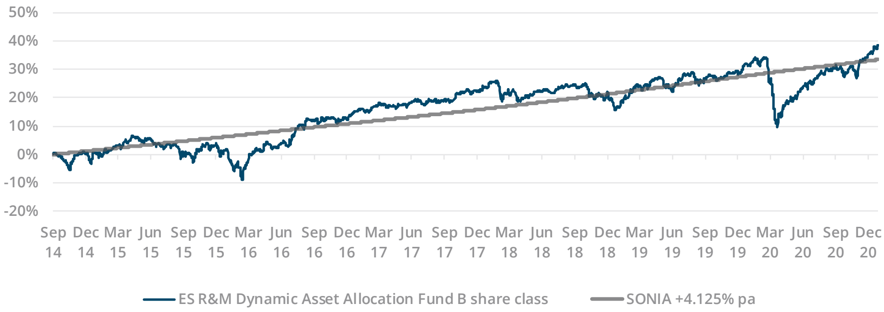
31 DECEMBER 2020

ES River and Mercantile
DYNAMIC ASSET ALLOCATION FUND
CLASS B GBP (Accumulation)

PAST PERFORMANCE
The charts and tables below show the performance of the fund's GBP B (Acc) share class since the fund's inception date of 2 September 2014.

Source: River and Mercantile Asset Management LLP. Fund performance is calculated using midday published prices. Benchmark performance is calculated using close of business mid-market prices.
Past performance is not a reliable guide to future results.

PERFORMANCE SINCE INCEPTION


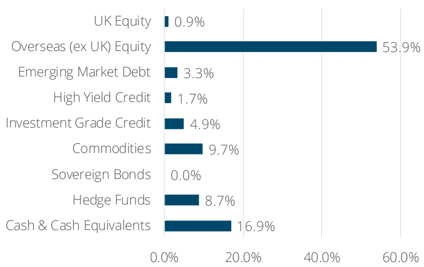
CUMULATIVE PERFORMANCE

	1 month %	3 months %	1 year %	3 years %	5 years %	Since inception %
B share class (Acc)	3.1	7.8	5.6	12.0	36.2	38.4
Benchmark	0.4	1.1	4.4	14.8	25.5	33.4

DISCRETE 12 MONTH PERFORMANCE

	12 months to 31/12/2016	12 months to 31/12/2017	12 months to 31/12/2018	12 months to 31/12/2019	12 months to 31/12/2020
B share class (Acc)	13.3%	7.3%	-5.5%	12.2%	5.6%
Benchmark	4.6%	4.5%	4.8%	5.0%	4.4%

ALLOCATION BY ASSET CLASS
This table shows the fund's asset allocation by portfolio weight.



Source: River and Mercantile Investments Limited

TOP 10 POSITIONS
This table shows the fund's ten largest positions by weight.

	Weight (%)
Vanguard FTSE Emerging Markets UCITS ETF	9.9
Insight GBP Liquidity Fd	6.7
River and Mercantile Global Macro Z GBP Acc	6.1
Neuberger Berman Global Flexible Credit Fund	4.9
Vanguard S&P 500 ETF	4.8
BlackRock ISC Sterling Liquidity Fund	4.6
iShares Physical Gold ETC	4.5
Vanguard S&P 500 UCITS ETF	3.4
T Rowe Price Funds SICAV - Global High Income	3.3
iShares Physical Silver ETC	3.1

Source: River and Mercantile Investments Limited

INVESTMENT OBJECTIVE
To achieve an average return (income and growth in the value of your investment (known as "capital growth")) of 4.125% per year above cash (based on the SONIA interest rate) (the "Benchmark") over a rolling 3-year period, after the deduction of all fees.

PORTFOLIO MANAGERS
Mike Faulkner and Joe Andrews

KEY FACTS

Fund launch date	02/09/2014
Share class launch date	02/09/2014
Benchmark	SONIA +4.125% p.a
Total fund size	£235.1m
Domicile	UK
Fund type	UCITS
SEDOL	BLZH7L2
ISIN	GB00BLZH7L20
Bloomberg	RMDAABA
Distribution type	Accumulation

FEES & CHARGES

Initial charge	Up to 5.25%
Annual management charge	0.55%
Ongoing charge (includes AMC)	0.82%

DEALING INFORMATION

Dealing frequency	Daily
Dealing cut-off time	12pm (UK)
Valuation point	12pm (UK)
Settlement	T+4
Minimum investment	£1000

SYNTHETIC RISK & REWARD INDICATOR (SRRI)

1	2	3	**4**	5	6	7

Lower risk — Higher risk

Typically lower rewards — Typically higher rewards

MANAGER'S REVIEW

The last two months of 2020 were extraordinary in market terms, both in terms of the magnitude of the reversal into cyclical stocks within equity markets, and strength of the rally that followed. To illustrate, the Russell 2000 index rallied 29% in the last two months of the year.

We have been advocating equity exposure in general for some time, and higher cyclical exposure since October, so have been able to benefit from this. But the strength of these moves does beg the question, how long can it continue? And how does this influence our approach to investment strategy going forward?

A great environment for listed equities

As we stand today, our best guess is that we ought to see a correction (downwards) or at least a pause in equity markets. How long that takes if it happens is anyone's guess, but markets are often completing these moves relatively quickly (within a month or two).

Our underlying thesis – that this is a great environment for listed equities – remains. Government bond yields are still very low and. in several cases, negative. Credit spreads are back to levels consistent with a "things are pretty decent" economic environment.

Real estate has significant supply issues because the change in working practices in a post COVID world means that less space is needed than before. Couple this with the question "what do we do with all those redundant shopping malls?" and we've got a supply issue that will take some time to work through.

All of this is great for companies themselves. The cost of borrowing is very low by any standard, which means projects need a lower return threshold to be viable. The benefits of more projects being viable flows to the equity holders. Depressed real estate rents given the supply issues will also benefit companies.

All of this leads back to listed equities being the engine of returns going forward. If volatility and cashflow weren't issues, it's conceivable that portfolios might be dominated by equities in this kind of environment.

In a sense that makes strategy easy, but it also presents another problem, which is price.

Does price matter?

There is no question that historically the highest returns on equities have come from points of lowest prices, and vice versa. Simplistically, if you bought the equity market at the peak in 2000, it took you a long time to achieve a positive return. If you bought at the bottom in 2009, you've done incredibly well.

Clearly price matters. But equity price moves in the medium term can be influenced by more than just earnings expectations – for example, discount rates in the form of bond yields. Logically, companies that have very stable profit margins and low debt would see their share prices rise simply because bond prices rise (yields fall). The company itself has bond-like attributes. So when commentators say "this move was just a P/E (price-to-earnings ratio) expansion and not earnings-led, and therefore can't continue", they ignore the bond yield effect. It can continue if bond yields keep falling.

With bond yields falling dramatically in 2020, this is precisely what we've seen. The difference this time compared to prior periods of falling yields is that the very largest companies have been the beneficiaries, and it has skewed the pricing on the whole index. Apple, Microsoft, Amazon, Alphabet and Facebook together make up more than 10% of the MSCI World ACWI IMI index, which is intended to broadly represent global investible equities.

What we believe has happened in the last few years is that the attractiveness of these companies as relatively stable earning, low debt businesses has led investors to up-rate them because of falling bond prices. That in itself is not unusual - historically we have tended to see this in other companies with these characteristics. What is different this time is the size of these companies and their effect on the apparent valuation of indices. Together these companies have an average P/E ratio of close to 35. The long-term average P/E on the S&P index is around 16. So, are these companies worth that? We think they're great companies, albeit several them have some significant anti-trust problems ahead. They are decent growers. But does that growth rate justify these valuations? We think it's far more likely that the valuation is justified by low bond yields. If we look at the market excluding these companies, the multiples are quite different.

What we believe we have, in this market environment, is a relatively significant segment of the market that is essentially a view, not so much on the company, but on the direction of bond yields. If bond yields in the US drop to 0%, we believe we'll see significant rises in those large companies. But if they rise to 2% from here, it will create headwinds for them (however good companies they are) while being a tailwind for a range of other equities that will benefit from this environment.

What does all this mean? Simply we think there are dangers in implementing a strategy focused on listed equities through a passive strategy or something that looks a lot like the index. The real benefits will come in being more selective about the nature of the exposure you have. This issue is particularly acute because it seems more likely that there may be upward pressure on bond yields in the next 12 months or so.

Dynamism within equities proves its value

The wide disparity between different segments of the equity market will likely continue. We believe that in an environment where listed equities will be the primary driver of returns, allocation within equities essentially becomes the new asset allocation. Real value can be generated by making decisions to allocate to different segments. We have done this throughout the last year and particularly in the last quarter, and expect these sorts of decisions to form an increasing part of how we add value.

In the coming 12 months or so, we continue to expect cyclicals to outperform defensives, and the rest of the world (particularly emerging markets) to outperform the US. However, the opposite may well happen in the short run if we see a correction in Q1, and that is an influence on our current positioning.

The migration of capital out of the US to the rest of the world, as the world reflates, raises an interesting question around inflation, to which we want to turn next.

Are policymakers able to manufacture inflation?

There is lots of talk now about inflation and the inflation trade. We are seeing increasing amounts of inflation scaremongering going on, usually to persuade people to buy cryptocurrencies or gold. We have no problem with either asset, but the question about whether we will actually get inflation is a more involved one.

We have been making the argument for some time now that inflation is an increased risk, not least because governments and central bankers want it. There is plenty of stimulus in the system, and historically money printing has tended to lead to inflation, except post 2008/9.

The problem with this assumption as an automatic transmission mechanism is that it ignores another force. Left unchecked, one could argue that we are in a deflationary environment because the rate of technological improvement is very high. Technology, all else being equal, tends to be deflationary.

We want to use an example from history as a thought experiment. In the industrial revolution (in the period post-1870) the US economy grew dramatically. But it did that during a period of deflation. Perhaps this is not surprising, because the cost of "stuff" fell as production became more efficient (technological improvement). The market naturally cleared at lower prices, and the economy multiplied. At the time there was no central bank dictating monetary policy or stimulus.

But how would this play out today? In theory, an inflation-targeting central bank would look at the deflation level, determine that it was inappropriate, and stimulate. The net result would be a lot of money printing, but a relatively low level of inflation because the stimulus was simply offsetting a deflationary force.

We do think it is conceivable we could see genuine inflation if enough money is printed, but we are doubtful it will be high levels of inflation unless we have a tight labour market. That's hard to see in the near future with the degree of technological improvement going on. Commodity prices, especially in some of the metals, seems like the most likely source of inflation but whether that's enough is an open question.

Our point is that, while there is reason to worry about the resurgence of inflation, thought should also be given to the possibility that governments and central banks are unable to manufacture it. What does this mean? If inflation doesn't arrive, short rates will stay lower for even longer than people think. Ordinarily, that would argue for lower bond yields, but they're already low. The place this should show up is in reasonably priced growth companies, where the benefit of lower yields for longer will be felt in the discount rate effect we described for the mega-cap stocks above. Therefore, we will likely prefer a strategy that emphasises cyclicals and growth, with an increasing emphasis towards emerging markets, as a means of balancing these issues.

The possibility of inflation does raise the question of the value of monetary assets, such as precious metals and cryptocurrencies. We have favoured gold and silver for this reason. We do believe that there is value in these types of assets in an environment where the interest rate is running below the inflation rate (i.e. there is a negative real interest rate). But we advocate treating the asset more tactically because it doesn't produce a yield and therefore if it goes nowhere it is essentially dead capital. As a result, where we are able, these positions should be managed quite actively to avoid this issue.

MANAGER'S REVIEW (CONTINUED)

PORTFOLIO CHANGES

Several changes were implemented in December. We continued to trade precious metals tactically, increasing exposure to gold and adding silver. The equity portfolio was restructured while keeping the overall equity allocation unchanged. Exposure to emerging markets was increased at the expense of developed markets, whilst broad passive equity was reduced in favour of direct equities focussed on strong ESG characteristics, cyclicals and technology. Credit exposure was decreased in favour of cash as yields continued to fall, while US Dollar exposure was entirely removed from the portfolio.

Mike Faulkner & Joe Andrews
January 2021

FUND RATINGS

FE CROWN FUND RATING

OTHER INFORMATION

Authorised Corporate Director	Equity Trustees Fund Services Limited
Investment manager	River and Mercantile Asset Management LLP
Depositary	The Bank of New York Mellon (International) Limited