ASTUTE
INVESTMENT MANAGEMENT

VT Astute Funds

Quarterly Commentary

Q3 2020

Introduction

Thank you for taking the time to read our Q3 commentary. First and foremost, I hope that you and your loved ones all remain safe and well. We're all living through strange times, but it is important to keep the events of financial markets in perspective.

Since this is our first full length commentary, I thought I would include a brief introduction to its format. To the right, you will find some high-level thoughts on markets and a regular reminder of Astute's philosophy and approach to asset management.

In our **Astute Overview** section, we will look in more detail at one or two topics of particular relevance to the quarter just behind us, or the one we are heading into.

Astute Perspective will cover how we currently see the world and our conviction views on markets, while **Astute Positioning** shows how those views translate into the portfolios and how that has driven returns over the quarter.

Finally, **Astute Observations** highlights some of more interesting research, data or charts we have encountered recently with a few short and hopefully enlightening comments.

As always, we take a long-term approach to investing our client's assets, but success is a journey not a destination and the short-term views expressed herein are aimed at managing risk and making your investment journey as smooth as possible. By taking a risk adjusted approach to your investments, we aim to deliver reliable growth in line with our stated risk profiles and provide you and your financial planner the consistency and security to plan for your long-term financial future.

Thank you for your continued support. If you have any further questions or require any additional information, please don't hesitate to contact your usual financial planner.

Fund Management Team

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Near term pain, long term gain

Autumn feels like a good place to write our first commentary because it is typically when we harvest and celebrate the spoils of the summer, but also prepare ourselves for the approaching winter. Markets certainly enjoyed the summer, recovering, and in some cases surpassing pre-pandemic highs. However, the winter ahead looks challenging as we grapple with political risk, the withdrawal of economic support measures and perhaps most importantly, a second wave of coronavirus.

While the next 3 to 6 months may be challenging, we remain positive on life beyond COVID-19. Much like a natural disaster, if the permanent economic damage can be limited, the recovery should be straightforward as the artificial break on growth is removed. An effective vaccine and resolution of short-term political risks will help to bring a degree of certainty to the future. Although the logistical challenge of global vaccination is immense, the question will become when, not if, the storm will pass. Similarly, as the US election is decided, (see our Overview for additional details) focus will turn to stimulus plans for the next 5 years, not just the next 3 months, which should also provide a more certain environment for companies to operate in. With so much short-term uncertainty, it is difficult to maintain a long-term perspective. However, our investment process is structured to tactically mitigate those short-term risks as much as possible, without losing sight of the big picture and our long-term growth objectives.

This exceptional uncertainty we have had to live with for most of this year has also driven greater divergence in company fortunes. While there are fundamental reasons for some companies to be worth substantially more than they were before the pandemic (who had heard of Zoom before lockdown?), there are also strong behavioural biases that contribute to performance. To demonstrate one such bias, simply imagine you are offered a bet with a 98% chance of doubling your stake, how much would you bet? Now consider the odds are 99%, did your bet increase by much? Finally, imagine the odds are 100%... If, like me, you don't think purely in probabilities, then I expect that last 1% made a much bigger difference. The absurdity of a guaranteed return aside, the lesson here is that the perception of certainty can be very valuable. Anything less than certain and our aversion to loss reduces our willingness to take risk significantly.

In markets, certainty is never guaranteed but the perception that a company, for example Amazon, will still exist in 10 years' time is very valuable. It has become even more valuable as the probability that other companies can prosper (or even just survive) decreases. As the number of things you can be certain about decreases, the more valuable that certainty becomes. Within the Astute funds, we are biased towards these types of quality companies precisely because of this certainty and the innate behaviour that drives people towards them. Despite volatile markets, these companies have proven to be one of our strongest areas of performance.

The key risk to this positioning of course is valuation. Irrational behaviour can create price bubbles and we remain very cognisant of this when sizing our positions. It is also something that is considered within the underlying funds that we own, and a key aspect of our research process is understanding which managers are more prone to 'overpay' than others. As a result, we retain our conviction that quality growth will deliver strong risk-adjusted returns if uncertainty persists, and that we can effectively manage the risk to this view through careful fund selection.

Finally, while we have these conviction positions, it is important to point out that we are never 'betting big'. Instead, we tilt the portfolios one way, and if we're correct we should marginally outperform. We will not get every decision right, but we aim to build towards our investment objectives with consistent, marginal outperformance and, crucially, avoid permanent loss of capital. After all, making money when you're right is not very difficult, the skill is in not losing as much when you're wrong.

Scott Osborne PhD CFA
Chief Investment Officer

Astute Overview

POLITICAL RISK – CONTESTED & CONGESTED

As we look towards the end of the year, the US election and the resolution of Brexit negotiations undoubtedly stand out as near-term risk events. Firstly, on November 3rd, the US goes to the polls, or crucially for this election, the post box. The fact that a large portion of the population will vote by post is creating a huge amount of uncertainty around the result itself. Current national polling has 77-year-old Joe Biden with a healthy lead and something like a 70-80%[1] chance of winning. However, polling analysis shows a much greater proportion of Democrats intend to vote by post. This means it could take significantly longer to count votes and that the early counts, based on voting in person, will likely favour Trump. This is particularly important in key swing states like Pennsylvania, Minnesota and Michigan where late counts are increasingly likely.

This dynamic, combined with the hyper partisan environment, Trump's well publicised (and widely discredited) claims about postal voting fraud, and his past refusal to guarantee a 'peaceful transition of power' suggests a close-run election result will likely be contested. The permutations of this are endless but it could quickly end up in the Supreme Court, as it did with Bush-Gore 20 years ago. The smoothest path for markets looks to be a Biden win so large it becomes untenable for Trump to cling on. In this scenario, the Democrats almost certainly also reclaim the Senate in a so called 'Blue Wave', significantly improving the odds of a substantial government stimulus bill based on Biden's 'Build Back Better' plan. There is still plenty of time for last minute surprises however, and the road to Inauguration Day on January 20th could still prove to be long and winding.

Which brings me rather neatly to Brexit. The stakes continue to rise as the end of the transition period approaches and, unsurprisingly, the hyperbole increases too. Prime Minister Johnson's gambit to grant himself the power to override the withdrawal agreement won't have improved the level of trust at the negotiating table, but it may be the clearest demonstration yet that the UK is willing to go it alone if it has to. This outlines the quandary for investors at the centre of the process. All parties agree a deal is in their shared interests and while it is tempting to say both sides need to go to the wire for a deal, at what point do the steps taken to sell the bluff become substantial enough to turn the bluster into irreversible policy?

One thing at least does appear increasingly clear. That is disruption will occur no matter what. This is a view perhaps best summarised by the British Chambers of Commerce dashboard for assessing the quality of official Brexit guidance. This summarises official answers to the thirty-five questions most frequently asked by businesses, seven of which remain red or 'wholly inadequate on which to plan' and nineteen are amber, indicating 'gaps and/or quality issues'[2]. Simultaneously, UK businesses are already living through a period of tremendous uncertainty and disruption with COVID-19 restrictions. So, while the cost to leaving with no trade deal in place may be higher, uncertainty and disruption seem inevitable in the short term either way.

Astute Response:

In the US, we do not intend to adjust positioning but merely brace ourselves for volatility and focus on the long-term outlook post the election. In the UK, we expect there will be a time in the near future to be more positive on domestic companies, particularly smaller and more dynamic ones, but we are not there yet. In both aspects we remain nimble and ready to adjust our positioning as we see risks develop or opportunities arise.

MONETARY POLICY – THE COVID ECONOMY

Central banks once again came to the aid of markets in the heat of the March correction, but unlike previous market falls, central bank spending was matched by unprecedented fiscal commitments from sovereign states. The cost of this intervention is ballooning budget deficits, which in the UK stood at £174 billion at the end of September[3]. That is three times what was originally estimated for the whole financial year. As a result, we will likely borrow more through 20/21, as a share of national income, than in any year in history outside the two World Wars.

Although the nature and size of the spend will likely be debated for many years, there is little argument that governments imposing lockdowns had little choice but to act. However, it does raise crucial questions about near term withdrawal of support measures, and also the long-term implications of the debt burden. Paul Johnson of the Institute for Fiscal Studies summarised this into four phases. Phase one, back in March, focused on protecting as many jobs and businesses as possible through the lockdown phase. The economic update in July marked the beginning of phase two, and was designed to boost demand and improve animal spirits through incentive schemes like Eat Out to Help Out and reduced Stamp Duty (see Astute Observations on the back page).

Had we avoided a second wave, the Autumn budget would likely have included further measures aimed at boosting demand and stimulating a recovery. Instead, we have a 'Winter Economy Plan' and the focus has to returned to preservation. Unlike phase one, the less generous terms show Chancellor Sunak has abandoned the idea of a total preservation, and is focused instead on damage limitation while waiting for phase four - a recovery to 'normal' levels of activity. While I have discussed this in the context of the UK, the same pattern is present across Europe and in the US. Although far from certain, phase four will likely be accompanied by further fiscal stimulus, the shape of which, and how it is funded, will define economic growth for the next 3 years at least.

The additional cost of all this borrowing has so far been limited by Central Banks who have not only kept interest rates low, but also bought a significant portion of the debt directly. This so called 'debt monetisation' has always been feared as a source of runaway inflation, but with any kind of inflation hard to find, the benefits, it seems, outweigh the risks. Sentiment that Jay Powell, chair of the US Federal Reserve, expressed himself by saying the 'risk of overdoing' stimulus is smaller than not doing enough. Debt monetisation does mean raising interest rates will be even more difficult from here, and the US Federal Reserve has already changed its guidance to allow for inflation to rise above its long-term target of 2%, without having to intervene. This should make markets much less jumpy if inflation does begin to rise, but may be bad news for fixed income investors, for whom the real value of their income will be eroded by higher costs.

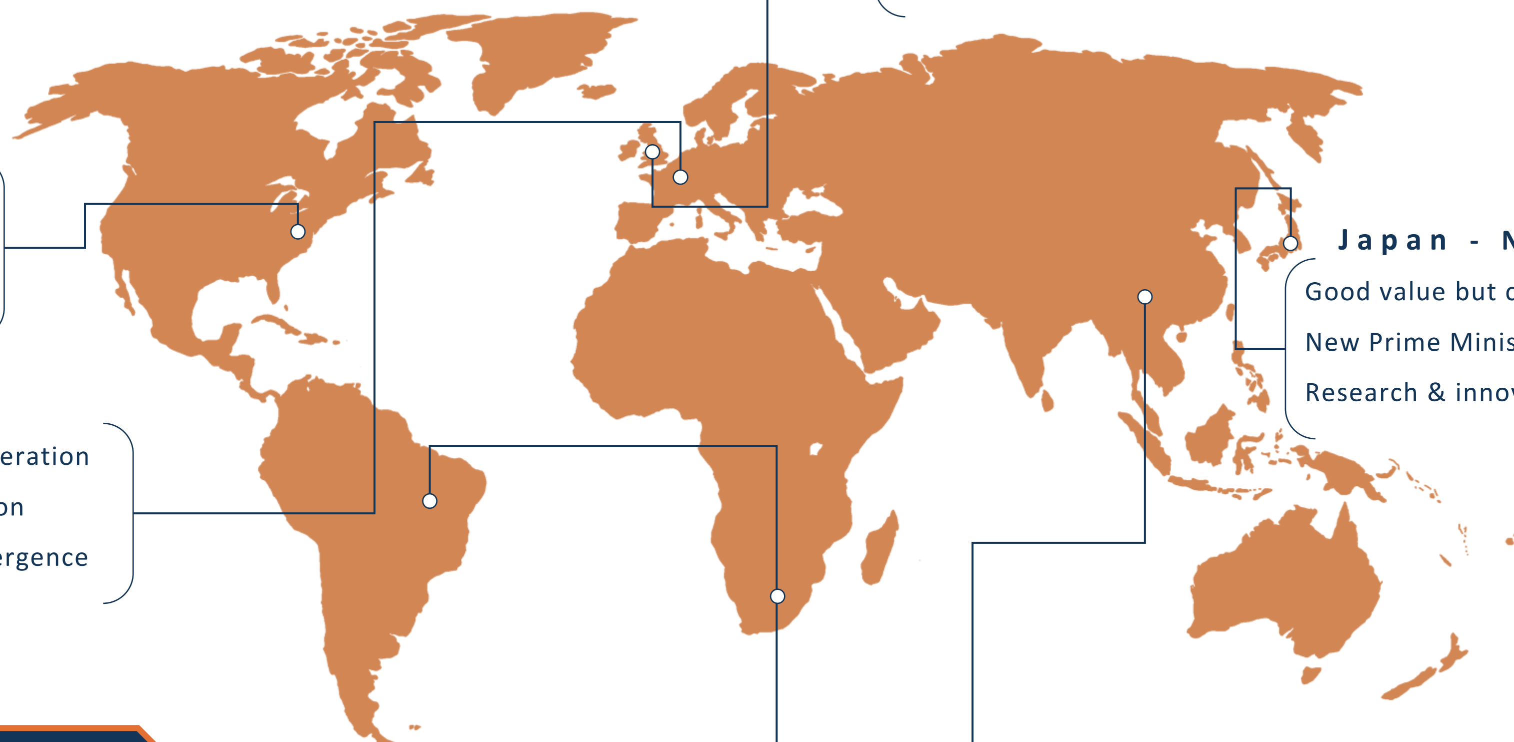
Astute Response:

Although we don't believe rates will rise in the near future, we retain our underweight to bonds given the limited potential for further upside, therefore, the risk return profile remains skewed to the downside. The improving outlook for inflation suggests inflation-linked bonds may provide better protection from capital erosion than nominal bonds, and we will look to position accordingly.

Sources: [1] FiveThirtyEight & YouGov Model Estimates as at 07/10/2020, [2] British Chambers of Commerce, [3] Office of National Statistics

Astute Perspective

ASTUTE INVESTMENT MANAGEMENT LTD



UK - Underweight

- Larger companies remain structurally challenged
- Prefer smaller companies with growth opportunities
- Uncertainty over future trade relationship with EU

N. America - Neutral

- Global leaders in technology & innovation
- Stretched valuation the biggest barrier
- Short term politics could be very uncomfortable

Japan - Neutral/Overweight

- Good value but corporate nationalism persist
- New Prime Minister to continue beneficial reforms
- Research & innovation remain strong suit

Europe - Neutral

- Increasing willingness for real fiscal co-operation
- ECB very supportive but low on ammunition
- Well placed to benefit from US/China divergence

Asia & Emerging - Overweight

- Long term growth from demographics & development
- Prefer Asia, stable regimes and regional synergies
- China/USA decoupling creates two track global economy

Conviction Views

A key part of our process is building conviction ideas which are then expressed across each of the portfolios. While asset class and regional views are an important input into this process, the opinions outlined below will be the driving force behind any potential future returns.

1. Bias to Quality Growth
   - A small number of excellent companies deliver the lion's share of market growth
   - Reliability of long-term growth potential is worth paying a **reasonable** premium for

2. Overweight Technology
   - Technological revolution will continue, lean into disruptive areas, the strong get stronger
   - Look beyond current global leaders and use specialists to stay ahead of the curve

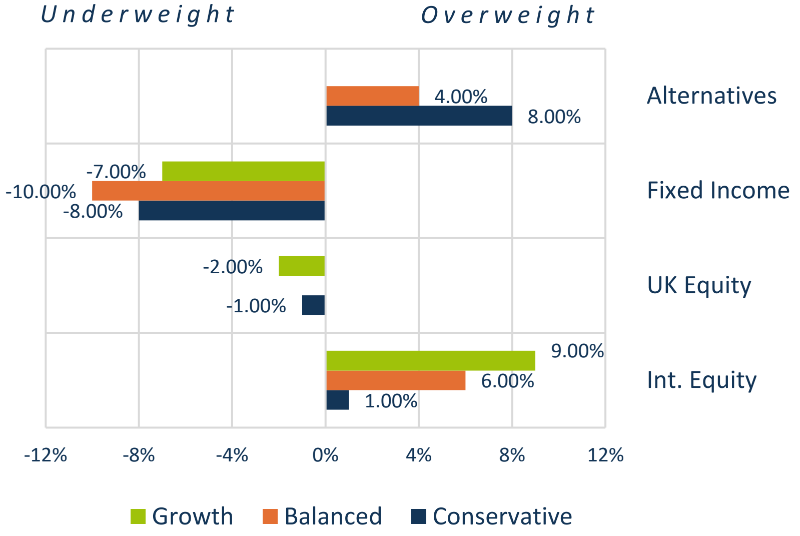
3. Invest Sustainably
   - ESG will become the default option, and the market will shift accordingly
   - If sustainable investing is the future, invest with those who have ESG way into their past

Asset Class Views

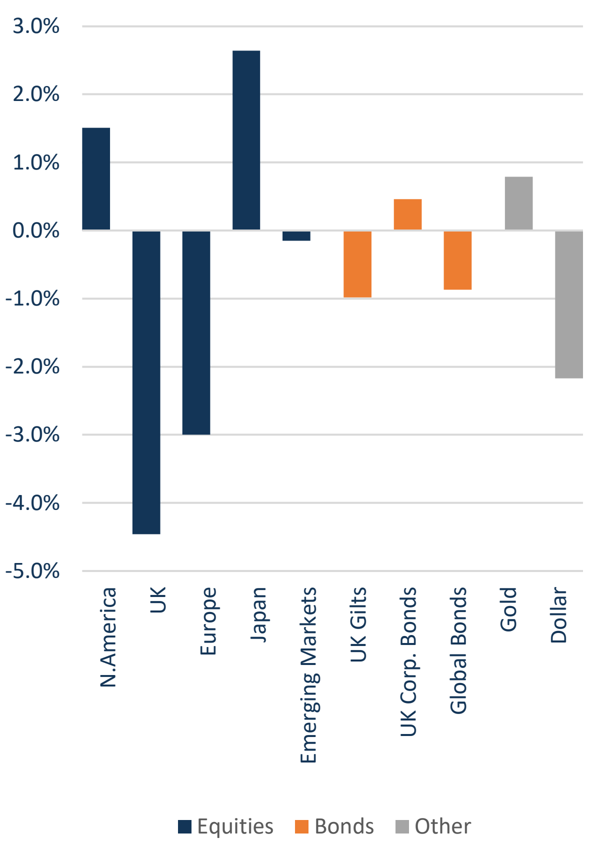
Fixed Income	Negative						Positive
Sovereign Bonds							
Corporate Bonds							
High yield bonds							
EM Debt							
Alternatives	Negative						Positive

Equities	Negative						Positive
UK							
Europe							
Asia & Emerging							
Japan							
US							

Tactical Asset Allocation[1]



Asset Class Returns[2]



Astute Positioning

Since the Astute funds launched, markets have seen distinctly mixed performance. Within equities, the UK underperformed international peers. Despite Sterling strength, particularly against the Dollar, UK equities remained out of favour as the re-emergence of Covid-19 and the continued overhang from Brexit negotiations weighed on sentiment. Europe also dipped towards the end of the quarter as a second wave of Coronavirus transmission took hold. Japan and the US delivered the best returns, while emerging markets were mostly flat. Bonds generally struggled. Riskier corporate bonds outperformed sovereigns with gold proving a better hedge to risk than traditional safe-haven bonds.

Performance over the period was driven more by fund selection than by asset allocation. The underweight to fixed income, and the bias towards international equity versus the UK, was a big contributor. However, strong outperformance from our underlying managers in their respective regions added more value, particularly within equities, where our growth orientated strategies were the top contributors to returns.

Within the Conservative fund, the asset allocation remains underweight fixed income, neutral to equity but with an overweight to alternatives. Some of the alternatives held within the fund have a high degree of correlation to equity markets during periods of increased volatility. Although longer term these offer good diversification, in order to manage this risk, the equity weight remains neutral.

Within the Balanced fund, the underweight to fixed income is matched by overweight positions in alternatives and international equity. This provides higher exposure to the house view that equities will outperform fixed interest, but balances that risk with a degree of diversification in the alternatives.

Within the Growth fund, we hold no bonds and retain only a small cash weight. The corresponding overweight position is in international equities, where we retain our positive stance on emerging markets relative to other geographies.

Across the range, the largest contribution to return came from our US funds. While the L&G ETF is the largest position, the strong performance of the Baillie Gifford American strategy pushed this fund to the top of the table in the Balanced and Growth strategies. Other growth orientated managers strongly outperformed their respective benchmarks, and both Miton European and Polar Emerging contributed meaningfully to returns.

It is pleasing to see some alternatives adding to the growth of the Conservative fund. The Blackrock European Absolute Alpha fund is an equity market neutral fund that continues to demonstrate excellent risk-adjusted returns. There was also a solid contribution from VT Gravis Clean Energy Income fund which invests in a range of physical infrastructure assets, and gold, which proved a better hedge to risk than Sovereign bonds over the period.

Top Contributors

Conservative	L&G US Equity ETF	0.33%
	Baillie Gifford American	0.24%
	BlackRock European Absolute Alpha	0.23%
	VT Gravis Clean Energy Income	0.18%
	Invesco Physical Gold ETC	0.16%
Balanced	Baillie Gifford American	0.61%
	L&G US Equity ETF	0.45%
	iShares MSCI USA SRI ETF	0.33%
	LF Miton European Opportunities	0.18%
	VT Gravis Clean Energy Income	0.18%
Growth	Baillie Gifford American	0.98%
	L&G US Equity ETF	0.70%
	iShares MSCI USA SRI ETF	0.54%
	LF Miton European Opportunities	0.26%
	Polar Capital Em Mkts Stars	0.23%

Data sourced: Refinitiv Lipper for Investment Management & Astute Investment Management as at 30.09.2020. As the Astute funds launched on July 20th this commentary only considers the period after launch to the quarter end and as such does not reflect the full calendar quarter i.e. 20.7.20 to 30.9.20. Past Performance is not a reliable indicator of future results.

[1] – Relative positioning is expressed versus Astute's long term strategic weights. [2] – Broad market indices are used to represent the performance of different regions over the period

Astute Observations

Nudging Behaviour

Over the summer months, as the UK emerged from a national lockdown, the Government explored incentives they could use to boost demand and help support the economy. The charts to the right show the impact of two of the most popular measures.

Firstly, the Stamp Duty holiday, which removed the tax on property purchases up to £500k in England and £250k in Wales & Scotland. This immediately addressed the alarming drop in mortgage approvals which appeared during lockdown. Interestingly, the same chart shows remortgage activity has not recovered, suggesting perhaps that distracted homeowners are dropping on to expensive standard variable rates more than usual.

The second chart shows the change in the number of people eating at restaurants compared to the same time last year. The distinctive spikes show the increase in people eating out Monday to Wednesday as a result of the 'Eat Out to Help Out' scheme, culminating in double the number of usual diners as the scheme came to a close at the end of August.

Both sets of data demonstrate that well directed incentives can drastically alter consumer behaviour. Crucially, the real success of the schemes was the reversal of 'lockdown mentality', which encouraged people to take their first steps towards normal life.

Sources: Bank of England & Open Table