MFS Bespoke Model Portfolio Service Quarterly Report

Q1 2024 market review

Macroeconomic landscape
Q1 2024

In the first quarter, bond and equity markets ‘decoupled’, or moved independently. Data continued to show US economic resilience, and equity markets in developed countries reached record highs, encouraged by the Federal Reserve appearing to engineer a **soft landing**. However, pessimism surrounded China due to concerns over its industrial and property sectors, although recent data suggests the stimulus will help to boost activity.

At the start of 2024, investors anticipated significant interest rate cuts by year-end, pricing in cuts between 1.50% and 1.75%. However, data showing US economic resilience has since tempered these expectations, highlighting the difficulty in reducing inflation to 2%. As the rate of disinflation slowed, markets now anticipate rate cuts to start in June, strategically timed ahead the US election.

Technology stocks, driven by AI optimism, soared, with Meta and Nvidia experiencing historic **market capitalisation** gains. The **rally** extended beyond tech, with broader **indices** like the S&P 500 Equal Weight Index and the Russell 2000 also experiencing gains. Corporate bond markets mirrored this enthusiasm, touching multi-year lows. European stocks, including the EuroStoxx 600 and FTSE 100, also posted strong gains. In the UK, Chancellor Jeremy Hunt's spring budget had minimal impact. With inflation decreasing and projected to approach 2% in the near future, there is potential for the Bank of England to lower rates this summer.

The Bank of Japan shifted from negative interest rates and adjusted its asset purchase program, leading to a weak Yen and a surge in local equities. Equities continue to experience a resurgence, with the Nikkei 225 reaching an all-time high in March, surpassing the previous high in 1989. Enthusiasm for stock exchange structural reforms and increased domestic participation helped equities perform strongly in Japan. China's targeted fiscal measures and growth targets failed to fully convince investors, but Chinese equities rebounded in the latter part of the quarter.

Investor confidence in inflation reaching target levels without a severe recession boosted equities and corporate bonds. However, the possibility of delayed rate cuts could keep borrowing costs high, emphasising the preference for quality companies with robust business models, low debt, and positive cash flows. Despite market fluctuations and geopolitical uncertainties, the first quarter of 2024 showcased resilience in equity markets fuelled by technology optimism and positive economic indicators. Central bank actions and geopolitical events will continue to influence investor sentiment and market dynamics as the year progresses.

Q1 2024 performance

Top Performers

Beutel Goodman US Value

The Beutel Goodman US Value fund gained 11.06% over the quarter. Whilst much of the focus has been on the **Magnificent 7** companies, the equity rally in the US has broadened, and some previously unloved stocks have also performed very well, boosting returns for **value** strategies. In particular, holdings such as the financial services company, American Express, did very well, with a strong economy increasing the demand for consumers to utilise credit facilities.

L&G US Index

The L&G US Index Fund gained 10.76% over the quarter. Despite fears that valuations are beginning to look frothy, the US economy rallied once again in Q1. Continued substantial gains in tech **mega-caps** like Nvidia, Microsoft and Meta Platforms were key to the stock market's resilient performance. During the first quarter, Nvidia's stock rose by 82%, Microsoft went up 12%, and Meta gained 37%, boosting performance of tracker funds such as the L&G US Index.

Bottom Performers

Vanguard UK Long Duration Gilt

The Vanguard UK Long Duration Gilt Fund fell 3.52% over the quarter. UK government bonds gave up some of their large (+14%) gains seen in Q4 2023, as higher-than-expected inflation data prompted investors to lower their expectations for interest rate cuts over the next 12 months. With fewer interest rate cuts expected now than at the start of the year, government bond prices (which move inversely to interest rates) fell accordingly.

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Ruffer Diversified Return

The Ruffer Diversified Return fell 0.99% over the quarter. With equity markets broadly going from strength to strength, Ruffer's negative positioning has led to their protective positions suffering. In particular, **put options** purchased to protect the portfolio against falling prices have expired, and the cost of these options proved a drag on performance.

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Model portfolio performance as at 31 March 2024

Portfolio	3 months	6 months	1 year	3 years	Since inception
MFS Disc Cautious	2.33	6.99	6.44	6.96	23.73
MFS Disc Balanced	3.13	8.31	7.40	6.68	27.91
MFS Disc Adventurous	4.39	9.56	8.89	7.02	35.63
MFS Disc Speculative	5.09	10.22	8.86	2.93	33.81
MFS Disc Cautious Income	2.14	6.70	7.07	11.28	29.90
MFS Disc Balanced Income	2.75	7.49	7.73	12.79	32.12
MFS Disc Adventurous Income	4.09	9.21	10.30	17.37	37.06

Portfolio changes and rationale

The currently downward sloping shape of the **yield curve** means that there is incredibly good value to be had when allocating to short-term **bonds** due to the attractive yields (the interest you receive on a bond) on offer. Additionally, credit spreads, which impact lower quality bond funds, remain very narrow which reduces the attractiveness of increasing allocations to this area of fixed income. Whilst nothing in investing is free, guaranteeing a healthy yield from higher quality, short term bonds is an attractive opportunity.

For years, Japan has had the reputation of being a “value-trap” – a market where stocks are cheap and remain so. But this may be about to change, as there has been a big drive by the Tokyo Stock Exchange to improve corporate efficiency, with the **index** instructing companies to increase profitability or risk being de-listed. These recent regulatory and structural changes have resulted in more share buybacks and dividend pay-outs. There is increasing evidence that investor capital once destined for China is now being allocated to Japanese equities, and that combined with the inherent **value** characteristics that come with Japanese stocks has encouraged an increase in model allocation to the nation.

Whilst the path to a **soft landing** is not certain it is becoming increasingly likely, with a reduced possibility of a significant economic slowdown or recession. Therefore, allocations to **absolute return funds** have been marginally reduced, particularly in models with more of a focus on capital growth. In those models we have an increasing willingness to embrace the **volatility** associated with growth-oriented investments. We do, however, still very much believe in the merits of absolute return funds, particularly those that perform in an uncorrelated manner to standard asset classes.

UK-based investors should be mindful of a concept known as 'home-bias', a behavioural bias whereby they are more inclined to invest in the UK than in other, often more attractive, overseas markets. The MSCI World Index only has a 4% allocation to the UK, whereas UK-based portfolios typically allocate far more. With more attractive opportunities elsewhere, we have been reducing UK allocations in favour of a more impartial approach, instead investing in regions with more attractive long-term growth rates.

Further material

Take a deeper dive into the Q1 2024 investment landscape with key members of the LGT Intermediary Investment Services team.

Click here

Click the link to watch a five-minute roundup of the last quarter with LGT’s CIO, Sanjay Rijhsinghani.

Click here

Glossary of terms

Absolute return funds	Absolute return funds are a form of alternative asset. They actively adjust their positions between equities, bonds, gold and other asset classes, typically with the aim of providing investment return across all market conditions.
Bonds	Bonds are debt securities issued by governments and corporations to raise money. Similar to an IOU, the investor lends money with the agreement that it will be paid back by a specific date, and they will receive periodic interest payments along the way. Bonds come under the umbrella of '**fixed income**' investments.
Defensive	Defensive positions prioritise preserving capital over growth. It is important to hold such positions in periods of market turbulence.
Earnings season	The period during which publicly traded companies release their quarterly financial results to the public.
Growth vs Value	Most stocks are classified as either value stocks or growth stocks. Generally speaking, a value stock trades for a cheaper price than its financial performance and fundamentals suggest it's worth. A growth stock is a company which comes at a higher price however, its profits are expected to grow significantly in the coming years as the company develops – this is typical for technology firms.
Index / indices	A benchmark that tracks the performance of a specific group of assets, such as stocks or bonds
Index linked bond	A type of government issued bond which has its interest payments and principal value tied to inflation.
Magnificent Seven	A group of high-performing technology companies considered industry leaders, including Apple, Amazon, Alphabet, Microsoft, Meta, Tesla, and Nvidia.
Put options	A form of downside protection. They provide an investor with the 'option' to benefit should an asset fall.
Quality	A quality stock is one from a financially sound company with stable earnings, consistent growth, and strong management.
Rally	A market rally is a sustained increase in stock prices driven by positive investor sentiment and economic conditions.
Sentiment	Market sentiment is the overarching attitude or outlook of investors towards a particular security, sector of the market or economy as a whole.
Soft vs hard landing	A soft landing refers to a gradual economic slowdown or adjustment, usually avoiding a recession, while a hard landing is a sudden and severe economic downturn often leading to a recession.
Strategic bond fund	Actively adjusts its portfolio of fixed-income securities, including government corporate bonds, to optimise returns in response to changing market conditions.
Market capitalisation / mega-caps	Market 'cap' is the market value of a company based on its current share price and total number of shares. Ultra-large cap companies have the largest market capitalisation. The largest companies by market cap are currently Apple, Microsoft, Alphabet (Google), Amazon, Nvidia and Meta (Facebook).
Yield	The income you receive on an investment, such as dividends from shares or interest from bonds.
Yield curve	A visual depiction of how the yields of bonds vary at different maturities. It shows how much you'd earn if you invested your money for a short time, e.g. 6 months, versus if you invested it for a longer time, e.g. 10 years.
Volatility	Volatility refers to the degree of fluctuation in a security's price or a market's performance over time. A highly volatile share experiences larger price changes compared to more stable investments, indicating higher risk.

Cover image Bauer brothers, Hortus Botanicus, detail from "Lilium," 1776/1804
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