Parmenion
Investment Management

Strategic Guardian

Quarterly Update, Q2 2024

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The big picture: Macro and Markets

In a nutshell

- **Risk assets continue to lead the way**

  Equities continue to outperform fixed interest and Emerging Markets maintain momentum.

- **Politics takes centre stage**

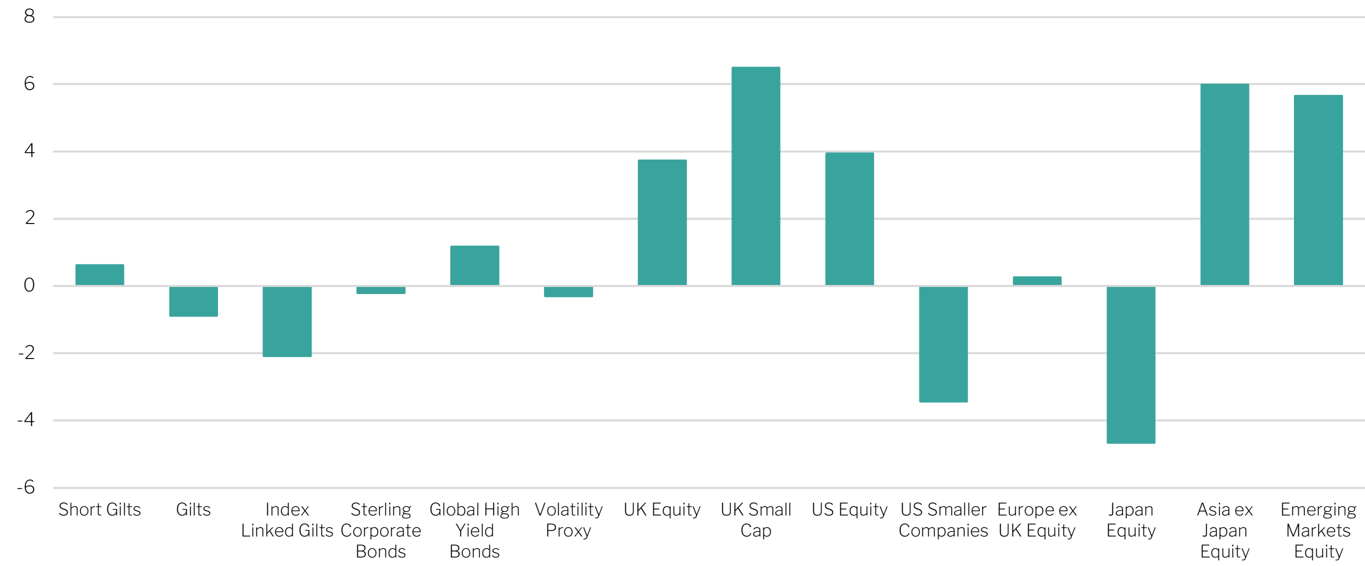
  Voters are rallying, with elections taking place across the world.

- **Inflation continues its downward path**

  The UK finally reached its 2% target but we're still waiting for rate cuts.

What's been happening in Q2 2024?

Asset class returns (Q2 2024)



Asia and Emerging Markets led the way in Q2, continuing their strong performance this year, while Fixed Interest returns were broadly flat with risk assets still providing the lion's share of returns.

Politics continues to dominate headlines, with campaigning and voting happening across the world. The US, UK, France, India, Mexico and South Africa have all had elections recently or are on the campaign trail. This means uncertainty for a large proportion of global markets. Though this hasn't materialised into any notable losses or volatility yet.

President Biden and Donald Trump had the first of their two presidential debates. Biden's performance was unanimously panned, though neither candidate shone. The lack of coherence from Biden has left many in his party wondering if it's not too late to put someone else forward. This combined with Trump being the first criminally convicted former president, makes all this somewhat of a circus.

Macron surprised everyone by calling an election after a poor showing in EU Parliamentary voting. A strong initial showing from the Rassemblement National (RN) party was surprisingly reversed in the second round of voting, following a left-wing coalition. A hung parliament now awaits.

AI mania continues to push Nvidia (and US equity indices) even higher, briefly overtaking Apple and Microsoft to become the world's most valuable company. Index concentration is extremely high which raises questions about diversification. How long the momentum can last is anyone's guess, but active fund managers will tell you it's a painful bet to be on the wrong side of.

Inflation continued to fall over the quarter. The UK hit its 2% target, although wage and services inflation remain elevated. This led the Bank of England to hold interest rates until at least August. The Fed is cautious not to cut rates too quickly - a recession is less concerning than the embarrassment of having to reverse course. The ECB has been on the front foot, taking their deposit rate down from 4% to 3.75%.

China announced support measures to revive the property sector and boost confidence amongst consumers. To hit its GDP growth targets, China needs its population to be spending not saving.

What does that mean for performance?

Cumulative Performance (%)

This table outlines the cumulative investment performance of this solution across various risk grades, versus their IA benchmark.

	Q2	YTD	1 Year	3 Year	5 Year
Risk Grade 1	0.69	1.21	5.65	1.35	3.10
IA Standard Money Market	**1.29**	**2.60**	**5.44**	**8.81**	**9.61**
Risk Grade 2	0.38	0.70	5.96	-4.68	-0.58
Risk Grade 3	0.79	2.10	6.85	-4.71	1.89
Risk Grade 4	0.95	2.89	7.40	-3.86	6.08
IA Mixed Investment 0-35% Shares	**0.63**	**2.14**	**7.59**	**-2.46**	**5.57**
Risk Grade 5	1.13	3.52	7.89	-3.44	9.46
Risk Grade 6	1.33	4.21	8.61	-1.85	14.20
IA Mixed Investment 20-60% Shares	**1.14**	**3.65**	**9.38**	**2.83**	**15.20**
Risk Grade 7	1.60	4.92	9.23	-0.90	17.79
Risk Grade 8	1.83	5.49	9.65	-0.75	20.62
IA Mixed Investment 40-85% Shares	**1.67**	**5.91**	**11.82**	**7.19**	**25.58**
Risk Grade 9	1.99	6.04	9.96	-0.59	23.63
Risk Grade 10	2.16	6.57	10.38	-0.93	25.78
IA Flexible Investment	**1.71**	**6.27**	**11.78**	**7.27**	**28.57**

Discrete Annual Performance (%)

This table outlines the discrete annual performance of this across various risk grades, versus their IA benchmark.

	2023	2022	2021	2020	2019
Risk Grade 1	4.68	-4.86	0.16	1.29	2.84
IA Standard Money Market	**4.74**	**1.28**	**-0.05**	**0.43**	**0.73**
Risk Grade 2	3.58	-9.76	1.37	2.63	5.55
Risk Grade 3	2.97	-10.98	2.96	3.64	7.65
Risk Grade 4	2.96	-11.32	5.06	4.67	10.02
IA Mixed Investment 0-35% Shares	**5.97**	**-10.87**	**2.84**	**3.90**	**8.70**
Risk Grade 5	2.97	-11.74	6.77	5.47	12.32
Risk Grade 6	3.49	-11.63	8.71	5.92	14.59
IA Mixed Investment 20-60% Shares	**6.81**	**-9.47**	**7.20**	**3.51**	**11.84**
Risk Grade 7	3.71	-11.73	10.02	6.56	16.34
Risk Grade 8	3.73	-11.93	10.86	7.64	17.91
IA Mixed Investment 40-85% Shares	**8.08**	**-10.04**	**10.94**	**5.32**	**15.78**
Risk Grade 9	3.84	-11.92	11.37	8.86	19.48
Risk Grade 10	4.13	-12.28	11.50	9.92	21.16
IA Flexible Investment	**7.08**	**-8.98**	**11.30**	**6.70**	**15.66**

What worked and what didn't?

Despite a small drag from bonds and hedge assets, strong returns from UK and US large cap, Asia and Emerging Markets as well as UK small cap meant all risk grades delivered positive returns.

Most returns are fully aligned through the risk grades. Risk grade 10 over 3 years is marginally behind risk grade 9 because of a higher allocation to Asia Pacific and Emerging Markets. Risk Grade 1 is also out of line over most time horizons given the weighting to Managed Liquidity.

Returns for the quarter can be attributed to the UK (large and small cap), Asia and Emerging Markets, and US large cap. The four UK asset classes combined delivered 65bp at the index level for a Risk Grade 5 portfolio, while Asia and Emerging Markets contributed over 1%. While the defensive assets were a lag during a risk-on quarter, the cost for Risk Grade 5 was a mere 5bp, allowing the growth part of the portfolio to flourish.

Asset classes

Equity returns were mixed over the quarter. UK, Asia Pacific ex Japan and Emerging Markets to perform well. Emerging Market returns were driven mainly by the biggest countries within the index: China, Taiwan, and India, with South Africa also performing well.

US Equities were once again one of the top performers. The return profile of the US index saw small and mid-caps struggle with large cap tech dominating returns. This is leading to severe concentration at the top of the index. We're diversified against this within our active fund selection. It was positive to see strong performance from UK Small Cap, an unloved asset class for the last two years.

Bonds offered a mixed outcome over the quarter, with the 10-year Gilt yield rising 40bp. However, the short end was marginally up, which combined with a 4% yield meant Short Gilts offered a small return. High Yield bonds also benefited from lower duration as well as a contraction in credit spreads, leading to positive returns. Despite good returns from much of the equity space, hedge assets were down a mere 30bp, offering very limited drag for an insurance asset class, and diversifying well away from bonds.

US small caps were a drag on returns over the quarter in contrast to the strong returns from their large cap neighbours.

Japanese equities were the worst performing asset class over the quarter. This was down to currency differences, with local currency returns positive, albeit portfolios receive the returns inclusive of currency moves.

Manager selection

Gresham House UK Smaller Companies had a strong quarter, returning 8.17% versus the UK small cap index which was up 6.49%. We also saw both Miton UK Multi Cap Income deliver strong returns for UK Income given its small cap bias.

Elsewhere, both Veritas Asian and Schroder Asian Income saw returns in excess of 6% in absolute terms, both marginally ahead of the index.

While Japan at the index level was the largest detractor, at the fund level returns were much better, with both holdings outperforming. Morant Wright was positive in absolute terms for the quarter, almost 5% above the index return.

Given the concentration of the US index and how narrow the return drivers have become we were pleased to see that Amundi Pioneer US Fundamental Growth kept up with the index. This fund is our highest growth active manager, however it is also very disciplined in terms of valuation and doesn't own all the top weighted tech names. Complementing Amundi was our passive holding which accounts for half of the US asset class.

Over what was a flat quarter across most fixed income sub asset classes our credit managers held up. However, we didn't see significant outperformance.

Premier Miton US Opportunities pulled down our US asset class versus benchmark and was the largest detractor. The fund is positioned very differently to the index with no allocation to large cap tech names and more cyclical exposure. The fund offers good diversification versus the now very concentrated index. This means it will perform differently. Over this quarter that was not in our favour, however we expect the fund to offer good relative returns if/when returns broaden out within the index.

Elsewhere, Brown US Smaller Companies also lagged its peer group, suffering almost entirely from the exclusion of two small cap AI stocks.

Fund changes

There were no fund changes over the quarter.

Asset allocation (%)

Risk Grade	1	2	3	4	5	6	7	8	9	10
Managed Liquidity	60.00	22.50	16.50	12.75	9.00	7.25	5.25	3.00	1.50	0.00
Short Dated Bonds	12.75	20.00	14.50	11.50	8.50	7.25	5.50	3.75	2.00	0.00
UK Gilts	7.75	12.25	9.25	7.50	6.50	5.25	4.00	3.00	1.50	0.00
Index Linked Government Bonds	6.50	10.25	7.25	6.00	5.25	4.25	3.25	2.50	1.50	0.00
Sterling Corporate Bonds	7.00	9.75	6.00	3.75	3.25	2.75	2.25	1.75	1.00	0.00
Global High Yield Bonds	3.50	4.25	1.50	1.00	1.00	1.00	0.75	0.50	0.00	0.00
Hedge Assets	2.50	11.00	15.00	15.50	14.50	11.25	8.00	5.50	2.50	0.00
UK Equity Income	0.00	1.25	3.50	5.00	6.50	8.00	9.50	11.00	12.25	13.25
Large Cap UK Equity Growth	0.00	1.00	3.00	4.00	4.25	4.50	4.50	4.50	5.00	6.00
UK Mid Cap Equity	0.00	0.50	1.25	1.50	1.50	1.75	2.50	3.00	3.50	4.75
UK Small Cap Equity	0.00	0.50	1.25	1.25	1.50	1.75	2.25	3.00	3.50	4.50
US Equity	0.00	2.25	6.75	9.50	11.25	13.50	15.25	16.75	17.25	17.25
US Equity Small Cap	0.00	0.50	1.75	3.50	5.00	6.50	8.00	10.00	12.50	14.00
Europe ex UK Equity	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.50	3.25
Japan Equity	0.00	1.00	2.75	3.50	3.75	3.50	2.75	1.25	0.00	0.00
Asia Pacific ex Japan Equity	0.00	1.25	4.50	6.50	8.75	10.75	13.25	15.25	16.75	17.00
Emerging Markets Equity	0.00	1.75	5.25	7.25	9.50	10.75	13.00	15.25	17.75	20.00

OCF & Yield

Risk Grade	1	2	3	4	5	6	7	8	9	10
OCF (%)	0.17	0.34	0.48	0.56	0.61	0.63	0.66	0.70	0.73	0.78
Yield (%)	4.05	3.39	3.08	2.80	2.55	2.27	2.09	1.91	1.65	1.43

A view on risk

	Volatility (%)			Max Drawdown (%)		
	1 Year	3 Year	5 Year	1 Year	3 Year	5 Year
Risk Grade 1	2.11	2.89	2.43	-0.39	-6.31	-6.31
IA Standard Money Market	**0.08**	**0.66**	**0.62**	**0.00**	**-0.08**	**-0.10**
Risk Grade 2	3.58	4.94	4.37	-1.07	-11.43	-11.43
Risk Grade 3	3.99	5.67	5.36	-1.04	-12.84	-12.84
Risk Grade 4	4.56	6.28	6.46	-1.25	-13.43	-13.43
IA Mixed Investment 0-35 Shares	**5.49**	**6.09**	**6.47**	**-2.37**	**-13.28**	**-13.28**
Risk Grade 5	5.28	7.04	7.72	-1.88	-14.20	-14.20
Risk Grade 6	6.03	7.69	8.95	-2.77	-14.35	-14.35
IA Mixed Investment 20-60 Shares	**6.23**	**6.89**	**8.36**	**-3.30**	**-12.14**	**-12.89**
Risk Grade 7	6.95	8.38	10.03	-3.82	-14.65	-14.91
Risk Grade 8	7.85	9.01	11.08	-4.82	-14.89	-16.86
IA Mixed Investment 40-85 Shares	**7.28**	**8.19**	**10.12**	**-4.39**	**-12.54**	**-15.41**
Risk Grade 9	8.83	9.65	12.18	-5.94	-15.39	-18.97
Risk Grade 10	9.69	10.34	13.26	-6.94	-16.53	-20.97
IA Flexible Investment	**6.98**	**7.81**	**9.97**	**-4.31**	**-11.20**	**-15.53**

What’s the outlook?

As we move through the year, politics looks set to keep the limelight. The run up to the US Presidential election in November is sure to create some headlines, with potential ramifications for international trade and relations top of the agenda for markets.

The narrative for the US economy is more and more that a ‘soft landing’ is most likely, with markets priced as though it’s a certainty.

We do see downside risk, like widening credit spreads or equities correcting. However, we still expect a shallow recession, with risk assets (particularly small cap) outperforming in the medium term.

Given the strong starting yields, we expect fixed interest to produce good, absolute performance regardless of how quickly interest rates might fall. We should also see the Bank of England cut rates next quarter, as long as inflation data is stable.

Finally, after years of post-Brexit uncertainty and all the changes at No.10, Kier Starmer’s sizeable majority might actually mean the UK is a relative stable political option. The idea of a Prime Minister staying in power for a full 4-year term could provide a catalyst to the UK market. Given the extent of recent underperformance (even with the FTSE 100 reaching a new high), any boost to sentiment would be welcome. UK valuations remain cheap, emphasised by the level of interest in private equity – just look at Hargreaves Lansdown.

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