LV= Smoothed Managed Funds

Investment Summary – as at 29 February 2024

Performance

- Global sentiment remained strong over the first two months of 2024. Global equities performed positively but global bonds were negative in February, returning 4.3%[1] and -1.3%[2], respectively.
- Despite an increase in bond yields, global equities rose to their highest ever level in February, owing in part to improved risk appetite due to the US economy's resilience and strong corporate results.
- Within this context, smoothed performance for the LV= ISA Balanced Fund was up 1.0%[3] over February and 1.7% year to date as positive returns over Q4 feed into smoothed prices.
- The main performance drivers for the Smoothed Managed Funds include:
  - Our bias to "Growth" and "Quality" styles has been positive over the month; "Growth" stocks have outperformed "Value" stocks, returning 5.9%[4] and 3.1%[5] in February, respectively.
  - A global diversified investment strategy continues to be beneficial, as global equities registered gains of 4.3%[1] over the month compared to UK equities which were up marginally at 0.2%[6].
  - The US Equity market was particularly strong over the month, registering a 5.3%[7] return. Despite a slight hawkish tone from the Federal reserve, the S&P reached historic highs; corporate earnings reports met or exceeded expectations for most companies and US economic data continues to point to resilience in growth. The 'magnificent 7' has been the 'magnificent 6' so far in 2024; Tesla disappointed markets due to fading momentum in its manufacturing arm whilst Nvidia's share price reached record highs.
  - Japan's export-heavy equity market continued its strong run, registering 5.5%[8] gains over the month. The Nikkei 225 has reached levels not seen since 1990, helped by recent shifts in corporate governance policies which are incentivising companies to spend their excess balance sheet liquidity.
  - European equities registered gains of 2.7%[9], underperforming wider global equities, as it grapples with higher-than-expected inflation levels, and an underperforming manufacturing sector, which has been impacted by weaker demand from China.
  - Bond market performance has been negative so far in 2024 as expectations of rate cuts pushed further into 2024 as central banks emphasise inflation remaining above target levels.

Economic Outlook

- Over the past 2 years, financial markets have experienced a complete reversal of accommodative monetary policy, as central banks, in the fight against inflationary pressures, have raised interest rates dramatically. The Bank of England have increased their policy rate by 5.15% in 18 months - the fastest increase in rates since the late 1980's. Global inflation has since peaked, and continues to fall towards target levels as the focus moves from interest rates remaining 'higher for longer' to the timing of interest rate cuts.
- We are continuing to monitor closely the elevated geopolitical risks this year which are arising from the conflict in the Middle East, the Ukraine/Russia war, and the upcoming global elections which are to take place.
- Despite such a rapid increase in interest rates, the European economies have narrowly avoided recessions, whilst the US has exceeded expectations in terms of growth. However, the outlook remains modest, and we remain cautious; particularly in the UK, which shows the lowest levels of predicted growth out of the three regions over the coming 12 months and entered a technical recession in the second half of 2023.
- Higher interest rate levels have improved the prospects for fixed income assets, as higher yields attract investors that have endured low or even negative yields over the last 2 decades. We expect these assets to play an essential role in diversifying more volatile equity holdings.
- We continue to have a bias towards quality companies that have strong balance sheets, lower leverage ratios, and have a strong customer base meaning future profits are more sustainable. These companies are more likely to be able to withstand economic weakness, particularly as borrowing costs put a strain on higher leveraged names.

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Equities Outlook

- We aim to be globally diversified across our equity allocation so as not to be overly exposed to any one region. This hurt our performance relative to peers in 2022, who tend to have higher concentration to UK assets. The UK outperformed in this period due to the energy and mining bias within the FTSE. This trend reversed over 2023 and our exposure to global stocks benefitted our funds; with double digit returns from our Japanese, European and US exposures over 2023, and continues to provide benefit in 2024.
- Economic growth forecasts are varied, as most economies grapple with tighter monetary policy. Falling inflation data in the US and Europe could mean a cut in central bank rates in the first half of 2024. In the UK, inflation is falling more slowly, and we could see rate cuts towards the second half of 2024. We believe global diversification continues to be a critical strategy for our funds.

Fixed Interest Outlook

- As you would expect in lower and moderate risk funds, our Cautious and Balanced funds have a significant amount of fixed interest (i.e. bonds) holdings. The funds have exposure to both Government and Corporate Bonds, here in the UK and overseas.
- The past 2 years has been extremely volatile for fixed interest markets due to rising interest rates and persistent inflation. As we have reached the top of this tightening cycle, fixed interest rate assets have become more attractive, as investors seek to lock in the higher yields.
- At current levels, yields on Government and Corporate Bonds also offer a return significantly above those seen for most of the last decade.
- The performance of bond markets was positive over 2023. Most returns were generated in Q4 2023 alone, as bond prices rallied strongly on the anticipation of falling interest rates in 2024. However, rising yields so far in 2024 have been a headwind for fixed income performance.
- The market is currently pricing in multiple interest rate cuts by global central banks by year-end, specifically: 4 for the Fed, 3 for BoE and 4 for ECB, bringing forecasted rates down to 4.5%, 4.5% and 3.0% respectively. These are expected to begin towards the end of Q1.

[1] MSCI All Country World Index, USD
[2] Bloomberg Aggregate Bond Index, USD
[3] LV= ISA Balanced performance used as an approximate measure of the wider SMF variants
[4] MSCI Growth Index
[5] MSCI Value Index
[6] FTSE 100 Index
[7] S&P 500 Index
[8] MSCI Japan Index, hedged
[9] FTSE Europe ex-UK Index

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Lines are open 8.30am - 5.30pm Monday to Friday. For TextDirect first dial 18001. Calls will be monitored and/or recorded for training and audit purposes.

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