WISE FUNDS

TB Wise Multi-Asset Income
Investment Review – Annual report
28th February 2021

Market background

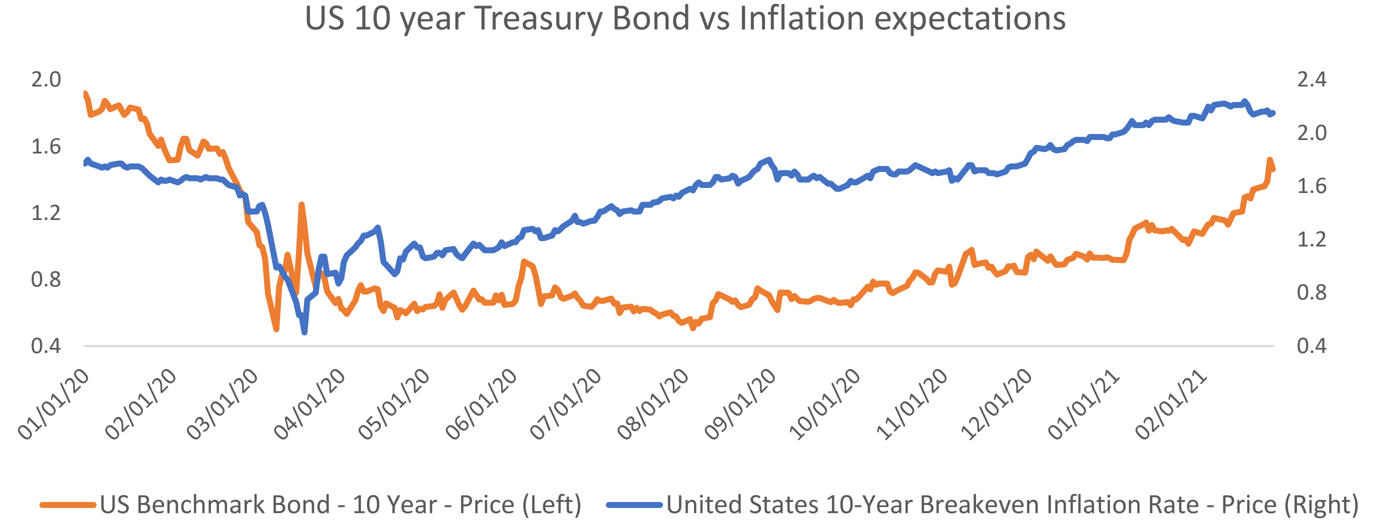
The start of the period under review marked the point at which it became apparent, unlike the previous SARs epidemic, that Covid 19's spread could not be regionally contained and that it had developed into a full-blown global pandemic. The initial consideration of the virus in terms of its localised economic impact and of its broader implications for global manufacturing supply chains evolved to one which reflected the fact its impact would affect all sectors of the global economy.

Beyond the awful death-toll of the virus, the social distancing and lockdown measures taken to supress its spread have led to the worst recession since the Great Depression and one far more severe than the Global Financial Crisis of 2008-2009. Faced with the unprecedented prospect of many companies' revenue disappearing overnight, the market reaction followed a pattern already familiar in other macro-economic shocks of recent years (Euro Crisis, Global Financial Crisis, Brexit) but on a far bigger scale. The progression of the pandemic has, however, been almost impossible to predict and in hindsight it is fair to say thankfully the initial market reaction discounted a far worse economic outcome than has materialised. Nonetheless, defensive assets such as government bonds went up and 'bond proxies', such as infrastructure funds, were spared the worst whilst stock markets fell precipitously. The sell-off in global equity indices in March represented the fastest bear market (a fall of 20% or more) on record yet the speed and extent of the falls told only half its story.

As on previous occasions value sectors fared worse than the overall market. Over the first three months of the period under review, UK 'value' equities fell 15%, reflecting their greater economic cyclicality, whilst 'growth' stocks, perceived as relatively immune to the impact of the crisis delivered a positive return over the same period of 2.7%. Entering 2020 we believed the relative valuation between these two camps was already at an extended level following a decade of austerity and subdued global growth. Tentative signs in the second half of 2019 that this underperformance might be showing signs of improvement were thrown into sharp reversal as the earnings outlook for value sectors deteriorated. For the UK market this was particularly evident given the make-up of its equity indices, with their relatively low exposure to the sectors deemed Covid winners and given how weakly the UK economy has fared during the crisis in a global context. Whilst the global economy is forecast to have contracted 3.5% in 2020 according to the International Monetary Fund, growth rates have varied significantly across different geographies. Emerging and Developed Asian economies are forecast to have fallen 1.1%, with China set to have grown 2.3%, whist the US economy is forecast to have contracted 3.4%. The Eurozone has been significantly impacted, down 7.2%, however, the UK sits at the bottom of the leader board having shrunk 10%.

Within global equity markets there has been a significant geographic divergence in stock market performance, reflecting which economies have dealt best with the crisis as well as the exposure within those markets to sectors that have seen increased demand during the pandemic. Technology, in particular, has seen increased demand as shopping moved online, employees adapted to remote working and pre-existing structural trends accelerated. Whilst we recognise the attractions of investing into areas of the market that have structural growth tailwinds, we maintain a valuation discipline in our process, reinforced by our investment objective of delivering a dividend yield in excess of the CBOE UK All Companies index. This process led to a portfolio asset allocation with a significant exposure to UK value equities and has led to much greater volatility through the course of 2020 than we would have anticipated. The market moves caused by Covid and Brexit uncertainties, however, led to a market in the Summer which exhibited extreme levels of distortion. The UK equity market sat at its biggest valuation discount to world equity indices for the last 30 years. Indeed, the discount was nearly twice as wide as it had been at previous troughs. UK market investors needed to go back to the 1980s to see similar valuation discounts being applied to value stocks whilst the premium being paid for defensive stocks over cyclical stocks was as wide as it had been in the financial crisis of 2008/9.

The level of risk aversion in fixed income markets was similarly extreme. In 2013 investors in UK 10-year government bonds could expect to receive an income return of 3.0%, a premium to the bank of England's target inflation rate of 2.0%. Investors could legitimately invest into 'risk free' areas of the market, accept a lower level of return, but at least see their investments protected from the expected impact of inflation. At the worst point last summer, however, this return had shrunk to 0.5%. In an environment of elevated uncertainty, bond investors were choosing the certainty of no return or most likely a negative return after adjusting for inflation over a 10-year period rather than embracing the opportunity to invest into companies where, in our opinion, the valuation opportunity was as attractive as any of us had seen in our investment careers. The risk, however, was that the outlook was particularly cloudy. Moreover, the challenge for investors seeking income at that point was exacerbated by the fact that the economic backdrop was causing an unprecedented number of companies to cut their dividends, of which we will write more later.



All data sourced from Factset at the 28th February 2021 .

Over the summer as we yo-yoed in and out of lockdowns and market nervousness grew about the effectiveness of potential vaccines, there were reasons for cautious optimism beyond that provided by the extreme valuation backdrop outlined above. In the face of such an extreme economic downturn, governments and central banks unleashed a level of fiscal, monetary and liquidity support multiple times greater than that seen in the Global Financial crisis. Interest rates have been cut, Quantitative Easing increased, furlough schemes introduced, and funding lines made available, all designed to protect businesses and employment until the easing of lockdown measures is well-established. Furthermore, it became increasingly apparent that the economy had bounced back faster than anticipated from the first lockdown and most companies had planned for a worst-case scenario that failed to materialise.

Against this backdrop, November witnessed two significant announcements that materially changed the investment outlook. Firstly, Biden won the US election. A couple of months later, the news that the Democrats has secured the two Senate seats in Georgia needed to gain a majority paved the way for the aggressive $1.9tn stimulus package enacted immediately after the period end. Such a large fiscal stimulus package, c.10% of US GDP, has implications for inflation expectations, especially when coupled with the Fed's commitment to maintain policy at looser levels than would historically have been the case. Most significant, however, were the announcements that all three vaccines have proved to be highly effective in combatting the virus and its transmission. This gave investors the opportunity to look to an investment environment no longer dominated by the uncertainty of Covid and to better quantify over how long to model its financial cost. This has led to a sharp recovery in performance of those sectors hardest hit by lockdown measures and which should benefit as they are eased. It has also changed the market's inflation expectations which has significant implications for asset allocation and market leadership.

The prospect of a sharp, synchronised recovery in global growth coupled with loose monetary policy and ongoing fiscal stimulus has seen a significant increase in inflation expectations such that they now sit at a 6 ½ year high. A decade of austerity coupled with the structural deflationary forces of technology, globalisation and demographics had conditioned investors to believe that inflation would remain benign well beyond any of our investment careers. The cyclical impact of Covid and the likely rise in unemployment was expected to keep inflationary pressures further at bay. This fuelled the collapse in bond yields described above as well as the expansion in valuation multiples for growth companies. A low cost of borrowing mainly impacts the value of high growth companies, where investors expect the bulk of their profits to be made a long way off into the future. When the cost of money is extremely cheap, these companies are implicitly not penalised for the time it will take to deliver these profits or the relative likelihood these growth expectations will be achieved. As investors discount future profits back at an abnormally low rate, £100 delivered in 10 years' time is valued the same as £100 made next year. The rapid rise in US 10-year government bond yields from their trough of 0.5% last year to 1.7% today that accompanied the changing view on inflation has not only led to the worst start to the year since 2015 for bond investors but has also caused a rotation out of growth stocks back towards value. The extent to which vaccine roll-outs progress and economies are able to re-open will determine whether this trend continues. We remain encouraged, however, that the valuation multiples still being applied to many value sectors remain modest in absolute terms. Historically this has been a key factor is predicting future returns for investors.

Performance

The performance of the fund was much more volatile than we would have liked, reflecting the heavy UK value equity positioning of the portfolio entering the period. This also had significant implications for the fund's dividend which informed much of the trading activity within the portfolio during the period. We stated in last year's annual report that TB Wise Multi-Asset Income has a wide and flexible remit allowing us to invest across the broadest range of assets, in whatever proportions we believe is appropriate. Given the extreme valuation opportunity then in a relatively narrow set of assets (broadly cyclical and domestic equities as well as property) and the unattractiveness of safer assets, such as bonds, the portfolio was poorly positioned for the extreme economic shock that ensued. In March alone, the fund fell by 24.5%, significantly more than the IA Flexible Investment Sector average of 11.0% (our comparator benchmark) and more than the UK stockmarket driven by the greater exposure to value holdings with its equity allocation. These market moves only served to accentuate pre-existing extremes in valuation between those assets deemed safe and those deemed risky. Against this backdrop of earnings uncertainty, an unprecedented number of companies elected or were forced to cut their dividends. We estimated at this time that the fund's dividend would fall by over half and were faced with the challenge of trying to rebuild the fund's dividend without sacrificing the significant capital upside we believed existed. The performance of the fund over the full period demonstrates the extent to which holding one's nerve at the bottom and having an investment process underpinned by longer term valuation metrics allowed the fund to retrace the relative underperformance, particularly versus the UK stockmarket. The performance against the comparator benchmark, the IA Flexible Investment sector, over the full year reflects the Fund's underweight positioning towards defensive assets at the beginning of the period (such as gold and government debt) as well as having limited exposure to equity markets whose domestic economies have fared better through the Covid Crisis, such as China, or have a higher exposure to technology stocks, such as the US. Our concern over valuation and the unattractive yields on offer explains our reluctance to invest in each of these areas. Over the 12-month period, the Fund rose 7.9% compared to its target benchmark, the Consumer Price Index, which returned 0.4% and the comparator benchmark, up 13%. The fund's dividend suffered significantly during the period, falling 43% compared to the previous year. This was hugely disappointing to us and we explain in more detail the reasons for this failure to meet the objective of growing the dividend in line with inflation. Having significantly underperformed the UK stockmarket in the first month of the year, the fact the fund ended up significantly ahead of it over the full year highlights the recovery and extreme rotation markets demonstrated post the March sell-off. Investment performance over the months through to November became increasingly sensitive to the twin forces of near-term uncertainty over earnings on the one hand and the highly attractive valuations on the other. We used this period to reduce our direct equity holdings where the outlook for dividends was less certain and reinvested into Investment trusts, where we believed a similar level of capital upside existed but whose structure allowed for the continued payment of dividends out of revenue reserves. In all cases these trusts stood at historically wide discounts to net asset value. We also added three fixed income holdings to the portfolio (Provident Financial 7% 2023 (+21% for the period the position was held over the year*), TwentyFour Income Fund (+27%) and Starwood European Real Estate Finance (+8%)) offering high running yields that also traded at wide discounts to par. November's vaccine announcement and the election of Biden led to a swift rotation back into the stocks and sectors that had been worst affected by the crisis.

	1 Month	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
TB Wise Multi-Asset Income B Inc	4.96	8.38	23.90	7.85	2.97	44.59	107.58
UK Consumer Price Index	0.09	0.18	0.46	0.37	4	9.32	18.59
IA Flexible Investment	0.61	3.07	8.83	13.04	16.82	50.42	82.12
Quartile	1	1	1	3	4	3	2

All data sourced from FE Analytics and quoted as total return at the 28th February 2021 .
Past performance is not a guide to the future and outperforming target benchmarks is not guaranteed.

The extent of the market falls in the first few months of the period is best demonstrated by the performance of our direct equity holdings that we switched into similarly positioned domestic, value funds and which failed, therefore, to participate in the subsequent market rally. These companies were directly impacted by the lockdown restrictions and in certain cases had weaker balance sheets than estimated, given the reduction in expected earnings. Shoe Zone (-47%), Photo-Me (-46%), Easyjet (-50%), Marstons (-53%), Bakkavor (-43%), Lookers (-40%) and Watkin Jones (-42%), as examples, were all significantly impacted by the restrictions on eating out, travel, the closure of non-essential retail and university students working remotely from home. We sold these stocks as all cut their dividends and we had limited conviction in their ability to return to paying dividends in the foreseeable future. As discussed above, however, we reinvested the vast majority of these proceeds into three UK Equity Investment Trusts, Temple Bar (+39%), Aberforth Smaller Companies (+59%) and Schroder UK Mid Cap (+18%) which helped capture the subsequent recovery in markets whilst improving the Fund's dividend.

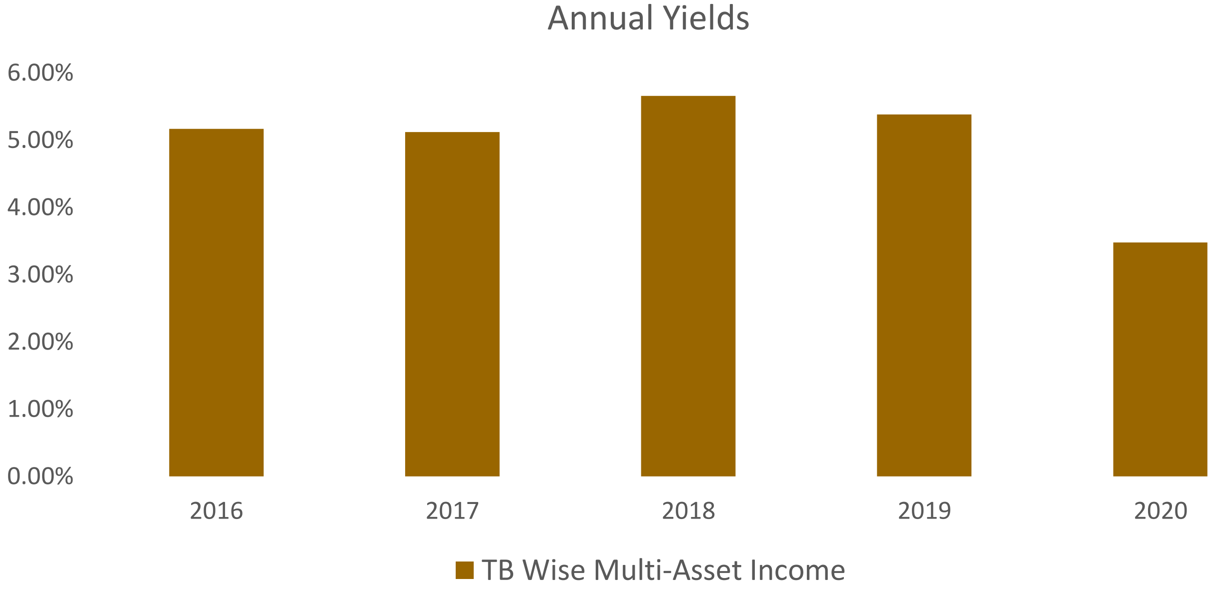
Covid has had a very different impact on markets globally as well as on different asset classes. Commodities, Emerging Market equities and Technology have all performed strongly. Whilst we have exposure to these sectors within the portfolio, our underweight positions driven by valuation concerns explains some of our relative underperformance this year. The biggest contribution in the period to performance for the fund comes from our mining holdings, Rio Tinto (+84%) and Blackrock World Mining 8(+9%). Despite being the source of the virus, China has emerged from the pandemic as one of the economies least affected by it. As a result, the supply/demand picture for global commodities has remained healthy given China's importance as a source of demand, particularly for copper and iron ore. Supply, however, has remained constrained. Longer term, the structural pressure for the global economy to decarbonise should benefit the sector as the growth in electric vehicles and investment in electricity infrastructure increases demand for these commodities. In an environment of dividends being cut, the mining sector has become a reliable source of dividends underpinned by strong capital discipline and extremely strong balance-sheets. Emerging Markets have performed well as their economies proved resilient as have sectors able to deliver earnings growth when others have seen earnings collapse. Aberdeen Asian Income (+21%), Princess Private Equity (+16%), European Assets Trust (+36%), XP Power (+70%) and Polar Capital (+42%) all provide the portfolio with exposure to higher growth and resilient end markets whilst delivering decent dividends to shareholders at the same time.

The Financials sector offers some of the best value in the market and its performance within the fund has seen some of the most divergent returns. These holdings are most sensitive to the outlook for the economy, the level of government bond yields and the steepness of the yield curve (the difference between long-dated and short-dated government bonds). Given its economic sensitivity and its position at the epicentre of the previous crisis, it is perhaps understandable that the market's immediate reaction was to sell the sector aggressively. This has led to some of the most volatile performance within the portfolio. Since the Global Financial Crisis, the sector has made significant strides in improving its capital strength making it significantly more resilient to economic shocks than it was. The extent of the moves in the summer suggested that an environment for impairments multiple times worse than the Global Financial Crisis was being discounted in valuations. Despite the regulator mandating that dividends should be suspended, we believed the potential capital upside was too great for us to reduce our holdings despite the impact this would have on the Fund's dividend. Whilst the performance of Legal & General (+9%), Natwest (+3%), Paragon (+2%) and Aviva (8%) appear robust over the twelve-month time period, this conceals the fact that each of these companies saw their share prices halve or worse between December 2019 and the end of March 2020. We believed Financials represented one of the most undervalued sectors in the market and again added to an Investment Trust at a significant net asset value discount, Polar Capital Global Financials Trust (+45%), as a way of increasing exposure to the sector whilst maintaining dividend income. Performance within the sector holdings was extremely divergent. Companies immune to the economic shock of Covid or deemed beneficiaries of increased volatility and the need to raise equity capital, such as Numis (+37%), Randall & Quilter (+24%) and Polar Capital holdings (+42%) have performed strongly whilst home collected credit companies, such as Provident Financial (-30%) and Morses Club (-40%), where loan collections have been restricted by lockdown, have performed poorly.

The final area of weaker performance for the fund during the period came within our property holdings as tenants refused to pay rent and the crisis highlighted pre-existing structural concerns, particularly over the need for physical retail, but also the impact working from home would have on demand for office space. U & I (-47%), New River REIT (-37%) and Palace Capital (-29%) were noticeably weak on the back of their retail or development exposure and higher indebtedness than comfortable. Nonetheless we believe these concerns have seen a number of well managed trusts with decent underlying property assets fall to underserving discounts to net asset value. Whilst dividends have been cut to reflect reduced rental income, they are now well covered by current rental income and pressure will grow for them to increase in order for the companies to comply with Real Estate Investment Trust tax rules that require 90% of earnings to be paid out as dividends. Furthermore, earnings themselves should grow as tenants are able to return to trading and landlords are able to enforce the payment of rental contracts. Ediston Property Investment Company (-6%), for example, yields 5.5%, which is covered 130% by its earnings. Its out-of-town retail parks have performed relatively strongly as its tenants have been largely focussed on essential retail. Once there is greater clarity over the return to relative normality, we can see further scope for recovery back towards its pre-Covid yield of 8.6%. Similarly, we added Standard Life Investment Property Income Fund (+16%) to the fund during the period. The Fund yields 5% and recently accelerated and increased its dividend pay-out whilst also announcing an increase in its latest net asset value. We believe this marks a turning point for the company. The persistent discount of 24% to its net asset value represents a significant fall from the level it traded at prior to the Covid pandemic (often at a premium to net asset value). We see scope in many of our property holdings for dividends to be restored and then grow, and for this to be reflected in an upward revaluation of the portfolios and tighter discounts.

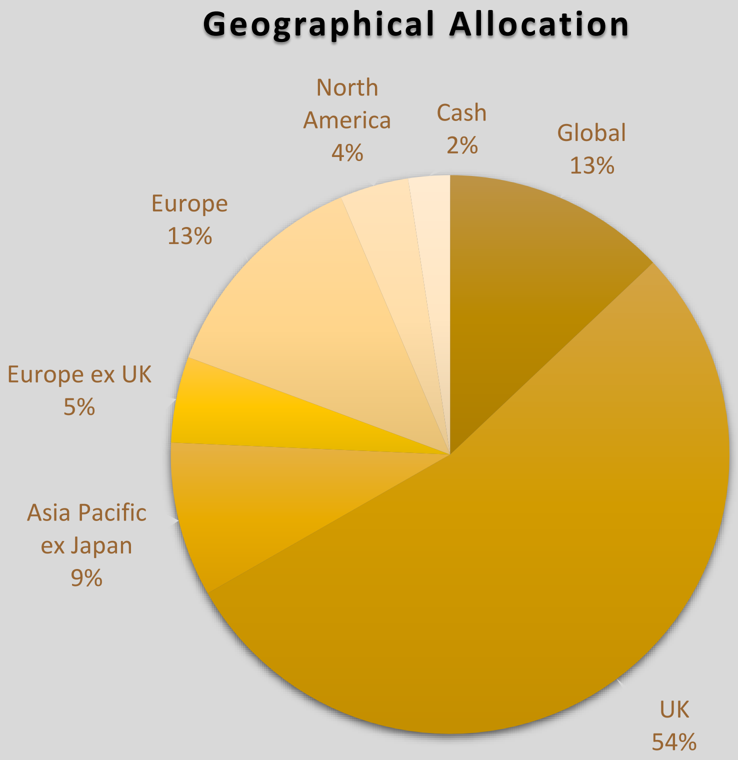
Dividends

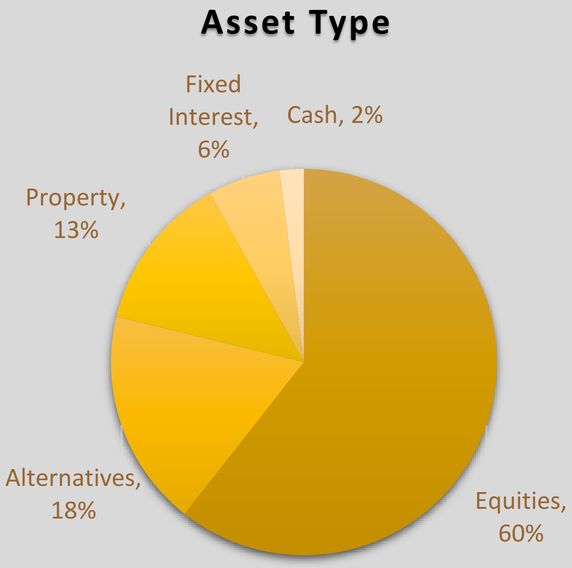
The biggest disappointment and challenge for us during the period was the extent to which companies elected to or were forced to cut their dividends. The immediate response of many companies to the pandemic was to adopt a 'safety first' approach to protect their balance sheets, to retain sufficient liquidity and to ride out the period of uncertainty. In certain cases, financial regulators forced or pressurised companies to withdraw dividends that had already been announced, and many companies which utilised government support schemes were required to cut dividends in order to do so. We believed that, for the vast majority of holdings within the portfolio, there was a strong desire to return to paying dividends as soon as possible. Our aim through this period, therefore, was to protect the fund's dividend as much as possible and to improve both its short and medium-term prospects. We invested in companies or funds that continued to pay dividends and that we believed were secure. We reduced low-yielding holdings that had held up well, or sold where we believed the prospect of permanently reduced or no dividends for a number of years was likely. Furthermore, given the extreme capital upside available in certain companies, we added to positions where we had no concerns about their balance sheet strength, where we believed that a resumption in activity back to normal levels was more likely, and a return to paying dividends was consequently more predictable. It is encouraging that in most cases these companies have now declared final dividends for the year ending 2020 as earnings have proved much more resilient than feared in the depths in the crisis. Our aim throughout this period was trying the get the balance right between restoring dividend income in the short-term without sacrificing the prospect of capital upside in the process. At the worst point of the crisis, we believed that the dividend for 2020/21 would fall by over half. In fact, the dividend per unit has fallen 43% over the period. This period, however, captures a complete hiatus in dividend payments and poorly reflects the ongoing impact of dividends for the fund, many of which have subsequently been declared but are not captured in this reporting period. Looking to the year ahead, we believe the fund should deliver a dividend per unit of 5.04p, representing a 22% reduction on the 2019/20 level. This is more reflective of the ongoing impact of the crisis on the dividend and puts the yield on the fund at 4.4%, which would be in line with the fund's objective to exceed that forecast for the UK Equity Market.



All data sourced from FE Analytics as of the 31st December 2020. This chart shows the annual yields for each calendar year.

Past performance is not a guide to the future and outperforming target benchmarks is not guaranteed.





All data quoted is by revenue of assets and sourced from FE Analytics as of the 28th February 2021.

Outlook

The extent to which the global economy recovers from Covid will be the primary determinant of the fund's performance in the year ahead. The news on the effectiveness of vaccines both in reducing hospitalisation rates and the spread of the virus is highly encouraging. However, vaccine protectionism and the uneven pace of vaccine rollouts globally open up the prospect of future waves of infection and the possibility that the virus might mutate and vaccines become ineffective. Despite the recovery in global equity markets and the recent pick-up in those sectors most impacted by the virus, we are encouraged firstly that earnings expectations for these sectors remain subdued, suggesting recovery is not being fully factored in. We are highly aware of the dispersion in valuation between value sectors and growth sectors within the market, and believe the exuberance shown towards technology stocks, in particular, echoes some of the irrational optimism shown in the technology boom of 2000. The question we constantly ask ourselves, therefore, is whether this extreme dispersion in valuations tells us more about the overvaluation of one narrow subset of the market or whether value equities retain their attractiveness in absolute terms. On this last point, we believe attractive longer term, cyclically adjusted valuation measures support the case that fundamental value still exists despite the recent rally. We believe it remains possible to construct a portfolio at an attractive yield that is well-covered by earnings with scope for growth and supported by strong balance-sheets. We maintain a heavy bias towards equities and property within the portfolio and remain underweight bonds. Inflation expectations have recovered back to pre-Covid levels, reflecting the monetary and fiscal backdrop as well as the expectation of a sharp economic global recovery over the next two years. Government bond yields still look low in the context of these inflation expectations, whilst credit spreads (the excess yield on corporate bonds compared to government bonds) have tightened to reflect the improved outlook for profits. There is scope for bond yields to rise to meet these improved inflation expectations and in so doing we would expect further headwinds for fixed income investments as well as a rotation out of defensive, growth sectors.

General Update

The TB Wise Multi-Asset Income fund started the period with £120.4m of assets under management and finished with £86.7m.

Our team started working from home in the middle of March 2020 and adapted very quickly. We are lucky that our job lends itself well to remote working. We are also fortunate that, operationally, we were already set-up to work outside of the office, which made the transition easy. Our meetings with external managers, if anything, are now even more productive than they used be as they are quicker and easier to organise. Going forward, we will surely resume meeting managers in person, as this personal rapport is important to our qualitative research, but there is no doubt that we will continue to make greater use of technology and reduce our travel. The fact that the whole world embarked on this virtual experiment together has helped make video calls more acceptable and those are likely to stay. That said, as a team, we are all eager to work altogether in our office again and will do so as and when it is deemed safe to do so.
Finally, all that is left is for me to thank, personally and on behalf of the Wise Funds team, all our investors for their ongoing support in what has been a challenging period. Please feel free to contact us if you would like a meeting or have any questions.

Philip Matthews, Fund Manager
Wise Funds Limited

Please note – this annual report the personal views of Philip Matthews as at February 28th 2021, and does not contain financial or investment advice.

***all performance figures quoted in brackets relate to the period over which the position was held in fund during the year, which is not necessarily the performance of the holding for the 12 months ended 28 February 2022.**

All performance is to be read in conjunction with the February 2021 factsheet found at the following website.
[TB Wise Multi-Asset Income February 2021 Factsheet]