UK: Suitable for retail and professional clients.

Quilter Investors

Cirilium Portfolios

Monthly commentary – Review of October 2023

Marcus Brookes
Chief Investment Officer

Our market summary

Global equities retreated by 2.3% due to concerns over the 'higher for longer' narrative for US interest rates. This was against a backdrop of ongoing hostilities in Ukraine and the outbreak of a bitter new Middle East conflict. Over the month, every major equity market gave up ground and bond markets also sold-off with a steep rise in US government bond yields (meaning their prices fell). UK government bonds fared better, but still declined as did corporate bonds (issued by companies).

Equity markets

Despite economic growth of 4.9% (annualised) in the third quarter, US equities fell by 1.7% in the face of the Federal Reserve (Fed) chair's indication that US interest rates might still need to rise further. Energy stocks were among the weakest performers as oil prices eased. Meanwhile, consumer discretionary stocks (companies that produce goods and services considered non-essential) also struggled with tech and consumer staples stocks (companies that supply goods and services that are always in demand) faring better, but still mostly in negative territory.

Although the European Central Bank (ECB) kept interest rates on pause at its October meeting and data showed annual inflation had fallen to 2.9%, European equities declined by 3.0%. While more defensive sectors such as utilities and consumer staples made some progress, healthcare was among the worst hit sectors after disappointing profit guidance in the sector.

UK equities lagged those elsewhere and declined 4.1%. UK inflation remained unchanged at 6.7%, which increased the prospect of a long inflation battle, even as house prices declined alongside consumer confidence and broader economic indicators. UK banks suffered as the mortgage market ground to a halt while the declining outlook for UK consumer spending hit consumer discretionary sectors, with UK smaller companies especially hard hit.

Emerging market equities lost 3.3% in October, outperforming China, Japan, and the UK but underperforming the US. Chinese shares fell further due to the country's unresolved economic woes, rising tensions with the US, and the ongoing implosion of its real-estate sector. Elsewhere, Turkey suffered as its currency declined still further in the face of 60% inflation while Brazil, Thailand, and India all beat the broader emerging market index.

Fixed income

The 'higher for longer' narrative for US interest rates continued to drive the yields on US Treasuries (government bonds) higher, meaning their prices fell. The price of US Treasuries fell by 1.35% as the yield on 10-year issues returned to levels last seen prior to the global financial crash of 2008. Meanwhile, UK government bonds (gilts) fell 0.4% while UK corporate bonds (issued by companies) suffered a more modest 0.2% decline.

Source: Quilter Investors as at 31 October 2023. Total return, percentage growth in pounds sterling except where shown, rounded to one decimal place. The performance shown for global equities is represented by the MSCI World Index; US equities by the MSCI USA Index; European equities by the MSCI Europe ex UK Index; UK equities by the MSCI United Kingdom All Cap Index; emerging markets by the MSCI EM (Emerging Markets) Index; US Treasuries by the ICE BofA US Treasury (GBP Hedged) Index; UK government bonds by the ICE BofA UK Gilt Index; and UK corporate bonds by the ICE BofA Sterling Corporate Index.

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Portfolio Manager

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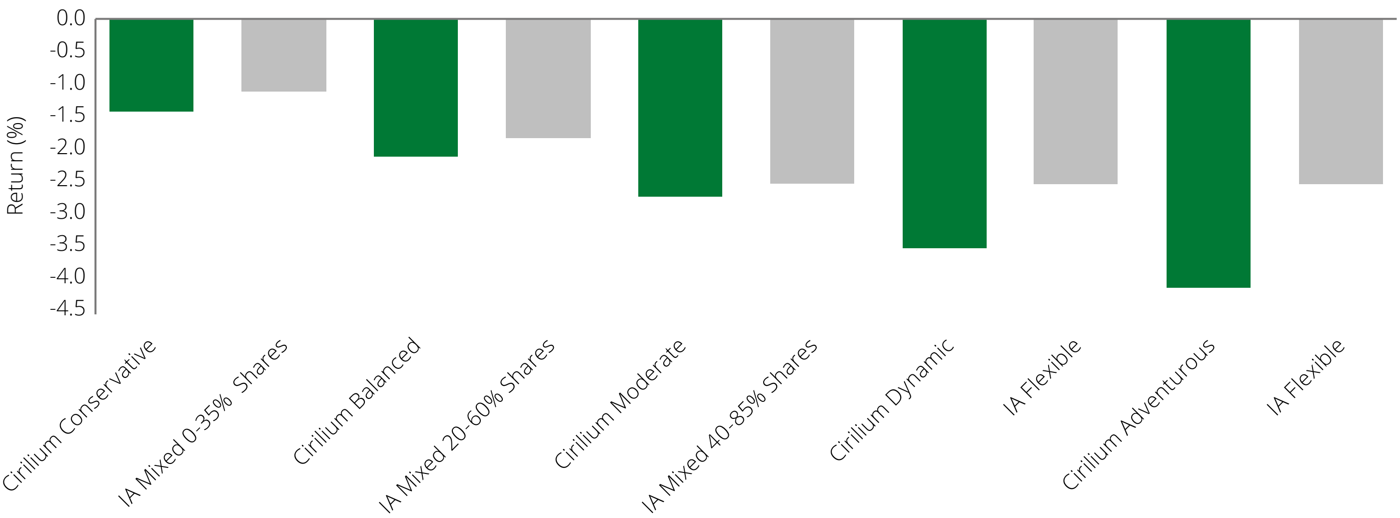
Portfolio Manager

Performance review

The Cirilium Portfolios lost ground as both equity and bond markets sold-off. The losses were more muted for the lower-risk portfolios where equity exposure is lower. The Cirilium Conservative Portfolio declined 1.4% while the Cirilium Adventurous Portfolio fell by 4.1%.

Monthly performance (%)



Performance summary (%)

	Cumulative performance						*Discrete annual performance to end of October*				
	1 month	*YTD*	*1 year*	*3 year*	*5 year*	*Since launch*	*2022 - 2023*	*2021 - 2022*	*2020 - 2021*	*2019 - 2020*	*2018 - 2019*
Cirilium Conservative	**-1.4**	**-2.7**	**-0.2**	**-6.2**	**-2.0**	**34.5**	**-0.2**	**-12.9**	**7.9**	**0.9**	**3.5**
IA Mixed 0-35% Shares	-1.1	-0.8	0.9	-4.2	1.9	33.4	0.9	-11.1	6.8	0.4	5.9
Cirilium Balanced	**-2.1**	**-1.4**	**1.2**	**0.4**	**5.0**	**106.2**	**1.2**	**-13.3**	**14.5**	**-0.2**	**4.7**
IA Mixed 20-60% Shares	-1.8	-0.7	1.7	2.9	7.8	70.3	1.7	-10.7	13.3	-1.7	6.7
Cirilium Moderate	**-2.7**	**-1.6**	**1.9**	**3.8**	**9.4**	**149.6**	**1.9**	**-15.2**	**20.1**	**0.4**	**4.9**
IA Mixed 40-85% Shares	-2.5	-0.4	2.0	9.4	17.5	101.9	2.0	-10.6	20.0	-0.7	8.2
Cirilium Dynamic	**-3.5**	**-2.4**	**1.7**	**5.6**	**10.7**	**154.8**	**1.7**	**-17.7**	**26.1**	**-0.2**	**5.1**
IA Flexible	-2.5	-0.6	1.9	10.9	20.2	99.8	1.9	-10.1	21.1	0.7	7.7
Cirilium Adventurous	**-4.1**	**-2.5**	**1.1**	**9.1**	**12.3**	**13.2**	**1.1**	**-16.9**	**29.8**	**-0.9**	**3.9**
IA Flexible	-2.5	-0.6	1.9	10.9	20.2	21.1	1.9	-10.1	21.1	0.7	7.7

Source: Quilter Investors as at 31 October 2023. Total return, percentage growth, net of fees, rounded to one decimal place of the R (GBP) accumulation shares. The Cirilium Conservative Portfolio launched on 30 March 2012; the Cirilium Balanced Portfolio, the Cirilium Moderate Portfolio, and the Cirilium Dynamic Portfolio launched on 2 June 2008; and the Cirilium Adventurous Portfolio launched on 1 June 2017.

How our equity holdings performed

US large caps defend better

The underperformance of small-cap stocks versus their larger peers has been a consistent headwind for active managers over the past two years, as active managers typically buy smaller, less researched companies where they have an analytical edge. This strategy struggles when market returns are driven by a handful of mega-cap names. The SGA US Large Cap Growth Fund was the best-performer among our US holdings. However, it was still down around 1.5%.

> Small-/mid-/large-/mega-cap refers to the market capitalisation (market cap) or size of a given stock. This is based on the total value of all the shares it stock has issued.

UK smaller companies struggle

The same small-cap underperformance theme was also apparent in the UK with the Montanaro UK Income and the Premier Miton UK Value Opportunities funds down 7.3% and 6.5%, respectively. Larger-cap exposures, such as the City of London Investment Trust, fared better. However, even the Liontrust UK Growth Fund, the top UK performer, was down more than 3.5%, highlighting the challenging market environment.

Solid relative performance in Asia and emerging markets

Although there were few places that delivered positive returns in October, we saw strong relative performance from our Asian and emerging market equity managers. The Fidelity China Consumer Fund outperformed the Chinese market by almost 2.5% while the Jupiter Global Emerging Markets Focus Fund also fared somewhat better than the broad emerging markets index.

How our fixed-income holdings performed

Active managers provide a buffer

Our underweight to bonds, relative to our strategic asset allocation, was helpful in October as US Treasuries (US government bonds) fell.

Despite modest aggregate losses for both government and corporate bonds (issued by companies), performance from our fixed-income managers was generally ahead of their benchmarks in October. The top performer was the Wellington Emerging Local Debt Advanced Beta Fund, which continued its strong run as emerging market central banks, which were quicker to raise interest rates following Covid, are now embarking on rate-cutting cycles. Meanwhile, the Premier Miton Financials Capital Securities Fund, which invests in high-yield bank debt, was up 0.6%.

> Our strategic asset allocation (SAA) is the long-term weightings assigned to each asset class, such as equities, bonds, property, alternatives, and cash. These weights differ according to the risk level of each portfolio.

How our alternative holdings performed

Alternatives make solid gains

The returns from our alternatives holdings were almost uniformly positive in October, which was especially rewarding against the backdrop of falling equity and bond markets. The Brevan Howard Absolute Return Government Bond Fund was up 1.3% while the AQR Managed Futures Fund, which employs a systematic strategy that seeks to capitalise on trends in equity, bond, and commodity markets, gained 1.6%.

Portfolio activity

We have been reducing our underweight position to bonds in the Cirilium Conservative, Balanced, and Moderate Portfolios after government bond yields moved materially higher (meaning their prices fell) since the summer. To implement this change, we added to funds such as Janus Henderson Strategic Bond.

Elsewhere, we increased the healthcare equity exposure in the portfolios through an addition to the Alliance Bernstein International Health Care Fund. This allowed us to take advantage of the underperformance of the sector compared to global equities over the past six months or so. We had previously reduced our overweight position here after a period of healthcare sector outperformance.

Investment outlook

Economic growth in the US has been surprisingly resilient, although it is slowing, while the data from Europe and the UK have been weaker for some time. Inflation remains above central bank targets but has moderated significantly and investors are growing in confidence that interest-rate hiking cycles are ending. Our central expectation is that the global economy experiences a 'soft-ish' landing from the post-pandemic boom, with low but positive economic growth and asset market returns.

A soft-landing is where economic growth and inflation both slow without a severe economic downturn taking place.

1. Too early to expect rate cuts

In this environment, it's natural to speculate on the timing of interest-rate cuts. However, if market pricing runs too far ahead of the current reality it risks loosening financial conditions so that growth and inflation picks up again. Central banks are attuned to this risk and don't want a re-run of the 1970s, where policy was eased prematurely allowing inflation to resurface. Consequently, we expect them to maintain their 'higher for longer' policy narrative for some months yet.

2. Tentative signs of economic weakening

While many leading indicators of economic growth have been weak for over a year, realised growth in the US has been comparatively strong. The same cannot be said for Europe where the economy has stagnated for over a year. Elevated government spending and resilient labour markets may continue to support corporate earnings and equity markets, but risks are increasing as we see tentative signs of weakening employment data and waning sentiment among investors.

3. Risks are rising but balance is the order of the day

In the latest US corporate earnings season, companies performing below expectations found their share prices were disproportionately punished compared to those who positively surprised, which could indicate a looming market correction. Meanwhile, the risk that other Middle East powers are dragged into the Gaza conflict has increased the risk of market falls. While caution is warranted, our allocation remains balanced, reflecting the range of possible outcomes.

A market correction is usually defined as a decline of 10% but less than 20% in the price of an index from its most recent peak. A market correction can last anywhere from days to months, or even longer.

Thank you for investing with us

Keep an eye out for your next Cirilium Portfolios monthly commentary available in December.

Want more updates about your portfolio?

Please visit our website at ***www.quilter.com*** for all the latest news, views, and portfolio information.

Your financial adviser is on hand to discuss anything related to your investment decisions or the suitability of the products mentioned in this document.

If you are a financial adviser and you have any questions or want to find out more about our solutions, please speak to one of our investment directors on +44 (0)207 167 3600, email us at ***enquiries@quilter.com***, or visit our website at ***www.quilter.com***.

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