Heritage

Quarterly Newsletter & Investment Review

Issue 100 Quarterly news & investment review from Heritage Quarter 4 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

A bright finish to a difficult year

Global markets finally managed a small recovery in the final quarter but it was not sufficient to prevent 2022 from being an historically bad year for investors. The main causes have been the war in Ukraine and the resultant shock rise in inflation and interest rates. Overall equity markets have suffered their worst year since the 2008 global financial crisis with a fall of close to 20%, and bonds have had their worst ever year on record on most measures, with an overall estimated loss of around 16% for all global government and corporate debt.

The Heritage Funds have also had a tough year, although a final quarter gain of over 4% has at least managed to pare the full year loss to under 10%. As usual further details for the Heritage Managed Portfolio Fund can be found on page 3 and the SVS Heritage Balanced Portfolio Fund on page 4.

Heritage reaches 30 year milestone

Whilst 2022 has certainly not been a vintage year for investors, we do at least have something to celebrate, as Heritage has recently reached the 30th anniversary of its formation, which we are pleased to report in this, the 100th edition of our newsletter.

Heritage was founded in 1992 with a view to providing a personal service to private clients who are primarily concerned with preserving and enhancing their accumulated wealth. Our investment approach has therefore always been fairly conservative and fortunately this has helped us to navigate some fairly turbulent times over the years, including the bursting of the technology bubble which followed the internet mania of 2000, the great global financial crisis of 2008, and more recently the global coronavirus pandemic.

One of our early major developments was the establishment in 1996 of the Heritage Investment Funds, as this allowed us to genuinely pool our own family money with our clients and enabled us to more efficiently and effectively manage larger amounts for a growing number of clients. From under £20 million at inception, our managed funds have increased significantly in size and stand at over £200 million today. Our largest fund, The Heritage Managed Portfolio Fund now has a track record of over 20 years and £1,000 invested at launch would be worth over £3,400 today.

We are proud to say that as we have no sales or marketing team, the increasing amounts entrusted to us to manage over the years has arisen entirely from doing a good job for our existing clients and relying on them and our network of contacts for referrals - for which we continue to be very grateful.

Another important factor has been the stability of our team. Whilst nearly all of our peers and competitors have succumbed to endless changes in corporate identity ownership and personnel, our core team at Heritage is very well established. This longevity has allowed us to build genuinely long-term investment strategies as well as long-standing relationships with our clients and in many cases we are now looking after second or even third generations of families.

Hopefully the foundations and principles that we have established, together with the experience that we have gained over the past 30 years, leave us well placed to meet the inevitable challenges that we will face in the years ahead and we can look forward with optimism to the next 30 years.

Heritage Capital Management Limited

Review for the quarter ended 31st December 2022

Market Commentary and Outlook

Whilst a decent final quarter rally brought some relief to investors, it was not sufficient to save 2022 from being the worst year for global markets since the financial crisis in 2008.

The main problem was that Russia's invasion of Ukraine in February changed the inflation outlook completely. The war sparked a global commodity price shock, which combined with supply chains that had not yet fully recovered from Covid, pushed inflation to levels that had not previously been contemplated. Central banks were caught off guard and as they scrambled to raise rates to try and contain the inflationary threat, investors were given a reminder of just how much damage rising yields can inflict on the capital value of all financial assets.

Whilst 2022 was a painful experience as yields moved higher and prices fell, at least the starting point from where we stand today looks more encouraging. Government bonds that were yielding around 1% at this time last year now yield close to 4% and higher yields can be found in the corporate bond market. Shares also look better value with PE ratios having fallen to more realistic valuations and dividend yields have risen.

United Kingdom

For the first time in a number of years the FTSE 100 index has comfortably outperformed the other major market indices, helped by its relatively high weighting of energy and commodity companies and decent performances from a few global multinationals that have benefitted from a weaker pound such as AstraZeneca, HSBC and Unilever.

However, for investors in the broader UK market the results this year have been more in line with the other major global markets, with both the FTSE 250 mid cap and the FTSE small cap indices ending the year down by around 20%.

Following the political chaos of the previous quarter, Liz Truss was rapidly replaced by Rishi Sunak as the UK's latest prime minister and thankfully some stability has been restored and the pound has also staged a decent recovery over the final quarter. However, there remains much to do with inflation still running at over 10% and widespread public sector strikes over pay.

Meanwhile the Bank of England has continued to raise interest rates from 0.25% at the start of the year to the current rate of 3.5% with further rises expected in 2023, although this is a delicate balancing act with the risk of a deep recession if rates rise too far.

United States

The S&P 500 index ended the year down by 20%. Just as it was the large technology companies that drove the markets higher in the bull market, it has been the same group that has led the market into the current bear market with the tech heavy Nasdaq index now down by 33% this year.

Rising interest rates are particularly harmful to growth stocks whose expected future earnings extend well into the future and are discounted back to a much lower present value. The list of big name stocks that fit into this category include Tesla down 65% this year, Meta (Facebook) down 64%, Amazon down 50% and other large growth stocks including Apple and Alphabet (Google) were also down by over a quarter.

With US inflation still running at over 8% the Federal Reserve has continued to raise rates to their current level of 4.50% and expectations are that they could reach 5% by the end of 2023.

Europe

Of all the major markets Europe has enjoyed the strongest rally in the final quarter but it was not enough to prevent an overall double digit loss for the full year.

In common with other regions, inflation is also of major concern across Europe with the German rate currently running at 10%. Having been slow to react to the inflationary threat the European Central Bank has belatedly been raising Euro interest rates which now stand at 2.5%.

Japan

Japan was the one major market that did not really participate in the final quarter rally, although over the full year the loss was lower than most at just under 10%. However, for international investors losses would have been much higher due to a severe weakening of the Yen this year.

Emerging markets

Emerging markets have also had a tough year with the overall emerging market index down by around 20%. As always there has been a wide range around this from Korea which was down 35%, to Brazil and India which were marginally up over the year.

However, the biggest reminder of the risks involved in emerging markets is the near total loss suffered by investors in Russia this year.

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Investment Statistics - 31/12/2022

Equity Markets	Q4 2022	2022	2021	2020	PE Ratio	Dividend Yield	Central Bank Interest Rates	10 yr Gvnmt Bond Yields	Exchange Rates	
									vs GBP	vs USD
TR Global ($)	9.81%	-17.91%	18.84%	15.73%						
US (S&P 500)	6.50%	-19.92%	26.89%	16.26%	19	2.2%	4.50%	3.83%	1.2097	1.0000
UK (FTSE 100)	8.09%	0.91%	14.30%	-14.34%	11	3.9%	3.50%	3.67%	1.0000	1.2097
Europe (STOXX 50)	14.33%	-11.74%	20.99%	-5.14%	13	3.5%	2.50%	2.56%	1.1304	1.0702
Japan (Nikkei 225)	0.61%	-9.37%	4.91%	16.01%	14	2.3%	-0.10%	0.42%	158.58	131.11

Total returns- including dividends

Source: Thomson Reuters

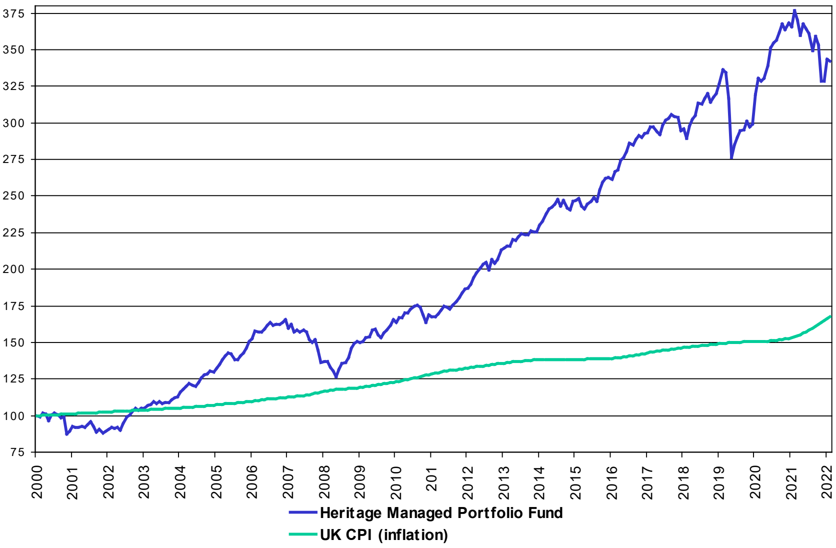
Heritage Managed Portfolio Fund

Review for the quarter ended 31st December 2022

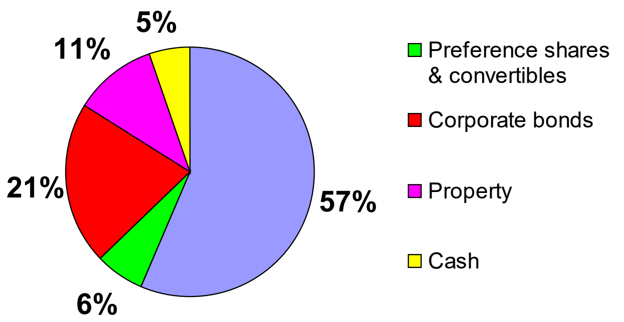
Performance	Managed Portfolio Fund	Inflation (UK)
Return for the quarter (net)	4.12%	2.68%
Year 2022 return (net)	-9.14%	8.97%
Year 2021 return (net)	14.07%	2.20%
Year 2020 return (net)	-1.87%	0.93%
Year 2019 return (net)	16.31%	1.82%
Year 2018 return (net)	-2.76%	2.51%
Year 2017 return (net)	11.50%	2.72%
Year 2016 return (net)	7.48%	0.68%
Year 2015 return (net)	6.80%	0.04%
Compound annual return since 2001	5.76%	2.37%

Fund information	
Price at 31st December 2022	£342.16
Fund size	£181.6 million
Fund domicile	Guernsey
Fund status	Non-distributor (“roll-up”)
Subscriptions/redemptions	Monthly dealing
Further Information	www.heritage-capital.co.uk
Risk	**Annual Volatility**
Managed Portfolio Fund	7.6%
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 final quarter has seen a much welcome partial recovery in markets, which helped the Fund produce a positive return of 4.12% and for the full year the fall was 9.14%.

Amongst our shares there were a number of notable contributors this quarter, with most also being the best performers for the full year with Beazley, Shell, Astrazeneca, Hiscox, Bloomsbury and Lancashire all gaining over 20% this year. However, overall there were many more negative contributors in 2022 across a variety of sectors and our international and far eastern funds also generally had a poor year.

Our property holdings also had a difficult year as the market digested the impact of higher interest rates on property values. Fortunately most of our property companies had previously fixed their borrowings at what now look like very attractive levels and with much of their rent set to rise through inflation index linking, the prospects for income growth look attractive.

Our bond portfolio has also had a poor year with the fall in capital values outweighing the interest income that we received. However, with the income yield now standing at 7.5% and an average yield to redemption of over 8% there is good potential for decent returns in the years ahead and we have been selectively topping up some holdings and adding a few new ones.

Whilst the near term outlook remains uncertain, we believe that our portfolio of well diversified investments is well positioned to generate attractive returns for long-term investors.

Bonds are finally starting to look more attractive

With most bond market indices and funds suffering their worst year on record in 2022, it may seem odd to be writing about the merits of fixed interest securities as an attractive investment but as explained below bonds are finally starting to look interesting again.

For well over a decade now government and high quality investment grade bonds have been on paltry yields of close to zero. In fact less than a year ago it was even estimated that nearly $20 trillion, or over 20% of all government bonds were on negative yields and 90% of government bonds yielded less than 1%.

Apart from making bonds fundamentally unattractive, low yields also reduced the ability of bonds to provide diversification benefits in an economic downturn.

The return of inflation in 2022 has resulted in a dramatic increase in both interest rates and government bond yields and this rise in rates has negatively impacted the values of all financial assets including bonds, shares and property.

However, whilst this correction was painful, the income on offer from bonds is now much more attractive. Bonds also now offer potential diversification benefits as any further downside in stock markets could be cushioned by fixed income returns if yields come down from current levels to combat a recession. Thus, the ability for investors to build diversified portfolios using bonds has improved.

It is also important to note that the key difference between bonds and equities is that unless the issuer of the bond goes bust you know what your future cash flows and hence return will be. So whilst the future for equity markets remains as uncertain as ever, bond investors know what their future yield will be if they hold the bond to maturity and for the first time in over a decade the prospective returns are looking quite reasonable. Investment grade bonds that were previously yielding under 1% can now be bought on yields of around 3% to 5%. This has also had a knock on effect for higher yielding bonds and for investors who are prepared to do a bit more credit analysis it is possible to find sound bonds offering yields of 5% to 10%.

Overall, whilst 2022 has provided a painful reminder of how low yielding bonds can be a poor investment, the higher yields on offer from bonds today provide much more positive prospects for decent future returns. In fact we are even considering starting a new bond fund, which will also depend on the level of interest from clients, so please do let us know if this is something that might be of interest.

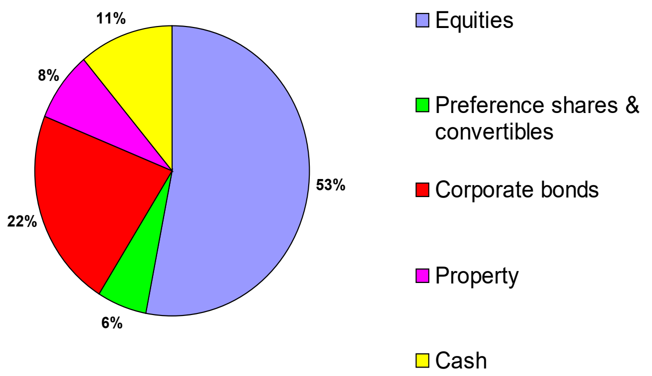
SVS Heritage Balanced Portfolio Fund

Price at 31/12/22	1.364p (launched at 100p 1/12/16)
Fund size	£31.67 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	Evelyn Partners

Performance

Return	2022 Q4	2022	2021	2020	2019	Inception 01/12/16
SVS HBPF	5.65%	-8.27%	15.00%	-1.52%	18.29%	36.40%
UK CPI	2.68%	8.97%	2.20%	0.93%	1.82%	20.67%

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 up by 5.65% this quarter and down by 8.27% for the full year. 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.

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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