ASSET ALLOCATION & RESEARCH

MONTHLY REVIEW

AUGUST 2023

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Monthly Commentary – August 2023

As investors hit the beaches in August, markets hit a speed bump in their otherwise steady climb this year. There are several reasons for the August slump. Seasonally volumes and news flow dry up in August leading to greater volatility and a lack of buyers. The end of Q2 earnings reporting season has left investors with little to ponder outside of mixed economic data. In addition, Federal Reserve Chairman Powell's comments at the Jackson Hole Symposium suggesting that further rate hikes may be needed, put pressure on both bond and equity prices. Finally, China's struggling economy has raised concerns of further global economic weakness later this year as one of the world's economic engines continues to struggle.

This type of trading action is not out of line for late summer. Over the past 10 years, the S&P 500 has averaged a gain of just 0.1% for August — making it the third-worst month for the index. Go back 20 years and the performance gets worse with the benchmark index averaging a monthly loss of 0.1%. The good news for equity investors is that the upward trading channel that began in October remains intact. The bad news is that Treasury yields reached five-month highs in August making them more attractive to short term investors. Although, later in the month US equities outperformed their foreign counterparts. Developed markets outperformed emerging markets, with the MSCI All World Index down 2.8% vs. EM down 6.1%. In commodity markets, global oil prices remained relatively flat over the month as growth risks in China counterbalanced the impact of production cuts. Gold moved lower in August while cash was the best performing asset over the month.

United States

August began with the credit rating agency Fitch downgrading the US government's credit rating from AAA to AA+, citing unsustainable debt and deficit trajectories and increased political dysfunction. While the announcement caused heated debate in political and economic circles it had little impact on the economy or Treasury yields, coming ten years after a downgrade by Standard & Poor's. So, factoring in the seasonal weakness of August and light trading volumes, every economic report took on greater scrutiny.

Overall, incoming economic data remained solid with the US. Labor market data pointing to a cooling but still strong jobs market in July, with payroll job gains of 187,000, slightly below consensus expectations for 200,000. Unemployment ticked down to 3.5%, while average hourly earnings were slightly stronger than expected at 4.4% year on year. Retail sales increased 0.7% month on month in July, well above expectations of a 0.4% month over month rise. On the inflation front, the headline Consumer Price Index (CPI) increased slightly in July to 3.2% year over year due to higher food and energy prices, while core CPI decelerated slightly to 4.7% year over year from 4.8% year over year in June. The core PCE reading, which strips out food and energy prices and is often described as the Fed's favorite inflation measure, was also in line with expectations, showing a 0.2% monthly rise, while the year-over-year rate ticked up to 4.2% from 4.1%.

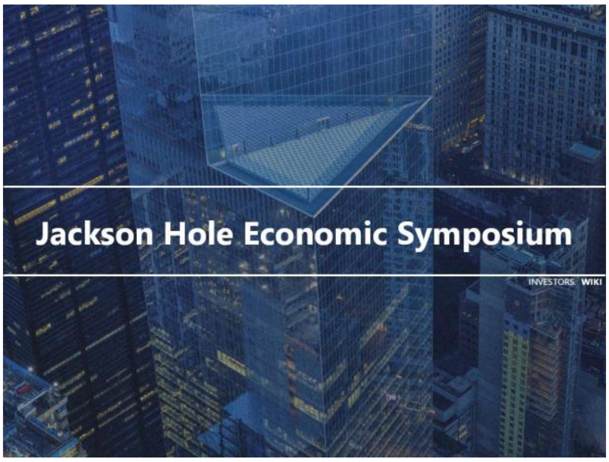
Although the data seems to suggest a "soft landing" for the US economy is still possible, investors took advantage of the spike in short term yields caused by the strong economy to move out of stocks. Adding to the problem, August looks to have been one of the worst months for ETF flows ever, with just $11.1 billion of inflows through 30 August, most of which went to short term bond funds. With a lack of buyers in the market, equities drifted lower.

The weakness was felt across all segments of the market with nine of the eleven S&P sectors posting a negative result in the month. The artificial intelligence-led rally that drove the market higher for most of the year took August off and tech stocks slumped. The three major stock indexes wrapped up a volatile month with the large-cap S&P 500 index suffering its first monthly loss since February, while the Nasdaq Composite logged its first monthly slide since December 2022. The final numbers for the month were not as bad as they might have been as equity markets rallied in the last week of August. The Dow Jones ended the month down 2.4% and the Nasdaq Composite slipped 2.2%. The S&P ended August down 1.8% at 4,507.66, well above initial technical support of 4400 and far above major support of 4200.

While September has historically been the worst performing month for stocks there are some positive signs developing. First, stock-market sentiment has retreated sharply in the last few weeks from bullish levels in late July, this should provide some support for equities as the selling pressure abates. In addition, the intermediate term peak in the US dollar and Treasury yields, as evidenced by the pullback in both at month end, should bring bottom fishers off the sideline. Finally, the market is a forward-looking mechanism and will begin to price in 2024, a year in which the Fed should not be hiking interest rates.

The Federal Reserve/Interest Rates

The long anticipated and possibly overhyped St Louis Fed Jackson Hole Economic Symposium finally arrived. Federal Reserve Chairman Jerome Powell spoke on the last day of the conference opening his remarks by telling the gathering of prominent members of government, academia, and financial markets that his comment would be longer than his thirteen-minute speech in 2022 but the message was the same: It is the Fed's job to bring inflation down to our 2 percent goal, and we will do so. While acknowledging that progress has been made and saying the Fed will be careful in where it goes from here, the central bank leader said inflation is still above where policymakers feel comfortable. He noted that the Fed will remain flexible as it contemplates further moves but gave little indication that it's ready to start easing anytime soon.



"Although inflation has moved down from its peak, a welcome development, it remains too high," Powell said in prepared remarks. "We are prepared to raise rates further if appropriate and intend to hold policy at a restrictive level until we are confident that inflation is moving sustainably down toward our objective."

Powell indicated it's too soon to declare victory, even with data this summer running largely in the Fed's Favor. June and July both saw an easing in the pace of price increases, with core inflation up 0.2% for each month, according to the Bureau of Labor Statistics. While admitting that the risks are two-sided, with the danger of doing both too much and too little. However, he gave no clear indication of which way he was leaning. "Given how far we have come, at upcoming meetings, we are in a position to proceed carefully as we assess the incoming data and the evolving outlook and risks," he said.

Powell's remarks follow a series of 11 interest rate hikes that have pushed the Fed's key interest rate to a target range of 5.25%-5.5%, the highest level in more than 22 years. In addition, the Fed has reduced its balance sheet to its lowest level in more than two years, a process which has seen about $960 billion worth of bonds roll off since June 2022.

What concerns the FOMC is that despite the rate hikes the US economy has remained strong, Gross domestic product has increased steadily since the rate hikes began and the third quarter of 2023 is tracking at a 5.9% growth pace, according to the Atlanta Fed. Employment also has stayed strong, with the jobless rate hovering around lows last seen in the late 1960s.

As long as inflation continues to weaken the FOMC seems content to watch the data. Current market expectations place an 89% probability that the Fed will leave rates unchanged at its September meeting, placing a near 40% chance that the Fed's next hike will come in November. There will be plenty of new economic data for the Fed to review before then.

The minutes of the July Federal Reserve meeting were released on 17 August with far less anticipation than the Jackson Hole meeting but provide some insight into the FOMC's thinking. The vote to raise rates was unanimous, but at least two members felt raising rates may have been premature. The division among the committee members was mild but indicated some members favour holding rates at current levels. The other point of interest was that the committee made no mention of lowering rates in the near term, something the market has begun to price into 2024 expectations.

The US bond market saw a significant sell-off in August, driving the yield on the 10-year note to a 16-year high. The yield on the benchmark 10-year Treasury now sits at 4.10%, down from a high of 4.35% earlier in the month. The 30-year yield now sits at 4.21%. Shorter term 2-year were little changed for the month, yielding 4.85%. The yield curve has remained inverted for over one year.

Commodities & the US Dollar

A solid run of strong economic data and spiking Treasury yields helped the dollar rebound in August. The United States was the only one of the world's ten largest economies to see upward revisions to its growth forecasts this month. The ICE U.S. Dollar Index, a measure of the currency against six major rivals, slumped to a 15-month low in mid-July but rebounded by more than 4% by late August. The dollar rose over 1.7% in the month yet remains down nearly 8% since last September's peak.

A spike in the dollar normally would be bad news for commodities but with most major asset classes falling in August, commodities were the second-best asset class in the month, with the iShares S&P GSCI Commodity-Indexed Trust posting a 0.5% gain for the month.

In the metals complex, gold finished the month down 2.2%, silver dropped 0.6%, copper dipped 4.6% while platinum bounced 1.7% higher.

A summer rally for oil, attributed in part to production cuts that saw Saudi Arabia voluntarily reduce production by one million barrels a day beginning in July, stalled in August on worries over the global economic outlook. Soft Chinese economic data and concerns about the country's ailing property sector raised doubts about demand from the world's second-largest crude consumer. However, crude prices regained their upward momentum over the last six sessions of the month as it became more widely expected that Saudi Arabia would extend its million barrel-per-day cuts through October. The reality of tighter supplies pushed prices to a third straight monthly gain and levels not seen since November 2022. Furthermore, it appears Russia will announce a deal with OPEC to curb its oil production adding additional price support.

Oil bulls were further encouraged by the formation of a so-called golden cross on the daily price charts, a pattern that technicians see as lending weight to expectations for a continued uptrend for the commodity. West Texas Intermediate crude posted a gain of 2.2% for the month while Brent recorded a 1.5% rise.

It is worth noting that wheat prices had their worst month in a year, a potential sign that the CPI number is headed lower.

Global Markets

While stock markets in the US have been watching rising interest rates, markets overseas have their eyes on China and it's not a pretty sight. Economic data out of China has been lacklustre, to say the least. On the inflation front, CPI turned negative in July at -0.3% year over year, while producer price index (PPI) deflation continued for the 10th month in a row. Chinese manufacturing activity contracted for a fifth straight month in August but came in better than last month's reading and a consensus forecast. Meanwhile, services activity in the country remained expansionary, but posted the lowest reading in eight months. Retail sales missed expectations by a wide margin, growing 2.5% against expectations of 4.5%. Although consumer sentiment has begun to improve on the back of promised government stimulus, a rebound in the coming months seems unlikely as households remain sceptical the government is committed to western style reform.

Chinese investment data also highlighted low business confidence as private investment decreased 2.3% year over year in July. Real estate was the weakest sector, with an 8.5% fall in investment between January and July compared to the same period last year. The difficulties of Country Garden and Evergrande, two of China's largest property developers, also highlighted real estate weakness in August.

To address these difficulties as well as deflationary risks, the People's Bank of China (PBoC) lowered its interest rate twice in August, but so far credit demand remains weak. At the end of the month, Beijing also took several initiatives to support financial markets, such as halving the stamp duty on stock trading. Despite these measures, the Renminbi lost 1.6% against the US dollar over the month, while the CSI 300 index dropped 6.2%.

A continued slowdown in China's economy could spell trouble for markets around the world, including the U.S., given the sheer number of major corporations that rely on the country as a strong source of revenue. However, the impact may be felt differently, hurting Europe which depends on Chinese manufacturing activity while exporting deflation to the US, something the Fed would welcome.

In Japan, the economy expanded by 6.0% quarter over quarter in the second quarter of 2023 on the back of a strong contribution from net trade. Activity indicators such as the Tankan index point to a continuation of this strong momentum in the coming months. Japan also seems to be turning the page on its deflationary period, with core CPI up 10 basis points to 4.3% in July and spring wage negotiations leading to the biggest wage increases in 30 years. Compared to other markets, Japanese equities proved relatively resilient in August as the Topix posted a modest gain of 0.41% but the Nikkei 225 dropped 1.67%.

Eurozone headline inflation was reported at 5.3% in August, flat month over month but above economists' expectations. While improving, inflation nevertheless remains well above the European Central Bank (ECB)'s target and markets continue to price further ECB rate increases before the end of the year. Food inflation was again the largest contributor to the headline rate, rising 9.8 percent from a year earlier on average across the 20 countries that use the euro currency. Inflation was also given some upward momentum by energy costs, which rose 3.2 percent in August from the previous month.

The acceleration of inflation in some of the region's largest economies arrives two weeks before the European Central Bank's next policy meeting, opening the debate to a hike at the September meeting. Last month, Christine Lagarde, the president of the central bank, said she and her colleagues had "an open mind" about the decision in September and subsequent meetings.

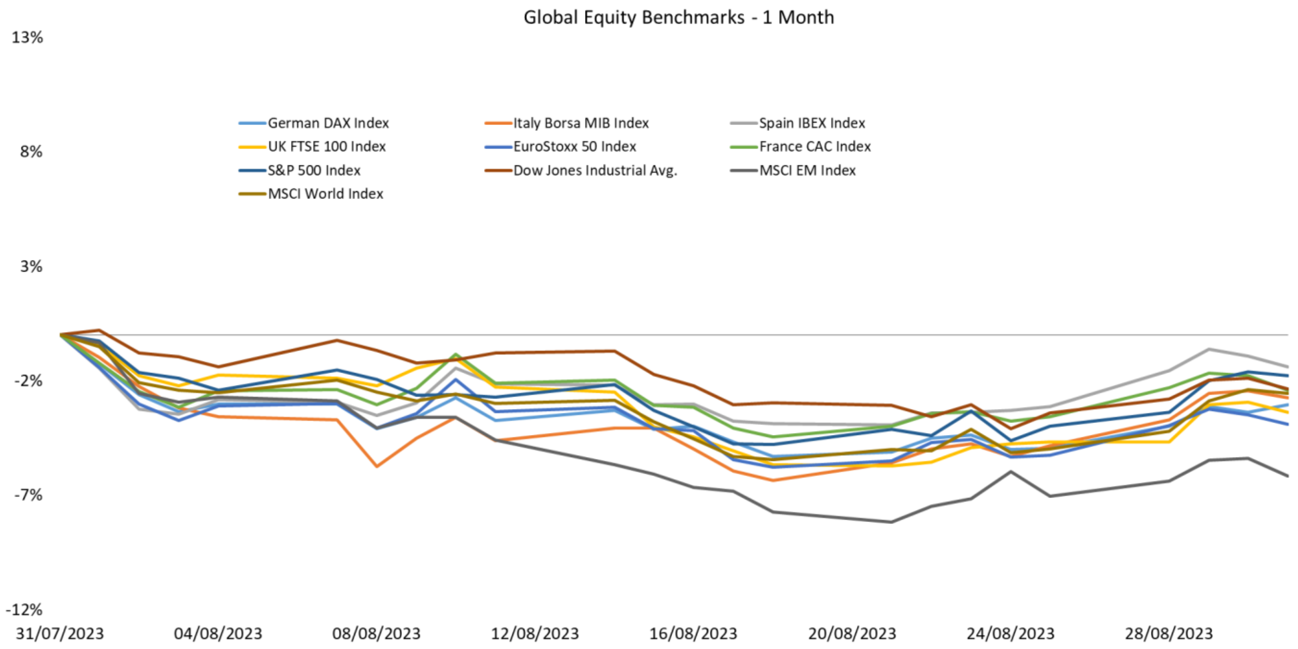
The MSCI Europe ex-UK index dropped by 2.2% in August, dragged down by the banking sector, after the Italian government announced a tax on banks' "excess" profits. European bond yields remained broadly stable in August and the Bloomberg Euro Aggregate rose 0.3% over the month. The pan-European Stoxx 600 declined by 2.64% in August.

In the UK, the Bank of England (BoE) hiked its policy rate by 25bps at the start of August, bringing the Bank Rate to 5.25%. The BoE highlighted its intention to hold rates at restrictive levels for some time. Despite this tighter monetary policy, the UK economy surprised to the upside during the second quarter of 2023, as GDP rose by 0.2% quarter over quarter vs. a consensus expectation of flat.

UK headline CPI eased in line with expectations to 6.8% in July, down from 7.9% in June. Labor market data showed growth in regular pay (excluding bonuses) was 7.8% in the period April to June 2023, the highest rate since comparable records began in 2001. In this context, markets continue to expect further rate increases from the BoE this year. Against this backdrop, the 10-year Gilt yield rose 5 bps to 4.4% in August, while the FTSE All-share underperformed its developed market peers, declining 2.5% over the month.

Global Market Performance

Global equities struggled in August as Treasury yields climbed and the Chinese economy slowed. The S&P 500 posted a loss of -1.77% for the month while the Dow Jones declined -2.36%. The Pan-European Stoxx 50 fell -3.90%. In European markets, the German DAX slid -3.04%, while the Italian Borsa decreased by -2.74%, the Spanish IBEX drifted -1.41% lower and the French CAC lost -2.42% in August. The UK FTSE 100 Index dropped -3.38% for the month. The MSCI World Index sank -2.55% and the MSCI EM Index led all markets lower, falling 6.36% in August.



Market Outlook

Although at times it has not been abundantly clear, the US economy remains on solid ground. Whether the "soft landing" scenario investor are betting on plays out is not clear but what is clear is that the US remains the most stable of the global equity markets. China's difficulties will inevitably weigh on the global economy in the coming months, given the country contributes almost a third of global growth, putting more pressure on central banks still struggling in their fight against inflation. As investors turn their attention to 2024 and US growth continues to remain steady, we believe the US equities markets will continue to perform. While September may be volatile as aways, we expect markets to hold current support levels and would add to position on pullbacks. If the US labor market can remain solid, large cap stocks should continue to do well even in a slowing economy. We maintain our belief that the strong balance sheets of the large technology companies will allow them to continue to lead the market. Bond yields are likely nearing a peak and we would be buyers of large cap US equities on any pullback.

ASSET ALLOCATION & RESEARCH - MODEL PORTFOLIOS

The table below illustrates the monthly returns of the Asset Allocation & Research Model Portfolios.

Index	MTD Return (GBP)	YTD Return (GBP)	MTD Return (USD)	YTD Return (USD)
AAR Cautious Model Portfolio GBP/USD	-1.11%	2.87%	-2.24%	5.25%
AAR Balanced Model Portfolio GBP/USD	-1.56%	6.55%	-2.55%	10.08%
AAR Growth Model Portfolio GBP/USD	-1.73%	12.79%	-3.01%	17.01%
AAR Equity Only Model Portfolio GBP/USD	-2.18%	13.41%	-3.59%	16.68%
AAR Concentrated Cautious Model Portfolio GBP/USD	-1.11%	2.89%	-2.29%	5.22%
AAR Concentrated Balanced Model Portfolio GBP/USD	-1.19%	7.65%	-2.04%	12.14%
AAR Concentrated Growth Model Portfolio GBP/USD	-2.14%	13.37%	-3.28%	16.16%
Legal & General Cautious GBP/ Legg Mason Conservative Fund USD*	-1.01%	-0.54%	-1.87%	2.31%
Legal & General Balanced GBP / Legg Mason Balanced Fund USD	-1.16%	-0.47%	-2.10%	5.84%
Legal & General Adventurous GBP / Legg Mason Performance Fund USD	-1.53%	2.70%	-2.31%	9.08%
FTSE 100 TR Index GBP / S&P 500 TR Index USD	-2.50%	3.02%	-1.59%	18.73%

Model Portfolios

Below you will find the top and the bottom two performers of each Asset Allocation & Research Model Portfolio:

USD Model Portfolios								
	Cautious		Balanced		Growth		Equity Only	
Top	PIMCO INV GRADE CORP BD ETF	-1.11%	SPDR GOLD SHARES	-1.28%	BLUEBOX GLOBAL TEC FD-C USDA	-1.47%	BLUEBOX GLOBAL TEC FD-C USDA	-1.47%
	SPDR GOLD SHARES	-1.28%	ISHARES IBOXX INVESTMENT GRA	-1.57%	SPDR S&P 500 ETF TRUST	-1.63%	SPDR S&P 500 ETF TRUST	-1.63%
Bottom	ISHARES MSCI ALL COUNTRY ASI	-7.02%	ISHARES MSCI EMERGING MARKET	-6.63%	AQA-CASTLESTN NEXTGEN-EUSDA	-7.09%	SPDR S&P CHINA ETF	-9.50%
	ISHARES EUROPE ETF	-3.80%	ISHARES CORE S&P SMALL-CAP E	-4.17%	WISDOMTREE EMERGING MARKETS	-5.24%	AQA-CASTLESTN NEXTGEN-EUSDA	-7.09%

GBP Model Portfolios								
	Cautious		Balanced		Growth		Equity Only	
Top	ISHARES CORE UK GILTS	-0.37%	ISHARES CORE UK GILTS	-0.37%	IFSL MRLBGH US MULTI CAP-IN	2.70%	BLUEBOX GLOBAL TECH-C GBP	0.05%
	ISHARES CORE GBP CORP	-0.38%	ISHARES CORE GBP CORP	-0.38%	BLUEBOX GLOBAL TECH-C GBP	0.05%	DOMINION GT-MGD FD-GBPR	-0.38%
Bottom	ISHR MSCI AC FAR EAST X-JP	-6.38%	VANG FTSE EM USDD	-4.38%	AQA-CASTLESTN NEXTGEN-EGBPA	-7.13%	AQA-CASTLESTN NEXTGEN-EGBPA	-7.13%
	ISHARES MSCI EURP X-UK GBP-H	-3.45%	CASTLESTONE FAANG+ UCITS-B	-3.00%	VANG FTSE EM USDD	-4.38%	VANG FTSE EM USDD	-4.38%

Note About Portfolio Performance

Losses were felt across all portfolios in August as both equity and bond prices fell. The USD Cautious portfolio fell -2.24%, the USD Balanced portfolio declined -2.55%, the USD Growth portfolio sank -3.01% and the USD Equity Only portfolio retreated by -3.59%. The S&P 500 Total Return Index was down -1.59% (including dividends) in August.

The best performing USD holding in the month was the PIMCO Investment Grade Corporate bond ETF.

The GBP Cautious portfolio fell -1.11%, the GBP Balanced portfolio declined -1.56%, the GBP Growth portfolio slumped -1.73%, and the Equity Only GBP Portfolio decreased by -2.18%. In August, the FTSE 100 TR Index fell -2.50%, (including dividends).

The iShares Core UK Gilts ETF was the best monthly performer in the GBP portfolios.

CONCENTRATED PORTFOLIOS

Below you will find the top and the bottom two performers of each Asset Allocation & Research Concentrated Portfolios:

USD Concentrated Model Portfolios						
	Cautious		Balanced		Growth	
Top	SPDR GOLD SHARES	-1.28%	INVESCO QQQ TRUST SERIES 1	-1.48%	BLUEBOX GLOBAL TEC FD-C USDA	-1.47%
	ISHARES IBOXX INVESTMENT GRA	-1.57%	ISHARES IBOXX INVESTMENT GRA	-1.57%	SPDR S&P 500 ETF TRUST	-1.63%
Bottom	ISHARES MSCI ALL COUNTRY ASI	-7.02%	ISHARES MSCI EMERGING MARKET	-6.63%	AQA-CASTLESTN NEXTGEN-EUSDA	-7.09%
	ISHARES EUROPE ETF	-3.80%	ISHARES CORE S&P SMALL-CAP E	-4.17%	ISHARES MSCI EMERGING MARKET	-6.63%
GBP Concentrated Model Portfolios						
	Cautious		Balanced		Growth	
Top	ISHARES CORE UK GILTS	-0.37%	ISHARES CORE UK GILTS	-0.37%	BLUEBOX GLOBAL TECH-C GBP	0.05%
	ISHARES CORE GBP CORP	-0.38%	ISHARES CORE GBP CORP	-0.38%	ISHARES CORE UK GILTS	-0.37%
Bottom	ISHR MSCI AC FAR EAST X-JP	-6.38%	VANG FTSE EM USDD	-4.38%	AQA-CASTLESTN NEXTGEN-EGBPA	-7.13%
	ISHARES MSCI EURP X-UK GBP-H	-3.45%	ISHARES CORE FTSE 100	-2.45%	VANG FTSE EM USDD	-4.38%

NOTE ABOUT CONCENTRATED PORTFOLIO PERFORMANCE

In August, the USD Cautious portfolio lost -2.29%, while the USD Balanced portfolio fell -2.04% and the USD Growth portfolio declined -3.28%. The SPDR Gold ETF was the best performing USD asset over the month.

The GBP Cautious portfolio decreased by -1.11%, the Balanced portfolio dropped -1.19% and the Growth portfolio slipped -2.14%. The iShares Core UK Gilts ETF was the best performing GBP holding in August.

DISCLAIMER

Note: Please be aware that hypothetical or simulated performance results have certain limitations. Unlike an actual performance record, simulated results do not represent actual trading. Past performance cannot be relied on as a guide to future performance.

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Differences in performance have occurred due to the historical restatement of the underlying securities in the portfolios for the period 01/01/2020-30/10/2020. These restatements now have been considered in the performance for the period 30/10/2020-31/11/2020. The Discrepancies were created due to a reporting method within Bloomberg.

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