reports and MI) and processes which are expedited by the use of technology. Therefore, it is important to view the platform as a way of delivering the total wealth management service proposition to clients and not as yet another financial product.

The provision of information like this to clients is a great example of cost reduction for the business. For example, if all client information is held online then it is much easier to answer any queries from clients regarding their investments. Similarly, the number of inbound queries will also be reduced if clients have their own (read-only) online access to their pension and investments.

Process efficiencies are also achieved as client portfolios can be reviewed and updated using automated tools, such as for portfolio rebalancing purposes. What might usually involve spreadsheets and manual requests is now replaced by clicking just a few buttons online instead. Other processes like switching, report production etc can also be transformed with the adoption of such platform technology. Indeed, cost savings can also be passed on to advisers where research tools (like FE Research tools which can be accessed via Novia Global) are integrated and available as part of the platform infrastructure.

For most clients the consolidation of their assets and having access to them online 24/7 is seen as a valuable benefit. Total wealth and how it is performing can be accessed easily with the added benefit of reducing time and effort for them and their tax advisers when completing any annual tax returns.

One of the major benefits for clients is a reduction in the need for paperwork. For example, Contract Notes are stored online in the client document library and can easily be downloaded and shared with professional advisers if required. Valuations are also available and stored online and if tax wrappers are also held (e.g. International SIPPs), then the documentation produced from the platform is accessed centrally rather than via separate 3rd party providers.

In summary, key benefits to advisers using a platform to support their proposition are:

- Business cost reductions through efficiencies of process
- Consistency of the client investment advice process across the business together with other tasks such as risk profiling, client reports and reviews
- Reliable delivery of the adviser proposition, eliminating the errors which typically might otherwise happen with the equivalent manual processes

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## Editorial Comment

# Training and collaboration

Our professional development services and benefits continue unabated, not least with this, the most recent issue of the Trade Press.

October saw the commencement of the latest series of our **Masterclass seminars.** This month will see a further one of these, in Marbella. You can see full details and register **here**.

A little while ago, we uploaded a number of presentations from our Spring Conference and these are still relevant and exclusively available, as Video on Demand (VoD), for our members.

These can be accessed at ***https://feifa.eu/videos/*** (the first four below the anniversary video) and are eligible for CPD. Contact me if you need the passwords.

Finally, we are now looking to significantly expand our Associate Members and thus the professional network available to you, our core members.

Regards *Paul*


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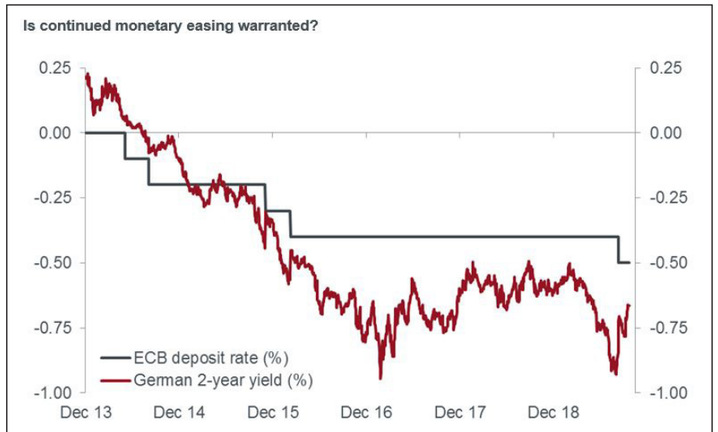
# Whatever he could

**Oliver Blackbourn, a Portfolio Manager on the UK-based Multi-Asset Team at Janus Henderson, comments on the imminent departure of Mario Draghi as ECB president, as the central bank itself potentially reaches the limits of what it can achieve using the levers of monetary policy.**

As Mario Draghi's tenure as President of the European Central Bank (ECB) comes to an end, it is difficult not to recognize that the central bank is now reaching the limit of its monetary toolkit. Uttered at the height of the eurozone debt crisis, "whatever it takes" is quickly turning into "whatever they can do." The truth is that there is only so much a central bank, hemmed in by competing interests and ideology, can achieve with its monetary policy mandate. Draghi's consistent call for structural reform has gone unheeded but any future slowdown is likely to require government fiscal action, rather than yet further monetary policy easing.

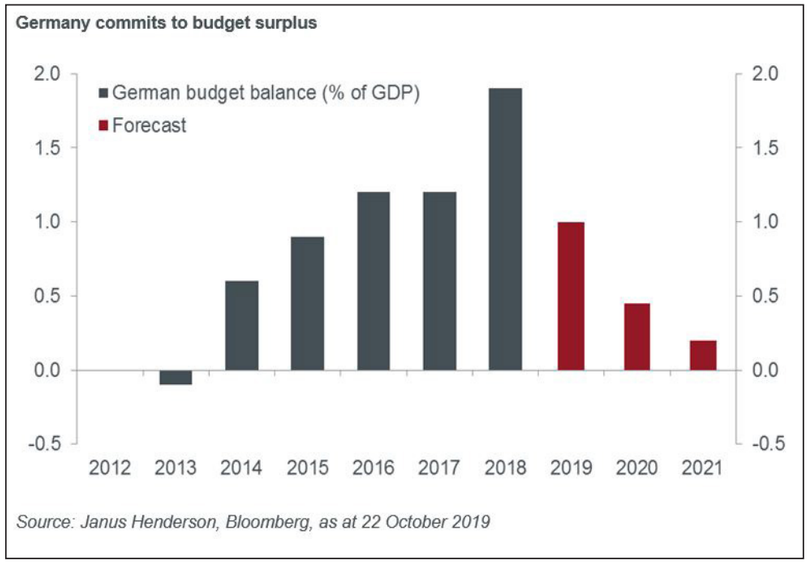



*Source: Janus Henderson Investors, Bloomberg, as at 22 October 2019*
*Past performance is not a guide to future performance*

Despite the seemingly fractious end to his time in office, Mario Draghi is likely to be remembered as a dynamic central banker, prepared to push the boundaries when others stuttered. Whether you agree with the policy decisions or not, he was prepared to act to drag colleagues and politicians with him. However, he may be leaving at an appropriate time as it is difficult to see how much more innovative the ECB can be within the restrictions of its mandate. Interest rates sit well below zero and quantitative easing has already pushed various major European sovereign bond market yields into negative territory. The chart on the left shows the policy-sensitive 2-year German bund yield has moved within a fairly narrow range for the last three years, suggesting that policy has been reaching a limit. At the same time, concerns have risen about the negative consequences of such environments and whether continuing to 'ease' further would actually be helpful to the real economy.

The start of ECB monetary policy decision press conferences has habitually seen Draghi call for eurozone governments to take action on structural reform to boost growth. Having fallen on deaf ears, fiscal stimulus may now remain the only meaningful action left to counteract a future slowdown in the eurozone economy. Whereas other central banks may look to help governments finance future fiscal stimulus via low borrowing costs, any suggestion of this within the strict boundaries of the eurozone's rules would prove highly controversial. Added to this, the budget and debt limits set out under the Maastricht Treaty mean that many larger eurozone countries have limited room for manoeuvre on the fiscal front. Germany is an exception following its commitment to a budget surplus in recent years, as can be seen in the chart on the right. Attitudes appear to be changing but it is a slow process. Investments in infrastructure and environmentally-friendly projects are possible exceptions and may be the vanguard in a new regime of looser fiscal policy. Just don't expect too much, too quickly.

The implications of a shift to fiscal easing may be profound. Despite likely being anchored by low interest rates, bond markets could begin to move to price in greater future inflation and higher real yields, due to the expectation for stronger economic growth. With yield curves steepening as longer-term yields rise, we would expect to see more cyclical stock markets outperform, such as the eurozone. However, we are at best seeing the first signs of a change in attitude, there is still a lot of resistance to be overcome before it turns into reality. In the meantime, as Christine Lagarde replaces Mario Draghi, you have to wonder if the ECB has done almost everything that it can do in terms of monetary policy.




*Source: Janus Henderson, Bloomberg, as at 22 October 2019*

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# Life transitions and the value of advice

**By Edden Kift from the PortfolioMetrix business development team.**

Advisers have a unique opportunity to materially affect peoples' lives. This is especially true during times of transition. While technical skills are essential, it is often the softer skills and ability to engage and empathise with clients that lies at the heart of appropriate and sound advice. Advisers should not underestimate the value of asking the right questions and then listening. Remaining silent a little longer than may feel comfortable is a skill worth mastering. And guarding against being the expert problem solver too quickly may uncover invaluable information.

Life transitions may be planned or unplanned. They may also be positive or negative. Below is a table containing examples of such transitions. While not an exhaustive list, it does provide an indication of the potentially multiple events related to work, family and financial status that can impact the financial positions of clients. The likely effect of informed advice is obvious. A transition may at times feel unmanageable for a client. It may also feel uncomfortable as it involves a move away from what is familiar. Furthermore, transitions don't necessarily follow a desired and predictable course. By assisting clients to cope with their fears and doubts and provide a sense of order, especially relating to their financial security, advisers are able reduce the risk of bad decisions from which clients may never financially recover.

| Planned | Unplanned |
|---|---|
| Getting married | Divorce / Separation |
| Birth of a child | Loss of a spouse / partner |
| A child going to school | Becoming disabled |
| A child entering university | Serious illness |
| Buying / selling a home | Redundancy |
| A promotion | A parent / child needing special care |
| Starting / selling a business | Unplanned expenses |
| Preparing for retirement | Loss of a business partner |

Life transitions come with unavoidable emotion. Not all advisers have the natural ability to be able to deal with emotional clients. At a recent presentation an adviser admitted that in the early part of his career he wanted nothing more than to dig a very deep hole into which he could disappear when clients shed tears. It wasn't that he didn't have empathy. It merely boiled down to him not knowing how to handle the situation appropriately and effectively. To his credit he took steps to learn how best to engage with clients in a situation that created a great deal of discomfort for him.

While the value of good advice may be obvious to many, it could be argued that the fee for good advice potentially eclipses the value of any other service in the "cost chain". The advice layer is perhaps the single most important factor driving the accumulation and preservation of investor wealth.

Evidence suggests that the behaviour gap, which is the difference between the returns potentially available to investors (based on actual investment returns) and those they achieved through their own investing behaviour (ill-advised changes to portfolios and deviation from strategy) is significant. The role advisers play in a) deriving suitable strategies and b) keeping investors composed is real.

Life decisions, such as sacrifices that need to be made now versus consumption often involve tough trade-offs and decisions that clients are not well-positioned to make on their own. Balancing preferences and personalities with hard mathematics is no simple task.

Most importantly, advice is not a once-off "fire-and-forget" service, but a lifelong journey with a client that may involve constant tweaking as the real world behaves differently to expected and the client's circumstances and needs change.

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# Cash is king

**Julian Chillingworth, Chief Investment Officer, Rathbones, asks: "is it worth paying for the privilege of holding government bonds?".**

**We've all heard the phrase 'cash is king'. It gets used a lot when investors think the prices of other assets are getting too high and they would rather sit on cash while waiting for prices to fall.**

This is very much a 'cash is king' moment. We would argue that government bond yields are unsustainably low. Some $15 trillion of global debt is now trading with negative yields — yes, negative. That means buyers of these bonds are paying for the privilege of lending money to the issuers of this debt. The return on their investment, if held to the bond's maturity, is guaranteed to be negative.

Back in the day, before this 'new normal', if a borrower didn't pay back the full amount of the loan that was called a default. Now it's just called a negative yield. Central banks have cut so deeply into interest rates that there is nowhere else for them to go but to the subterranean territory of negative rates. You could argue this is default in a different guise. The big question is: how much lower can rates go?

## The cost of carry

This brings us to what is known in the markets as the 'cost of carry'. It's the cost of holding an asset, including financial costs (such as interest rates) and storage costs (for example, to store commodities in a warehouse). If an asset has a negative yield, there is a large cost of carry compared to an asset that yields a positive return. At what point does it make financial sense to take cash out of the bank and pay to keep it in a safe deposit box?

At some point this will cost less than leaving the money in the bank at negative rates (which is actually happening in Switzerland and elsewhere where central bank rates are negative). At some point central bank rate cuts will start to become useless.

We may be nearing that point in Europe. That's why outgoing European Central Bank President Mario Draghi's parting shot was to call for fiscal easing (governments loosening their purse strings) to help economies; central bank stimulus could be at its limits.

Cash rates in the UK are still positive, albeit not that positive with the Bank of England base rate at 0.75%. This is well below inflation, eroding the purchasing power of cash deposits. But we would argue that cash is king in the UK right now too. Cash rates may be below inflation, but yields on gilts that mature as long in the future as 12 years are below cash rates.

## The Brexit factor

We see risks that UK yields could rise (prices fall), for example if Brexit turns out not to be the unmitigated disaster for the UK economy that current ultra-low yields seem to be anticipating. Or inflation expectations go higher. At least you get some return for holding cash in the UK; government bonds — which yield even less — are an unattractive option. Of course, gilt yields could keep going lower (prices higher), but we don't think the economic fundamentals are on their side.

With the global economy slowing, and an outside chance of recession, there may also be better opportunities for those who wait to invest their cash in assets that offer better returns.

Right now, the additional return on offer for investing in corporate bonds rather than safer government debt is the lowest it's been in about a year. That doesn't square up very well with all the talk of recession risk — corporate bond markets seem to be taking a more positive view. Equity markets have also continued to rise so far this year, again defying recession talk for the moment. In both cases, these markets are vulnerable if recession does come, or even a deeper slowdown from what's currently being experienced.

However, with yields so low or even negative, government bonds may not provide the diversification benefits they have in the past. To offset a big fall in stocks you need a huge fall in government bond yields to compensate for that risk. For reasons discussed above, that may not come through. Cash just might be king.

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# Prospect theory

**An analysis by Investec Wealth & Investment.**

**One of the best ways to avoid stress when it comes to long-term investing is to make less frequent observations of your portfolio. Prospect Theory argues that humans feel the pain of loss more sharply than they enjoy the benefit of an equal gain. Which leads us to report that, for equity investors in particular, the last few months have produced no convincing direction for markets in the end, even if the noise levels have been consistently high.**

Major turning points in markets are relatively rare, but short-term swings can be driven by temporary factors such as sentiment and liquidity, especially in today's febrile political climate. The equity market setback in August was triggered by news of further tariffs on imported goods from China being imposed by President Trump. That happened just as global economic data was going through a soft patch, with Citigroup's Global Economic Surprise Index (CGESI), which tracks data releases relative to economists' expectations, sitting close to six-year lows. Subsequently, Trump's negotiating tactics have been slightly more constructive – although the tone continues to shift on an almost daily basis – while CGESI has returned to neutral.

One reason not to hit the panic button in August was that it was becoming increasingly evident that global central banks were once again prepared to deploy the safety net for both markets and economies in the event of further setbacks. They came to the rescue as expected, led by the US Federal Reserve (Fed) and the European Central Bank (ECB). It is easy to forget that less than twelve months ago the Fed was tightening monetary policy by raising interest rates and shrinking its balance sheet, while the ECB was planning to start raising rates again around now. In the event, the Fed has cut rates twice already this year, while the ECB has moved its deposit rate deeper into negative territory, with a 0.1% reduction to minus 0.5%.

A few notable market moves deserve mention. There was the 20% jump in the oil price in response to an attack on key Saudi oil infrastructure on September 14th. This evoked memories of previous oil shocks in 1973, 1979 and 1990, all of which were associated with recessions. However, the fear was short-lived, and the oil price is currently back down at pre-attack levels. Gold is one of the best performing asset classes over the last year bolstered by low bond yields and interest rates, which reduces the opportunity cost of ownership. It has also benefitted from geopolitical tensions, and retains its long-held safe haven status when the world is feeling more uncertain.

The Eurozone's unemployment rate, now at 7.4%, and down from over 12% in 2013, is just a whisker away from the low of 7.3% it hit in 2007. And yet there remains a pervasive air of pessimism. Admittedly there is some divergence between the rates in northern and southern Europe, but the overall trend is down everywhere. Much of the woe stems from Germany, which would appear to be in recession, mainly as a result of a stumbling manufacturing sector. Part of this is down to the weakness of global trade, with

Germany being a major exporter, but some is self-inflicted, notably in the automotive sector, where the industry has been caught off-guard by the rapid shift away from the internal combustion engine. Negative interest rates also weigh on the profitability of the financial sector. Any sign of a US/China trade deal and/or a general recovery in economic growth would be highly beneficial to European markets.

Our equity selection process focuses on companies that we deem to have a durable competitive advantage bolstered by strong finances and sound management, which sounds a lot easier to define than it is in practice. We apply similar rigour to our fund selection and bond investments, ever cognisant of the fact that losing money, as we observed earlier, is a lot more painful than making it.

For more information about Investec Wealth & Investment's bespoke Euro mandate service please contact **Richard West – richard.west@investecwin.co.uk** or **James Fraser-Sampson – james.fraser-sampson@investecwin.co.uk**

# Healthcare caught in the US political crosshairs

**By Matthew Wintour, Head of Adviser Solutions, Brooks Macdonald.**

"Our industry is right in the crosshairs" said CEO of pharmaceuticals giant Merck, Kenneth Frazier, recently. He was commenting on a recent poll which found that the US pharmaceutical industry ranked last among 25 US industry sectors in terms of reputation. Indeed, the industry received a negative score rarely matched during the poll's 19-year history and it unseated the US Federal Government, which has been the lowest rated 'industry' for the past eight years. As Frazier observed, "We're below Congress, below bankers, below tobacco - that's not a good place to be … every person running for President has a plan to reduce pharmaceutical pricing".

A separate poll has shown that healthcare is the most important issue facing US voters, more important than the economy, the environment, and immigration.

## Investment backdrop getting cloudier

Healthcare is often used as a political football in US elections. Regardless of the desire and success of political parties to effect meaningful change once in office, volatility can increase within the sector in the months leading into US elections. With the next elections due to be held on 3 November 2020, we are cognisant that political rhetoric is likely to weigh on sentiment towards the sector over the coming year. We note that in the 12 months before the last US Presidential election, the MSCI World Healthcare index underperformed the wider MSCI World Index by -8.5%.

The road to the White House clearly has a long way yet to travel, but there appears to be an appetite to target healthcare with rhetoric on both sides of the political divide.

Senator Elizabeth Warren has emerged as a leading candidate to secure the Democrat nomination. She has been an outspoken critic of US pharmaceutical pricing, demanding greater regulation and public scrutiny, saying previously that "in market after market, competition is dying as a handful of giant companies spend millions to rig the rules, insulate themselves from accountability, and line their pockets at the expense of American families".

The language has been equally challenging from Republicans. In the last election, President Trump highlighted the need to "create new bidding procedures for the drug industry, because they're getting away with murder. Pharma has a lot of lobbies, a lot of lobbyists, and a lot of power, and there's very little bidding on drugs… we're the largest buyer of drugs in the world, and yet we don't bid properly. We're going to start bidding. We're going to save billions of dollars."

## Our view

History shows that it is difficult for political parties to effect significant change to healthcare policy once in office. However, this does not mean that there will not be heightened volatility for the sector as election campaigning takes place. As such, we have decided to reduce our outlook for our healthcare theme to neutral on a tactical basis.

Longer-term, healthcare remains a key thematic preference for us and its weighting within our asset allocation remains unchanged. Around the world, populations are aging, driven by improved mortality rates and lower birth rates, especially in developed economies. Against such a backdrop, we continue to see a virtuous circle where advances in healthcare drive progress in medicine, biotechnology, public health, nutrition, access to medical services, incomes, and education.

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# Find a new perspective on Asia

**The thoughts of Fidelity.**

The rise of Asia has been one of the most significant developments in the global economy and financial markets this century. With over half of the world's population, rapid urbanisation and wealth creation, led by China and India, we have seen Asia grow up over recent decades. It has matured from a frontier market characterised by relatively low-cost labour and cheap exports to a more sustainable and higher quality growth model driven by domestic consumption.

Part of this shift is down to the ongoing natural development of the middle class, but it is also being driven from the top, with regional governments increasingly recognising the need for structural reforms to ensure that these growth prospects translate into real-time economic activity.

Over the last decade, for example, we have seen an emphasis on opening up of both economic sectors and financial markets to global investors, as well as addressing the need to revitalise some of the domestic structures that support activity in key economies.

In China, for example, programmes like Made in China 2025 underpin a strategic objective to move up the value chain into future-oriented industries. The government has made it known its vision for China to become a high value manufacturer and a global leader in fields such as artificial intelligence, robotics, information technology and clean energy.

China has also launched the US$1tn Belt and Road Initiative (BRI) with a view to enhancing transportation routes and energy corridors across South East Asia, Africa and Eastern Europe.

We also continue to observe encouraging developments in other large markets such as India and Indonesia under the market-friendly leadership of Prime Minister Narendra Modi and President Joko Widodo. Looking ahead, it will be important to continue to monitor the implementation and effectiveness of individual reforms in individual markets, but this broader policy thrust will strengthen Asia's economic foundations and support the region's long-term growth story.

## Maturing leaders

Change is also unfolding at ground level where over recent years we have seen disruptive beginners mature into established market leaders within their respective fields. Asia today is home to a number of franchises that - whether it is due to an embedded position in global supply chains, brand strength or unique product offering - possess the strength and resilience to deliver sustainable returns across the economic cycle.

An example is smartphone camera manufacturer Sunny Optical. Our on-the-ground research in China highlighted early, the increasing penetration of smartphones and looking at their use in social media and online purchases, it was evident that phone upgrades were here to stay.

Back in 2013-14, Sunny was a relatively small company operating in a market dominated by Apple-focused Taiwanese company Largan Precision. But it was clear that there was room for another player. Over the subsequent years, Sunny has scaled-up its product offering at a time when the market has also moved from single phone cameras to dual cameras and now tri-camera phones are gaining traction. Sunny has benefited from this shift and has grown into the market-leader in the camera module space in the android phone segment - a local winner of a global shift.

## A question of sustainability

The dividend story is a good example of how Asian companies are improving their governance and it is notable that we are also now starting to see progress on environmental and social issues - areas where regional firms have historically lagged their European counterparts.

As relationships between family and state-owned companies and minority shareholders open up, Asia offers active managers a unique opportunity to engage more systematically with investee companies to drive change in their environmental, social and governance (ESG) practices.

So far priority has been given to health and safety, working conditions, and supply chain management, but environmental concerns are fast gaining prominence as the economic and health implications of air pollution in major Asian cities becomes apparent. We expect this focus on broader sustainability issues to sharpen as we see increasing international capital flows alongside regulatory initiatives from regional governments.

This is a new world for investors where these high returns can confer as much risk as reward and raises the game for us as asset managers to be effective as stewards of our clients' capital.

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# Rethinking portfolio protection

**The thoughts of Tavistock Wealth.**

Our ageing demographic, changing employment patterns and shifting attitudes towards risk and future savings mean both investors and advisers need to alter their approach when planning for retirement. For this reason, advisers should consider:

- Protection that increases with the portfolio value, not simply on the initial investment itself.
- Choosing a portfolio that offers a volatility control, to minimise the impact of significant market shifts.
- Seeking lower cost protection - while historic protected portfolios had ongoing charges (OCFs) of circa 4%, they are now available with OCFs of sub 1.5%.

It is up to wealth advisers to factor in the new challenges that this new environment brings to approaching their strategies, to ensure that they deliver on their customers' needs whilst balancing their appetite for risk and returns.

It is for these very reasons that Tavistock Wealth offer a range of protection portfolios.

The ACUMEN Capital Protection Portfolio and ACUMEN Income-Protection Portfolio offer 90% and 85% protection respectively and have been designed to address the numerous problems experienced by similar products in the past. The protection relates to the Net Asset Value (NAV) or the unit price and increases each time the portfolio reaches a new high. This is different to historical products which may have applied a guarantee on the initial investment only.

With the ACUMEN Protection Portfolios, clients could one day find themselves with a protection level that is greater than their initial investment amount, and as such the dynamic would shift from one of limiting the downside, to locking-in the upside. The protection comes in the form of a contractual guarantee.

The investment strategy is managed by Tavistock Wealth and the protection comes in the form of a put option. As the value of the underlying investments goes down, the value of the put option goes up. Consequently, the value of the risk assets combined with the value of the put option will always equal the protection level. The put options used are 4 years in duration which is long enough to cover the timeframe typically associated with a market crash/recovery. This gives the portfolio managers considerable flexibility.

The portfolios are managed to strict volatility targets (5%-7% and 7%-9% respectively). The second key component is a volatility control which means when market volatility increases, and the volatility target would otherwise be breached, the portfolio will sell down the risk assets and increase cash. As the market recovers the portfolio will then re-invest the cash into the risk assets.

A result of the put option combined with the volatility control is that these portfolios will not cash-lock like many competitor products in the past. Historical products may have operated using Constant Proportion Portfolio Insurance (CPPI), however once a claim was made, the client would essentially be left sitting in a pile of cash for the remainder of the term, which could be as far out as 10 years depending on the product. A further benefit of the Tavistock Wealth portfolios is that they are daily dealing UCITs funds meaning there is no fixed term and clients can sell their holding on any business day.

Historically the cost of protection was expensive. This can have an adverse impact on returns over the long-term. In some cases, the cost of the protection may have increased over the life of the product and/or the term may have been increased. Neither of which are good client outcomes. The Tavistock Wealth portfolios have an OCF of 1.25% and 1.32% respectively. This compares favourably to a range of historical products which may have cost anywhere from 1.5% to 4.0%.

The Tavistock Wealth portfolios may be suitable for clients who are risk averse or have a conservative risk appetite. They may be appropriate for clients approaching retirement, taking drawdown or who have made gains elsewhere that they wish to lock-in. They can be attractive to any client seeking a "cash plus" level of return or to clients who are simply looking to benefit simultaneously from a contractual guarantee and daily liquidity. This has led to significant take up in the portfolios from a retail perspective as well as attracting institutional interest from both pension and trust mandates. The portfolios will clearly appeal to an investor looking for certainty and who is willing to forego a small part of the upside in return for limited downside (which one day could turn into locked-in upside).To find out more, please visit: **https://tavistockwealth.com/**

For further information contact **Connor Stewart – connor.stewart@tavistockwealth.com** or tel: **+44(0)1753 867 000**.

# Ireland as a jurisdiction

**An insight from Octium.**

Ireland established its international market with the creation of the International Financial Services Centre in 1987. Over half of the world's top 50 banks and over half of the world's top 20 Insurance companies have established operations there. The sector is growing further as UK financial services companies seek an EU home post Brexit.

The international life sector continues to flourish with new premium income in 2018 of €18.9bn and the total technical reserves for the market stood at €268bn at the end of 2018. Just to put that in perspective, the Luxembourg life sector had total technical reserves of €180bn at the end of 2018.

## Policyholder risks

Policyholders want to know their assets are safe and secure, the easiest way to quantify the risk is to compare a Unit Linked life insurer to a bank. Unlike a bank, a unit linked life insurer always matches assets and liabilities 100%. It cannot lend assets out and those assets are segregated, ring fenced and protected. Third party risk of investment is borne by the policyholder, so the failure of an underlying custodian or investment does not affect the stability of the insurer. As with all EU insurers, Irish insurers adhere to the Solvency 2 protocols and in addition policyholders in an Irish insurer retain preferential rights over any other creditor. The Irish segregation of assets regime does not conflict with the possibility to appoint a custodian based in any white list country, as opposed to Luxembourg where with a few exceptions, only an EEA or Swiss custodian can be appointed. In addition, an Irish insurer can appoint any organisation as a custodian that has the appropriate regulatory permissions and oversight.

## The Irish Advantage

*Flexibility of investment management - the structural advantage*

Ireland maintains a flexibility of investment management and custodians that is unique in the offshore planning arena in Europe. All investment managers and custodians are fully regulated in their own jurisdictions. Ireland is ideally placed to take advantage of new technology led investment solutions that are developing rapidly. This system crosses all markets from the bank assurance solutions to those of independent advisers.

Where a jurisdiction permits it, an Irish insurer can accept a variety of assets including unquoted.

This flexibility takes into account local investments restrictions, the Irish admissible investment rules and the risk factors inherent in Solvency 2.

*VAT on investment management - the fiscal advantage*

It is important to note that in contrast to other jurisdictions, the investment management of a life policy is exempt from VAT in Ireland. Comparing that to the UK at 20% and Luxembourg at 17% an Irish policy has a distinct fiscal advantage.

## Experience

With 30 years of operation in the cross-border environment, Ireland has a breadth of experience and knowledge across the market of the major member states.

## Working together

With the raft of regulatory changes, it is important that insurers and distributors work together. Ireland provides a regulatory framework that encourages flexibility and innovation. IDD defines the way that we as insurers and our distributors operate. It creates new responsibilities for both, but also opportunities to learn from our past successes and shape them for the new world. Innovation in product and customer experience is vital. We recognise our distributors are at the front line and best placed to determine customers changing needs and expectations.

For further information contact **Nick Hockney – nhockney@octium.ie** or tel: **+44 (0)7931 383 516**.

# Currency choice can play a key in your advice process

**Karen Blatchford, Head of International Marketing, Old Mutual Wealth, provides her insight.**

Which currencies your clients' portfolios are exposed to can have a significant impact on their investment returns.

A robust and repeatable investment advice process should always start with understanding the key needs and objectives of your clients. Every client is different and when assessing suitability and building investment portfolios for your clients, it is important to understand their individual investment goals along with their attitude to risk.

There are many factors that need to be considered when constructing a portfolio for investors looking to invest internationally. As part of your portfolio construction and fund selection process, an important element that needs to be factored in is which currencies your clients are exposed to, the additional risk they provide and how they reflect on your clients' risk profiles.

## The impact of currencies on investments

Like most asset classes, currencies go up and down over time and these movements can have a significant impact on investment returns, both positive and negative. This is why choosing a currency should be an integral part of any investment decision and should be considered a risk. The greater the risk, the greater the potential for return which means that sometimes it may be beneficial to have some currency exposure.

One of the key questions is what happens to the value of the currency of a chosen fund. Many global funds tend to be denominated in USD, so when the value of the USD rises relative to the investor's home currency, the value of their overseas assets goes up. On the flip side, if the value of the USD goes down, the value of the assets compared to the home currency will also go down.

## How to mitigate the risks of currency

Investors who do not want to take currency risk have two options: either to invest in their own home markets using funds that are denominated in the home currency, or to 'hedge' their foreign currency exposure when investing in assets that are priced in currency other than their home currency. The decision on which option to go with should be based on each investor's personal circumstances, risk appetite and their views on what will happen to the interest rates and exchange rates. Ultimately, they need to ensure that they choose the most appropriate investment for them.

Over the long-term currency hedging may offer some valuable protection especially in volatile markets or when the currency of the fund is appreciating and foreign assets of the fund expressed in that currency are worth less and less. However, this is not always the case and sometimes currency hedging can have a negative impact which may come from the additional hedging costs or from missed opportunities by giving away the appreciation of the currency of the funds' assets.

As an example, so far this year GBP has been depreciating compared to USD. As a result of this, investors who have chosen to invest in GBP hedged share classes of funds which invest in a USD portfolio have been suffering as they hedged away the appreciation of the USD currency and paid for the hedging costs. If they had invested in unhedged share classes and exposed their investment to the currency exchange risk, the story could be different. However, as mentioned earlier, like most asset classes, currencies move up and down over time, impacted by many factors such as monetary policies and geopolitics.

This is why the impact of currency on the performance of a global portfolio over the long term should be considered as an integral part of any initial investment decision and reviewed as part of regular client discussions.

For further information contact **David Matthews – david.matthews@ominternational.com** or tel: **+44 (0)1624 655 555**.

# Analysis of chance and scale of gains

**A look at Global Wealth Management Solutions' partner, Levendi Investment Management, and its UCITS V, daily traded, Levendi Thornbridge Defined Return Fund; which can offer the prospect of positive returns that do not rely on rising markets. An analysis of its portfolio is below.**

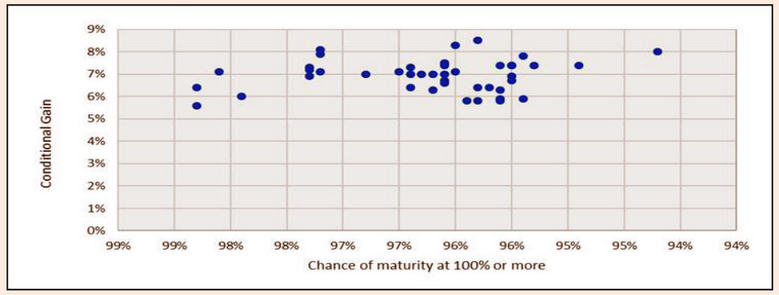
One of the benefits of investing in a fund like the Levendi Thornbridge Defined Return Fund is that the maturity value of each investment held by the Fund is "defined". There is no ambiguity about the maturity value. Typically, investments held will pay a return provided that the underlying indices close above the initial level at the end of any year prior to maturity. At the end of the full term, the condition required to pay the full return is that indices close above 60% of the initial levels. Provided both indices close above 50% of the initial levels, the maturity value will be 100%. This level of certainty and transparency gives us and investors the ability to look at the assets held by the Fund and form an independent view about the risk/return profile.

We run detailed stress test analysis of the holdings held by the Fund and calculate a range of numbers for risk and return. We can use the aggregated values from the stress test to illustrate how likely we think it is that the assets we hold will mature at 100% or more, and the sort of returns that we expect to generate.

The output from our analysis shows that based on our stress test:

- There is a 97% chance that assets mature at 100% or more
- There is a 93% chance that assets mature at more than the current price
- The average gain when there is a gain is a return of 6.9%
- The best-case return is an annual return of 9.5%

## Conditional gain / chance of maturity >100%

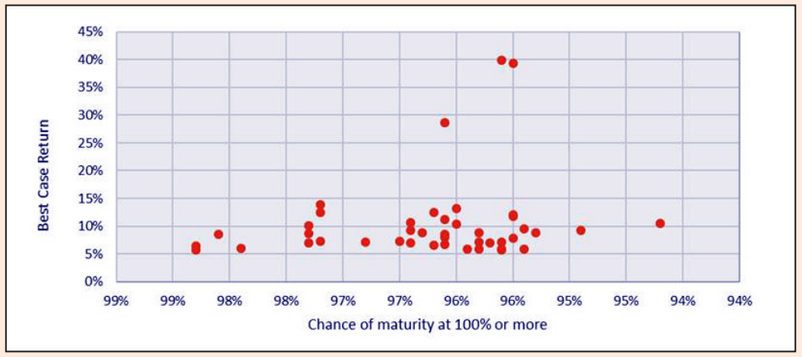



The first chart shows the chance that the maturity value of each product is greater than 100% and the Conditional Gain. The Conditional Gain is the average annual return (based on the current price) in scenarios where the maturity value of the product is greater than the current price.

The chart shows that all the products have a high chance of maturing at 100% or more. The average is 97%. Because many of the investments held by the Fund are trading at more than 100%, if they mature at 100% then this would be a loss. There is a 93% chance that the maturity value will be more than the current price. The Conditional Gain ranges from 5.6% to 8.5%, the average being 6.9%. This profile is exactly in line with the return objectives of the Fund.

## Best case returns

To estimate the best case, we calculate the 10th best annual return out of 100 scenarios. The average value is a return of 9.5% per annuum.




## Conclusions

The analysis from our stress test illustrates that the return profile of the assets held by the Fund are expected to deliver the gains that the Fund aims to deliver. It is important to remember that the stress test is only an estimate of the chance and scale of returns.

For further information contact your **GWMS Regional Sales Partner** or call our **Head Office** on tel: **+44 (0)1525 861 983**.

# Fund risk profiling for the investment journey ahead

**Jim Henning from Dynamic Planner discusses.**

Strange times are these in which we live, given the uncertainty currently pervading the global political and economic climate. And the impact of ongoing financial stimulus measures by central banks continues to have unprecedented consequences. So much so, that around 30% of global bond issuance, representing circa $17 trillion in value, currently requires creditors to pay for the privilege of lending their money to debtors! Nor is there any sign of interest rate "normalisation" likely in the foreseeable future, meaning that investors need to continue to embrace some form of financial risk to stand any chance of capital preservation let alone growth in real terms, once all related charges are factored in.

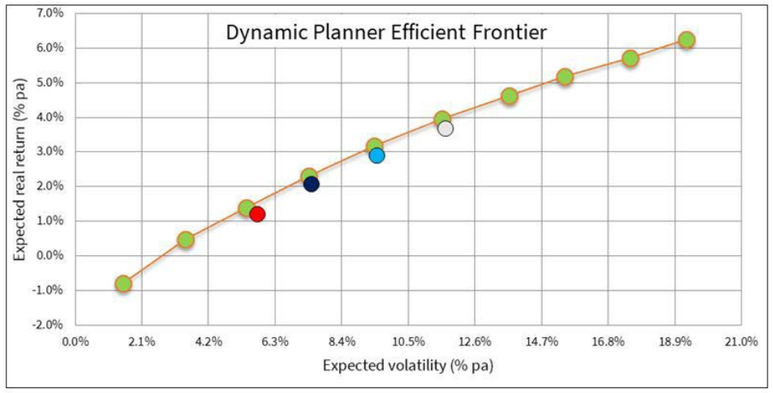
Those who have done so over recent years have been rewarded pretty handsomely, but it's important not to become complacent as a result of these generally benign market conditions post the 2008 GFC.

The assessment of suitability is one of the most important requirements for investor protection within the MiFID II and IDD frameworks and the importance of consistent and accurate data on which to compare funds is a vital for a whole-of-market financial adviser. However, to justify an initial portfolio recommendation and subsequently be reviewed via the obligated annual suitability report can be a very complex and time-consuming task.

Ensuring that risks associated with an investment fund can be properly assessed to meet the needs and personal characteristics of the end investor has often been completed with the help of statutory disclosure documentation. The requirement for asset managers to provide KID documents is a sensible starting point, as this includes a definition of the investment objectives and policy alongside the associated risks, in a descriptive format and also typically a 5-year look-back of experienced volatility.

However, the fundamental challenge when using experienced volatility to establish a uniform risk scoring mechanism across different fund types is that it may not fully equip the client with a clear understanding as to what to expect in future. For example, there is currently little distinction in the ex-post risk scores across sovereign, investment grade credit, high yield and emerging market debt funds, but risk levels in future could diverge significantly should market conditions change.

At Dynamic Planner we risk profile in total over 1400 multi-asset investment solutions from many leading global asset manager firms. The approach we adopt is fundamentally different and can perhaps be best described by the analogy of the driver who needs to be mainly focused on the road conditions ahead but also prudently uses the rear-view mirror. Our proven asset and risk model, launched in 2005, is the essential engine that drives all our forecasting capabilities and Dynamic Planner is now used by over 1800 licenced advisory firms, a number of whom are based outside the UK, to align their customer risk tolerance to an agreed risk-adjusted set of asset allocation benchmarks.

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|---|---|
| Dynamic Planner Asset Allocation Benchmarks | ● |
| Multi Asset Family of Funds | ● ● ● ○ |

This framework then supports an independent outsourcing solution for a robust assessment of the expected risks for multi-asset funds or discretionary model portfolios, fully aligned to the client's agreed risk mandate. Over 20,000 individual securities are risk modelled by Dynamic Planner and calibrated into a range of 49 separate asset class definitions. These assets are commonly held within retail investment solutions and each are assigned a set of expected returns, volatility and co-variance assumptions, which are updated each quarter. This grid framework is then applied to the asset allocation data provided directly to us from those many fund managers who have requested us to formally risk profile their products on a forward-looking basis. The process is consistently applied and is run continuously with refreshed data from the asset manager every quarter. Understanding how the investment solution is managed is also vital within the profiling process, as this avoids the potential pitfall of short-term tactical decisions or one-off data points unduly impacting the longer term strategic assessment of its risk journey.

Rear-view sense checking the observed volatility of the solution relative to that experienced by the Dynamic Planner strategic benchmarks is also conducted by tracking error analysis. This can be used to highlight any potential inconsistencies between what was expected and the actual outcome delivered. Such an occurrence would prompt further direct engagement with the asset manager to fully understand the reasons why and assess whether the risk profile would need to be changed and for advisers to re-appraise their client's portfolios accordingly.

Such a combination of proven risk modelling, wide fund and asset class coverage plus golden-sourced holdings data is a very powerful and efficient engine that can drive the provision of high-quality MiFID II compliant ongoing suitability reports. And when used in conjunction with the full suite of Dynamic Planner client risk and cash flow modelling tools, advisers can professionally demonstrate the true value of their ongoing advice service.

If you would like to find out more about how Dynamic Planner can help you deliver MiFID II investment suitability and also get involved with our future development plans for international based advisers, please contact **Jim Henning – jimhenning@dynamicplanner.com** or tel: **+44 (0)7715 999 639** or **Imran Mahmood – imranmahmood@dynamicplanner.com** or tel: **+44(0)7872 693 504**.

**'Our grid framework is then applied to the asset allocation data provided directly to us from those many fund managers who have requested us to formally risk profile their products on a forward-looking basis.'**

# The benefits of a multi-asset approach

**Linda McLaren, Head of Business Development for the Marlborough Group's IFSL International, explains how volatile markets have underlined the value of multi-asset portfolios.**

Volatility returned with a vengeance in the final quarter of 2018 and global equity markets have been buffeted by further bouts of turbulence in 2019.

US-China trade tensions and concerns about a slowing global economy have both played a role in undermining investor confidence, while in the UK and Europe there has been additional uncertainty around Brexit and the broader political landscape.

The heightened volatility in equity markets has underlined the value to investors of holding a portfolio with a balance of different assets, designed for the long term and constructed to weather unpredictable market conditions along the way. Diversifying in this way is an important way to help manage risk.

In the Marlborough Group's range of Irish-domiciled UCITS multi-asset fund of funds, our highly experienced team invest across a range of key asset classes, with underlying funds selected primarily from Marlborough's award-winning UK-registered range.

As stablemates in the Marlborough Group, we can access the expertise and resources of these respected fund managers at institutional rates, which keeps costs for our investors as low as possible.

## Risk-graded portfolios

The four funds – Marlborough Defensive, Marlborough Cautious, Marlborough Balanced and Marlborough Adventurous – are risk graded and can be used in conjunction with client risk-profiling questionnaires. Used in combination, the four funds can be used to target seven risk grades in all. Maximum equity exposure ranges from 20% in Marlborough Cautious to 100% in Marlborough Adventurous.

In the context of Brexit uncertainty, the Irish domicile of our UCITS funds provides reassurance and clarity for advisers serving clients across the European Union. Regardless of the twists and turns around Brexit, these funds will continue to be available to investors in the EU.

Many advisers are also finding that, given current market uncertainty, they value the flexibility of the fund of funds model. It means that if, for example, a client wants to switch from our balanced portfolio to our cautious one this can be done more quickly and straightforwardly than might be the case with, for example, a managed portfolio service.

## Investment process

Our investment team is made up of highly experienced fund of funds managers and at the heart of their investment process are asset allocations based on detailed analysis of how different asset classes have performed over the long term.

The fund managers have modelled returns over 20 years from a range of asset classes – including different equity markets, bonds, property and alternatives such as commodities.

Backdating performance over two decades means their data covers a range of different market conditions and avoids excessive emphasis on the impact of any single market event.

Using this analysis, they have created a range of asset allocations designed to achieve the best possible returns for different investor risk profiles.

The team do not make tactical asset allocation calls, believing it is difficult to consistently make such short-term market calls correctly and that they do not fit with their careful risk management process.

Instead, they focus on their long-term modelling of asset class performance to construct portfolios that are carefully calibrated to investors' risk profiles.

Alongside Marlborough's single strategy funds, the fund managers provide diversification by holding expertly selected low-cost passive funds.

The result is that each portfolio is a carefully constructed blend of funds, built around a risk-graded asset allocation and designed to achieve the best possible returns for the level of risk taken.

Volatility is a fact of life in the world of investment, but these all-in-one portfolios are designed to help investors manage the impact of these bouts of turbulence as they navigate the path to long-term returns.

For further information contact **Linda McLaren – linda.mclaren@marlboroughgroup.com** or tel: **+44 (0)7986 972 844**; **Andy Gibson** (Switzerland, Cyprus and northern Europe) **– andy.gibson@marlboroughgroup.com** or tel: **+44 (0)7946 064 558**; or **Vasco Moreira** (southern Europe) **– vasco.moreira@marlboroughgroup.com** or tel: **+44 (0)7946 064 535**.



# Reassuring the insured:

## Luxembourg's Triangle of Security for policyholders

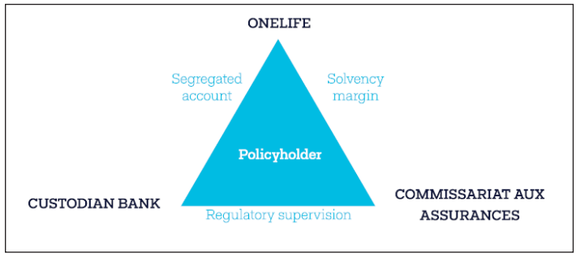
Life assurance is the bedrock of any person's financial plan, ensuring that assets are safeguarded and family members protected. Luxembourg's 'Triangle of Security' system is designed as a gold standard for investor protection, and part of the country's broader 'protection for all' principle.

The legal framework of Luxembourg's life insurance sector incorporates three key elements:

- The regime protecting policyholders - the Triangle of Security.
- Protection against the bankruptcy of the insurance company.
- Protection against seizure of policy claims by third parties.

## Triangle of Security

The Triangle of Security has been the foundation of Luxembourg's position as a leading European centre for life insurance. It is a legal mechanism designed to protect the policyholder, creating strict controls over how their assets can be held and used. It is based on a tri-party deposit agreement signed by the industry regulator, the Commissariat aux Assurances, the life insurance company and the custodian bank - the three sides of the Triangle.




- The insurer must deposit all the assets linked to life assurance polices with an independent custodian bank. Policyholder assets must be segregated from those of the insurance company and of the bank itself.
- The regulator approves the custodian bank, and has powers of oversight, investigation and sanctions - including the power to freeze the assets of a life insurance company if it identifies a significant risk.

## Protection against the insurer's bankruptcy

If the insurance company runs into financial problems, the CAA may use its powers to protect policyholders from loss, for example by freezing the segregated accounts of policyholders and beneficiaries. This means no further transactions may be carried out involving the accounts without the regulator's authorisation. It may also sell liquid assets or register a mortgage on fixed assets.

Policyholders enjoy a so-called Super Privilege - first-rank preferential rights over the assets held in separate accounts, giving them priority over all other creditors of the insurance company.

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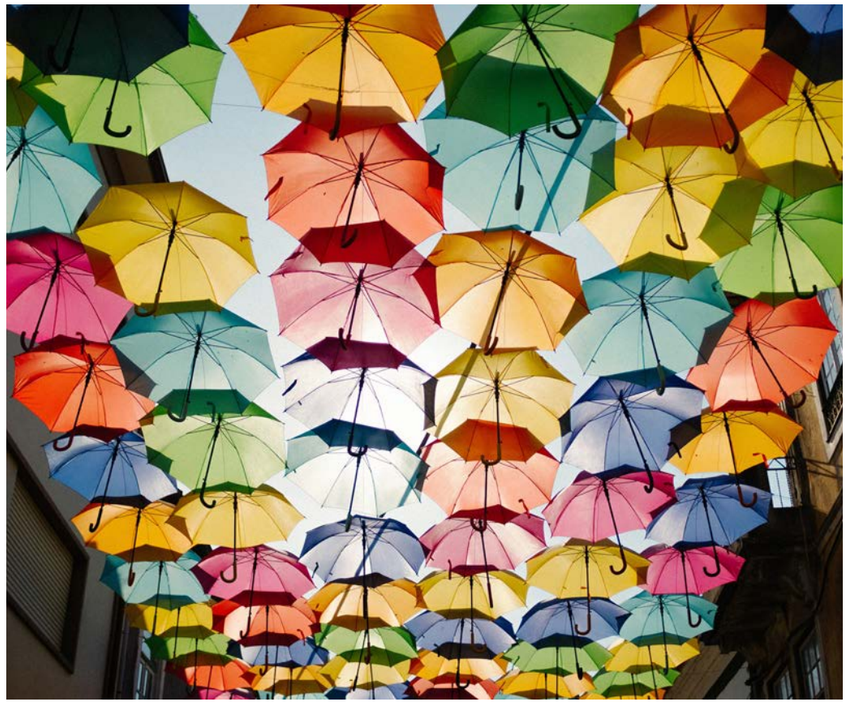
# Reassuring the insured:

## Luxembourg's Triangle of Security for policyholders



### Protection against the seizure of policy claims by third parties

The rights to redeem, advance and pledge the policy belong exclusively to the policyholder and cannot be seized by a third-party creditor. If a policyholder has an unpaid debt, the creditor cannot seize the policy or force the holder to redeem it.

While policyholders' creditors may seek redress from the insurance company to recover their claim, they will receive no payment unless the policyholder freely decides to redeem the policy.

### Strengthening of the protection framework

This fundamental framework has recently been tightened even further with new rules that align protection with the policyholder's risk profile and investment strategy. Whereas under the previous regime policyholders were treated equally regardless of whether they opted for a high-risk/high-return or a conservative investment strategy, now each policy is considered as an individual cell on which the super privilege is exercised, rather than the pool of all policyholder assets.

The changes illustrate how the authorities strive continually to ensure the maximum protection for Luxembourg life insurance clients. After all, life insurance is about Security and peace of mind whatever the future holds.

### Key points:

- Luxembourg's Triangle of Security is designed as a gold standard for investor protection in Europe.
- The regulatory framework provides protection against the bankruptcy of the insurance company and against claims laid against the policyholder by third parties.
- Under new rules, protection is personalised according to the policyholder's profile and strategy.

For more information, please contact **Bert Opdeweegh**, Director Business Development & Sales Support – **bert.opdeweegh@onelife.eu.com** or tel: **+352 621 705 204**, or **Marie Salvo**, Key Account Manager – **marie.salvo@onelife.eu.com** or tel : **+352 671 886 331**.



# Currency update

## GBP

Sterling has been under pressure due to Brexit uncertainty for some time, but this month brought some progress in the negotiations that were beneficial to Sterling. European Commission President Jean-Claude Juncker suggested that a reasonable alternative to the Irish backstop proposal could be acceptable to the EU, lessening fears of a no-deal departure. It wasn't all smooth sailing for the Pound; after the Supreme Court ruled that the extended suspension of parliament was unlawful, Sterling lost an average of 1.4% against a basket of currencies as investors viewed the tensions in parliament as a sign of more challenges to come. However, as the date of the EU meeting drew closer, the PM's meetings with Irish leader Leo Varadkar appeared to yield results and a breakthrough. This came despite reports that a deal was "overwhelmingly unlikely" as Donald Tusk expressed his frustration at the latest proposals and both Emmanuel Macron of France and Angela Merkel of Germany were pessimistic about the possibility of a deal. Ahead of the EU meeting on 17th October, the PM appeared confident that a deal could be reached and this was reflected in the Pound's performance as it spiked on the news that a deal would be presented ahead of the crunch meeting. There was a further challenge for the PM and the Pound, however, with Parliament instead voting to delay a vote on the deal until after he had written to the EU requesting an extension. The letter was sent, but not signed, as the Prime Minister must now attempt to pass through the Withdrawal Agreement Bill by 31st October (at the time of writing!).

While the Brexit breakthrough helped Sterling as the month progressed, investors largely ignored the Eco stats. The Manufacturing PMO came in better than expected at 48.3 and Services was within the sub-contraction zone at 49.5; together this threatens a recession but at the moment investors appear to be concentrating on Brexit as the key mover of the Pound. As hopes of a Brexit deal rose, the impact of any negative data was diminished. In addition, disappointing CPI inflation data which showed that growth had slowed to 1.7% was largely counteracted by the Bank of England holding interest rates at 0.75%, although again Brexit took all the focus and appeared to be the main influence on the Pound's performance. Michael Saunders, an external member of the Monetary Policy Committee, stated that, "it might well be appropriate… perhaps to loosen policy at some stage". This was in contrast to the official Bank of England party line that rates could move in either direction. Regardless of the Bank of England's plans, it appears that until there is greater clarity on Brexit it is set to continue to dominate the Pound. With so many key events on the political calendar in the final quarter, the next few months have the potential to be dramatic for the Pound, one way or the other.

## EUR

The slowdown across Europe has cast a shadow over the Euro; in addition, a rise in oil prices saw investors flocking to the US Dollar. The losses against the greenback were short-lived, however, and the Euro gained 0.1% against the US Dollar following the latest announcement of the Fed. Progress on Brexit may be good news for the Pound but the Euro touched its lowest point in four months as hopes of a deal grew. In general, the Euro has been somewhat overshadowed by events in the UK and the US; despite this, there was little reaction to the news that the US will impose tariffs on a range of EU goods.

The main challenge for the Euro, however, has been the slew of data which points to the slowdown of the economy and is detrimental to the Euro. It wasn't all bad news - IFO's measures of German business confidence showed a slight improvement, described by IFO as "the downturn taking a breather", and Gfk's consumer confidence index was a touch higher at 9.9, probably as a result of the European Central Bank's new stimulus. However, the composite PMI for Europe only just managed to remain in the growth zone at 50.4 and the provisional manufacturing PMI for Germany was of particular concern, coming in at a ten-year low of 41.4. Despite the gloomy picture, or perhaps because of it, one of the biggest movers of the Euro was news from the European Central Bank towards the end of the week caused a stir that helped the Euro make gains against the US Dollar.

Reports of internal opposition to resuming the Quantitative Easing programme and heated debate in September's ECB policy meeting was positive for the central currency. There is currently no confirmation on whether plans to resume QE on 1st November to stimulate growth will change, but as the global trade landscape continues to shift and the numbers offer no solace, the ECB's actions will continue to have an impact on the performance of the Euro.

## USD

The impeachment proceedings have not yet had a significant impact on the US Dollar, but remain an underlying issue which causes some nervousness in the market. A surge in oil prices gave the US Dollar a boost, but the ongoing tensions associated with the drone attacks in Saudi Arabia which caused the rise also meant that JPY, CAD and NOK benefited, and rose against the US Dollar. The rate cut from the Fed to 1.75% - 2% was expected, but did little to boost the currency. Investors had hoped for a larger cut of 50 basis points, and also were hoping for greater clarity on the plans for future cuts for the rest of the year and into 2020. Consumer confidence took a dive, falling nine points to 125.1 according to the Conference Board index and the "escalation in trade and tariff tensions" was highlighted as an issue that "rattled consumers." Even as news of a "currency pact" with China as part of a partial trade agreement emerged, it did not do much for the US Dollar. While commodity oriented currencies such as the Australian and New Zealand Dollars made gains, it was not particularly beneficial for the greenback as investors awaited more concrete proof that the trade war could be drawing to a close.

The Fed remained tight lipped as the US-China trade war continued to have an impact on the US economy and the Dollar. Federal Reserve Chairman Jerome Powell's speech on the data dependency of the Fed's monetary policy highlighted that there was increased market volatility and appropriate measures would include "increasing our securities holdings to maintain an appropriate level of reserves, " although he was clear that this programme would not be the same as the quantitative easing following the financial crisis. His reassurance appeared to settle investors and the US Dollar was unmoved following the speed. In the meantime, disappointing PMI data did nothing to dispel concerns over political developments. The pace of growth is slowing more rapidly than expected; the Institute of Supply Management Manufacturing PMI came in at 47.8, two points lower than expected. The news sent share prices in the US and Europe 3% lower and the US Dollar lost out as investors rushed for the cover of the safe haven Yen. As with the Pound, greater clarity on the way ahead may benefit the Dollar but as the US heads into an election year in 2020, there may be choppy waters ahead as the year draws to a close.

For further information contact **Meyrick Green – FEIFA@moneycorp.com** or tel: **+44 (0)203 823 0404**.