Canaccord Genuity Wealth Management

MPS investment update
September 2023 (written 10 September 2023)

Portfolio asset allocation

	Risk profile 3	Risk profile 4	Risk profile 5	Risk profile 6	Risk profile 7
Debt and fixed interest	**60.07**	**47.59**	**32.64**	**17.59**	**2.02**
International	17.10	17.35	13.17	4.95	–
Government	21.35	13.61	8.47	4.06	–
Corporate	21.62	16.63	11.00	8.59	2.02
Equities	**17.90**	**38.13**	**57.36**	**77.95**	**95.64**
Emerging Markets	1.59	1.82	1.65	2.20	2.65
Far East	1.51	3.21	4.65	6.21	7.48
Japan	–	1.06	2.02	2.35	2.79
North America	2.95	7.76	10.82	16.49	20.01
Thematic	3.82	7.61	11.26	15.46	18.69
United Kingdom	6.87	13.24	21.32	28.07	34.91
International	1.16	3.44	5.64	7.18	9.12
Alternative investments	**17.12**	**12.14**	**7.25**	**2.54**	**–**
UCITS funds	14.60	9.62	4.71	–	–
Commodities	2.52	2.53	2.54	2.54	–
Cash	**4.91**	**2.12**	**2.75**	**1.90**	**2.33**

As at 31 August 2023

Core inputs to our asset allocation framework

The economy

Not a huge amount has changed over the last month, as the global economy remains mixed with the US still growing healthily, European growth stuttering and China's recovery from zero-COVID-19 faltering. Our base case remains for low, but positive global economic growth, with the chance that the US slows, and China improves, a fair bit. This is particularly the case given that we expect the lagging effects of the major monetary policy efforts in the developed world to soon start to bite, while it appears that the Chinese authorities are set to further stimulate the wilting economy in the Middle Kingdom.

Inflation

Evidence is growing that inflationary pressures are broadly subsiding and that we continue to see disinflationary trends. Admittedly it might still take a while and restrictive rates for inflation to fall to central banks' targets, but a lot of the heavy lifting has been done, in our opinion, even if the recent rise in the oil prices muddies the waters somewhat. In the UK, inflationary pressures remain intense, particularly with wages and in the services sector, highlighting the Bank of England's (BoE) challenge. However, we should see inflationary trends in the UK also follow the lead from other regions, albeit with a lag.

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Interest rates

We believe that the US Federal Reserve has now finished raising interest rates, even if they still claim to be ready to raise rates further. The base case that we hold remains, that rates will be on hold in the US for some time to come. In the UK, we expect that there might be one or two further hikes, taking the BoE base rate to 5.75%, but this expectation might need to be adjusted considering recent comments from Andrew Bailey, the Governor of the BoE, that a peak in rates might be near.

Earnings

The recent corporate results season can be described as 'satisfactory' and 'better than feared'. Whilst global corporate profitability remains high, earnings are no longer growing, as revenue growth is offset by shrinking company profit margins. Corporate results released recently were neither strong enough to propel markets higher, nor weaker enough to inspire a material sell-off of shares. Much is expected going forward from corporate results, and this is something we need to monitor closely as we approach the end of 2023 and the start of a new year.

Valuation and positioning

There has been plenty of volatility in the last month, but nothing has structurally changed. In the last couple of years we have gone from rampant enthusiasm at the end of 2021, indicating a good time to reduce risk, to excessive pessimism in 2022, heralding an opportunity to buy, to a situation currently where overall sentiment is balanced. Maybe like us, many investors are in a 'stay neutral and wait and see mode', reflecting that so many factors remain unresolved, and questions remain unanswered.

Key subject of the month – is cash 'king' once again?

Recent conversations with clients and advisers have shown that the new paradigm that we exist in with higher interest rates is gaining attention, as we suspected it would The change in interest rates available on cash, fixed term deposits, money market funds and short-term gilts has shifted the dial on investment opportunities and several current and would-be investors are fairly asking the question of whether they should invest at all, given there are options for 'risk free returns' in the order of 5-6%. Our thoughts on this subject therefore are:

- It would be naïve and irresponsible for any adviser or investment manager to pretend that investors should not be taking advantage of the higher rates of return on offer on cash or near-cash investments
- However, such options are not necessarily an alternative to wealth management
- Long term investments can help investors by providing diversification benefits to a wider portfolio, as well as finding ways to protect against inflation
- There are also the risks of reinvestment when fixed term deposits mature, particularly in volatile markets
- Wealth management can also help with tax efficiency while cash-like investments might be less efficient
- Finally, one of the reasons investors are seriously considering cash is the lacklustre performance of investment portfolios in the last few years - the issues around balanced portfolios in 2022 failing to provide diversification is often cited as a key factor
- But it could well be that although the rise in interest rates can benefit cash, fixed interest could benefit more from a falling interest rate environment, enhancing the ability of a balanced portfolio to protect against shocks once again, which should be comforting to all investors.

Key asset allocation positioning

- We became more cautious on equities at the start of the year and had taken a tactical underweight position through the first half of 2023. We have moderated that position, adding back to US equities, although we remain underweight. We felt that events had broadly turned out better than we had feared and the extent of the equity underweight was unnecessary, even if some of the concerns from the start of the year still existed.
- Other markets around the world look better value than the US and we like UK equities, Asian equities, elements of 'value' equities and specific thematic investments.
- We remain underweight in UK gilts and are overall 'short' duration in fixed interest allocations, but we have now moderated our underweight. We will remain underweight duration and have a lower allocation in gilts than we might have, due to concerns over the amount of UK government issuance of fresh debt to finance our deficit and sticky inflation, but having no exposure no longer feels right.
- We remain structurally more comfortable taking credit risk over duration risk, where we believe investors are sensibly compensated for the risks ahead.
- Alternatives can add value in volatile markets, as 'relative value' trades contribute. Gold has been a positive contributor behind our outperformance of peer groups in 2023.
- At the start of the year, we suggested that being balanced, diversified, and operating with a 'flexible mindset' would be appropriate and our view has not changed.

We have defined the terms we have used in this document in the glossary below. If you would like any further explanations, your Investment Director would be pleased to answer any specific questions.

Glossary

Lagging effect is the amount of time between the time action is taken and an effect is realised.

Money market funds invest in high quality, short-term debt securities and pay dividends that generally reflect short-term interest rates.

UK gilts are government bonds in the UK, similar to US Treasury bonds. The term gilt describes a bond with a low risk of default and a low rate of return, and the name comes from historical certificates with gilded edges issued by the British government.

Balanced portfolios are typically divided between stocks and bonds, either equally or with a slight tilt, such as 60% in stocks and 40% in bonds.

An underweight position in one or more securities in the portfolio occurs when the return on the financial asset is going to underperform in its sector or below its benchmark.

Duration is a measurement of a bond's interest rate risk that considers a bond's maturity, yield, coupon and call features. These factors are calculated into one number that measures how sensitive a bond's value may be to interest rate changes.

Credit risk is related to the borrower's ability to repay the debt while duration risk is related to interest rate changes.

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The investments discussed in this document may not be suitable for all investors. Investors should make their own investment decisions based upon their own financial objectives and financial resources and, if in any doubt, should seek advice from an investment adviser.

This is not a recommendation to invest or disinvest in any of the companies, themes or sectors mentioned. They are included for illustrative purposes only.

Where investment is made in currencies other than the investor's base currency, the value of those investments, and any income from them, will be affected by movements in exchange rates. This effect may be unfavourable as well as favourable.

Charts are for illustrative purposes only and should not be relied upon for any other reason. Information is correct as at date of publication.

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