Church House Investment Management

Quarterly Review

Summer 2020

Issue No. 81

Investment Risk

Investing in ordinary shares and other assets that will be included in your investment portfolio entails risks to your capital and the income that it might generate. The paragraph below is an important reminder, please always remember that:

> *The value of investments and the income you get from them may fall as well as rise and there is no certainty that you will get back the amount of your original investment. You should also be aware that past performance may not be a reliable guide to future performance.*

The second half of this Review, from page 16 onwards, gives information on the Church House fund portfolios that we manage for our clients. Some, or all, of these funds feature in most portfolios and the risk warning above is pertinent to each of them as well as to investment portfolios generally.

It is crucial to our approach to the management of risk to utilise these Church House funds to construct portfolios; each has a specific 'building block' role. This approach ensures a proper diversification and that we know in detail the risks that we are undertaking on your behalf - not something that we are happy to delegate to others.

These fund portfolios are authorised by the Financial Conduct Authority under the Collective Investment Schemes regulations with which we must comply at all times. We are also required to point out that the main risks faced by them arise from market price and interest rate risk; they have no borrowings, or unlisted securities of a material nature (so there is little exposure to liquidity or cash-flow risk) and that we review the policies for managing these risks on a regular basis.

As ever, do please get in touch with any questions about your portfolio, this report or any change in your circumstances that you feel we should know about.

Church House Investment Management

www.ch-investments.co.uk

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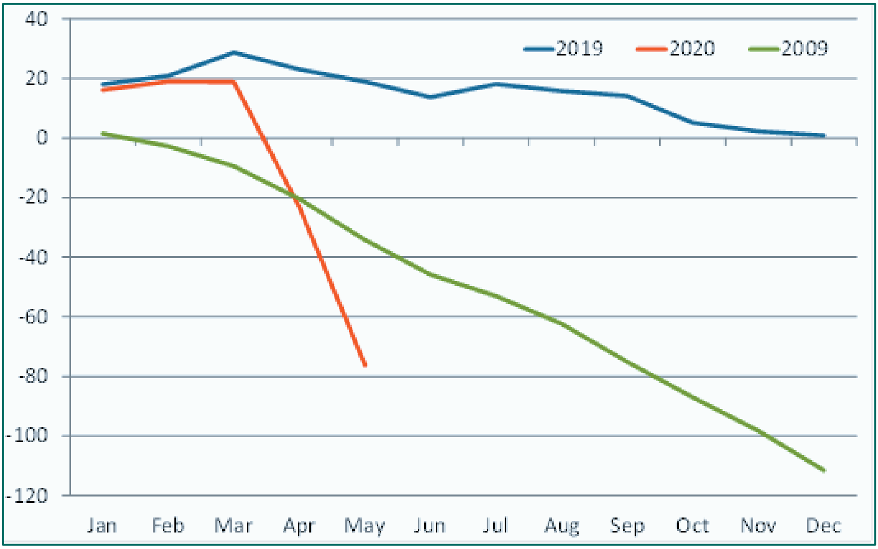
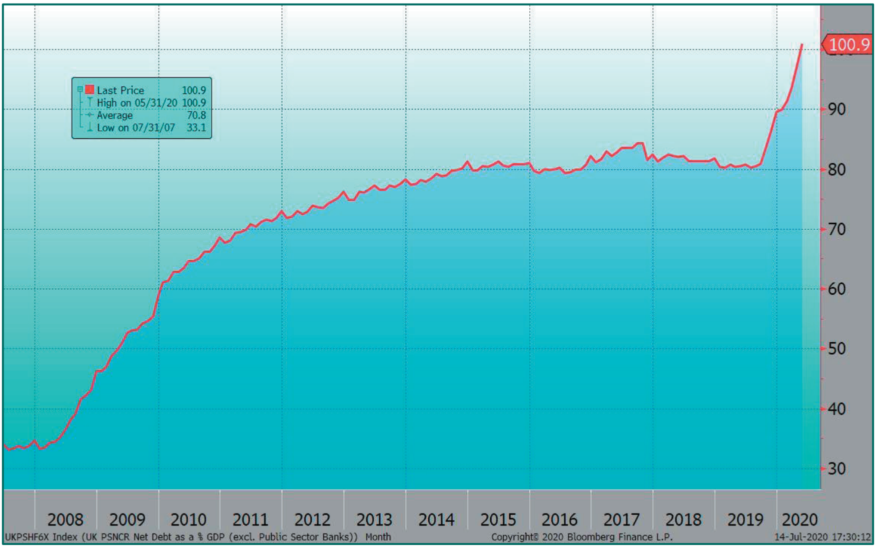
Extraordinary times require extraordinary measures. £75bn of support for employment, £28bn of support for businesses, £16bn for public services, etc. adds up rapidly. On the other side of the public accounts, tax receipts are plummeting, so the budget deficit is deteriorating fast and the Government is borrowing at a record pace (around £60bn per month) and public debt now exceeds 100% of annual output:

UK Public Sector Current Budget (£ billions)



Source: Berenberg, ONS

UK Public Sector Net Debt as % of GDP



Source: Bloomberg

THE ECONOMIC & MARKET BACKGROUND

The second quarter of the year was rather calmer for the investment markets. The swift action of central banks in March provided a firm base on which to build a recovery and the whiff of panic that pervaded in March gradually dissipated. Much has changed in a remarkably short period and we must get used to the reality that this change will be permanent in a number of areas. The problem for governments and politicians of all persuasions will be the management of this change and not succumbing to a desire to return to 'normal'.

Clearly, none of us can know with any certainty how the pandemic will play out. We are encouraged by the massive medical effort in support of vaccine development and other drugs to help with the treatment of COVID-19, but mystified by the antics of a number of the more shameful heads of state. We would still expect the virus to run its course within the well-known statistical pattern in due time, and this is probably still our central expectation, but, first, we must run the gamut of concerns over second waves and economic after-shocks.

As far as the investment markets are concerned, it really is all about the Fed. The US Federal Reserve under Chairman Jerome Powell has led the way in providing monetary support, closely followed by other central banks around the world. They have provided massive liquidity and continue to surprise with the extent of 'doing whatever is required'. The lessons of 2008/9 have been respected and their actions have probably insured that a nasty COVID-19 induced recession does not turn into a full-blown financial crisis with dire consequences for employment. What their actions have done is re-price assets after the collapse in March. Over the past three months, American stock markets have recovered the bulk of the losses incurred, while other stock markets have also recovered, though not by as much. Sadly, the UK markets are lagging, being over-represented in some failing industries.

At Church House, we remain upbeat and functioning normally. Daily meetings over the internet are now the norm, and this has produced some surprising benefits in corporate access. It remains to be seen how much damage will eventually be seen to have been done to our economy. While Europe is clearly recovering from the pandemic, the UK has been something of a laggard, but is improving. Let's hope that some good can come out of this (climate change policy? the demise of President Trump?).

James Mahon *July 2020*

As our Quarterly Report returns to printed form, we have made a few changes to the content. Most of the investment team are writing regular pieces now, all part of 'communication under lockdown', so I felt that it would be interesting to include a selection of these. I have cut back on a number of the more detailed statistics to do this, please let us know if anything is missing that you would like to see reinstated.

The UK Economy and Interest Rates

The UK economy is limping back to life as we emerge, blinking, from varying degrees of lock-down. Retail sales surprised with their strength in May, after sharp contractions in March and April, as on-line sales boomed. Confidence appears to be seeping back and unemployment figures have not (yet) been as dire as predicted, the furlough scheme has clearly been a huge success. A mini-budget is due shortly from the Chancellor, Rishi Sunak, I hope he can maintain the sure-footed behaviour that he has demonstrated to date.

To pay for the level of support that the economy is getting, the Government is issuing debt (borrowing money) at record levels. Adding around £60bn of debt per month over the past quarter, and this pace is unlikely to slow any time soon. While inflation and long-term interest rates remain as low as they are at present, this does not present a problem and the long-term health of the economy is the greater concern. But, if a decent recovery is secured, the Bank of England's Monetary Policy Committee (MPC) will face an interesting dilemma. With thanks to Barclays excellent *Equity Gilt Study 2020* for this great quote:

> *"Isn't it a shame that future generations can't be here to see all the wonderful things we're doing with their money?"* Earl Wilson, American journalist and commentator (1907-1987)

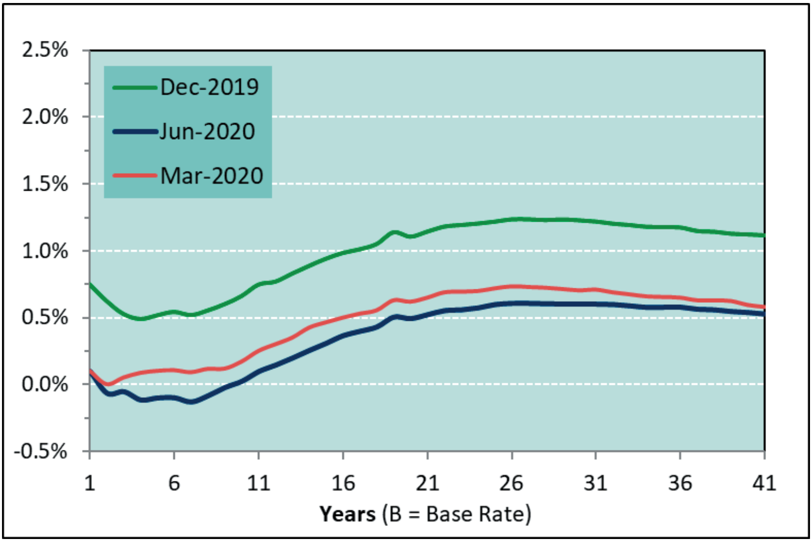
Of course, none of us can really estimate how the recovery will manifest itself, there are simply too many unknowns at present. COVID appears to be in retreat but the UK's record on this has not been without blemish, Europe appears to have made a better fist of it, but either could suffer a relapse. The shock of the changes brought on the economy at such pace could easily trigger a really unpleasant employment shock. I tend to the optimist, but governments and companies do need to exhibit a degree of agility that they have not always been noted for. Back to that Barclays *Equity Gilt Study* (now in its 65th year), this from their introduction:

> There was the world before COVID-19. And then there was the world after. A world which, in our view, stands to change greatly over the medium to long-term, even if the pandemic fades.
>
> In "The post-COVID economy", we argue that greater awareness about health threats from close human interaction and travel, and a new focus on securing supply chains will change how corporates, households and governments behave. The global services trade, the rise of global 'mega-cities', international leisure and education; all these seemingly irreversible trends will likely change course. Global value chains stand to be re-configured, with 'just-in-time' and cost efficiencies being trumped by 'just-in-case' and a focus on resiliency instead. In the new economy, safety, self-reliance and sustainability should win over cost-efficiency and speed.

Meanwhile, the MPC is maintaining base rates at rock bottom levels (see below) and providing massive additional monetary support. This is by way of liquidity (buying Gilts in the market puts cash into the system) and purchases of corporate fixed interest securities in support of credit markets, which also puts cash into the system. This latter being particularly important as it allows companies to borrow at highly competitive rates, which they have been doing in record amounts.

This is how interest rates look now, note that rates out to around seven years are actually negative at the moment:

UK Interest Rates (Base and the income yield from Gilts) **– The Yield Curve**



Source: Church House, Bloomberg

Short-term:	Base Rate 0.1%	3-mnth LIBOR 0.1%	SONIA* 0.1%.

Longer-term:						
Gilt maturing in:	2 years	5 yrs	10 yrs	20 yrs	30 yrs	50 yrs
Yield**	-0.1%	-0.1%	0.2%	0.5%	0.6%	0.6%

Source: Bloomberg **Sterling overnight index average.* ********The yield to maturity, taking into account interest received and price paid.*

Our negotiations with the EU over Brexit will be returning to centre stage over the next few months. With the UK refusing to extend the transition period beyond 31st December, we have less than six months to agree on our future relationship. In practice, we *ought* to have an agreement in place before the mid-October European Council meeting, allowing November and December to ratify the deal. This will be tight, expect all-night sittings (presumably on Zoom).

Credit Market Commentary – Jeremy Wharton

The US Federal Reserve continued its corporate bond buying program, after switching from buying Exchange Trade Funds to purchasing individual bonds in the secondary market, to create its own index. The Fed has only bought $1.3bn of bonds so far, but has capacity to buy $250bn. They can include bonds from American subsidiaries of foreign companies, which has raised questions over whether their funds are correctly targeted, but I would point out that the Bank of England (the Bank) and the European Central Bank (ECB) have already been doing the equivalent. The Fed also have the capacity to buy $500bn of new issuance but are yet to use this facility. Not surprisingly, this continues to support credit spreads and, in the face of volatility due to worries about a resurgence of virus cases in the US (thanks to the incompetence of those in charge), spreads have been resilient.

Hertz is the biggest bankruptcy of 2020 so far. Its bondholders have seen the stakes raised as it seeks to convert the master lease over its asset-backed securities, containing 494,000 vehicles leased to the rental company, into 494,000 separate agreements so that it can reject a third of them, save $80mn a month, and exit bankruptcy as a going concern. Not great for the holders of those credits (and see opposite for the experience of hapless equity investors).

The ECB has its own brand of financial engineering in times of duress. It is fair to say that their Pandemic Emergency Purchase Programme (PEPP) has mitigated much downside risk, but with it having a limited effect on stimulating inflation towards their target it looks as though they will have to conduct more, much more, asset purchases than they have already committed to. There is speculation about a further €1.5tn over and above what has already been planned (!)

The summer slowdown in issuance feels as though it has come earlier this year, but the first half of the year broke all records. **BP** brought the largest corporate hybrid deal ever, which was well received and has traded strongly in the secondary market. In contrast, **BBVA** came to market with just a £300mn issue, which was over-priced, and they were only just able to raise the money.

Lack of liquidity in the market has impacted the pace of the Bank of England's modest corporate bond purchase plan, but is therefore supportive to spreads and they are busy enough with their other, extended, Gilt purchase plan. UK government debt rising to more than 100% of GDP, for the first time since the 60's, means that future generations will certainly still be dealing with it. The Bank's Governor, Andrew Bailey, stated the obvious that the business landscape has changed to such an extent that some previously viable companies would collapse. Rishi Sunak continues to have empathy with the human side of this situation and his mini-budget of £30bn aimed at younger generations and those sectors hardest hit, had merit, despite being rather cynically received by some.

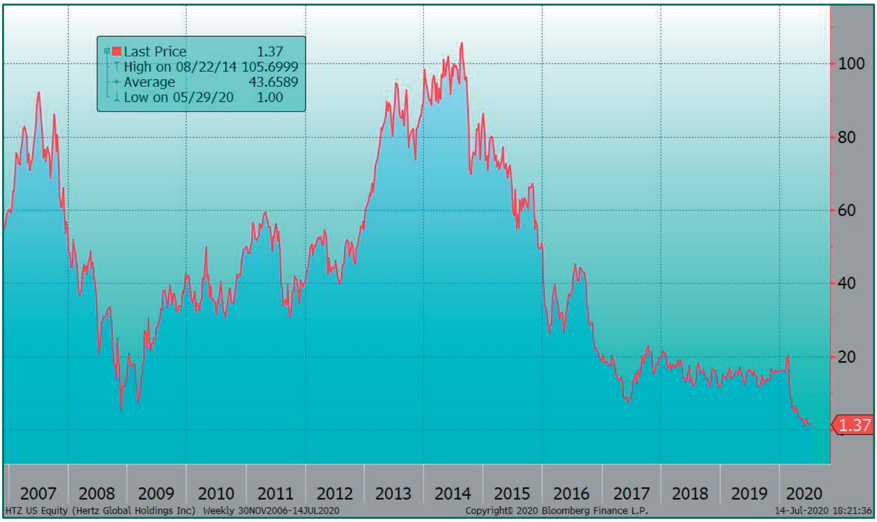
Jeremy Wharton *July 2020*

This first chart shows the (enormous) scale of the US Federal Reserve's balance sheet as a proportion of national output (in red) and the Bank of England's (in blue). The Fed's balance sheet used to run at around 5%/6% of annual output, but jumped as they came to the rescue during the financial crisis and its aftermath. Until the pandemic, they had been doing a good job of gradually bringing it back down again…

US Federal Reserve and Bank of England Balance Sheets as % GDP

Source: Bloomberg

Hertz Coproration was re-listed on the New York stock Exchange in November 2006 (it had been a subsidiary of Ford for many years), it has not been a happy experience:



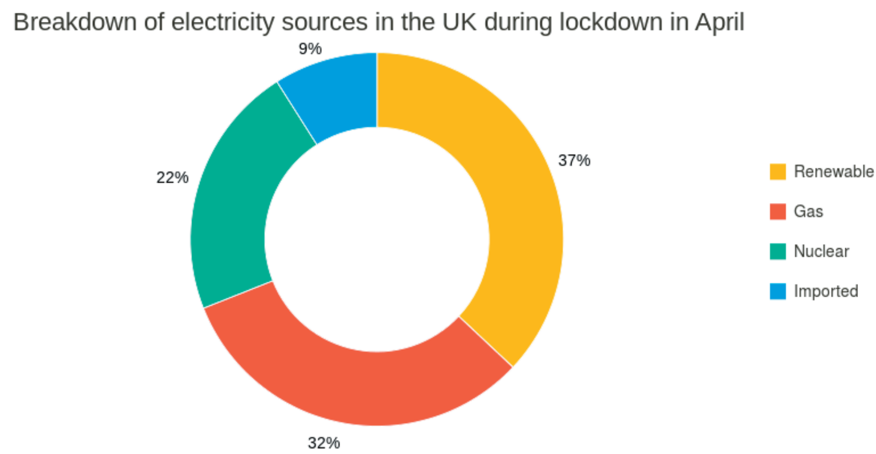
Source: Bloomberg

COVID-19: A renewed Opportunity to Tackle Climate Change

So far 2020 has not been the year we anticipated when clinking our glasses on New Year's Eve. The first few months saw raging bushfires in Australia, locust swarms in sub-Saharan Africa and flooding in the UK. Little did we know that this was to be followed by the coronavirus changing the shape of our daily lives - possibly forever.

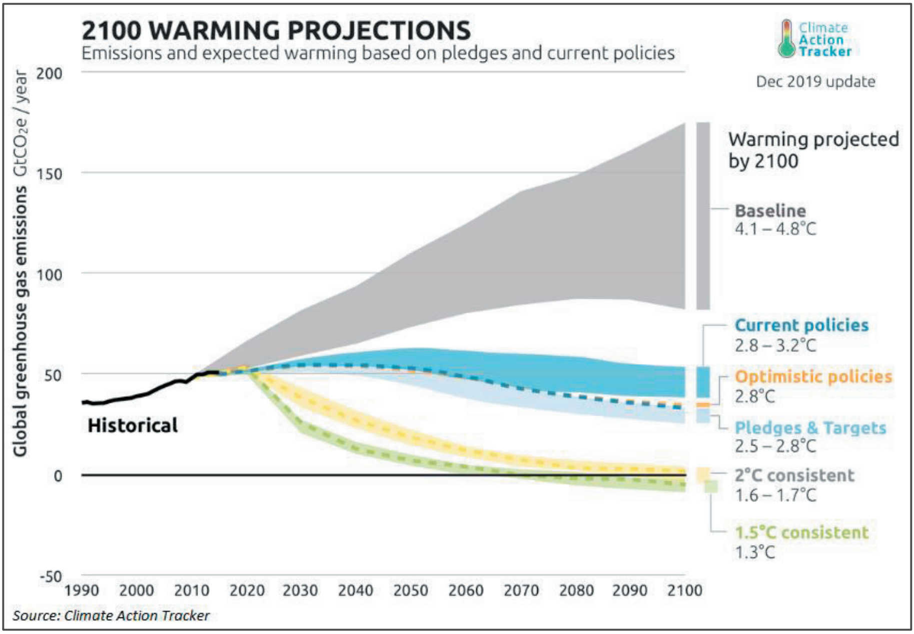
The outbreak of COVID-19 has created tremendous global disruption: the threat posed to human life has prompted a third of the world to go into lockdown and, as a consequence, world leaders now face the challenge of retrenching what the IMF are saying will be the worst economic recession since the Great Depression.

One could be forgiven for thinking that the planet has suffered enough but, like many things, amongst all the chaos there is often a silver lining. In the short time since households first closed their doors to the outside world, the planet has begun to return to its 'natural rhythm'. *The Economist* reported that the water in the canals of Venice is now running clear, ocean life is venturing up to ports, and a general notable increase in water and air quality (with a 50% drop in toxic particles in some big cities, according to *The Independent*). The MSCI has already predicted global emissions this year to be 2.1% lower than in 2019 in their blog, 'Will coronavirus reduce emissions long term?' This represents an impressive 8.3% drop from the carbon emissions forecasts for 2020 prior to the pandemic. In April, the UK broke a new record: the longest continuous period of time using coal-free power generation since the Industrial Revolution. As a result, renewable energy accounted for 37% of electricity supply, a significant contrast to 2012, which saw coal supply 43% and renewables only making up 7% (see pie chart below). This increase in supply of renewable energy was aided by an almost 20% decrease in demand for electricity, as well as powerful winds and an abundance of sunshine.



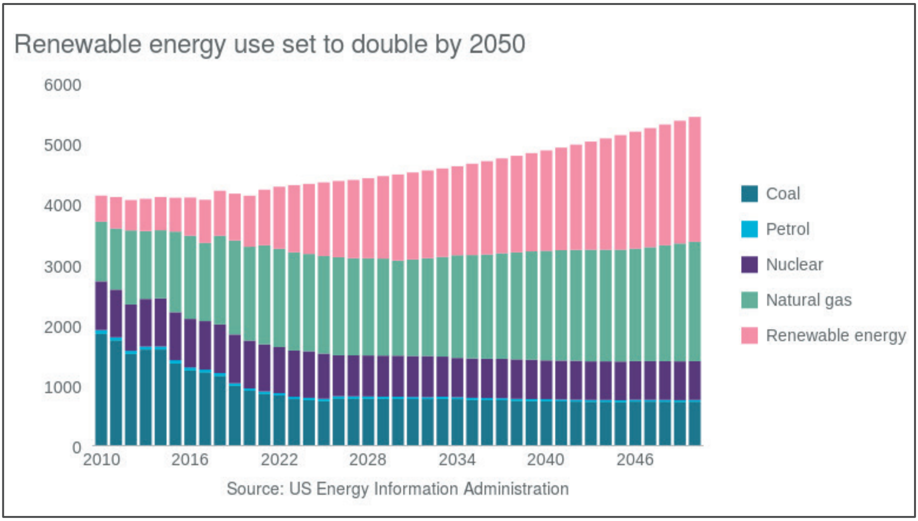
Source: Carbon Brief. Date ranges 9-28 April 2020.

According to analysis from Carbon Brief, where “Five key datasets and projections are identified, covering roughly three-quarters of the world’s annual CO2 emissions”, the virus-driven lockdown could result in 2020 having the most significant annual drop in carbon emissions than any past financial crisis. However, this is not enough to reach the 1.5 degrees c. Paris Agreement, with an annual decrease of 7.6% needed over the next decade (see chart). It is important to recognise that the reductions in emissions we have seen so far are unlikely to hold, with the MSCI predicting that an increase back to usual high levels once lockdown has been lifted, is inevitable.



However, the visible effects of climate change and the environmental impact of the global lockdown could be driving factors towards a re-evaluation of ethical and environmental considerations - both in government policy, as well as increased awareness, and action at an individual level. An economist at University College London wrote in *the FT* that: “We may now see a similar symbiosis between a new way of thinking about the economy and new policies and institutions to tackle climate change and guard against future pandemics.” We can only hope that something constructive can come out of such calamity.

In the UK, the Committee on Climate Change (CCC) released a report highlighting the opportunity to retrain those who have been made unemployed as a result of COVID-19 in ‘green’ industries across the country. The CCC Chairman, Lord Deben, said: “The Covid-19 crisis has shown the importance of planning well for the risks the country faces… The government must prioritise actions that reduce climate risks and avoid measures that lock-in higher emissions”.



We now have an opportunity to speed up the transition to a net-zero economy and become better prepared to tackle the ever-more imminent issue of climate change. With the help of governments changing their environmental policies, and companies meeting their environmental targets, or even surpassing them, we could move into a more sustainable future and stop our reliance on fossil fuels. This pandemic has certainly caused a lot of harm, but if we can create one positive, why not make it the catalyst for moving the UK to cleaner energy and a net-zero economy?

Harriet Evans *May 2020*

Commodities

	30 Jun 2020	31 Mar 2020	Quarter
Oil – Brent (barrel)	$41.2	$22.7	+81.5%
Gold (troy ounce)	$1782.5	$1591.5	+12.0%
Copper (25 metric tons)	$6015	$4951	+21.5%
Commodity Price Index	138.0	121.8	+13.3%

Source: Bloomberg

After the collapse in oil prices over the first quarter, the major oil producing nations attempted a patch-up of their differences and prices bounced back. Despite this dramatic rise, they remain around 40% lower than early January levels, with question marks over the likelihood of a return to 'normal' levels of demand. More encouraging has been the recovery in the price of copper, which is back to January's levels and is more of a bellwether for the world economy.

UK Equity Markets

Index:	30 Jun 2020	31 Mar 2020	Quarter
FTSE All-Share	3419.4	3107.4	+10.0%
FTSE 100	6169.7	5672.0	+8.8%
FTSE Mid 250	17152.5	15101.1	+13.6%
FTSE Small Cap	5011.7	4262.5	+17.6%
FTSE AIM All-Share	883.0	682.3	+29.4%

UK equities did recover over the quarter, but it was rather lacklustre as the headline indices were held back by continuing poor performance from a number of the heavyweight companies. The weak relative performance of the FTSE 100 Index in our table, by comparison to the smaller company indices, underscores this and is illustrated below:

FTSE 100 (dark blue) and AIM 100 Indices –2020

Source: Bloomberg, FTSE International

All the banks have suffered over the year to date (they are also not being allowed to pay dividends at the moment): despite the rally, **Lloyds** is still down 50% over the year as is **RBS**, while the others are not far behind. Big oil is struggling, **Royal Dutch Shell** and **BP** still being 35%/45% lower over the year and, naturally, the travel and hospitality companies: **Whitbread** (Premier Inns), **IAG** (British Airways) and **Carnival** having halved in value. There are bright spots: **Ocado**, **Reckitt Benckiser**, **Astra Zeneca**, **Halma** and **Spirax Sarco** are ahead for the year. But these were the exceptions in the FTSE 100 and the sheer scale of the first group (rather less now) has weighed down the index.

The sheer pace of developments has left company analysts with a difficult task in keeping up with individual company's prospects, naturally enough, estimates is what they are at present. Though one benefit we have found during this period has been improved access to company managements. It is much easier to organise a video conference than a round table discussion and most company managements welcome the interaction. We expect that this is another thing that will persist in a post-COVID world. Though, having said that, we will return to visiting companies, which is something that we do miss.

As shown in the table below, earnings estimates for the year ahead have come down markedly, and dividends are an area of particular uncertainty at the moment. It would seem likely that many companies will take the opportunity to retain the lower levels of dividend that are being paid (or not) at present.

Fundamental Valuation Indicators

FTSE All-Share Estimates*	30 Jun 2020	31 Mar 2020	31 Dec 2019
Earnings (per Share)	260.5	294.8	329.2
Price / Earnings Ratio	13.1	10.5	12.7
Earnings Yield	7.6%	9.5%	7.8%
Dividends (per Share)	144.0	183.4	189.6
Dividend Yield	4.2%	5.9%	4.5%
Dividend Cover	1.8X	1.6X	1.7X

**Bloomberg aggregate earnings estimates for the year ahead*

Fred Mahon discusses some of this in the next article, the first of a series:

'Everybody has a plan until they get punched in the mouth'
Mike Tyson

COVID-19 has laid a powerful blow to all of our best-laid plans for 2020. The human tragedy is of course the primary distress and never in my lifetime has the importance of the scientific and medical professions been clearer. In this series of thematic articles, I will be taking a look into how the world of business has coped during the outbreak and picking out a few examples of companies that are weathering the storm best in 2020. I will attempt to pick-out the key factors that have allowed these businesses to perform under stress and which I believe will allow them to come out on top in the future.

In a recent interview, Sir Martin Sorrell (the powerful and equally controversial advertising mogul), said that:

> *'Now all bets are off because Q2 is going to be a bloodbath … And so now the gloves are off, there's no status quo to upset, there's no applecart to upset, so you might as well get on with it.'*

Sir Martin went on to argue that now more than ever "agility is the key corporate attribute". I wholeheartedly agree with Sir Martin on this point and it has been fascinating to see how businesses have adapted to COVID-19 conditions. **L'Oréal** (a Church House holding) have form in leading the way with innovation and they certainly have not let us down in recent months. As the lockdown took hold, the cosmetics giant increased their online budget from 50% of their total marketing spend to over 70%.

L'Oréal were already comfortably ahead of their global consumer goods peers in moving online and with features such as virtual try-ons (give ModiFace a go!) and one-on-one beauty consultations via video chat reportedly seeing lots of interest. I am confident that L'Oréal will have extended their lead in ecommerce this year. The combination of innovation that was already underway with a rapid response to challenging conditions has, to paraphrase L'Oréal's Chief Digital Officer, allowed them to achieve in eight weeks what it would have otherwise taken them three years to do.

Snap Inc (Snapchat) is another example of a business that moved rapidly from the start of lockdown to remain relevant to their customers, accelerating the development of new Snapchat Originals content, such as 'Will From Home' (starring Will Smith) and 'Frontline Heroes'. This has won Snap millions of new subscribers in a fraction of the time that this might usually take. **ByteDance** (owner of **TikTok**) goes down as one of the great success stories during lockdown as use of the 15-second video platform has gone through the roof. TikTok is the most downloaded app in America this year and they now have over 800 million monthly active users.

Now compare these nimble and innovative businesses to companies that do not have such flexibility due to factors like high debt, crippling dividend targets or a cash-hungry asset base. Imagine being an oil company that has seen revenues more than halve in Q1 as the oil price fell from $80 to $30 (I have rounded here), but you still have investors that expect to be paid their cash dividend and oil fields that still cost the same to run. Equally, cruise ships and planes that are not allowed to take customers but still need to be maintained or multinational banks with a long heritage in Hong Kong that are surely more concerned with Chinese/Hong Kong politics than innovation during this pandemic. Even if these types of business did want to be proactive in adjusting to the lockdown, their ability to do so is limited by their circumstances.

This covers just a few examples, but I hope my point is clear that businesses that had flexibility going into COVID-19, and leadership that took positive actions to adapt to the crisis, are those that have performed best. These companies have already made great headway on their peers that were slow or unable to react and this advantage will only increase in the months ahead.

Fred Mahon June 2020

International Equity Markets

Index:	30 Jun 2020	31 Mar 2020	Quarter*
US - S&P 500	3100.3	2584.6	+20.0%
US - NASDAQ	10058.8	7700.1	+30.6%
UK – FTSE All-Share	3419.4	3107.4	+10.0%
Germany - DAX	12310.9	9936	+23.9%
France - CAC 40	4936	4396	+12.3%
Switzerland - SMI	10045	9312	+7.9%
Japan - TOPIX	1558.8	1403.0	+11.1%
Brazil - Bovespa	95056	73020	+30.2%
China – Shanghai Comp.	2984.7	2750.3	+8.5%
Hong Kong – Hang Seng	24427	23603	+3.5%
Australia – ASX 200	5897.9	5076.8	+16.2%

**Change in local currency*

A positive table right across the board after the damage inflicted in the first quarter. UK stocks look quite dull by comparison, Switzerland and China had a much better first quarter, Hong Kong is clearly (and sadly) a special case. American stocks did, briefly, get back to beginning of the year levels but have faded since. The US NASDAQ index, which is much more focussed on technology companies, is comfortably ahead for the year (see below). Other markets have also been strong, but have yet to regain pre-COVID levels.

S&P 500 and NASDAQ Composite Indices - 2020

Source: Bloomberg

These moves have caused some consternation but overall there is a solid rationale in the light of sovereign bond yields. The US 'risk-free' rate, the ten-year US Treasury bond yield, has more than halved over the year (1.9% down to 0.8% currently), with a similar pattern in the UK (a jump in the equity risk premium if preferred), leaving stocks looking good value by comparison.

Of course, this has to be balanced against what the COVID-19 recession will do to corporate earnings, which will be significantly lower in many areas. At which point it gets much more complex and one can no longer talk about 'markets' in general terms, it is down to the mix of companies within the various indices/markets. The US market has (rightly) benefitted from its heavy weighting in major technology-related companies (Apple, Microsoft, Amazon, Alphabet, Facebook, etc.), who are likely to see little earnings damage or improvements, hence its out-performance.

The actions of the US Federal Reserve in support of credit markets have been critical (and very welcome). Companies have been able to raise funds, at highly competitive rates, either to bolster their finances or establish firepower for expansion. Naturally, it has been easier and cheaper for corporates with good balance sheets to raise funds, something that will only accelerate the trend to the strong getting stronger.

The sharply contrasting moves in different sectors and individual company share prices has left some stark pricing differentials, mostly between the 'winners' in technology and healthcare and the 'losers' in the financials, leisure and oils. If the recovery does take hold and the COVID picture improves (notably in America) we could easily see a reversal of this picture. Commentators are pointing out the apparent extremes in value vs. growth investments at present, we would just observe that such broad categorisations do tend to miss a lot.

Foreign Exchange

	Cross Rate:	**30 Jun 2020**	**31 Mar 2020**	**Quarter**
£	$/£	1.237	1.241	-0.3%
	euro/£	1.100	1.128	-2.5%
	£ Exchange Rate Index	75.5	77.8	-3.0%
$	US$/euro	1.125	1.101	-2.5%
	Yen / US$	107.8	107.8	0%
	Renminbi / US$	7.06	7.08	-0.3%
	$ Exchange Rate Index	97.3	99.2	-1.9%

Source: Bloomberg

Foreign exchange markets have been quieter. Sterling was inclined to drift lower (expect more activity here as Brexit negotiations unfold) as was the US dollar. The euro benefitted from a clearer recovery picture, notably in Germany.

Church House Investment Grade Fixed Interest

	30 Jun 2020	31 Mar 2020	Quarter
CH Investment Grade* - Inc.	116.2	110.6	+5.1%
iBoxx AA Corporate 5-15 year	103.1	95.2	+8.3%
CH Investment Grade - Accum.	175.9	166.6	+5.6%
iBoxx £ ABS 5-10 year TR**	343.2	336.8	+1.9%

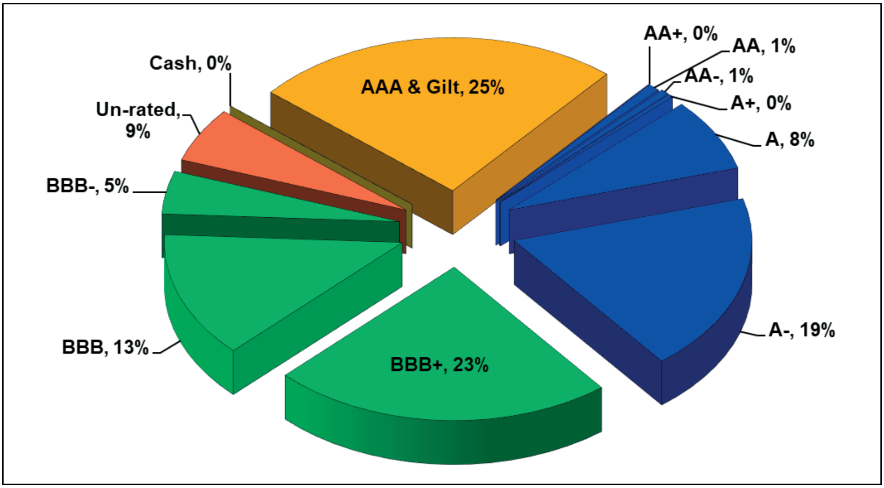
**bid price to bid price, excluding income.   **Total Return Index.*

We have had an unusually active quarter in the Investment Grade Fixed Interest portfolio as credit markets came to life. The profile of the portfolio has changed markedly over the period:

CH Investment Grade Fixed Interest	Jun 2020	Mar 2020
Short-dated Securities (less than 7 years)*	53%	74.0%
Medium-dated Securities (7 to 15 years)	33%	21.0%
Long-dated Securities (over 15 years)	14%	5.0%
Duration of Portfolio	5.2	2.9
Volatility (past year)	6.1%	5.4%
Number of Holdings	114	102
Yield	2.2%	2.2%
Portfolio Value	£360m	£353m

Volatility is annual standard deviation expressed as a percentage

CH Investment Grade Fixed Interest – by Credit Rating – 30 June 2020



Source: Church House

Top 15 - 30 June 2020	
Bank of America 7% 2028	2.5%
Goldman Sachs Group Inc 7.25% 2028	2.3%
ANZ Covered 1.380% 2022	2.0%
Royal Bank of Canada (SONIA) 1.18%	1.9%
GCP Infrastructure 8% 2044	1.8%
AP Moller-Maersk 4% 2025	1.8%
III Group 3.75% 2040	1.8%
M&G Plc 5.625% 2031	1.7%
Barclays Plc (Holdco) 2.375% 2023	1.7%
Southern Water Services 2.375% 2028	1.7%
Yorkshire B/S Covered (SONIA) 1.3%	1.7%
Orange SA Hybrid 5.875% 2022	1.6%
Citigroup 5.15% 2026	1.6%
SSE Hybrid 3.74% 2026	1.5%
Tesco Personal Finance Group 3.5%	1.5%

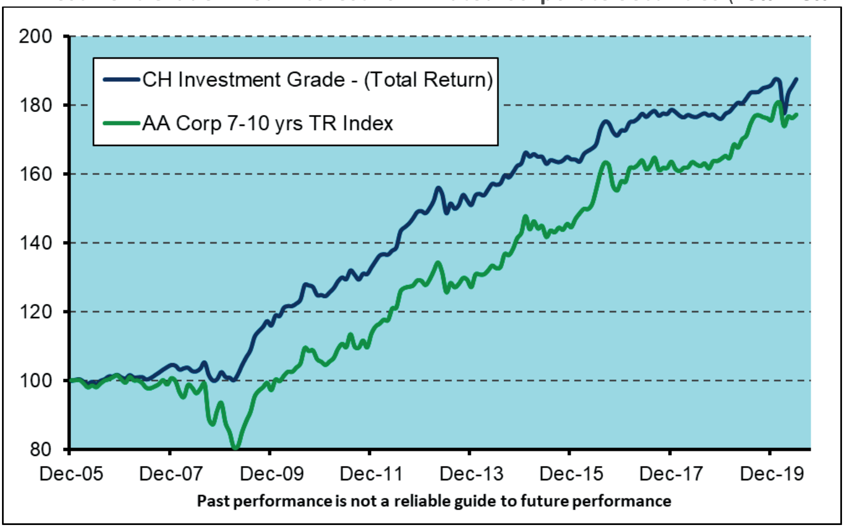
June started with cash from sale of **Lloyds** Covered FRNs, we had tendered three tranches of short-dated bonds. We added to our **Close Brothers** and **Orange** holdings and took profit from the new **Siemens** bond that we bought in May. We took several new issues, all have performed strongly in the secondary market. First was one from **Lloyds Bank** Corporate Markets followed by a **Legal and General** bond paying 5.625%. We switched out of our **SSE** 3.875 bonds, due to be called in September, into a new issue from SSE with a call in 2028. We took some longer issues, notably the rolling stock leasing company **Eversholt** issued a thirty-year, helping the duration of the fund to continue to move out, it now stands at 5.2.

Calendar Year Performance:

2020ytd	2019	2018	2017	2016	2015
0.9%	5.6%	-1.5%	3.3%	4.6%	0.1%

Source: Church House, bid price to bid price, accumulation units.

CH Investment Grade Fixed Interest vs AA rated Corporate Securities (Total Return)



Source: Bloomberg, Church House

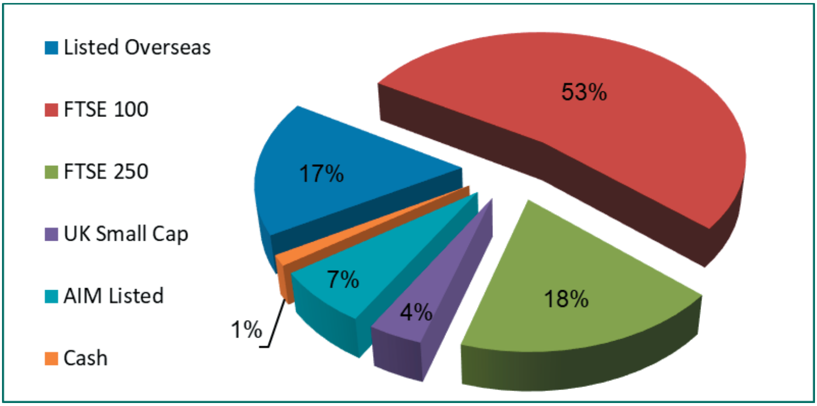
Church House UK Equity Growth

	30 Jun 2020	31 Mar 2020	Quarter
CH UK Equity Growth*	164.2	144.8	+13.4%
FTSE 100 Index	6169.7	5672.0	+8.8%
FTSE All-Share Index	3419.4	3107.4	+10.0%

** Bid price to bid price, excluding distributions of income (capital performance)*
Management fees are charged to income.

The UK Equity Growth portfolio recovered over the second quarter and we made some significant changes to underlying holdings. Here is the overall disposition:

CH UK Equity Growth – Disposition – 30 June 2020



Source: Church House

Rory Campbell-Lamerton and Fred Mahon write:

We continue to see plenty of opportunities in these volatile markets and this is reflected in recent activity. We look to be proactive in uncertain markets (such as we have now), and always to focus on the long-term fundamentals of the businesses that we invest in. We initiated two new positions during June, investing in antibody manufacturer **Bioventix** and **Greggs**, the purveyor of sausage rolls, both pork and vegan. These purchases were funded from the sale of **Royal Dutch Shell** and **BP.** We have been materially underweight in the major oil companies for a long time and decided that now was the moment to completely exit these positions. We no longer have any exposure to oil and gas within the Fund as we believe the sector is structurally challenged by the declining use of fossil fuels and that the dividend payments from these oil majors are not sustainable. The share prices of consumer goods giants **Unilever** and **Diageo** have continued to lag the market recovery and remain well below previous levels. We have added to our holdings in both businesses in June, investments that we have held in the Fund for almost twenty years. These are exceptional businesses and we are confident that they will come out the other side of 2020 stronger than ever. We also added to our positions in some more recent

Top 15 - 30 June 2020	
Halma	4.4%
Unilever	4.3%
Roche Holding	4.1%
RELX	3.9%
Diageo	3.9%
Smith & Nephew	3.8%
Diploma	3.7%
Spirax-Sarco Engineering	3.6%
Microsoft Corp	3.0%
Rio Tinto	2.9%
Schroders	2.8%
Croda International	2.8%
Investor AB	2.5%
Avast	2.2%
Intercontinental Hotels	2.1%

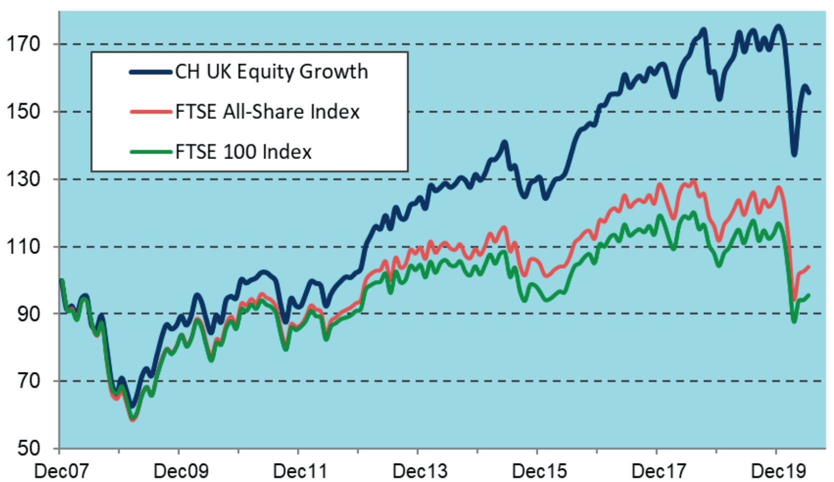
investments, namely **Trainline, Judges Scientific** and **IntegraFin,** as shares in these quality businesses slipped back. To highlight one expert analyst call, we had a fascinating afternoon hearing about developments in veterinary pharmaceuticals during the pandemic. This is especially relevant for our investment in **Dechra Pharmaceuticals**, known best for 'companion animal' (essentially, dogs and cats) drugs. We always believed that Dechra should prove relatively recession proof in that the last thing that people would compromise on is keeping their family animals healthy – this has been proven emphatically true during lockdown and, with the price of dogs and cats reportedly going through the roof, we think that Dechra has a busy few years ahead.

Calendar Year Performance:

2020ytd	2019	2018	2017	2016	2015
-11.0%	15.7%	-5.1%	9.0%	17.6%	1.7%

Source: Church House - bid price to bid price, accumulation units.

CH UK Equity Growth vs FTSE Equity Indices
Bid Prices, excluding income – Capital Performance



Past performance is not a reliable guide to future performance

Source: Church House, Bloomberg

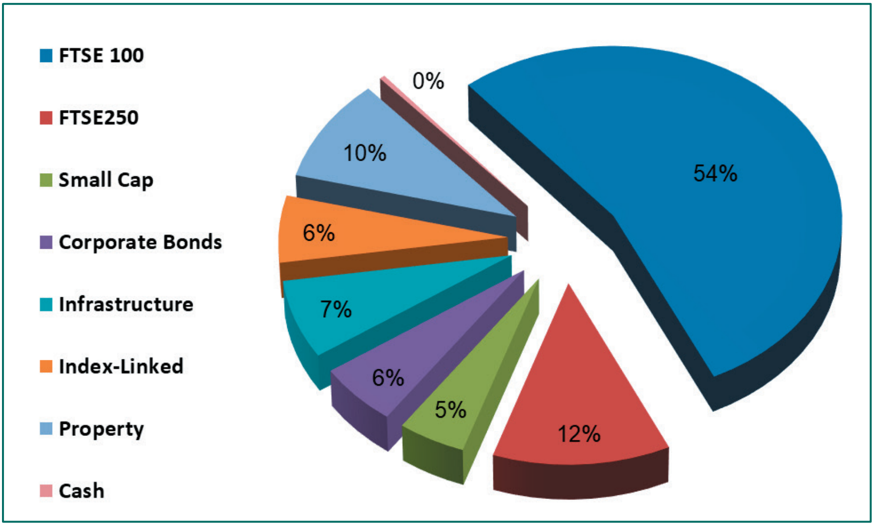
Church House Balanced Equity Income

	30 Jun 2020	31 Mar 2020	Quarter
CH Balanced Equity Income*	165.5	155.7	+6.3%
FTSE Higher Yield Index	2725.9	2622.7	+3.9%
FTSE All-Share	3419.4	3107.4	+10.0%
FTSE Index-Linked All Stocks	760.3	690.1	+10.2%
Composite Benchmark**	99.6	92.4	+7.8%

**Bid price to bid price, excluding income payments (capital performance)*
***36% FTSE Higher Yield, 42% FTSE All-Share, 23% FTSE Index-Linked All-Stocks Indices.*
The management fee in CHBE is split 50/50 between capital and income.

The Balanced Equity Income portfolio recovered over the quarter but was held back by the dire performance of so many of the major companies, as illustrated above in the performance of the FTSE Higher Yield Index. This was the disposition at the end of the quarter:

CH Balanced Equity Income – Disposition – 30 June 2020



Source: Church House

Having added to a number of the core long-term holdings in the dark days of March, this was a much quieter period with fewer transactions. Stock prices did dip again in mid-May and we used this to add further to **Berkeley Group** and **Shaftesbury**. The catering group **Compass** raised a further £2bn in a placing of new shares in May (in which we participated). We like this company and are long-term holders, but they have omitted their interim and final dividend payments this year, while awaiting developments. Many companies have done this and many of the financials are not permitted by the FCA to pay dividends at present.

Top 15 - 30 June 2020	
GlaxoSmithkline	3.9%
RELX	3.3%
AstraZeneca	3.2%
Halma	3.0%
Barclays FRN	2.9%
Unilever	2.7%
Smith & Nephew	2.6%
Croda International	2.5%
Diageo	2.4%
Rio Tinto	2.4%
BHP Group	2.3%
Civitas Social Housing	2.2%
Sage Group	2.2%
Royal Dutch Shell	2.1%
Primary Health Properties	2.1%

What is sensible management for Compass Group and probably prudent behaviour by the FCA, does though present a problem for an income portfolio like Balanced Equity Income. We are most unlikely to be able to maintain the level of income that the portfolio has been providing over the past few years without the stream of dividend payments. Let us hope that this is a temporary situation.

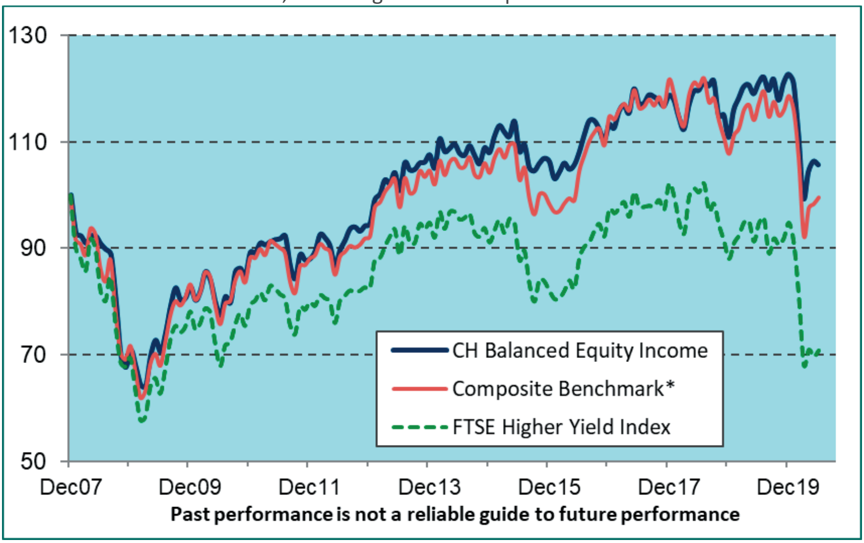
On the fixed interest side of the portfolio, we accepted a cash tender offer for our holding in a short-dated FRN from **Lloyds** and added two new issues, one from **Barclays** and one from the utility **SSE**.

Calendar Year Performance:

2020ytd	2019	2018	2017	2016	2015
-12.6%	14.2%	-3.6%	8.3%	10.3%	2.0%

Source: Church House, bid price to bid price, accumulation units

CH Balanced Equity Income vs Composite Index* & Higher Yield
Bid Prices, excluding Income – Capital Performance



*Source: Church House *36% FTSE Higher Yield, 42% All-Share, 23% Index-Linked All-Stocks*

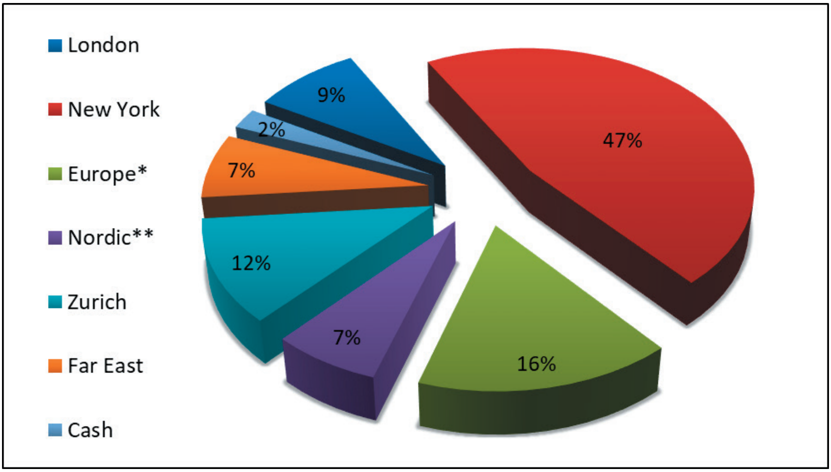
CH Esk Global Equity

	30 Jun 2020	31 Mar 2020	Quarter
CH Esk Global Equity*	321.9	272.3	+18.2%
CH Global Index in £	1020.1	855.6	+19.2%
FTSE 100 Index	6169.7	5672.0	+8.8%

** Bid price to bid price, excluding distributions of income (capital performance)*

The Esk Global Equity portfolio picked-up well over the quarter, in the wake of good performance from a number of the international holdings in the portfolio.

Esk Global Equity Constituents by Country of Listing – 30 June 2020



*Source: Church House *Amsterdam, Paris, Frankfurt **Copenhagen, Stockholm*

June was the most active. In the major sectors, we further increased our weighting to Staple Goods along with Healthcare and Technology, but, in contrast, we no longer have any exposure to Oil Production & Services companies. Gone from the portfolio are the remaining two oils: **Total** and **Phillips 66**, and, in a similar vein, we sold the remaining **BHP Group** to focus on **Rio Tinto** (our sole holding in the mining sphere). We sold all of our **Monster Beverage**, which had been a good investment for us, but after a solid increase over the year was looking fully valued. Around the same time, we participated in the initial public offering of shares in **JDE Peet's**, principally suppliers of coffee in Europe but also includes the Peet's coffee shop chain in America. Coffee also influenced a further addition to our holding in **Nestlé,** whose stock price had dipped in early June. We sold the smaller holding in **Henkel** after the rally, it had been a disappointing holding for us and though it is still a good company, it is difficult to see what will improve their rather dull performance. A lurch in the share price of **Essity** (a Swedish producer of personal care products) in early June gave us an opportunity to build a new position in this company.

Top 15 - 30 June 2020	
Microsoft Corp	4.0%
Roche Holding	3.3%
Nestle	3.1%
Amazon.Com	3.1%
Rio Tinto	2.9%
Alphabet Inc.	2.9%
L'Oreal	2.8%
Stryker Corp	2.6%
Unilever	2.6%
Lonza Group	2.5%
LVMH	2.5%
Johnson & Johnson	2.4%
Intuit	2.3%
Mastercard	2.3%
Illumina	2.3%

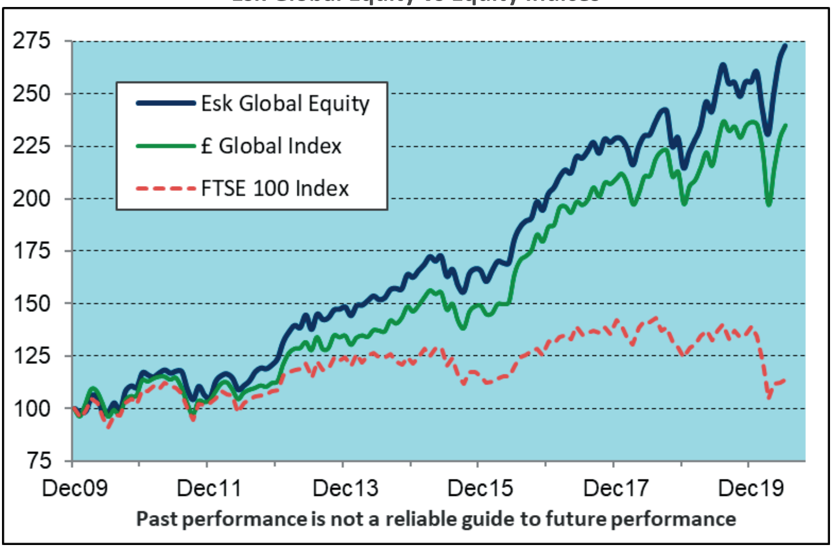
Lonza Group has been a star performer this year but, after a steep rise, the stock was in our top five so we reduced the holding. Around the same time we added to **Johnson & Johnson**, whose stock had drifted back. **Roche Holding**, had also drifted off in early June and we added there too. Returning to the portfolio is **Gilead Sciences**, last held in August 2014 (their share price was higher then). The stock looks appealing again and it is not surprising to see AstraZeneca expressing interest in a 'merger'. In Technology, we decided to take the profit from our holding in **SAP**, a good company but we felt that there were better opportunities to be found. We continued to build the relatively new position in **Mastercard** and added again to **Ansys**, and a new holding is **Verisign**, which provides domain name registry services and internet infrastructure.

Calendar Year Performance:

2020ytd	2019	2018	2017	2016	2015
+6.7%	20.2%	-5.6%	13.9%	23.1%	3.0%

Source: Church House - bid price to bid price, accumulation units

Esk Global Equity vs Equity Indices



Source: Church House Bid prices of income units (i.e. capital return, excluding income)

CH Tenax Absolute Return Strategies

Quarter and Calendar Year Performance	30 Jun 2020	31 Mar 2020	Quarter
CH Tenax Absolute Return Strategies	155.8	149.0	+4.6%

2020ytd	2019	2018	2017	2016	2015
-0.7%	3.4%	-1.7%	2.5%	7.6%	1.3%

Source: Church House, NAV to NAV, 'A' accumulation shares Portfolio value: £477m

A few weeks ago, one of our professional clients (a major investor in the Tenax Fund) requested some "high level thoughts" about the year ahead and what were the greatest risks/opportunities facing the Fund. This was our response:

The first general point that we should make is a reminder that we don't manage Tenax on the basis of economic/strategic prognostications for the year/period ahead. Naturally, we study many economic forecasts and analysts from a wide range of sources, many of whom have interesting points to make. But our decisions on investing Tenax are a response to the prices and values that we see in individual assets and classes of assets.

That is why we started the year with such high proportions in cash and near-cash (approaching 60% of the Fund's portfolio). We had no prescience as to the risks of a pandemic, we simply could not find attractively valued assets and viewed many as over-priced. As an absolute return fund, Tenax always returns to cash when we cannot see attractive alternatives. This table shows the development of our broad asset mix over the first half of the year:

CH Tenax Fund – Allocation to Asset Classes

	31-Jan-20	31-Mar-20	30-Jun-20	Since January
Cash	0.7%	7.4%	1.2%	0.5%
Treasury / T-Bill	9.1%	3.5%	3.2%	-5.9%
FRN (AAA)	47.0%	42.9%	33.6%	-13.4%
Floating Rate	5.2%	4.4%	3.1%	-2.1%
Fixed Interest	17.8%	19.1%	33.1%	15.3%
Index-Linked	0.3%	0.3%	1.2%	0.8%
Infrastructure	3.6%	4.2%	4.9%	1.3%
Convert / ZDP	8.4%	8.6%	9.3%	0.9%
Hedge Funds	0.0%	0.0%	0.0%	0.0%
Property / Real	1.5%	1.3%	1.4%	-0.1%
Equity	6.3%	8.4%	9.0%	2.7%

Source: Church House

The table shows the shift away from cash and near-cash after the markets broke down in March and we began to see opportunities. Most notably, the shift away from our favoured near-cash asset, AAA-rated floating rate notes (FRN).

Initially, when the markets broke down in late February/early March, we were concerned to ensure that we had plenty of actual cash available to avoid the risk of the recession collapsing into a credit crunch. As it became clear that the Federal Reserve (and other central banks) were acting quickly and in sufficient scale to avoid this risk, we shifted our focus to the credit markets.

Here are some high-level thoughts about the next twelve months and the biggest risks / opportunities that we see, from a Tenax perspective:

Gilts and other sovereign bonds. Following the massive intervention of the central banks (CB), these assets are even more expensive than they were at the start of the year. There really is no value to be found in the sorts of medium and long-term yields on offer. But we expect that this will persist for some considerable time as CBs will not wish to reduce their support until it is clear that we are out of recession. We have no interest in holding such assets on the basis of being able to 'pass the parcel' at some later stage.

Corporate Credit. This is the area of greatest interest to us at present, hence the big shift in Tenax' allocation. At the beginning of the year credit spreads were back in to 2007/8 levels and 'high yield' debt was anything but high yield. The crash blew spreads out again but, in late March, as CBs came in to support credit markets and a few new issues got away, this market came to life. Spreads have closed but there is still value to be had and an active new issue market.

Equities. This heading is probably too broad as markets moved from out-and-out panic in March to a much more selective situation since then. Hence a number of perceived 'winners', Amazon, Netflix, Roche etc. have moved ahead strongly and are now comfortably up for the year while the 'losers' are still on the canvas. In general terms, we added quite significantly to equities in March but switched our focus to credit from April onwards. We would be reluctant to make predictions for 'the market' as it is so disparate at present, but there is good value in some areas.

Convertibles. We have been pleased to see the convertibles market coming back to life over the past couple of months. This is an area that really attracts Tenax as the risk profile of a convertible bond (from a good credit) ideally matches what we seek. We are actively looking to increase this weighting.

Infrastructure. This area went through similar gyrations to the equity markets with notable panic selling in the third week of March. We have been adding selectively in the area of availability-based infrastructure, energy storage and energy efficiency. More to come in this area, but particularly important to be close to the companies.

Rishi Sunak

Simon Walker **HM Treasury**

Rory Campbell-Lamerton writes: Born in Southampton to Punjabi Indian-East African parents and educated at Winchester College and Oxford University. Sunak became MP for Richmond, Yorks in 2015 succeeding William Hague, following a career in Investments with Goldman Sachs and The Children's Investments Hedge Fund. As Chancellor of the Exchequer since February 2020, Sunak had led the government to its most stimulating fiscal rescue packages since the Second World War, pledging to provide £362bn to date in a bid to stave off economic crisis for the nation…