NEWSLETTER

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Strongbox
tailored wealth management

What should you be doing?

Last time we wrote in this column about the fact that the markets, despite numerous uncertainties and reasons for investors to be very nervous, were carrying on ever upwards.

Well somebody was obviously listening because the last quarter has been crazy! In 2017, according to CNN Money, there were only eight days when the S&P moved by 1% or more. In 2018, there have already been 23 of those days.

So has a whole new set of information come to light, or have market participants just started to focus in on some of the many risks – rising interest rates, potential for trade wars and geopolitical risks that have been apparent for quite a long time? No, we have not had a whole slew of new information, and yes, it seems that the markets have now decided to respond to issues that have been apparent for quite a long time.

This week the Federal Reserve said “Inflation on a 12-month basis is expected to run near the Committee’s symmetric 2 per cent objective over the medium term” which analysts take to mean that interest rates will rise several more times this year, with the next increase expected in June. Rising rates are expected to put pressure on corporate returns (as borrowing becomes more expensive) so that puts a damper on the market – it seems that any possible good news, including the Trump tax cuts, is now fully reflected in stock prices.

On the issue of trade relations with China, the news does not seem to be good either, with both sides digging in for a long-term battle, and although things seem to be settling down a bit on the Korean front, there is no great improvement in other aspects of geopolitics such as the Middle East.

So all in all, it seems as though we might be in for a continuing period of increased volatility leading to – at best - sideways trading in the markets.

However, as many analysts have pointed out, short-term volatility only really matters to day traders. To long term investors, this is just noise, and in fact can be a blessing in disguise – it’s very difficult to find any buying opportunities in a constantly upward moving market. In a more volatile market, it can be easier to find stocks to add to one’s portfolio.

So as always, the key piece of advice is to look to the long-term – choose carefully, buy well, and be prepared to hold for a long time.

Equities comment

The top performing stock in the model portfolio year to date is the VIXY Exchange Traded Fund. This fund is a bet on volatility increasing in the US S&P 500 market index. We have held this for many years and have lost money on it since we bought it - we bought it purely as a hedge against the market falling, the only problem was that we misjudged how long the bull run in US equities would continue! But now we are getting our pay-off - year to date, the price of VIXY has increased by around 41%. While this may seem spectacular, it was off a very low base and it still has a lot of ground to make up to reach positive territory. Nonetheless, with the markets at around fair value, we do expect an increase in volatility and we are happy to hold this fund for the foreseeable future.

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Model Portfolio

It is depressing to note that a lot of the gains we made last year have been whittled away by the nervousness of the markets in the first quarter of 2018.
We made only one significant change to the model portfolio this quarter - we sold our holding in Weir Group at a profit of 82%. We will continue to look carefully at the portfolio and not hesitate to sell anything that is looking overvalued, although we'll also pounce on any under-valued quality we find. But having said that, we expect that the bias will continue to be more towards selling than buying for the next couple of quarters.

Model Portfolio
Initial value $1m **Current Value** $2.14m
Cash 40% **Shares** 60%

Performance		**Bottom Performer Shares (ytd)**		**Top Performer Shares (ytd)**	
6 months	-2%	Noble	-22%	VIXY	+40%
12 months	-4%	Alaska Air	-19%	Tapestry	+16+%
since start	+114%	Qualcom	-16%	TBT	+7%

Back to basics 1: What is investment?

We have traversed this topic before, but we don't think a refresher ever goes amiss!

There are many definitions of investment, but we like this one – investment is what you do with your savings to make them increase in value over time. It doesn't matter whether you put your cash in the bank or dabble in futures and options – you are doing it in the hope of increasing the value of your money. We like this definition it because it reduces what can be a complex and jargon ridden subject to its first principle – no matter where or how you invest, increasing the value of your savings is the key objective.

Why do you need to increase the value of your savings?

When you save, you are deciding to spend, or consume, less than you are earning today. This is done in the expectation that at some point in the future you will need to consume more than you will be earning. The fact that these two periods in your life can span a long number of years is what makes your investment decisions so important – with increasing longevity, it is entirely possible that the savings accumulated during a working life of, at best, forty years will have to fund a retirement that could be as long as thirty years.

Your investments therefore need to (i) compensate you, in real terms, for the deferral of consumption (ii) compensate you for the impact inflation will have on the real value of your money over time and (iii) compensate you for the level of risk you are willing to take in your investment. There is never any guarantee of the future value of your investment, and you need to be rewarded for the risk you are taking by not consuming all of your money today. But more on this next time…….