LOWES
INVESTMENT MANAGEMENT

Mixed Investment 40-85% Shares (Bond)

Quarterly Report to 30 September 2024

Objective

To provide a combination of both income and capital growth over the medium to long term.

Strategy

The portfolio invests in a diversified range of funds across multiple asset classes, such as equities, fixed interest and alternatives. Investing in line with the parameters of the Investment Association Mixed Investment 40-85% Shares sector, this portfolio will always have at least 40% of its assets invested in equity funds but never more than 85%. Usually having the majority of its assets invested in equities, this portfolio should provide capital growth as well as allowing a certain level of income to be taken. Whilst exhibiting more volatility than the portfolios with a lower equity exposure, this portfolio would still hopefully provide some protection compared to a pure equity portfolio in a falling market. This portfolio does not invest in direct property, to make it more suitable to be held within a Bond wrapper.

Market Commentary

From an economic perspective concern clearly shifted from inflation to economic growth. For now, inflation appears to be behaving itself. In the euro area the rate has fallen below 2%. In the UK, consumer price inflation has now held steady at 2.2% for two consecutive months. In the US, meanwhile, we have also seen a move down towards target, falling most recently to 2.5%. Whilst there are still some components of the inflation basket which remain sticky, such as housing rents, concerns are dissipating.

Narrative is now more closely focussed on economic growth and how central banks protect it. Whilst the most recent forecast from the Organisation for Economic Co-operation and Development (OECD) remains relatively positive, investors are keen to understand how western central banks will navigate from the current higher interest rate environment to one more commensurate with lower inflation. There was concern that the US Federal Reserve (Fed) had left it too too long after a weak August jobs report. This triggered them into action, with their first move being a 0.5% reduction. The market also priced in a number of subsequent cuts in quick fashion. It has not been uncommon for the market to get ahead if itself, a point in case being the fourth quarter of last year. It may have done so again this time too, following a stronger than expected employment report for September which appears to have reinforced the soft landing thesis.

The Fed, European Central Bank (ECB) and Bank of England are all expected to continue their path of cutting moving forward. The exception to the rule is the Bank of Japan who appear to be in hiking mode. They caught the market off guard with their most recent hike at the end of July, which sent equity markets into a downward spiral. Whilst the hike was only a small 0.15%, it was enough to unsettle investors.

With US interest rates moving one way and Japanese in the other, we saw what appears to be a partial unwinding of the carry trade in early August, the carry trade being where investors borrow in a lower yielding currency, i.e. the Japanese yen, to invest in higher yielding currencies/assets. No one is quite sure exactly how large the positioning in the carry trade is, with some wide ranging estimates. The general consensus is that positions in the carry trade still exist and therefore a keen eye will likely be kept on the Bank of Japan.

The weakness in markets was met this time with investors keen to get back into the market at lower valuations. Liquidity is certainly abundant, with the Investment Company Institute reporting $6.46 trillion in money market funds in the US. The question is, is this money likely to make its way into investment markets or stay parked where it is. Plenty to monitor as we enter the final quarter of 2024.

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Performance

For the quarter the portfolio posted a return of 1.59%. This was marginally behind the sector average return for the period of 1.64%. There was a wide dispersion of returns delivered by the underlying funds within the portfolio, being almost 12%.

Many of the top performing funds in the portfolio were those which responded positively to interest rate cuts and the expectation that more will be seen before the end of the year. The top performing fund was VT Gravis UK infrastructure Income. Infrastructure assets are typically long duration and therefore benefit from a fall in rates and bond yields. The yield offered by these assets also becomes more attractive, particularly those which have some inflation linkage or are guaranteed by government or government agencies.

Fixed income funds were also beneficiaries, with funds such as Nomura Global Dynamic Bond and Schroder Sterling Corporate Bond performing strongly. Both funds carry a reasonable length of duration, currently in excess of 6 year, therefore displaying more sensitivity to such interest rate movements. The GAM Start Credit Opportunities fund was also a strong performer during the period, although this was not due so much to duration positioning but driven by further spread compression within financial bonds.

Within the equity allocation the strongest performing fund was FFSA Asia Focus. The fund had been in the doldrums for much of periods, only coming to life in the final few weeks of September. This was on the back of the release of stimulus measures from the Chinese authorities with a view to supporting the economy and reigniting consumer confidence. There was a strong positive response from Chinese equities.

Source: FE Analytics, Bid-Bid, Total Return

Portfolio Activity and Positioning

There were a number of changes made to the portfolio during the period. The first saw the removal of the M&G Global Macro Bond fund. This was on the back of the announcement of Jim Leaviss, who has been lead manager on this fund since its inception. Whilst Eva Sun-Wai will assume the position as lead manager, previously deputy manager, we believe this to be too big a loss for the fund. Leaviss has been instrumental in this fund in terms of its creation, decision making and allocation decisions.

The FSSA Japan Focus fund was also removed from the portfolio. This followed a period of weaker performance, much of which can be attributed to the investment style of the fund, which was not in favour with investors. Whilst we could foresee a turnaround here in a different investment environment, the fund was put on internal review by FSSA due to dwindling assets. The decision was therefore made to exit the position. In its place a position in the Fidelity Japan Index fund was taken. This tracks the MSCI Japan Index and therefore provides exposure to both large and mid-cap stocks.

A new position was added to the portfolio in the form of the Vanguard Global Small Cap Index fund. Global small cap companies, from a valuation standpoint, potentially offered an attractive entry point. Across the US, Europe ex UK and the UK they were trading at a discount to their long term average valuation. At the same time, Smaller companies in the US and Europe were trading at a lower valuation than their large cap counterparts, something which is against the norm. Interest rates coming down should be a positive for small cap equities, along with a soft rather than hard economic landing.

Disclaimer

The portfolio is managed on a discretionary basis therefore the investment manager may make changes to the investments held without notice. Investors are agreeing to the investment model as recommended by an Adviser and may not be investing into the specific assets included in this report.

Past performance is not a guide to future performance. The value of investments and any income from them can fall as well as rise and are not guaranteed, so you may get back less than you invested. If you invest in currencies other than your own, fluctuations in currency value will mean that the value of your investment will move independently of the underlying asset.

Consideration should be given to whether it is felt that the outcome of any risk assessment is accurate and advice should be sought for factors such as investment objectives, the investment term, attitude to risk, capacity for investment loss and the level of inflation.

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