# MODEL PORTFOLIO SERVICE
## MONTHLY COMMENTARY

**SUCCESSION**
MODEL PORTFOLIOS
POWERED BY
**7IM**

## 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.

| | Q2/2017 – Q2/2018 | Q2/2018 – Q2/2019 | Q2/2019 – Q2/2020 | Q2/2020 – Q2/2021 | Q2/2021 – Q2/2022 | 3 Year Ann. Return | 5 Year Ann. Return | Succession Matrix Expected Parameters – Ann. Return |
|---|---|---|---|---|---|---|---|---|
| Defensive | 2.21% | 5.66% | -3.74% | 3.46% | -9.22% | -0.08% | 0.72% | 3.0 – 4.5% |
| Cautious | 6.06% | 1.14% | 0.52% | -4.92% | -8.68% | 1.41% | 1.56% | 4.5 - 6.0% |
| Balanced | 11.87% | 4.84% | 5.78% | -0.77% | -7.40% | 3.08% | 2.70% | 5.2 – 7.5% |
| Moderately Adventurous | 16.94% | 12.94% | 10.27% | 10.94% | -6.03% | 4.68% | 3.70% | 6.0 – 8.0% |
| Adventurous | 20.14% | 9.31% | 13.19% | 5.45% | -5.64% | 5.47% | 4.26% | 7.0 - 10.0% |
| Income | 6.80% | 12.94% | -1.47% | 10.94% | -8.59% | 1.63% | 2.30% | |

Source: 7IM/FE. Annualised return is defined as 'Ann. Return' in the performance table above and is as at end November 2022. 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

*Bear market rally, dead cat bounce, market turnaround, it's coming home...* these are just a few of the phrases you wouldn't have been able to miss in November.

But what is *actually* going on, and who is right? Some commentators will tell you that the bear market is reaching its end, but others will tell you that this is just an overreaction to some slightly positive data. Similarly, some pundits will tell you that football is indeed coming home, while others will tell England fans to get a grip and stop dreaming.

Markets as a whole performed pretty well over November. US inflation came in at 7.7% - just below expectations – leading to a wave of positive sentiment. Both stocks and bonds responded positively as the S&P ended the month 5.6% up.

There was also a good story in emerging markets as China's Covid policy looked to ease a little, with a push for vaccination instead of lockdowns. Markets took this news very positively and emerging markets shot up by a massive 15% over the month. Dissecting this change is tough as the actual change in policy was marginal, but markets took it to be a sign of a momentum change in Chinese Covid policy.

These market moves represent a bear market rally – a short upturn in markets in the context of a broader bear market. But of course, if markets keep going up, then we'd just be in a bull market.

Typically, markets perform best just after a bear market ends. Despite bull markets lasting an average of 4.8 years, half of the returns are usually made in the first year of bull markets. So, as an investor, you don't want to be late to the party... but you also don't want to turn up to a party that has been cancelled. Bear market rallies are some of the hardest environments for investors – they lure people in, just in time for another dose of pain.

The bear market rally examples below show this pretty neatly:

1. 1929 DJIA – **the BIG bear rally**. The Dow Jones rebounded 48% from mid-November through to mid-April 1930 and then proceeded to **fall 86%** before actually hitting the bottom in 1932!

2. 2000-2001 Dot.com – **the bear that rallied again, and again, and again**. During the dot.com crash, the Nasdaq entered eight bear market rallies greater than 18%, none of which materialized into a bull market. The total peak to trough drawdown was **83%**.

3. 2020 Covid 19 – **blink and the rally is over**. Between 20 February and 12 March, the S&P lost 20% before rising 9% on the 13 March. After this, the market continued to tank. The total peak-to-trough drawdown was **34%**.

So, in conclusion, bear market rallies are a massive pain for investors to navigate. They can give us false hope, but they can also turn into highly lucrative bulls. The best course of action in these periods is to stay invested in a range of diversified positions, and focus on the economic fundamentals, rather than market movements.

### Portfolio Positioning and Changes

During November, we made the following changes to the model portfolios:

• Small increase to government bond exposure, positioning portfolios close to neutral as interest rates have reached more interesting levels

• Removed the tilts towards value and emerging markets on a deteriorating outlook for the global economy

• Took profits on the US mortgage-backed securities position in favour of adding back to diversified global corporate bonds, where the returns on offer look the most attractive in years

• Tilted the UK exposure towards larger companies through the addition of Vanguard FTSE 100 tracker.

### Core 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 twelve months, we think markets will generally move sideways with 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:

• A global manufacturing downturn is unavoidable… but the service sector should be resilient

• Inflation will fall eventually… but the short-term outlook is less clear

• Central bankers are under pressure… so the interest rate outlook changes frequently

• Corporate profit margins have peaked… but most companies will keep growing earnings.



**Investor sentiment overreacts to economic turning points …**

Greed/optimism

Economic fundamentals

Investor sentiment

Fear/pessimism
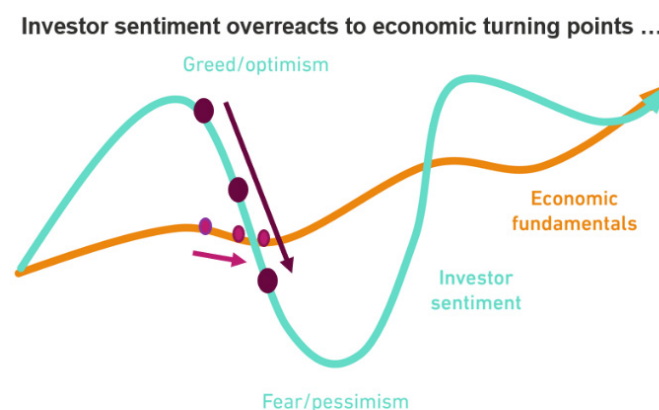
**… with *slightly* weaker data leading to panic right now**

Source: 7IM

And so, investors are starting to worry about what's next for financial markets. The next economic data isn't likely to stabilise until the end of 2022, so 'sideways with volatility' is the most likely scenario for the next few months.

We know our investment identity helps us to deliver in just these kinds of environments. We have positions that can generate returns despite this volatile backdrop.

# ASSET ALLOCATION

## Detailed asset allocation

| | Defensive | Cautious | Balanced | Moderately Adventurous | Adventurous | Income |
|---|---|---|---|---|---|---|
| UK Equities | 3.25% | 6.50% | 15.25% | 18.50% | 21.00% | 8.00% |
| US Equities | 3.00% | 4.25% | 8.50% | 9.00% | 10.00% | 4.50% |
| European Equities | 1.50% | 2.25% | 3.50% | 7.00% | 7.75% | 2.75% |
| Japan Equities | 1.50% | 2.50% | 3.50% | 7.25% | 8.25% | 1.75% |
| Emerging Markets Equities | 4.00% | 6.50% | 6.75% | 10.00% | 13.25% | 6.50% |
| Global Themes | 4.00% | 6.25% | 9.75% | 13.75% | 17.75% | 3.00% |
| Global Government Bonds | 18.50% | 6.75% | 3.50% | 0.00% | 0.00% | 9.50% |
| Gilts* | 9.00% | 1.50% | 1.00% | 0.00% | 0.00% | 4.00% |
| Global Inflation Linked Bonds | 6.00% | 3.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Global Corporate Bonds | 13.25% | 18.50% | 7.00% | 0.00% | 0.00% | 21.50% |
| UK Corporate Bonds | 0.00% | 3.50% | 0.00% | 0.00% | 0.00% | 10.00% |
| Global High Yield Bonds | 10.00% | 10.00% | 10.00% | 5.50% | 0.00% | 12.50% |
| Emerging Markets Bonds | 3.00% | 6.00% | 6.00% | 5.00% | 0.00% | 11.00% |
| Real Assets*** | 0.00% | 2.50% | 3.25% | 2.50% | 3.25% | 3.50% |
| Alternatives/Hedge Funds | 21.00% | 18.00% | 17.50% | 16.50% | 13.50% | 0.00% |
| Cash | 2.00% | 2.00% | 4.50% | 5.00% | 5.25% | 1.50% |

Source: 7IM.    *Includes Short Term Sterling Bonds    **Includes Convertible Bonds    ***Includes Infrastructure

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.
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