

# MODEL PORTFOLIO SERVICE

## MONTHLY COMMENTARY

SUCCESSION  
MODEL PORTFOLIOS

POWERED BY

7IM

AUGUST 2023

### Portfolio Performance

At 7IM, we believe that taking a long-term view is essential when investing. We can't always avoid the short-term bumps and shocks that the financial world has in store, but a well-diversified portfolio goes a long way towards smoothing out some of the journey. The long-term nature of our strategic and tactical process is a good complement to the Succession Matrix Expected Parameters.

	Q2/2018	Q2/2019	Q2/2020	Q2/2021	Q2/2022	3 Year Ann. Return	5 Year Ann. Return	Succession Matrix Expected Parameters – Ann. Return
	-	-	-	-	-			
	Q2/2019	Q2/2020	Q2/2021	Q2/2022	Q2/2023			
Defensive	2.84%	3.35%	4.61%	-5.95%	-1.55%	-1.11%	0.48%	3.0 – 4.5%
Cautious	2.45%	2.74%	8.37%	-5.50%	0.36%	0.76%	1.56%	4.5 – 6.0%
Balanced	2.08%	1.96%	12.90%	-5.09%	2.80%	3.08%	2.68%	5.2 – 7.5%
Moderately Adventurous	1.59%	0.44%	17.07%	-4.27%	5.04%	5.23%	3.60%	6.0 – 8.0%
Adventurous	1.45%	-0.95%	20.11%	-3.83%	5.63%	6.30%	3.90%	7.0 – 10.0%
Income	5.40%	-2.60%	11.95%	-4.99%	1.19%	2.48%	1.99%	

Source: 7IM/FE. Annualised return is defined as 'Ann. Return' in the performance table above and is as at end August 2023. Market returns have been poor in absolute terms since the beginning of 2020 with the Covid pandemic and then the inflationary shock of 2022. While portfolios have held up well relative to peers, the 3 and 5 year absolute returns are lower than average, even though the since inception longer term numbers are in line with expected parameters..

### Summary

After a strong rally for global equities this year, the financial markets faced the first monthly decline in US equities since February. The S&P 500 lost 1.6%, while the technology-heavy Nasdaq lost 2.1% over the month of August.

As we mentioned last month, the S&P 500 has relied heavily on the 'Magnificent Seven' (Meta, Microsoft, Alphabet, Apple, Amazon, Tesla and Nvidia) this year. However, it has been Nvidia who has grabbed the headlines and been the main driver of the seven's performance.

While it used to be a gaming company, now it is all about data centres. The AI revolution boosted the demand for data centres as everyone raced to build their own ChatGPT rivals. Hopes for the company's quarterly results were high, but Nvidia's whopping US\$13.5bn in revenue surpassed analysts' wildest expectations by US\$2bn.

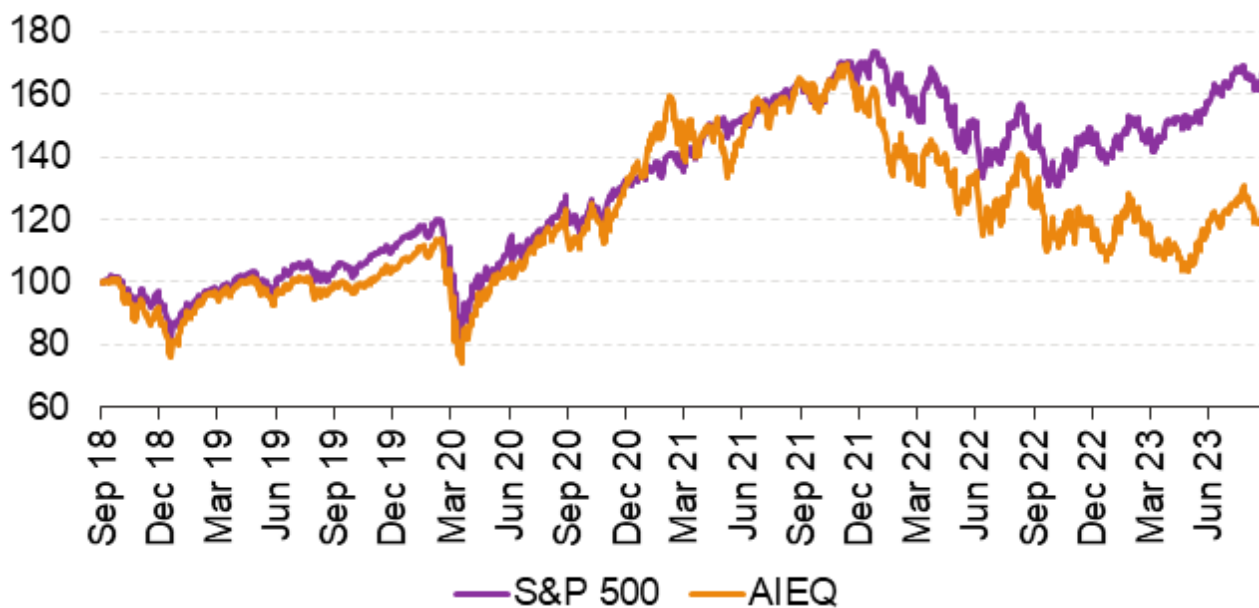
The concept of AI has been around for decades now, from AI vs humanity in the Terminator franchise, to creepy AI realities in the Netflix series *Black Mirror*. But now it has invaded real life.

So, are we in an AI stock bubble? Investopedia summarises the five stages of a stock bubble as follows, and we can see whether AI fits into this:

1. Displacement occurs when investors get enamored with a new paradigm – ✓
2. Price rises slowly at first, then gains momentum –✓
3. Euphoria in markets as prices skyrocket and valuations reach extreme levels – ✓
4. Profit taking when warning signs show the bubble is about to burst – X.
5. The bubble is pricked and bursts – X

It is looking increasingly likely that we are in an AI-related bubble. We've had bubbles before, and we know that they correct in due course – often violently.

Ironically, in the midst of all this AI hype, it looks like AI-powered ETFs are not keeping up with the AI computing boom!



Source: Bloomberg Finance L.P

This just shows AI can't replace everything, human intervention and expertise is still vital in the world of investing.

Taking a deeper look at why we had a dip in the equity markets this month:

- US Treasury Yields increased given better-than-expected economic data, dragging down US stocks. The Fed has reaffirmed that they are determined to get inflation back to 2%, meaning the interest rate could stay higher for longer. US credit was also downgraded by Fitch earlier in the month due to "a high and growing general government debt burden, and the erosion of governance"<sup>1</sup>, although this had a limited impact on yields
- Closer to home, we also saw a decline in FTSE 100 and Eurostoxx 50, returning -2.6% and -3.8%, respectively, as the inflation and interest rate story continues
- China also played a part in August's loss. Beijing has put in measures, such as lowering the interest rate, to boost sluggish growth, but fears of economic slowdown and property crisis persist. Economic data came in weaker than expected, with youth unemployment at record highs.

### Portfolio Positioning and Changes

In August, we moved some of our US exposure into a low-cost equal-weight index, diversified across S&P 500 constituents. This aligns with our preference of avoiding tech-weighted US exposure.

### Core investment views

At 7IM, we have a number of long-term core views that help to guide our investment decisions and allocations within portfolios.

Over the next 12 months, we think that **the global economy will slow down – prompting bouts of volatility**. In this environment, it is important to rely on a stable identity. Economic uncertainty creates fear and investor sentiment tends to overreact to economic turning points. Going forward, we believe that:

- **Inflation is coming down:** Across the developed world, inflation has peaked, and is mostly falling. Supply-chain disruptions have eased, energy prices are a little more settled, and companies are no longer reporting issues with finding workers. Of course, slower inflation still means rising prices – so the cost of living pain isn't going away quickly

- **Interest rates are high:** We're now over a year into the rate hiking cycle. Interest rates are unambiguously high when compared with the past decade. The impact of higher rates is always the same – although time-to-effect changes in every cycle
- **The economy is slowing:** For consumers and companies, day-to-day life is getting harder – whether it's rising costs or increased debt, there's less money left at the end of the week or month. As the flow of money around the economy slows, strong growth is more difficult to achieve. The world may or may not slip into a 'technical' recession in the next three months, but a sluggish growth environment is already here.

Sluggish and sideways... In an environment with lots of uncertainty and a lack of confidence, we want to make sure portfolios are insulated against shocks, while still generating sufficient returns to make investing worthwhile. And we think our portfolios are set up to do just that.

There's no one answer... When managing a diversified long-term portfolio, there shouldn't be a single 'big' call. For an outlook that calls for selectivity, especially in the medium and short term, we're finding lots of different opportunities – both to protect capital and to grow it.

## ASSET ALLOCATION

### Detailed asset allocation

	Defensive TAA	Cautious TAA	Balanced TAA	Growth TAA	Aggressive TAA	Income TAA
UK Equity	7.50%	9.50%	17.50%	20.50%	23.50%	20.50%
North American Equity	6.00%	10.00%	16.00%	17.00%	15.50%	12.50%
European Equity	3.00%	3.50%	4.00%	6.00%	6.50%	5.00%
Japan Equity	2.00%	2.50%	4.50%	7.00%	8.50%	3.50%
Emerging Market Equity	2.00%	3.00%	2.00%	4.50%	8.00%	4.00%
Global Themes	5.50%	7.00%	10.50%	16.00%	20.50%	6.50%
Global Govt Bond	23.50%	7.00%	6.50%	0.00%	0.00%	9.00%
Gilts	6.50%	3.50%	1.50%	0.00%	0.00%	1.00%
Sterling Corporate Bonds	0.00%	3.50%	0.00%	0.00%	0.00%	4.00%
Global Corporate Bonds	7.50%	13.00%	6.00%	0.00%	0.00%	9.00%
Global High Yield Bonds	3.50%	3.50%	4.50%	5.00%	4.00%	7.50%
Emerging Market Bonds	1.50%	3.00%	3.00%	2.50%	0.00%	4.50%
Emerging Market Bonds Local	1.50%	3.00%	3.00%	2.50%	0.00%	4.50%
Global Inflation Linked Bonds	6.00%	3.00%	0.00%	0.00%	0.00%	0.00%
Real Estate	1.50%	4.00%	3.00%	2.50%	4.50%	6.00%
Alternative Strategies	20.50%	17.50%	15.00%	13.50%	6.00%	0.00%
Cash & Money Market	2.00%	3.50%	3.00%	3.00%	3.00%	2.50%
Infrastructure	0.00%	0.00%	0.00%	0.00%	0.00%	5.00%

Source: 7IM.

<sup>1</sup> <https://www.fitchratings.com/research/sovereigns/fitch-downgrades-united-states-long-term-ratings-to-aa-from-aaa-outlook-stable-01-08-2023>

The past performance of investments is not a guide to future performance. The value of investments can go down as well as up and you may get back less than you originally invested. Any reference to specific instruments within this article does not constitute an investment recommendation.

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