

“Too many firms pay lip service to outcomes-based investing – the current volatility will test their commitment”

James Klempster, CFA

There has been a noticeable increase, over recent years, of investment management firms professing to target outcomes. This is a welcome development. This is because, at Momentum, we believe that we should never lose sight of the reasons why we invest. At the heart of our Outcome Based Investment (OBI) philosophy and process are three key tenets. It is these tenets that we believe to be the acid test for investing for outcomes and the adoption of this approach should be taken to the very heart of an investment process. The three tenets of OBI for us are targeting the outcome that clients want, making the journey to the outcome as palatable as possible and, finally, keeping clients invested.

The ‘investing for an outcome’ requirement should be a given but beware, even managers that state they do so may only be paying lip service to this approach. In our opinion an OBI approach needs to start at the very beginning - at the strategic asset allocation of the strategy in question.

Inevitably there are several different combinations of assets that give a good chance of beating the target and so we spend a large amount of time deciding between the different iterations. We do that by focusing on making the journey palatable to our investors. Real risk for investors comes in the form of surprises on the journey to the outcome in terms of shortfalls over the entire period and also shorter term drawdowns that can try even the most understanding investor’s resolve. As a result, we run millions of simulations that incorporate real observed returns to find what we believe to be the optimal strategic asset allocation that solves for the outcome and finds the best compromise on the various risk factors identified. All this happens before we’ve spent a single penny.

Once the portfolios are launched we must invest for the here and now and most pertinently the future. So then, when constructing portfolios, the key decision for the investment team is what gives us the highest probability of achieving the targeted return today based on what is presently being offered up by the markets. We choose asset classes that appear cheap according to our valuation models and try to avoid those that look expensive. We believe that risk management should be an integral part of the portfolio management process.

True OBI managers understand that from time to time markets will be difficult and it is times such as these that will really test their mettle. Managers that are using OBI as a flag of convenience rather than as a belief system are being severely tested now. Their natural inclination will be to resort to classical relativistic measures of performance ‘at least we did better than the benchmark’ and so on. We understand that despite our best efforts our strategies are not immune from market weakness and we ensure that our investors are aware of these factors. When the going is tough we take the care to explain what has dragged on performance and why, and we are constantly updating our valuation work to ensure our portfolios provide the best chance of achieving their targeted outcomes on a forward looking basis. That is because one rule of thumb for investors tends to ring true again and again. That is when it feels difficult to make an investment it will often provide a great payoff in the long run.

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Market Focus

- » US and China reach temporary trade truce at G-20
- » Fed's Powell says rates are just below neutral
- » Brent crude fell 0.2%, ending the week at \$58.7
- » Gold ended the week 0.2% lower at 1220.7 per ounce

US

- » US and China reach temporary trade truce, the US will defer a tariff rate increase for 90-days to allow for a more comprehensive trade agreement, while China agreed to substantially boost purchases of US goods and negotiate on structural changes
- » Following Federal Reserve Chairman Powell's comments on Wednesday, the yield on the benchmark 10-year Treasury note briefly dipped under the 3.0% threshold for the first time since mid-September. Jerome Powell stated that the federal funds rate is "just below" a neutral level that would neither stimulate the economy nor rein in growth to curb inflation
- » The combination of more constructive trade rhetoric and dovish-leaning comments from Fed officials, caused US equities to rally 4.9% over the week
- » The core PCE price index, which excludes the volatile food and energy components, advanced 1.8% year-on-year, following a 1.9% gain in September

UK

- » UK Parliament will vote on Prime Minister Theresa May's withdrawal agreement on December 11th
- » The Bank of England and UK government published their assessments of the economic impact of Brexit on Wednesday. The Bank of England warned in the event of a "disorderly" exit from the European Union GDP would contract -8% within in a year, while house prices would fall by -30% and Sterling would fall by -25%
- » UK equities ended the week up 0.4%, the pound was 0.5% weaker on a trade-weighted basis and UK Gilts fell -1.0%

Europe

- » The November euro-area manufacturing PMI hit 51.8, revised up from 51.5 and down from October's 52.0. Euro-area economic confidence fell for an 11th straight month, to the lowest level since May 2017
- » In Italy, expectations for a budget compromise with the European Union supported Italian debt, as Italian 10-year bond yields fell 19 basis points to 3.2%
- » Major riots and political protests occurred for the third weekend in Paris
- » Despite the geopolitical tensions, European equities advanced 1.3% last week

Rest of the World/Asia

- » Argentina hosted the G-20 summit on Friday and Argentine stocks rose 2.5% over the week
- » Japanese equities recorded strong gains, advancing 2.4% last week
- » In China, the official November composite PMI continued to soften at 52.8 versus 53.1 in October. The manufacturing PMI fell to 50.0 this month, at exactly 50 points indicating neither growth nor contraction

Past performance is not indicative of future returns.

Source: Bloomberg, returns in local currency unless otherwise stated.