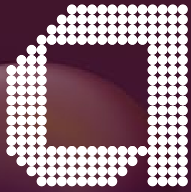


1825 Portfolio 4

Commentary third quarter 2021

This summary provides market commentary from our investment experts, and details any changes made to Portfolio 4 during the third quarter of 2021. The commentary is intended to give you a general overview of the market, and does not constitute advice.

In brief:

- Most major global indices rise, helped by upbeat company results
- US equities reach all-time highs, but fall sharply in September
- Challenging quarter for global bonds, due to increasing inflation concerns

Environment

Global equities rose on aggregate over the third quarter, with most major world indices rising thanks to solid corporate earnings results and supportive central bank comments. Despite a steady rise in Covid-19 Delta infections worrying investors, US equities posted strong returns, and most major US indices reached record highs. However, US equities fell in September, as inflation fears and falling bond prices triggered equity market losses. Similarly, European and UK equities fell at the end of the quarter, with global supply chain disruptions, fuel shortages and slowing growth fears weighing on markets. In comparison, Japanese equities had a weak start to the period, as Covid-19 cases hit new highs, but performance improved thereafter. The market reacted positively to news that Prime Minister Yoshihide Suga would step down, and news that the state of emergency, imposed in April, was to finally be lifted.

It was another challenging quarter for bonds, as rising inflation fears and hawkish comments from the US Federal Reserve (Fed) triggered a sell-off in government bonds that spilled over into corporate bond markets. UK government bonds were among the weakest performers. While corporate bonds performed well until July, they fell in August amid concerns about a withdrawal of central bank support following comments from Fed Chair Jerome Powell. Overall, high-yield debt generally performed better than investment-grade bonds. However, European investment-grade bonds ended the quarter slightly up, as the European Central Bank continued to maintain a relatively dovish stance.

Activity and performance

Please refer to Page 4 for a full breakdown of portfolio holdings.

Strategic Asset Allocation (SAA)

Strategic asset allocation (SAA) had mixed results during the third quarter. Lower-risk mandates delivered marginally negative returns, while medium- and higher-risk mandates delivered firmly positive absolute returns.

The third quarter turned out to be reminiscent of the first quarter of 2021, with the imbalance between supply and demand for goods, services, materials and labour shaping the views of central bankers and market expectations for growth, inflation and monetary policy.

The economic outlook broadly deteriorated as the Delta variant of Covid-19 affected the speed at which economies could reopen. Economic expansion is expected to remain well ahead of the trend seen in the years preceding the pandemic, albeit we are likely past the peak with much of the rebound from the lows of 2020 behind us.

Supply chain issues have left many businesses unable to fulfil orders, while demand has continued to increase, leading to both higher input and output costs. This, in turn, has led to the highest inflation levels in more than a decade.

Central bankers have been keen to reiterate that this is largely transitory. Although their tone is largely reassuring, their plans for reducing monetary stimulus and increasing interest rates have undoubtedly been brought forward.

It proved to be a challenging quarter for emerging market debt. The hard currency, hedged to sterling, allocation within mandates was negatively affected by the rise in US treasury yields, leading to marginal losses. The local currency bond allocation also delivered a small loss over the quarter, though sterling weakening against a broad basket of EM currencies helped to negate this.

Equity markets returns diverged considerably. Developed market equities were largely positive albeit the journey to achieve these varied. US, UK and European bourses performed reasonably in line (up 3.05%, 2.23% and 0.76% respectively) with a strong showing until the end of August. At that point, higher and more persistent levels of inflation in some geographies made central banks (the US Federal Reserve and Bank of England in particular) turn more hawkish on their policy stance. That led to a spike in government bond yields and, as a result of these higher rates, equities took fright and there was a reasonably broad-based sell-off throughout September. The developed market that took a decidedly different path was Japan. Japanese equities lagged western markets during July and August as its zero tolerance Covid policy coupled with relatively low vaccination rates meant that a national lockdown was enforced over the summer months, albeit the Olympic Games were allowed to take place. Following Prime Minister Yoshihide Suga's popularity plummeting in the polls and his surprise resignation in early September, Japanese equities rebounded amid the prospect of a large fiscal package being announced before the year-end. This saw the Japanese market handsomely outperform during September and end the quarter up 7.34%. Further afield, Asian and emerging markets lost ground, however. Difficult environments from a Covid perspective combined with a raft of Chinese government regulation across the education, healthcare and technology sectors and latterly the interruption to energy supplies in some provinces negatively affected these markets, which fell 6.06% and 5.71%, respectively. A difficult regulatory and macroeconomic backdrop deteriorated even further in China with the news that Evergrande, China's second largest property developer, was on the brink of defaulting on a proportion of its US$300 billion debt.

Moving onto alternatives and there was a strong showing from infrastructure assets. Uncertainty remains over the timescale and overall size of the infrastructure bill to be passed by the US government, rumoured to be between US$2 trillion and US$3.5 trillion, but there continues to be strong demand for infrastructure assets among investors who recognise the benefits of holding real assets.

Tactical Asset Allocation

Tactical asset allocation (TAA) made a marginal contribution, both positive and negative, to abrdn Financial Planning MPS mandates during the third quarter.

The abrdn Financial Planning MPS 4 mandates were underweight alternatives (mainly infrastructure) during the quarter, which was marginally negative for performance. This underweight helped to fund overweight positions in equities in our preferred regions of the US, UK and emerging markets (EM). The increased allocation to EM equities detracted from performance, while the overweight to both US and UK equities proved beneficial.

Manager selection

It has been a tricky period when it comes to manager selection.

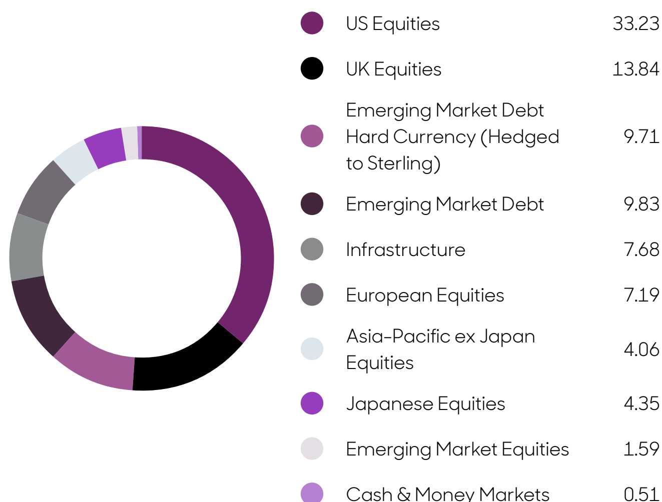
In UK equities, the JPM UK Equity Core and JO Hambro UK Dynamic fund outperformed the FTSE All-Share Index while Lazard UK Omega fund delivered slightly weaker returns.

European equities (in the main) provided strong returns with the Invesco European Equity Income, BlackRock European Dynamic fund outperforming their benchmarks, while the Barings European Select Trust lagged marginally.

US equities have been one of the strongest performers this year, but choppiness during the third quarter favoured defensive growth companies. As a result, the mega cap S&P 500 outperformed the Vanguard US Equity Index Fund, which has broader exposure to small and mid-sized companies as well as mega and large caps.

It was a weak quarter for Asian ex Japan equities, and the more growth orientated Fidelity Asia Fund lagged the market. In contrast our emerging markets (EM) equity paring proved more successful, with mild underperformance from the RWC Global Emerging Markets being more than offset by strong returns from Artemis SmartGARP Global Emerging Markets which not only outperformed but posted a strong positive return in a negative quarter for EM equities.

1825 Portfolio 4 Asset class breakdown



The comments above refer to the past. Past performance is not a reliable guide to future performance. As with any investment, the value of your portfolio can fall as well as rise – you may get back less than you pay in.

Outlook

Company fundamentals remain supportive for equity markets, but with good news already priced in, returns are likely to be modest. Bond yields are expected to rise and this environment usually favours value shares, with cyclicals expected to outperform defensive companies. Despite this, growth companies are unlikely to fade materially as economic growth is weakening from supply chain pressures and higher energy prices. Chinese political risk has also resurfaced and is weighing on investor sentiment. Although the government's regulatory clampdown focused on technology companies, there is a risk it could broaden out. With commodity inflation and supply-side strains, there are likely to be individual pockets of earnings pressure for many businesses. Companies in Europe and the UK also face additional pressure from delivery driver and fuel shortages.

Within fixed income, increasing vaccine dissemination, the easing of restrictions and improving macroeconomic and corporate fundamentals are supporting economic activity and sentiment. Meanwhile, a key focus of investor attention is on whether rising inflation will be transitory or more long-lived. Evidence suggesting the latter would not be seen favourably.

1825 Portfolio 4 breakdown	Q3 2021
Holding	Weights %
Asia-Pacific ex Japan Equities	**4.06**
Fidelity Asia Fund Accum W GBP	4.06
Cash & Money Markets	**0.51**
British Pounds	0.51
Emerging Market Debt	**9.83**
Legal & General Emerging Markets Govt Bond (LC) Index Fd Accum Units Class C GBP	9.83
Emerging Market Debt Hard Currency (Hedged to Sterling)	**9.71**
Barings Emerging Markets Sovereign Debt Fund GBP Tranche B	9.71
Emerging Market Equities	**1.59**
Artemis Funds (Lux) SICAV Global Emerging Markets FI Capitalisation	0.81
RWC Global Emerging Markets Fund S GBP Capitalisation	0.78
European Equities	**7.19**
Aberdeen European Equity Enhanced Index Fund accum N GBP	2.17
Barings Europe Select Trust Units I GBP	1.07
Blackrock European Dynamic Fund Class FD GBP Units	1.77
Invesco European Equity Income Fund (UK) Y GBP	1.11
Invesco European Smaller Companies Fund	1.08
Infrastructure	**7.68**
First Sentier Global Listed Infrastructure Fund B GBP	1.94
L&G Global Infrastructure Index Fund	3.83
Legg Mason ClearBridge Infrastructure Fund	1.91
Japanese Equities	**4.35**
Legal & General Japan Index Trust Class C GBP Units	4.35
UK Equities	**21.85**
JOHCM UK Dynamic Fund Class Y GBP	5.40
JPM UK Active Index Plus Fund Class E GBP Accum Shs	8.76
Lazard UK Omega Fund Class EA GBP	5.51
LF Tellworth UK Smaller Companies Fund Accum F Unhedged GBP	2.18
US Equities	**33.23**
Vanguard US Equity Index Fund Institutional Plus Class GBP Ptg Shs	33.23
	100.00%

Each client portfolio is reviewed and rebalanced regularly where necessary. Fund selection and asset allocation are monitored on an ongoing basis, and will be changed as considered appropriate by the Portfolio Managers.

Charges

The ongoing charges figure quoted below includes the abrdn discretionary investment management charge (0.20%) and fund level management charges. It does not include product and adviser specific charges – speak to your abrdn Financial Planner for full details.

Ongoing charges figure	0.57%

Note: the Portfolio holdings,asset class breakdowns, and ongoing charges, figure shown on this page are correct as at 30/09/2021. They will change from time to time. Source: abrdn.

For more information visit abrdn.com/financial-advice

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