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INVESTMENT COMMITTEE
REBALANCE UPDATE

Investment Committee October 2023 - MPS Rebalance

General Overview

Asset/Region	Current Stance	Previous Stance
US Equities	Neutral View	Neutral View
UK Equities	Cautious	Cautious
European Equities	Cautious	Cautious
ROW Equities	Positive View	Positive View
Fixed Income	Selective Approach	Selective Approach
Property	Cautious	Selective Approach
Infrastructure	Cautious	Neutral View

Following the Federal Reserve's (Fed) September meeting, the market has been positioning for higher for longer in respect to interest rates. This has led to rate cuts being pushed further down the road, with the US consumer and jobs data not yet showing major signs of weakness, despite the accelerated tightening in monetary policy over the last two years.

Many market participants haven't witnessed a double event of higher rates and Quantitative Tightening (a contraction in monetary policy by decreasing money supply). Nonetheless, the prospect of higher rates is less of an issue going into year-end given we feel we are near to peak rates. As the global economy gets to grips with the higher cost of capital, investors are now craving stability in this key metric, something we feel we are nearing.

Liquidity does continue to be drained from the markets, and both conventional bonds and equities have suffered over the summer. Equities had enjoyed a good first half, although the breadth of the US equity rally this year has been poor. This has been led by a small handful of stocks known as the 'Magnificent Seven', with a majority of these companies falling out of our universe due to ESG concerns. Large capitalised names continue to outperform small capitalised names, with the concentration at the top of the market, smaller cap valuations are at their most compelling levels in decades.

Nonetheless, the re-balance did see us massively reduce the Montanaro Better World fund. We do feel there are opportunities in the longer term and are monitoring a number of small and mid-cap names, where active managers are able to seek out high-quality businesses who are able to withstand higher rates and continue to grow, compounding earnings over time. We have had a particular focus on the US in our research, given the benefits of policy support such as the Infrastructure Investment and Jobs Act and the CHIPS and Science Act, where funds from this policy support are beginning to flow, leading to an expansion in Capex. For now, we have cut back, but we have room to allocate into this area over time, but it will be incremental.

Given the continued headlines around Donald Trump, the committee discussed the US election taking place next year, where it appears Joe Biden will come up against Trump in what we expect to be a nasty election campaign. When Trump previously came into power, he sought to roll back environmental policies, notably leaving the Paris Climate Agreement. We have seen the sporadic news article place the US Inflation Reduction Act at risk should a Republican candidate win the election next year, however we see this as highly unlikely given the bipartisan support for the bill. Speaking to peers in the States, they have highlighted that there is a noticeable consumer shift, with younger generations caring much more about the environment, across not just the Liberal regions. They suggest this, alongside policy support, is changing how companies allocate capital in a positive way, and we expect to benefit from this over time.

Earlier in October we put out a piece that discussed near term performance. In this, we covered the impact of the negative screen and the particular weakness we have experienced in clean energy names. You can find this commentary by clicking here. Given this weakness across various sub-sectors, we have introduced the RobecoSAM Smart Energy fund into portfolios, given its track record and exposure to larger cap names than other clean energy funds we have reviewed. As long-term investors, we feel there are opportunities in clean energy, despite the near-term headwinds. We feel we are at capitulation in sentiment towards the sector at a time when fossil fuels have the attention of many.

It is likely we will also face a UK election in Q4 next year, given the deadline is January 2025, which is an unlikely month for the electorate to be sent to the polls. The poll of polls has Labour receiving 45% of the vote, with the Conservatives at 27%, a reflection of the dismay over Conservative infighting and policies during the cost-of-living crisis. We expect some giveaways next year as the Tories battle to stay alive, with Inheritance Tax one area likely to be reviewed. We have reduced our UK exposure, despite the cheap valuations on offer. We feel there is limited catalysts in the near term for this to change.

A leading Wall Street CEO recently commented that, “this may be the most dangerous time the world has seen in decades”. We couldn’t agree more given the geopolitical landscape, with ongoing fighting in Ukraine and now a potential conflict in the Middle East following catastrophic events in Israel and Gaza. These events are testing the foreign policy reach of a number of nations, no more so than the European Union. Given the heightened security concerns, EU member states may see a shift to the right, as we are seeing in Belgium, where the far-right party Vlaams Belang is already polling as the biggest party. When it comes to an allocation to the region, we are happy with the selective approach we receive through the global funds held.

Inevitably, growth projections in 2024 are subdued for advanced economies, with the World Bank expecting the US, Euro Area and Japan to grow 0.8%, 1.3% and 0.7% respectively. With the global economy expected to grow by 2.4% next year, the growth story comes from emerging and developing economies, with the likes of China and India expected to grow by 5.6% and 6.3% respectively.

We have topped sliced a small element of our exposure to India in the near term, rotating into the UBAM Emerging Market Positive Impact fund which has a slightly different emerging and developing nation exposure. However, the mid-to-long term Indian investment thesis remains intact, with the growth story rather appealing. Their bond market has been added to a leading global index which opens up their $1 trillion dollar market to investors. The current leader, Mr Modi, is most likely to be re-elected which will continue the 'Made in India' story, advancing the Production Linked Incentive plan, which pushes domestic manufacturing. An area which is likely to be increased in the 2024 budget. China has been weak with continued concerns over their delayed Covid recovery and ongoing issues in their real estate sector. Policy has been eased and selective China exposure would have increased as part of our changes highlighted above.

Bonds

The supply and demand dynamic, led by fears over higher government and corporate borrowing has meant higher longer-term rates. Central bank balance sheets still need unwinding, and liquidity will drain. As a result, we see some value in shorter term rates, at the expense of infrastructure and property. Here we added to the AXA Short Duration Green Bond fund.

Infrastructure/Property

Whilst the asset class looks cheap, headwinds remain and sentiment has not improved despite various asset sales and share buybacks supporting valuations. In the near term, we have trimmed back our exposure in order to allocate to the short duration fund mentioned above. On top of this, we also sought to diversify our exposure and added RM Funds Alternative Income fund into portfolios, given it is more defensive and provides some diversification on underlying assets. Sustainable Real Estate was also trimmed in order to allocate to fixed income.

Equities

Global growth equities are on their worst stretch for a number of years, a situation likened to the earlier 2000s. In the rebalance, we have moved portfolios allocation to equities to just over our neutral level.

We have sought to counter some of the existing small-cap exposure in portfolios with the addition of some new funds that provide exposure to larger, market leading names which will complement the more disruptive and solutions-based companies within the portfolio. This includes a small allocation to Premier Miton Global Sustainable Optimum Income fund, and Polar Capital Healthcare Opportunities (on top of the addition of RobecoSAM Smart Energy fund).

Focusing on healthcare, as with the wider market, less capitalised healthcare companies have suffered, but larger names have also disappointed. We have engaged with a number of fund houses on this sector, and the investment thesis is rather compelling. We have introduced the Polar Capital Healthcare Opportunities fund as a core holding to portfolios. The team have vast amounts of experience, and have spoken of "*extremely attractive*" entry points, with a "*dislocation between stock market performance for the sector and healthcare fundamentals is the widest it has been by a significant margin with utilisation, new product cycles and M&A all tracking in the right direction.*"

We have removed Pictet Water fund, given we could no longer justify the cost given the viable alternative thematic funds in a similar sector whose performance we have been monitoring for the last year or so. As a result, we added the Regnan Water and Waste fund in its replacement.

Other changes already discussed include the rotation in our Emerging/Developing market exposure, and a reduction in our UK allocation by selling Ninety-One UK Sustainable fund, and a sale of Montanaro Better World fund. More specific portfolio changes can be found below:

Portfolio changes

Defensive

Bonds - we introduced a new fund into portfolios – the AXA Green Short Duration Bond fund. This fund works from an ethics and asset allocation play given where we wish to be allocated along the yield curve.

Equities - we removed Ninety-One UK Sustainable (no real catalyst for outperformance), Pictet Water (cost and rotation of thematic exposure) and Montanaro Better World funds (expect some near-term weakness before recovery). We used the proceeds to add some new funds into portfolios, Polar Capital Healthcare Opportunities fund (good thematic and valuation opportunity, plus some healthcare exposure is seen as Defensive, additionally we really like the team behind the fund on meeting them), and RobecoSAM Smart Energy Equities fund (more diversification and larger names to complement existing holdings). We also added slightly to the M&G Positive Impact fund, given its bias to larger cap more defensive investments. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added the Premier Miton Global Sustainable Optimum Income Fund, who we see as an ESG leader. It's a fund we have been following for quite a while and following our recent engagements with the team, this highlighted our view to allocate.

Infrastructure - we sliced back our holdings in the Foresight UK Infra and Gravis Clean Energy Income funds (we still like the areas, but not wanting to add). We wanted to diversity the exposure in this area, so we added the RM Alternative Income fund, that provides diversification and some short-dated bond exposure.

Sustainable Real Estate - we sliced back our allocation to the Foresight Sustainable Real Estate Securities fund.

Cautious

Bonds - we introduced a new fund into portfolios – the AXA Green Short Duration Bond fund. This fund works from an ethics and asset allocation play give where we wish to be allocated along the yield curve.

Equities - we removed Ninety-One UK Sustainable (no real catalyst for outperformance), Pictet Water (cost and rotation of thematic exposure) and Montanaro Better World funds (expect some near-term weakness before recovery). We used the proceeds to add some new funds into portfolios, Polar Capital Healthcare Opportunities fund (good thematic and valuation opportunity, plus some healthcare exposure is seen as Defensive, additionally we really like the team behind the fund on meeting them), and RobecoSAM Smart Energy Equities fund (more diversification and larger names to complement existing holdings). We also added a percent more to the Janus Henderson Global Sustainable fund give its focus on larger cap investments. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income Fund, who we see as an ESG leader. It's a fund we have been following for quite a while and after our recent engagements with the team, this highlighted our view to allocate.

Infrastructure - we sliced back our holdings in the Foresight UK Infra and Gravis Clean Energy Income funds (we still like the areas, but not wanting to add). We wanted to diversity the exposure in this area, so we added the RM Alternative Income fund, that provides diversification and some short-dated bond exposure.

Sustainable Real Estate - we sliced back our allocation to the Foresight Sustainable Real Estate Securities fund.

Balanced

Bonds - we introduced a new fund into portfolios – the AXA Green Short Duration Bond fund. This fund works from an ethics and asset allocation play give where we wish to be allocated along the yield curve.

Equities - we removed Ninety-One UK Sustainable (no real catalyst for outperformance), Pictet Water (cost and rotation of thematic exposure) and Montanaro Better World funds (expect some near-term weakness before recovery). On top of this, to assist with the below allocations, we reduced our exposure to the M&G Positive Impact & WHEB Sustainability funds in this portfolio. We used the proceeds to add some new funds into portfolios, Polar Capital Healthcare Opportunities fund (good thematic and valuation opportunity, plus some healthcare exposure is seen as Defensive, additionally we really like the team behind the fund on meeting them), and RobecoSAM Smart Energy Equities fund (more diversification and larger names to complement existing holdings). In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income fund, who we see as an ESG leader. It's a fund we have been following for quite a while and our recent engagements with the team highlighted our view to allocate. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income fund, who we see as an ESG leader. It's a fund we have been following for quite a while and following our recent engagements with the team, this highlighted our view to allocate. Finally, we reduced slightly our exposure to the Stewart Asia Sustainability fund, to allow us to introduce the UBAM Positive Impact EM fund that we have held in our Adventurous portfolio for a while now.

Infrastructure - we sliced back our holdings in the Foresight UK Infra and Gravis Clean Energy Income funds (we still like the areas, but not wanting to add). We wanted to diversity the exposure in this area, so we added the RM Alternative Income fund, that provides diversification and some short-dated bond exposure.

Sustainable Real Estate - we sliced back our allocation to the Foresight Sustainable Real Estate Securities fund.

Balanced Growth

Bonds - we introduced a new fund into portfolios – the AXA Green Short Duration Bond fund. This fund works from an ethics and asset allocation play give where we wish to be allocated along the yield curve.

Equities - we removed Ninety-One UK Sustainable (no real catalyst for outperformance), Pictet Water (cost and rotation of thematic exposure) and Montanaro Better World funds (expect some near-term weakness before recovery). On top of this, to assist with the below allocations, we reduced our exposure to the M&G Positive Impact & WHEB Sustainability funds in this portfolio. We used the proceeds to add some new funds into portfolios, Polar Capital Healthcare Opportunities fund (good thematic and valuation opportunity, plus some healthcare exposure is seen as Defensive, additionally we really like the team behind the fund on meeting them), and RobecoSAM Smart Energy Equities fund (more diversification and larger names to complement existing holdings) and Regnan Global Equity Impact Solutions fund. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income fund, who we see as an ESG leader. It's a fund we have been following for quite a while and our recent engagements with the team highlighted our view to allocate. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income fund, who we see as an ESG leader. It's a fund we have been following for quite a while and after our recent engagements with the team, this highlighted our view to allocate. Finally, we reduced slightly our exposure to the Stewart Asia Sustainability fund, to allow us to introduce the UBAM Positive Impact EM fund that we have held in our Adventurous portfolio for a while now.

Infrastructure - we sliced back our holdings in the Foresight UK Infra and Gravis Clean Energy Income funds (we still like the areas, but not wanting to add). We wanted to diversity the exposure in this area, so we added the RM Alternative Income fund, that provides diversification and some short-dated bond exposure.

Sustainable Real Estate - we sliced back our allocation to the Foresight Sustainable Real Estate Securities fund.

Growth

Bonds - we introduced a new fund into portfolios – the AXA Green Short Duration Bond fund. This fund works from an ethics and asset allocation play give where we wish to be allocated along the yield curve.

Equities - we removed Ninety-One UK Sustainable (no real catalyst for outperformance), Pictet Water (cost and rotation of thematic exposure) and Montanaro Better World funds (expect some near-term weakness before recovery). On top of this, to assist with the below allocations, we reduced our exposure to the M&G Positive Impact, Janus Henderson Global Sustainable & WHEB Sustainability funds in this portfolio. We used the proceeds to add some new funds into portfolios, Polar Capital Healthcare Opportunities fund (good thematic and valuation opportunity, plus some healthcare exposure is seen as Defensive, additionally we really like the team behind the fund on meeting them), and RobecoSAM Smart Energy Equities fund (more diversification and larger names to complement existing holdings) and Regnan Global Equity Impact Solutions fund. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income fund, who we see as an ESG leader. It's a fund we have been following for quite a while and our recent engagements with the team highlighted our view to allocate. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income fund, who we see as an ESG leader. It's a fund we have been following for quite a while and following on from our recent engagements with the team this enhanced our view to allocate. Finally, we introduced the UBAM Positive Impact EM fund that we have held in our Adventurous portfolio for a while now.

Infrastructure - we sliced back our holdings in the Foresight UK Infra and Gravis Clean Energy Income funds (we still like the areas, but not wanting to add).

Sustainable Real Estate - we sliced back our allocation to the Foresight Sustainable Real Estate Securities fund.

Adventurous

Bonds - we added a percent to the Wellington Global Impact Bond fund, there were no other changes.

Equities - we removed Ninety-One UK Sustainable (no real catalyst for outperformance), Pictet Water (cost and rotation of thematic exposure) and Montanaro Better World funds (expect some near-term weakness before recovery). On top of this, to assist with the below allocations, we reduced our exposure to the M&G Positive Impact, Janus Henderson Global Sustainable & WHEB Sustainability funds in this portfolio. We used the proceeds to add some new funds into portfolios, Polar Capital Healthcare Opportunities fund (good thematic and valuation opportunity, plus some healthcare exposure is seen as Defensive, additionally we really like the team behind the fund on meeting them), and RobecoSAM Smart Energy Equities fund (more diversification and larger names to complement existing holdings) and Impax Environmental Leaders Fund. In place of Pictet Water we added Regnan Sustainable Water & Waste fund to broaden the thematic exposure. Finally, we also added Premier Miton Global Sustainable Optimum Income fund, who we see as an ESG leader. It's a fund we have been following for quite a while and after our recent engagements with the team, this highlighted our view to allocate. Finally, we introduced the UBAM Positive Impact EM fund that we have held in our Adventurous portfolio for a while now.

Infrastructure - we sliced back our holdings in the Foresight UK Infra and Gravis Clean Energy Income funds (we still like the areas, but not wanting to add).

Sustainable Real Estate - we completely sold our allocation to the Foresight Sustainable Real Estate Securities fund.

Income

Bonds - we sold out of Wellington Global Impact Bond fund and replaced it with the Columbia Threadneedle Social Bond fund, on the back of the CT fund being a better yielding asset.

Equities - we sold out of both the Liontrust UK Ethical and Montanaro UK Income funds. We replaced them by adding in the Premier Miton Global Sustainable Optimum Income fund, and the recently launched Columbia Threadneedle Sustainable Global Equity Income fund.

Infrastructure - we sliced back our holdings in the Foresight UK Infra and Gravis Clean Energy Income funds (we still like the areas, but not wanting to add). We wanted to diversity the exposure in this area, so we added the RM Alternative Income fund, that provides diversification and some short-dated bond exposure.