TAM INTERNATIONAL INVESTMENT NOTE

Review of the Second Quarter 2015

The second quarter of the year was a stark contrast to the first, with both global economic and geo-political events souring investor sentiments, leading to some increased volatility and overall decline in financial markets. Positively, despite these sharp falls recorded in many markets, our portfolios performed well, mitigating losses and out-performing their respective risk benchmarks. Over the first half of the year the portfolios have all recorded solid absolute and strong relative gains.

Portfolios	2015 Year to date Return	2015 YTD Benchmark	2015 YTD Outperformance	3 Year Return
Defensive	+0.35%	-2.22%	+2.57%	+12.99%
Cautious	+2.00%	-1.40%	+3.39%	+18.74%
Balanced	+4.25%	-0.79%	+5.04%	+26.58%
Growth	+4.38%	-0.01%	+4.59%	+30.68%
Adventurous	+5.39%	+0.54%	+4.85%	+40.33%
Speculative	+5.18%	+1.07%	+4.11%	+43.47%

Performance numbers are from TAM Premier GBP Portfolios and are net of all TAM fees.

The second quarter started on a positive note…

The second quarter can be viewed as one of two halves, albeit unequal ones. The first half of April and May saw a continuation of the positivity that drove equity markets to record and near-record highs. Indeed both the US and UK stock markets hit multi-year highs with the S&P 500 reaching 2,130 and the FTSE 100 index 7,100. Such was the positivity that even bad news was seen as good! The unexpectedly weak first quarter GDP numbers on both sides of the Atlantic were also greeted with acceptance. The thinking behind this positivity is that if growth is not too strong, interest rates will remain lower for longer. Indeed, given the central bank inaction and indications that the first interest rate hikes will not be until the fourth quarter of the year at the earliest, this seemed to be accurate.

The Greek saga rumbled along but was mostly ignored by markets who focused on valuations, a decisive UK election result, the benefits of cheap oil (although even oil regained some poise and moved back to US$65 a barrel), and the strength of the US dollar (hitting five year highs against Sterling for example).

Then we moved into June.

…But ended in a Greek tragedy

In June we were hit with the double barrels of the real possibility of a Greek default and exit from the Eurozone, coupled with sharp falls in the Chinese stock market, this had many commentators predicting the bursting of the speculative bubble that had driven the Hang Seng to lofty heights. The negative sentiment weighed heavily on financial markets, with equity markets selling off relatively aggressively. Major falls were seen in Europe where the fear over contagion and the renewed pressure that the euro trading block would come under (whether the Greece crisis was adverted or not) had a real impact, with the EuroStoxx 50 index falling over 8%. The UK was not immune, falling 6.6% from its highs by quarter end. Notably, the US equity market was less affected, only giving up 2.5% of its year to date gain.

With Greek banks shut, its political system descending into chaos and uncertainly regarding the forthcoming referendum - markets were unsettled. It is moments such as these where being able to look through the short term volatility and make rational decisions is essential. As we noted in our **'Stick to your principles'** investment note, we appreciated the volatility that the potential Greek default would cause but equally viewed it as a short term distraction from the improving fundamentals that would support markets over the remainder of the year.

We stuck to our principles, made some small changes to our fund selection detailed below but overall maintained our asset allocation and outlook. At the time of writing we have seen a resolution to the Greek issue (for now) and are enjoying a significant relief rally which we hope to be able to discuss in more detail next quarter.

The benefits of diversification

Such situations as these reinforce our belief and ethos that creating diversified portfolios with multiple sources of return offer greater comfort during times of market stress. When one asset class declines, others can often rise. Even within a declining asset class there are often geographical and sector opportunity. For example, whilst we have no direct exposure to the Greek stock market, we do to the broader European markets where we have seen attractive valuations and growth potential. Alongside this, however, we have exposure to the United States (which held up well compared to Europe) and to Japan. Our aim is to reduce the volatility (or risk) of our portfolios and dampen the impact of single market capitulation. This we successfully achieved in the second quarter as our portfolios out-performed their benchmarks.

A more defensive stance towards equity markets

As mentioned above our equity exposure remained relatively unchanged during the quarter, although we did reduce our overall exposure as the market appreciated during the early months. This reduction took us from a marginal overweight/neutral position to a marginally underweight/neutral position. By this we refer to the exposure to a given asset class against the exposure implied to the same asset class from the risk-profiled benchmark for a portfolio. For example, if a balanced risk portfolio has a neutral equity exposure of 50% we may have reduced exposure from 53% (mildly overweight) to 47% (mildly underweight). Our decision to reduce equity exposure was in part reaction to the volatility creeping into the market and the strong performance posted in the prior months.

At a sector level, as the quarter drew to a close we reduced our exposure to mid-capitalisation biased income focused funds which have served us so well, in favour of funds that focus in the larger capitalisation big-name stocks. We expect this process to continue into the third quarter. Many of these stocks (larger capitalised) are in unloved sectors which have under-performed the broader market this ear for a number of reasons, including the commodity and energy market rout. One such fund is the Investec UK Alpha Fund which focuses on the value, large cap sector. The fund is run by Simon Brazier who believes in investing in good firms that possess a sound business model, strong balance sheets and employ CEOs that will drive the firm to become the top performing company in their sector.

The investment process is a straightforward one which allows the manager freedom of mandate and is based on idea generation from the manager's experience, company meetings and external and internal research drawn from the considerable global research resources of the firm. Fundamental research analysis is carried out to determine valuations which are challenged and debated with all members of the team. The best ideas are used to construct a high conviction, risk-aware portfolio that is monitored by the EMA third-party risk system which assists in modelling. The manager has full discretion, responsibility and accountability for portfolio construction and balances the final allocation with consideration to benchmark, business and portfolio risk.

Whilst Simon has only recently taken the helm of the fund, he has a good track record of performance in his previous role as head of equities at Threadneedle (now Columbia Threadneedle). He outperformed the FTSE All Share in every year from 2010 to 2014, where the relative performance was accrued steadily and consistently. We are buying this Fund for prevailing market conditions.

Conditions for fixed income remain unfavourable

In contrast we continue to remain underweight in the broader fixed income markets, especially the government bond market which we reiterate (as we have for some time) is highly susceptible to future interest rate rises. It is interesting that the bond market dynamic in many developed nations has changed during the great quantitative easing experiment. The long held view that equity and fixed income markets are negatively correlated, for example, (when one goes up, the other goes down) has been seen to have been broken with both now often moving in concert.

However, as investors contemplated the withdrawal of quantitative easing and possible future tightening, bond market volatility has increased and exceeded that of equity markets. We have taken opportunity of this volatility to modestly increase our sovereign debt exposure on market dips. We believe this will not only offer some short-term return potential but also add further protection to our portfolios.

Not all that shines is gold!

Our view on the commodity sector remains unchanged. We believe the medium term fundamentals remain poor and hold no direct exposure. Interestingly despite its recent 'rally' oil prices remain weak and could come under further pressure given US stock piles are at fourteen year highs. Additionally, the possibility of lifting Iranian export sanctions will likely further increase supply, with little or no further demand. Gold continues its malaise given the strength of the dollar and low-inflation expectations. As an aside, even with the decline in gold prices there has been a few beneficiaries of this generally cited 'safe haven' asset – Russian investors have enjoyed an 80% gain in the value of their USD denominated gold holdings given the recent collapse of the Ruble.

Further investments in 'bricks and mortar'

During the quarter we increased our already overweight property exposure, believing the attractive yield still generated by the sector is a compliment to our other holdings and an ideal substitute, for now, to our underweight fixed income exposure. We continue to be focused on the very diversified and quality end of the commercial property space, principally in the UK. The funds we invest in are large with hundreds of investments in warehouse, retail parks, and other commercial premises. To increase our diversification even further we have added a position in the **Standard Life Global Property Fund.** The fund is designed to give investors access to the best global opportunities within the real estate market. The main bulk of the fund's investments are in direct 'bricks and mortar' properties, with satellite holdings in a number of real estate investment trusts (REITS).

By 'Bricks and Mortar' we refer to investment in real, physical buildings. As we are all aware the buying and selling of properties can be a fraught and cumbersome affair often taking far longer that we initially anticipate. It is important therefore to invest in highly diversified funds with many varied (and hopefully uncorrelated) underlying properties. We anticipate this will improve the liquidity of the fund and allows us to realise our investment more efficiently. REITS, by contrast are closed-ended funds traded on the stock exchange that can invest directly, indirectly or into the shares of property related companies. They are very liquid but can be highly affected by the vagaries of the equity markets and general sentiment rather than by the underlying value of their property holdings. Consequently they often trade at a discount or premium to their underlying asset value.

The manger of the Standard Life Fund starts by investing at the country sector level with markets displaying underlying price inflation, steady consumer growth and a buoyant property market with positive year on year capital appreciation. Once these macro markets are identified, the team looks for investment opportunities with the right indicators such as underlying value, average lease length, tenant default rate and opportunities within the structure to yield greater rental income. If the market identified presents attractive investments, but also regulation and taxation headwinds, then the fund will switch into listed real estate investments to ensure the underlying investor in the fund still gains access to the portfolios best ideas.

Overall however we remain very vigilant to any turnaround in this market as the funds in poor market conditions can quickly trend to illiquidity.

Absolute return offers consistent performance

We remain overweight in the absolute return sector, viewing our investments as both alpha-generative and, again, a good substitute for our reduced fixed income exposure. The sector has not performed as well as one would have expected over the quarter due to the high volatility and stock correlations we have encountered. Long term however, we believe these 'all weather' investments have the potential to add above inflation return to portfolios.

In conclusion

We have a mildly positive equity outlook for the remainder of the year and 2016. We see good ongoing potential in the equity markets and will seek to exploit the opportunities presenting themselves through the divergence in monetary policy across the globe. We see opportunity in both the European and Japanese equity markets and, in broader geographical terms, the larger and mega capitalization stocks that have underperformed their smaller mid-cap compatriots. Given the heighted currency volatility we have experienced this year, we will continue to focus on situations that offer the ability to hedge out the currency effect and allow us to capture the full market gains on offer.

The gorilla in the room remains the debate over when the US Federal Reserve will announce their first interest rate hike, as this will set the tone for the investment landscape for many years to come. We are positioning our portfolios in expectation of this move but believe the recent economic releases, including weaker harsh-winter induced lower GDP growth in the Q1 and a noted fall in inflation, plus the knock-on effects of the Greek 'Grexit', could be enough to defer any change in interest rates until the end of the year at the earliest. We remain vigilant for this and other events we see on the horizon.

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