Heritage

Quarterly Newsletter & Investment Review

Issue 98 Quarterly news & investment review from Heritage Quarter 2 2022

In this issue

Heritage Capital Management Limited

Heritage Capital Management Ltd is an independent, specialist investment management company based in London and regulated by the Financial Conduct Authority, providing a wide range of investment services to individuals, trusts, companies and pension funds.

Contacts - directors

Graeme Olsen
graeme@heritage-capital.co.uk
Graeme is responsible for client portfolios and advising the Heritage Managed Portfolio and SVS Heritage Balanced Portfolio Funds.

Jemma Spencer
jemma@heritage-capital.co.uk
Jemma is responsible for compliance oversight and assisting with the management of the Heritage funds.

www.heritage-capital.co.uk
Tel +44 (0) 20 7799 2110
Fax +44 (0) 20 7222 1599
Broadway House, Tothill Street,
London SW1H 9NQ

Global markets suffer worst first half year

The bad start to the year, due largely to the war in Ukraine and soaring inflation, has worsened further in the second quarter, with the MSCI World Index falling 15% to take the year-to-date loss into bear market territory at over 20% - making it the worst first half since the global index was created in 1990. And whilst bonds can often be relied on to provide some diversification benefits when equities are weak, this time they are also having a torrid time due to rising interest rates.

Consequently the Heritage Managed Portfolio Fund has also had a tough year so far, but has held up relatively well with a loss of just over 5% this quarter taking the year-to-date fall to 7.25%. As usual further details on the Heritage Managed Portfolio Fund are on page 3 and the SVS Heritage Balanced Portfolio Fund on page 4.

"Spotlight On" - The importance of investment income

It is a common misconception that the income from investments is of primary importance to retired individuals who need to produce a regular income stream from their investment portfolio and that longer term investors should be more concerned with capital growth. However, the truth is that income is a vital part of the total return for all investors due to the powerful effect of compounding of reinvested dividends. In fact £1,000 invested in the FTSE 100 index at the turn of the century would be worth just £1,080 today but with dividends re-invested the original sum would have more than doubled to £2,075.

This startling difference proves just how vital it is for long-term investors to reinvest the income from their portfolio in order to maximize returns and there are some practical issues that can help ensure that investors fully benefit from this effect.

Unlike a portfolio of individual shares and many other funds, the Heritage Managed Portfolio Fund is set up in a way that derives maximum benefit as all income in our offshore "roll-up" fund is retained within the Fund for reinvestment and because income received in the Fund is not taxed, it is the gross rather than net amount that is reinvested. This fund structure is not only helpful for those seeking to maximize long-term returns, but also tax efficient for those who do require an income, as the exact amount and specific timing of the required "income" can be generated through regular or ad-hoc small redemptions.

Our newer, UK regulated, SVS Heritage Balanced Portfolio Fund was also established with an "Accumulation" share class, which automatically reinvests all income rather than distributing it, to help investors benefit from the reinvestment and compounding of all dividends and interest received from the underlying holdings within the fund.

Importantly, our funds have a bias towards profitable companies that have established and sustainable business models that enables them to pay attractive levels of dividends. This helped us to avoid getting caught up in the bursting of the internet bubble as the fund was starting out over twenty years ago and this year it has also helped us, as we have not been exposed to the previously very highly rated "jam tomorrow" growth stocks that have endured a savage correction. It also means that we have totally avoided the recent fall out from the ending of speculative mania in cryptocurrencies such as Bitcoin – down 58% in the second quarter.

Continued on page 4.

Heritage Capital Management Limited

Review for the quarter ended 30th June 2022

Market Commentary and Outlook

It has been a very poor first half to 2022 for investors with both the overall World Index and the US as the largest single market falling into bear market territory, with losses for the year-to-date now standing at over 20%.

What makes things worse this time for investors is just how bad bonds are also performing. Most investors would not have experienced the last time that bonds also suffered such a major setback due to soaring inflation and rising interest rates, all the way back in the 1970s. For some time we have cautioned against holding long-term government bonds on very low yields as these are very exposed to the environment that we are now facing. Unfortunately many pension funds, who tend to be the major holders of these long bonds, are now facing big losses and the average UK gilt fund has lost 14% so far this year. In fact, incredibly it has been calculated that it has been the worst first half year since records began in 1788 for the benchmark 10-year US Treasury bonds.

Of course the major problem at the moment is the surge in inflation which is leaving central banks with a difficult balancing act. They could aggressively increase interest rates in order to try and curb inflation, but given the already fragile state of the global economy this would almost certainly result in a recession, which could be much harder to recover from than the recent short, sharp one as a result of the Covid pandemic.

United Kingdom

Having managed to buck the overall negative trend in the first quarter due to the FTSE 100 index's large weighting to energy and commodity companies, a weak second quarter means that the UK market is now also in negative territory for the year-to-date.

For investors in the broader UK market the results this year have been more akin to the other major global markets, with both the FTSE 250 mid cap and the FTSE small cap indices down by over 10% this quarter and around 20% for the year-to-date.

With UK inflation currently rising at the fastest rate for over 30 years the Bank of England's Monetary Policy Committee has made two further 0.25% interest rate rises this quarter and the base rate now stands at 1.25%.

United States

The overall S&P 500 index was down by 16.5% for the quarter resulting in a fall of over 20% for the year-to-date, making it the worst first half year for the US market since 1970, more than 50 years ago. One of the major reasons behind this has been a sell-off in technology stocks and the tech heavy Nasdaq index fell by over 20% in the quarter and is now down by 30% for the year-to-date.

Some of the previously high flying stocks that have suffered setbacks this year include Netflix which is down by 70%, Meta (owner of Facebook) down over 50%, Tesla, Amazon and eBay all down by around 35%, and even Apple, Microsoft and Alphabet (owner of Google) are down by over 20%.

US inflation has continued to surprise on the upside and currently stands at 8.6%, the highest rate since 1981. As a result, after a small initial interest rate increase in the first quarter, the Federal Reserve has started to move more aggressively, pushing rates up to 1.75% with further increases expected in the second half of this year.

Europe

European markets have also been having a bad year with a 11.5% fall in the second quarter taking the half year loss to just under 20%.

In common with other regions, inflation is also of major concern with the current rate of 8.6% being the highest ever recorded since the inception of the Eurozone in 1999. However, the European Central Bank has been very slow to respond having so far failed to increase interest rates from their historically low level of 0%, although ECB president, Christine Largarde, has finally indicated a small rise of 0.25% in July.

Japan

The Japanese Nikkei has held up relatively well with a fall of just over 5% this quarter, although for international investors losses would have been higher due to a weakening Yen. For the past few decades Japan has been battling with deflation and has constantly failed to meet the Bank of Japan's 2% inflation target. However, it has been down to the global inflationary pressures rather than any policy success that has finally seen Japanese inflation creep above 2% this year.

Emerging Markets

Emerging markets have also had a tough time, with a double digit percentage fall in the second quarter leaving the overall emerging market index down by around 17% for the year-to-date. Following the first quarter Covid lockdown, China was one of the few markets to post a positive return in the second quarter, although it was still down by over 10% for the first half.

Investment Statistics - 30/06/2022

Equity Markets	Q2 2022	2022 YTD	2021	2020	PE Ratio	Dividend Yield	Central Bank Interest Rates	10 yr Gvnmt Bond Yields	Exchange Rates	
									vs GBP	vs USD
TR Global ($)	-15.67%	-20.17%	18.84%	15.73%						
US (S&P 500)	-16.45%	-20.58%	26.89%	16.26%	19	2.2%	1.75%	2.97%	1.2175	1.0000
UK (FTSE 100)	-4.61%	-2.92%	14.30%	-14.34%	12	3.8%	1.25%	2.24%	1.0000	1.2175
Europe (STOXX 50)	-11.47%	-19.62%	20.99%	-5.14%	13	3.5%	0.00%	1.37%	1.1613	1.0482
Japan (Nikkei 225)	-5.13%	-8.33%	4.91%	16.01%	15	2.1%	-0.10%	0.23%	165.27	135.73

Total returns- including dividends

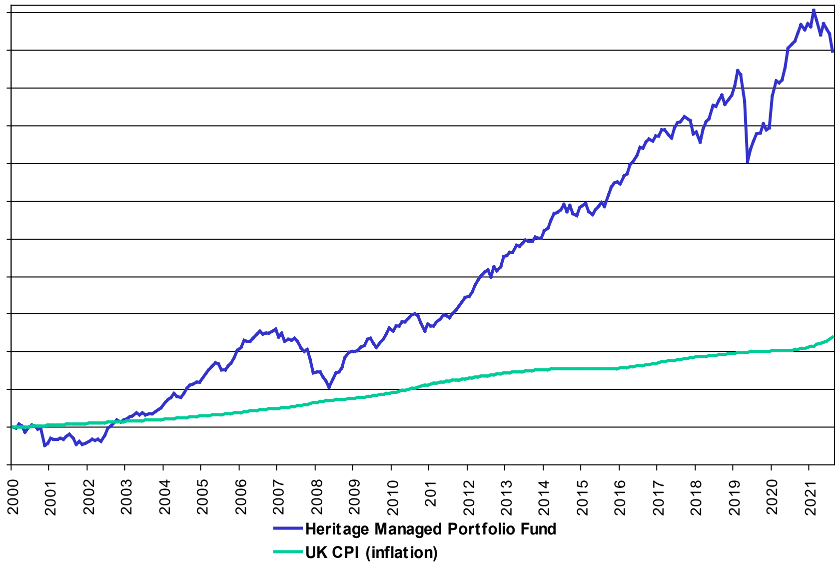
Source: Thomson Reuters

Heritage Managed Portfolio Fund

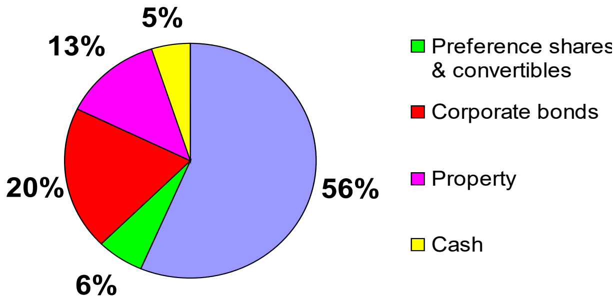
Review for the quarter ended 30th June 2022

Performance	Managed Portfolio Fund	Inflation (UK)	Fund information	
Return for the quarter (net)	-5.06%	2.11%	Price at 30th June 2022	£349.27
2022 year to date (net)	-7.25%	3.57%	Fund size	£204.3 million
Year 2021 return (net)	14.07%	2.20%	Fund domicile	Guernsey
Year 2020 return (net)	-1.87%	0.93%	Fund status	Non-distributor ("roll-up")
Year 2019 return (net)	16.31%	1.82%	Subscriptions/redemptions	Monthly dealing
Year 2018 return (net)	-2.76%	2.51%	Further Information	www.heritage-capital.co.uk
Year 2017 return (net)	11.50%	2.72%		
Year 2016 return (net)	7.48%	0.68%	**Risk**	**Annual Volatility**
Year 2015 return (net)	6.80%	0.04%	Managed Portfolio Fund	7.4%
Compound annual return since 2001	6.35%	2.12%	TR World Index	13.9%

Price Performance



Asset Allocation



Commentary

The Managed Portfolio Fund seeks to generate attractive long-term investment returns at a lower risk than that associated with pure equity market investment through active management of a well diversified multi-asset portfolio.

The weak start to the year due to the war in Ukraine and rising inflation has worsened further in the second quarter, with the World Index falling into bear market territory. Against this background the Managed Portfolio Fund has held up relatively well, with a 5.06% fall in the quarter leaving it down by 7.25% for the year-to-date.

Whilst the majority of our holdings have been negatively impacted by the general market weakness, there were a few notable exceptions with Beazley & BP Marsh (insurance), HSBC & Standard Chartered (banks) and AstraZeneca & GSK (healthcare) amongst the few making a positive contribution.

Our listed property companies have also generally had a tough time but overall performance was helped by Secure Income REIT, which received a take-over approach and Circle Property, which has begun realising assets in order to eliminate the large discount to net asset value.

It continues to be a tough environment for bonds, with rising interest rates and inflation hurting investment grade bond prices and general risk aversion weighing on higher yielding bonds. With the major asset classes all suffering at the moment it was good to see our alternative assets providing some diversification benefits with The Renewables Infrastructure Group for example, generating a positive return.

Whilst the near term outlook remains uncertain, we believe that our portfolio of investments is well positioned to generate attractive returns for long-term investors, whilst our relatively defensive positioning should provide some protection against the risks of any short term continued market weakness.

“ Spotlight On” - The importance of investment income (continued)

Furthermore, as a multi-asset fund we do not just rely on dividends from shares, as we also receive a decent level of income from the interest on our corporate bonds and the flow through of rental income from our property based investments.

The combination of reinvesting all of the income that we receive from our portfolio of investments and allowing it to compound, together with some reasonable long-term capital growth, provides a powerful and positive long-term force, all of which has helped £1,000 invested in our Managed Portfolio Fund at inception in 2000 to grow to be worth £3,493 today.

Bloomsbury - a small company example

Much of the commentary around investing tends to focus on overall markets, indices and macro-economic and geopolitical events. Whilst these topics can sometimes help to explain what drives short term market movements, it is the progress of the individual companies that it of most interest to us, as that is what drives long-term returns and Bloomsbury Publishing provides a good example.

The company first found fame as the small publisher that accepted JK Rowling’s Harry Potter script after the author had been rejected by all other publishers. Many thought that the company was just a one trick pony but it has astutely reinvested the proceeds from this initial success. A critical decision that we particularly liked a few years ago was to develop its own in-house digital publishing platform, rather than making an expensive acquisition and this year it met its target ahead of schedule by making over £15m turnover and £5m in profits from its Bloomsbury Digital division.

In fact Bloomsbury ticks many of the boxes that we look for. It is still run by its founder, Nigel Newton, who is also a major shareholder, it is conservatively managed preferring organic growth and small bolt on acquisitions to big deals and it has a strong balance sheet with net cash and no debt. Furthermore, as a small niche player in a large market it still has much potential to keep growing for many years to come.

We first invested in Bloomsbury seven years ago and since then it has doubled its profits and dividends and shareholders have also been rewarded by a doubling of the share price. A perfect example of how a well managed individual company can produce pleasing long-term returns without any need for us as investors to worry about Brexit, recessions, pandemics, wars and all manner of other macro-economic and geopolitical events.

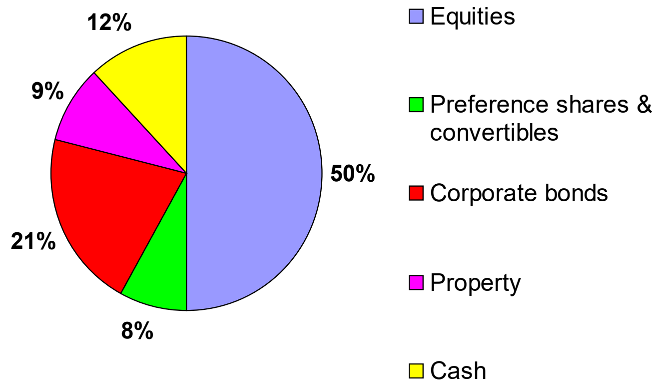
SVS Heritage Balanced Portfolio Fund

Price at 30/06/22	1.367p (launched at 100p 1/12/16)
Fund size	£33.5 million
Fund type	OEIC, UCITS (UK domiciled)
Eligible for	ISAs, SIPPs, Funds at Lloyd’s
Pricing and dealing	Daily
Minimum Investment	£10,000
Administrator/ACD	Smith & Williamson

Performance

Return	2022 Q2	2022 YTD	2021	2020	2019	Inception 01/12/16
SVS HBPF	-5.07%	-8.07%	15.00%	-1.52%	18.29%	36.70%
UK CPI	2.11%	3.57%	2.20%	0.93%	1.82%	14.69%

Asset allocation



Commentary

The approach adopted by the Fund is in line with the existing larger offshore version of the fund (the Guernsey regulated Heritage Managed Portfolio Fund) – i.e. to generate long-term investment returns at a lower risk than that associated with pure equity market investment through active management of a well diversified multi-asset portfolio.

The Fund was down by 5.07% this quarter and by 8.07% for the year-to-date. The more detailed comments on the Heritage Managed Portfolio Fund performance on page 3 of this newsletter also apply to the SVS Heritage Balanced Portfolio Fund.

Further details and the full fact sheet for the fund can be found on our web site at www.heritage-capital.co.uk.

The information set out above does not constitute an offer to subscribe to shares, which may only be purchased after reading the full Prospectus/Key Investor Information Document (KIID). The Prospectus and KIID can be found at www.heritage-capital.co.uk.

Heritage

Heritage Capital Management Limited
Broadway House, Tothill Street, London SW1H 9NQ
Tel: +44 (0) 20 7799 2110 Fax: +44 (0) 20 7222 1599
General email: info@heritage-capital.co.uk
Website www.heritage-capital.co.uk