Trustee MPI Low-risk portfolios

A GAME OF 'WAIT AND WATCH'

Managers still identify opportunity in defensive equities for low-risk mandates but choosing between fixed-income asset classes is increasingly challenging

Gary Shepherd

Risk assets have risen rapidly during the past year, remaining largely untroubled by the huge macro events that have unfolded, bringing fear to the lives of those of a nervous disposition. Still, wealth managers have trimmed their weightings to equities in low-risk mandates, falling from 31% prior to the UK's EU referendum in 2016, to today's 28%.

Fixed-income weightings have remained relatively steady, while the benefits of diversification have driven a rise in alternatives from 12% to 15%. Interestingly, cash is at a high of 9%, with more bearish professionals anticipating the next drawdown.

Waiting game

Rajat Sharma, CIO at Var Capital, says his team is currently in a "wait and watch" mode in terms of low-risk portfolios.

"We are overweight defensives, cash and 'event' names in equities," he explains. "Some earnings multiples on a cyclical-adjusted basis are at all-time highs, and that's something to be worried about.

"If you look at the Vix measure of volatility, it has been at historic lows, so it seems like everyone is thinking it's all hunky dory, but this is the time to be putting hedges on and taking risk off the table".

Sharma believes it is an "opportune time" to invest in the defensive sectors, such as telecoms and pharmaceuticals that have de-rated as cyclicals have stolen the limelight.

Still, he has exposure to those cyclicals and 'event' names that have been subject to restructuring, buybacks and special dividends. For example, the team bought into Monsanto prior to its acquisition by Bayer

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and was looking at French infrastructure firms ahead of the recent election there.

Within fixed income, Sharma has taken some risk-off moves in dollar-denominated EM debt. He has also increased the overall low-risk portfolio's duration given 10-year US treasury yields have fallen to about 2.2%.

Push and shove

Quilter Cheviot remains positioned for moderately higher bond yields, but expects this to be a gradual process.

"We need to see a more hawkish tone from the ECB and Bank of England to push yields up from their current levels," says MPS portfolio manager Simon Doherty.

"Overall, the MPS strategies remain underweight fixed interest – a function of our relatively cautious stance on bonds in general, given the low level of yields on offer.

"Value opportunities appear limited and we have just sold our long-standing exposure to index-linked gilts across the strategies."

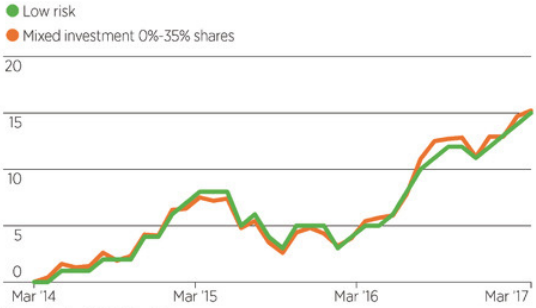
For the time being, Quilter Cheviot's fixed-interest exposure remains biased to conventional gilts, while the team is broadly positive on equities, particularly North America, Europe ex UK and Japan.

"Although there are no obviously 'cheap' financial asset classes, global equity valuations do not seem excessive given the outlook we envisage," Doherty adds.

"At the same time, absolute return, commercial property and fixed-interest funds continue to form an allocation within our medium and lower-risk strategies."

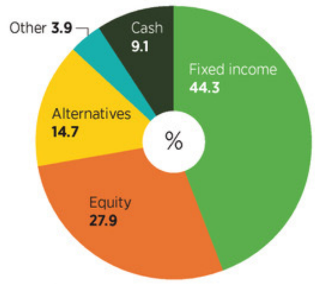
Favoured strategies include multi-asset thematic and long/short equity. Current holdings include GAM Star Absolute Return Bond, Invesco Perpetual Global Targeted Returns and Old Mutual Global Equity Absolute Return funds. **LW**

Low-risk vs benchmark
3 yrs %



Source: Trustee MPI, FE Analytics

Low-risk allocation
%



Source: Trustee MPI