

Passive Index Ethical Model Portfolios

March 2017

Market Data to 15 th August 2016	3m	6m	1yr	3yr
Ethical Passive Index Balanced Portfolio	5.58	4.17	17.90	24.31
Ethical Passive Index Moderately Adventurous Portfolio	7.04	7.39	25.13	31.46
Ethical Passive Index Adventurous Portfolio	7.64	11.83	33.29	46.66
FTSE 100 TR in GB	7.00	7.74	28.80	18.39
Moneyfacts 90 Days Notice 10K in GB	0.13	0.30	0.68	2.18
UK Consumer Price TR in GB	0.00	0.50	1.60	1.91

Market Commentary: Key Points for Last Period

This reporting period has been one of the most significant since the credit crisis and, potentially, marks a change in long term investment trends. Over the period the FTSE 100 index returned 7.74% which was close to that of the FTSE World index returning 10.01%. In contrast the FTSE UK Conventional Gilts All Stocks index returned -6.67% highlighting a continued downward trend away from the long term bull -run of the bond market.

The period began not long after the historic UK referendum result to leave the European Union ('Brexit') and ended shortly after the inauguration of Donald Trump as the 45th American President. Both of these events were once considered highly improbably with Brexit odds in the middle of 2015 indicating less than a 25% probability whilst in August 2015 the probability of Donald Trump securing victory was around 4%.

Although these events, at least prior to their occurrence, were considered as potentially negative outcomes the reality for most UK investors has been positive returns. A significant element of these returns has come from the fall in sterling after the Brexit vote which increased the value of overseas assets considerably. Nevertheless, global markets have also generally risen in local currency terms (including the FTSE 100) with the exception of fixed interest markets, which although positive after Brexit, fell back on the news of Donald Trump and this could be significant.

Periods of change are often quite difficult to spot until sometime after the event however it is hard not to notice that 2016 has witnessed dramatic events which will shape the future to be significantly different than previous expectations. There are potentially strong political and economic forces which can be identified that may combine to present both considerable risks and opportunities for investors.

The recent era, beginning in the late 1980s, has seen a prolonged period of fixed interest markets performing strongly and, most importantly, providing down-side protection during risk events. For example, fixed interest markets protected investors from the Asian currency crisis in 1997, the tech crash in 2000, the credit crisis in 2008/9 and each successive European credit crisis subsequently. As a consequence of their risk mitigating properties fixed interest markets are generally classed as low risk by the various rating agencies whose creditability remains high despite their well-publicised part in the credit crisis.

The yield of a 10-year gilt in the mid-1980s was around 15% which meant that even if it lost 30% in capital terms it would only take 2 years for the yield to 'fill in the hole'. The key reason that fixed interest investments have been as resilient is because the yield claws back the total return after losses. Unfortunately, the yield of a 10-year gilt today is under 1.5% and therefore the ability to reduce risk by 'filling in the hole' is far, far lower.

What factors have influenced the reduction in the Gilt yield so dramatically over 30 years and led to such strong capital performance? The most significant is inflation, as this economic force reduces the value of money and significantly effects the willingness of investors to hold fixed interest securities. Although 15% return may sound attractive today, in the 1980s many were basing their expectations on the experiences of the 1970s where inflation eroded the value of money even more quickly with average inflation in double figures and, at times, in excess of 25%. It has been a very high starting point and the gradual reduction in inflation and interest rates over a prolonged period has led to an exceptional period for fixed interest markets but with yields now so low and, even negative in some markets, the cycle appears fully mature and recent events may provide the catalyst for a new cycle.

If globalisation has been a driver for lower inflation, then the policies of Donald Trump in reducing free trade could revive inflationary pressures. Additionally, what are the long-term effects of the many billions of printed money throughout the various global quantitative easing programs which remain underway in Europe, UK and Japan? Finally, how will the anticipated move away from austerity to increased Government spending impact on these two factors and could it act as a further stimulus?

The answers to these questions are not clear but they do suggest strongly that future inflation expectations could be different to the past and the investment risk map may need some updating.

If bond markets do decline further the effect may be stimulatory as money which has been released through quantitative easing, but trapped in the icebergs of the frozen bond market, will begin to melt and the presence will begin to be felt within the real economy as a stimulus.

We expect that history will mark out 2016 as a year of change and we believe that investors who understand the changes which are occurring are able to increase their returns and avoid some losses as a consequence. Whilst the idea of returning to double digit inflation is out of the question, the very low inflation and interest environment could have bottomed leading to different future outcomes where traditionally higher risk investments which offer a natural protection against inflation behave with lower risk characteristics and vice-versa.

Strategy

We continue to favour investing in real assets, equities in particular. Our caution in bonds has been rewarded, however continued inflationary pressure may mean we need to reduce this exposure further in the near future. Ideally we would like to favour short duration mandates for the bonds, but due to the more restrictive ethical options we are unable to follow this strategy.

Model Portfolio Changes / Comments

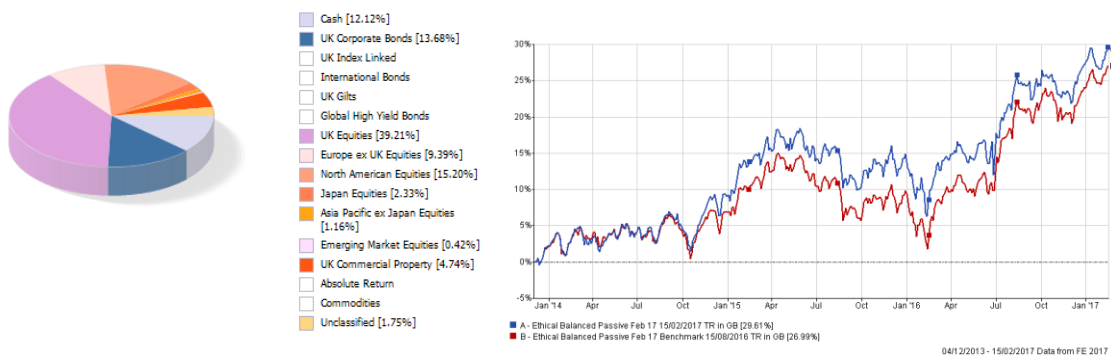
For the present, the portfolio asset allocations and funds will remain the same.

Portfolio Asset Allocation

Ethical Balanced Indexed Portfolio (Risk Level 5)

Ethical Balanced Indexed Portfolio Composition			1 yr	3 yr
Fund Manager	Name	% Holding	Perf %	Perf %
BlackRock	Cash D Acc	10	0.21	0.67
L&G	Ethical Trust R Acc	40	14.75	13.85
Threadneedle	UK Social Bond Z Ret Acc	20	9.06	20.38
Vanguard	SRI European Stock Acc GBP	5	27.23	20.65
Vanguard	SRI Global Stock Acc GBP	25	35.86	53.85

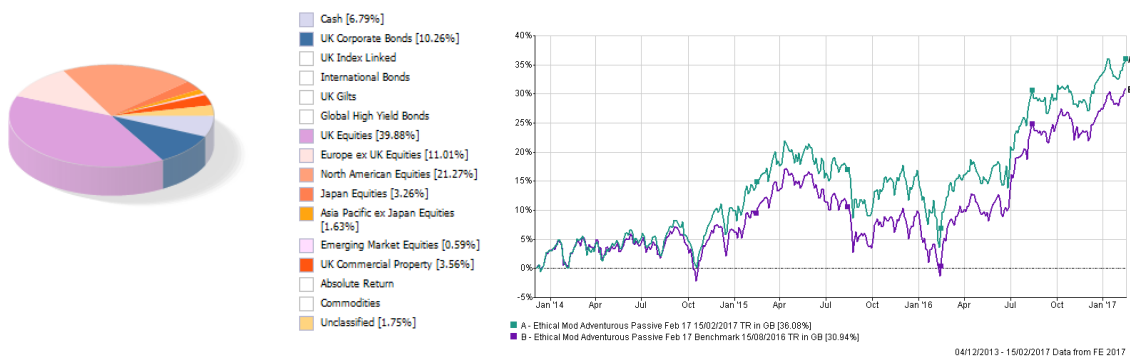
The following charts represent the performance history compared to the composite benchmark based on sector averages since December 2013 and the asset allocation in connection with the above funds which aims to replicate your agreed risk profile.



Ethical Moderately Adventurous Indexed Model Portfolio (Risk Level 6)

Ethical Moderately Adventurous Indexed Portfolio Composition			1 yr	3 yr
Fund Manager	Name	% Holding	Perf %	Perf %
BlackRock	Cash D Acc	5	0.21	0.67
L&G	Ethical Trust R Acc	40	14.75	13.85
Threadneedle	UK Social Bond Z Ret Acc	15	9.06	20.88
Vanguard	SRI European Stock Acc GBP	5	27.23	20.65
Vanguard	SRI Global Stock Acc GBP	35	35.86	53.85

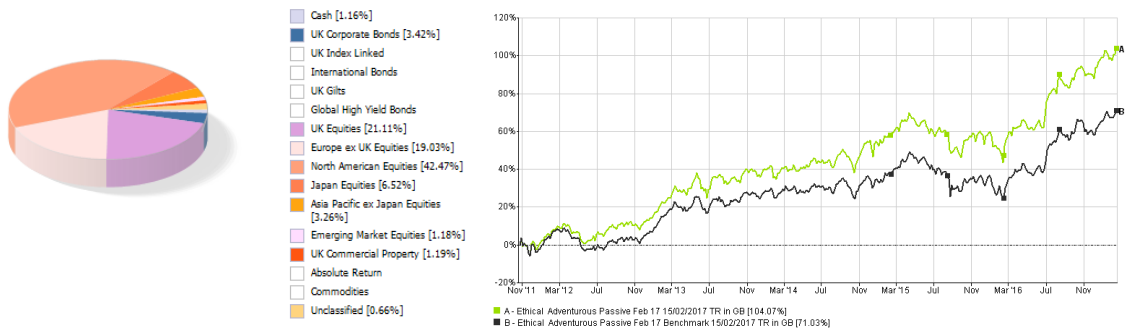
The following charts represent the performance history compared to the composite benchmark based on sector averages since December 2013 and the asset allocation in connection with the above funds which aims to replicate your agreed risk profile.



Ethical Adventurous Index Model Portfolio (Risk Level 7)

Ethical Adventurous Indexed Portfolio Composition			1 yr	3 yr
Fund Manager	Name	% Holding	Perf %	Perf %
L&G	Ethical Trust R Acc	15	14.75	13.85
Threadneedle	UK Social Bond Z Ret Acc	5	9.06	20.88
Vanguard	SRI European Stock Acc GBP	10	27.23	20.65
Vanguard	SRI Global Stock Acc GBP	70	35.86	53.85

The following charts represent the performance history compared to the composite benchmark based on sector averages since October 2011 and the asset allocation in connection with the above funds which aims to replicate your agreed risk profile.



Although the model portfolios are for clients with a particular attitude to risk, individual funds may be higher risk than the overall portfolio and some of lower risk; this is to achieve an overall portfolio in line with the risk. Data sourced through Financial Express (Analytics). All reasonable precautions have been taken to ensure that the information contained is correct. Past performance is based on a model and not an actual portfolio and should not be seen as a guide to future performance, the price of shares and the income from them can fall as well as rise. Please note that the actual performance of your portfolio may differ due to a difference in charges and timing of any investments, redemptions and switches.