MODEL PORTFOLIO SERVICE
MONTHLY COMMENTARY

SUCCESSION
MODEL PORTFOLIOS
POWERED BY
7IM

MAY 2024

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.

	Q1/2019 - Q1/2020	Q1/2020 - Q1/2021	Q1/2021 - Q1/2022	Q1/2022 - Q1/2023	Q1/2023 - Q1/2024	3 Year Ann. Return	5 Year Ann. Return	Succession Matrix Expected Parameters – Ann. Return
Defensive	-0.77%	9.27%	0.75%	-5.37%	4.97%	-0.68%	1.37%	3.0 – 4.5%
Cautious	-2.54%	13.96%	2.41%	-4.47%	6.95%	0.74%	2.86%	4.5 - 6.0%
Balanced	-5.05%	19.83%	4.45%	-3.23%	8.84%	2.36%	4.61%	5.2 – 7.5%
Moderately Adventurous	-8.14%	26.06%	6.32%	-1.56%	10.14%	3.99%	6.09%	6.0 – 8.0%
Adventurous	-10.58%	30.79%	7.86%	-1.42%	9.74%	4.35%	6.59%	7.0 - 10.0%
Income	-8.68%	18.97%	4.16%	-3.46%	7.51%	1.75%	3.17%	

Source: 7IM/FE. Annualised return is defined as 'Ann. Return' in the performance table above and is as at end MAY 2024. 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

Interest rate forecasts continue to make headlines, as there is still uncertainty around the economic data that underpins monetary policy decisions. In the US, the Fed's chair Jerome Powell said high interest rates might take "longer than expected" to lower inflation levels – all this on the back of a small, albeit unexpected, rise in inflation. Fed officials have given signs that US rate cuts are unlikely to be with us before the end of summer.

On this side of the Atlantic, while political developments took centre stage as a General Election is scheduled for 4 July, UK inflation fell sharply in April to 2.3% from 3.2% the previous month. This is the lowest in almost three years, edging closer towards the 2% target. Despite the fall in the cost of goods and services, it still did not quite meet analysts' expectations of 2.1%. Even still, it seemed to have a bigger influence on the announcement of the election rather than Gilt markets.

Market predictions for an interest rate cut from the Bank of England remain around November and then not another one until the first quarter of next year. A similar dynamic is playing out in US Treasuries, where there is an expectation for one cut this year. This means yields remain higher and attractively above long-term inflation expectations. In the meantime, Japan's monetary policy shift of recent months prompted its 10-year government bond yield to go above 1%, a first in more than a decade.

Elsewhere in the markets, the S&P 500 continued to reach new highs driven by strong returns in the technology sector. However, returns across markets seem to be broadening out with different sectors contributing to overall stock market returns as opposed to last year.

Finally, softer economic data are having a push-and-pull impact on markets at the moment. On the one hand, markets' weaker data suggests earnings may be impacted, which then can lead to softer markets. On the other hand, softer data could lead to interest rates falling quicker, which leads to positive economic sentiment, pushing markets higher. So far, the latter is winning out, but it remains to be seen if this will be the case going forward.

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Portfolio Positioning and Changes

This quarter, we have implemented the first phase of the move towards the 2024 Strategic Asset Allocations after completing our annual refresh. Additionally, we made a few tactical changes to portfolios this quarter.

Here are the combined asset allocation changes:

- A small strategic increase to equity, primarily through US and European allocations
- A small rotation from corporate bonds into government bonds
- A minor reduction in Alternatives exposure
- A trim to the AT1s position as prices recover back to their highest in two years
- Moving UK Mid Cap exposure back up to a neutral weight by rotating out of their larger UK peers following strong performance from FTSE100 companies
- Removing the Healthcare Innovation position and rotating the proceeds into the US diversified position (only relevant for higher-risk profiles).
- Added the HSBC European Index Fund to portfolios to provide exposure to larger European companies in a very cheap and efficient vehicle.

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.

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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	6.25%	6.25%	16.00%	19.75%	22.25%	19.00%
North American Equity	7.75%	8.25%	19.50%	22.25%	25.75%	15.00%
European Equity	3.00%	3.50%	6.50%	8.75%	11.00%	5.50%
Japan Equity	2.00%	2.00%	4.50%	7.75%	10.00%	3.25%
Emerging Market Equity	1.75%	1.75%	2.75%	5.75%	6.75%	3.75%
Global Themes	5.25%	5.25%	9.00%	11.75%	13.25%	6.50%
Global Govt Bond	22.00%	22.50%	5.50%	2.00%	0.00%	6.00%
Gilts	9.50%	9.50%	3.50%	0.00%	0.00%	3.00%
Sterling Corporate Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	4.00%
Global Corporate Bonds	7.75%	7.75%	6.00%	0.00%	0.00%	9.00%
Global High Yield Bonds	3.50%	2.50%	3.50%	4.00%	2.50%	5.50%
Emerging Market Bonds	1.50%	1.50%	2.50%	1.50%	0.00%	4.50%
Emerging Market Bonds Local	1.50%	1.50%	2.50%	1.50%	0.00%	4.50%
Global Inflation Linked Bonds	5.00%	5.00%	1.00%	0.00%	0.00%	0.00%
Real Estate	1.75%	0.75%	3.25%	2.75%	4.50%	6.25%
Alternative Strategies	16.50%	16.50%	11.50%	10.25%	2.00%	0.00%
Cash & Money Market	5.00%	5.50%	2.50%	2.00%	2.00%	4.25%

Source: 7IM

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.