News from the Investment Committee

Q1 2023

News from the Dynamic Planner nvestment Committee – End January 2023

The Investment Committee (IC) met on Monday 23 January and reflected on the downstream impact of the dramatic escalation in geopolitical risks, due to the Russian invasion of Ukraine, now almost 12 months ago, and the associated commodity price shocks.

The macro environment is radically different to the optimistic one prevailing at the start of last year. Global growth has slowed much more than anticipated, whilst the expected 'temporary' spike in inflation, rather than easing, further increased and has become embedded. As core measures of inflation remained far above central bank targets and headline rates reached double digits in most economies, this prompted global central banks to embark on the most rapid pace of policy tightening in 40 years.

The current macro perspective can perhaps be best described as a fiscal and monetary 'hangover'. The previous 10-year plus regime, where a 2% inflation target was made possible due to secular disinflationary forces, is not normal by historical standards. The supply chain problems that emerged in 2021, following the initial economic recovery from Covid, extended into 2022 as labour shortage issues and the ensuing commodity price shock embedded a higher level of inflation and lowered growth expectations.

Now the elephant in the room is high inflation, requiring rising global interest rates and a reduction in the bloated balance sheets of the central banks. This implies steeper yield curves, more quantitative tightening and ongoing high budget deficits. Alongside extended levels of bond market leverage (mainly due to widespread use within LDI strategies) and persistently high inflation, the risk of a liquidity driven global government debt crisis and ongoing bond volatility increases.

The impact of both the energy supply shock and the rapid tightening in monetary policy will slow global real growth, but also risks some economies flirting with moderate or intermittent recession in 2023. This is particularly pertinent to the UK economy, forecasted by the IMF to be the only G7 country to contract this year. It continues to grapple with supply chain issues following the Covid bounce back and has a higher dependence on expensive liquid natural gas, which has been driving up the cost of living even further. This is alongside rising taxes, labour shortages, widespread public sector worker unrest and the persistent lack of productivity growth in the economy.

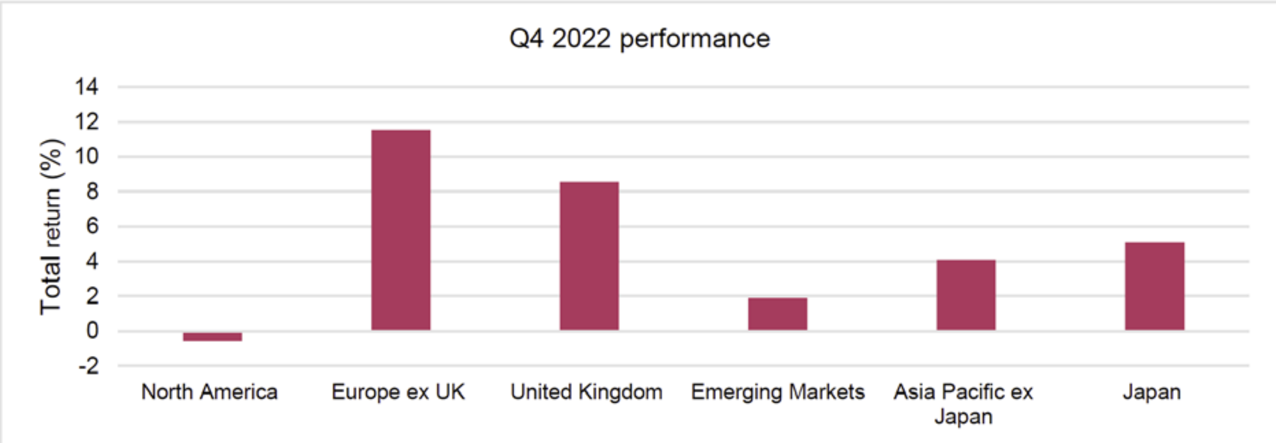
However, whilst there are significant short-term headwinds in the UK, markets always look forward and signs of inflation easing will help slow the pace and quantum of further rate rises. The IC discussed the latest proposed Capital Markets Assumptions (CMA's) to be applied in Dynamic Planner. The impact of the sharp rise in bond yields across the board over the previous quarter and the observed uptick in their volatility, has been reflected in the calibration process when setting the CMA's this quarter.

Given the considerable economic headwinds, the key unknowns are how close we are to reaching the peak in the interest rate cycle this year and the extent of potential corporate defaults, which are still running at low levels by historical standards. For equities, the focus is now on the extent of earnings downgrades and how much of the recession risk is already priced into current valuations.

Dynamic Planner's asset and risk model provides volatility, covariance, correlation and expected return assumptions, which are updated each quarter. They cover a wide range of bond maturities, equity market capitalisations and alternative assets, thereby equipping users with the flexibility to tilt portfolios relative to the risk-adjusted benchmarks as they see fit. Since the CMA's are updated each quarter, these remain sensitive to long-term secular trends and reflect the average expected outcomes for investors buying and selling at different times over the cycle.

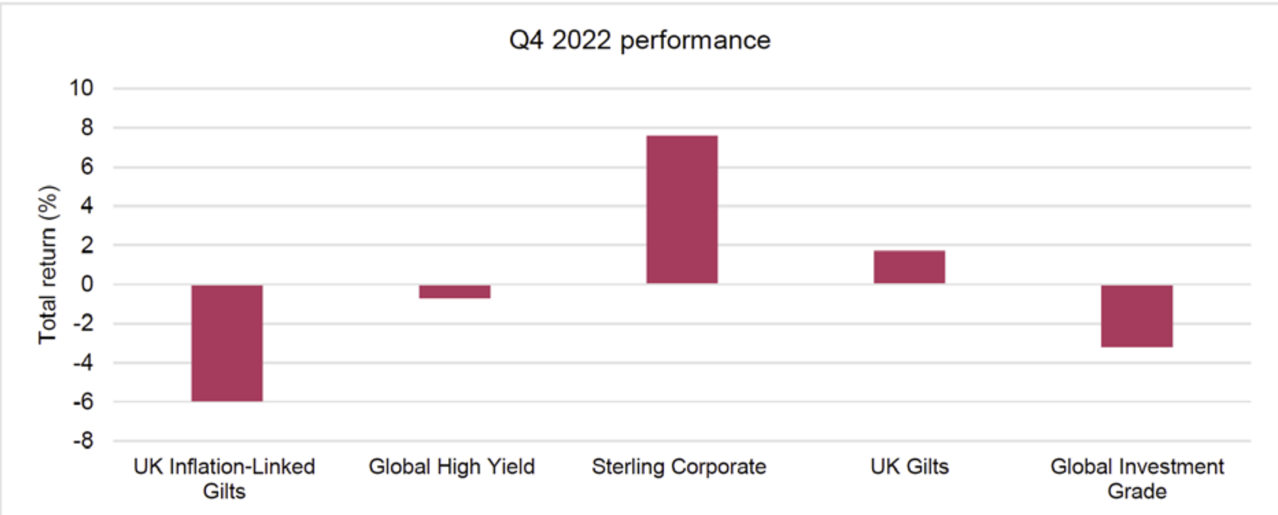
Previous quarter market overview

Equities



2022 was a truly tumultuous year, given the ongoing geopolitical risks and cost of living crisis, but in spite of the gloom and uncertainty, global stock markets mostly ended with gains in Q4 in Sterling terms. This was spurred by hopes that inflation may be peaking in the US and Europe as well as the long-anticipated relaxation of China's zero-Covid policy. Eurozone shares outperformed other regions, whilst in the US the Federal Reserve's final rate hike of the year slowed to a 50 basis points (bps) rise, after four consecutive 75 bps increases. In the UK, after the fall-out of the infamous mini-budget in September, an improving market sentiment saw economically sensitive areas of UK equities rebound well from their mid-autumn lows, as the battered gilt market recovered its poise alongside a reduction in the pace of interest rate hikes by the Bank of England..

Bonds



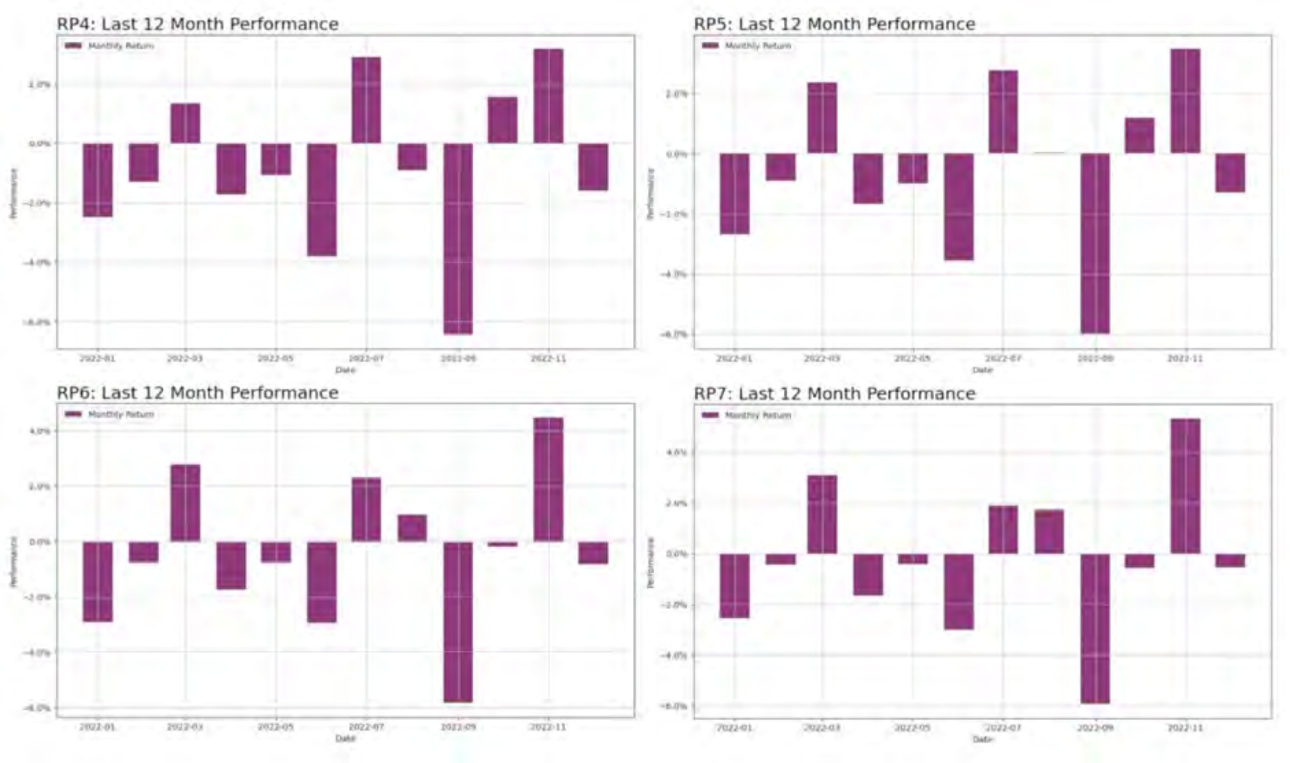
The UK gilt market suffered eye-watering losses as global bond investors lost confidence in the credibility of the government's fiscal framework, leading the Bank of England to intervene by temporarily buying long dated gilts.

Markets ended the year on a mixed note in the final quarter. Credit spreads between investment grade and government bonds tightened across the quarter on improved risk appetite. However, Government bond yields edged up towards the end of Q4, as both the Federal Reserve and the Bank of England raised rates twice, reaching 4.5% and 3.5% respectively. The European Central Bank (ECB) also raised interest rates by 50 basis points (bps) in December, a slower pace than its previous 75 bps hikes. Sovereign bond markets were however disappointed at the continuing hawkish tone from some central banks, despite mounting evidence of slowing economic growth and inflation rates peaking.

Review of the benchmark allocation performance

The key stand-outs were the September drawdowns across the lower risk benchmarks being of a similar scale to the medium risk series. This was attributed to the greater weighting in UK gilts and lower levels of diversification across global assets and currency exposures with the lower risk benchmarks.

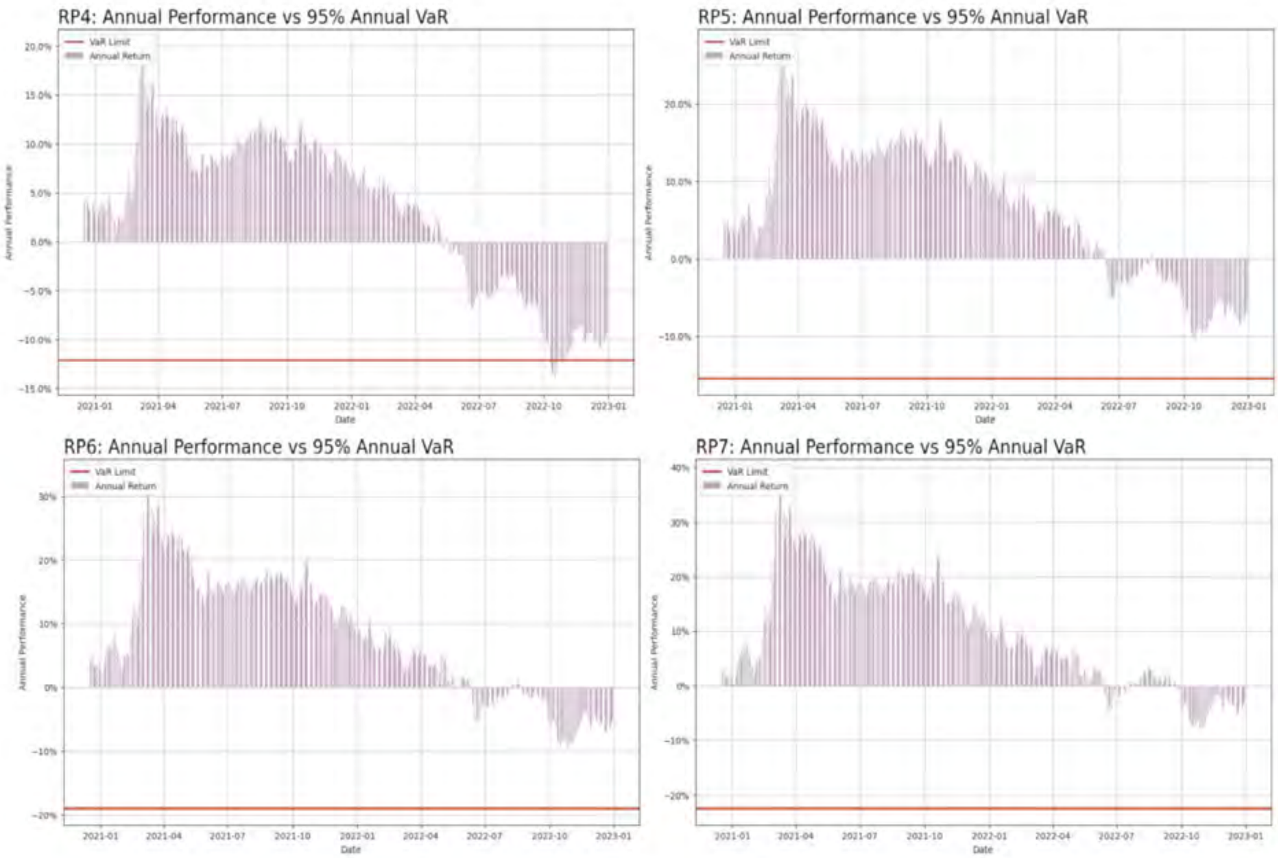
Monthly observed returns over last 12 months



DYNAMIC
PLANNER

Annual Value-at-Risk analysis

The charts below show the rolling annual returns calculated each day over the last two-year period versus their 95% VaR limit (the red horizontal lines). In September, Risk Profile 4 experienced falls in excess of its expected VaR limit, reflecting the extreme level of volatility endured by both Sterling and Sterling denominated debt.



Dynamic Planner Investment Committee
Jan 2023

Basis of Preparation and Use

You should not rely on this information in making an investment decision and it does not constitute a recommendation or advice in the selection of a specific investment or class of investments.

The information does not indicate a promise, forecast or illustration of future volatility or returns. The outputs represent a range of possible indications of volatility and returns for various collections of asset classes. Distribution Technology Limited ("DT") is not liable for the data in respect of direct or consequential loss attaching to the use of or reliance upon this information. DT does not warrant or claim that the information in this document or any associated form is compliant with obligations governing the provision of advice or the promotion of products as defined by the Financial Services Act.

www.dynamicplanner.com