Q3 2024 Overview – Countrywide Assured plc Balanced Managed Pension / Life Investing Fund

This report is provided by our Fund Manager Schroders and covers the portfolio activity on our main investing funds the Countrywide Balanced Managed Pension/Life Investing Funds, together with their short-term economic outlook. The report describes the current economic background and Schroders' perspective of this and how it impacts their management of the Countrywide Balanced Managed Pension/Life Investing Fund. It also covers all individual asset class sectors (UK & Global Equities; fixed interest; Property and cash).

Your policy will be invested in a specific customer fund of your choice which has its own fund objectives (see fund list and specific fund objectives) www.countrywideassured.co.uk/fund-centre/understanding-my-funds/fund-objectives/. All customer managed funds are invested in the Countrywide Balanced Managed Pension/Life Investing Funds, to a greater or lesser extent depending on the nature of the fund objective. If you're invested in an individual asset class sector fund, although no specific commentary is provided for these funds, the report does cover individual markets and other asset classes, which is consistent with the fund managers reasoning.

Portfolio Activity

While a wayward jobs report in the US led to some volatility mid-quarter, we retained our positive view on equities supported by the benign growth environment. This proved additive as September saw the Federal Reserve start its rate cutting cycle with a bang, and China announced an extensive monetary and fiscal stimulus package, pushing equities higher. As a result, the overweight position in equities was maintained, which was expressed through the US and UK markets. On the US side, earnings had improved for the S&P 500 and falling inflation had provided the Federal Reserve with greater flexibility. However, the overweight position was reduced slightly. On the UK side, the recent election has significantly enhanced market stability and sentiment, paving the way for a return to historical price levels.

In mid-July, we saw a severe rotation in markets and so we tactically diversified our view with an overweight US financials and overweight US financials versus US small caps position. The soft-landing scenario remained our base case, as we expected economic growth to remain stable and inflation to trend lower. Against this backdrop, companies delivering robust and resilient earnings were more likely to be rewarded, while unprofitable areas of the market were more likely to be penalised. This position proved beneficial and was subsequently closed towards the end of the quarter at a profit. Towards the end of the quarter, the portfolio's exposure to Chinese equities was increased following the announcement of stimulus measures which should provide a tactical boost to China in the short-term.

Fixed income assets contributed positively to performance, benefiting from growing excitement around impending interest rate cuts. The underweight position in global corporate bonds and the overweight position in US 10-year government bonds were closed mid-quarter. Following an aggressive repricing of interest rates, we introduced a short US 5-year government bond trade as we felt that expectations had moved too far, and yields may move higher in the short term. This position replaced the underweight position in global corporate bonds as a funding leg for our long equities position. We closed our allocation to US treasury inflation-protected securities in August as inflation has continued to move downwards.

In currencies, an overweight sterling versus euro (EUR) and Swiss franc (CHF) position was implemented at the start of the quarter. This aimed to capitalise on UK political stability and services inflation. Although the trade was volatile, it was closed in August. We also added overweight positions in the Australian dollar (AUD) and US dollar (USD) versus EUR. We expected the AUD to benefit from an underpriced hawkish stance by the Reserve Bank of Australia, and the USD to strengthen in a stable growth environment. We closed the USD vs EUR position mid-September. Towards the end of the quarter, an overweight Japanese yen versus CHF trade was added. This was

based on different local monetary policy trajectories, with Japan likely to reduce liquidity and Europe experiencing deflationary impulses.

Outlook

As it has been all year, our base case is a soft-landing for the global economy. Growth remains steady, if unremarkable, inflation continues to ease, giving central banks more room to manoeuvre and, with the starting gun fired in the US in September, the rate-cutting cycle is firmly underway. These dynamics create somewhat of a sweet spot for equities, leading us to be optimistic for markets into year-end. However, it is not an outlook without risks. While the Fed pleased markets with its bumper 50 basis points rate cut, the last mile is always the hardest when it comes to reducing inflation and there is the risk that rate cuts go too far, too soon leading to renewed upwards pressure. In the short term, the looming US election and hostilities in the Middle East could create further market volatility. Nonetheless, the immediately promising economic conditions support our positive outlook and positioning.

Our forecast for the global economy, consistent with our soft-landing central scenario, is broadly unchanged. From our perspective, concerns about an imminent US recession are overblown. Rising unemployment has not been driven by layoffs, but rather elevated inward net migration outpacing the normalisation in job creation. More broadly, labour market conditions have moved into better balance, which ought to see hiring and wage growth revert to a more typical pace. Taken alongside further disinflation and improving credit availability, this should serve to sustain solid household consumption and, by extension, economic activity more generally.

Elsewhere, the eurozone economy is being held back by a manufacturing malaise, leading us to scale back our growth forecast for next year. By contrast, we have become slightly more constructive on the outlook for the UK, such that we now expect it to outpace the eurozone both this year and next. However, disruptions to the supply side of the economy in recent years suggest that faster growth will ensure inflation pressures linger. China looks set to fall short of its 5% growth target this year with soft domestic demand and the housing crisis remaining a significant drag on confidence and investment. This has spurred policymakers into action, with a monetary stimulus package announced which may well boost asset prices in the short term. However, we think more comprehensive fiscal stimulus is required to boost the real economy and stymie deflation.

Against this backdrop, we are positive on equities and the US market in particular. Whilst valuations at the market level are not cheap, they are, in general, supported by earnings and, looking below the surface, better value does exist in sectors such as small caps, real estate and financials. Although noise around the US election may create episodes of market volatility, particularly if we see a contested result, the economic impact won’t be felt until later in 2025. But even with the forward-looking nature of markets, we don’t see this as an immediate threat to our positive view. A Harris victory would probably come with a divided Congress and therefore limited impact, while Trump’s reflationary policies could well boost the market short term.

The UK is also a preferred market; here, a more stable political environment and improved sentiment should allow prices to return to historical levels after a period of underperformance. Although emerging markets have been hampered by a slowdown in the manufacturing cycle, better prospects for Chinese stocks off the back of recently announced policy measures could boost the market.

In government bonds, we remain more cautious, particularly in the US where valuations look expensive, especially at the front end of the curve which is pricing in a recession we think is unlikely. Turning to currency, we have downgraded our view on the US dollar reflecting the fact that the Federal Reserve has started to cut rates, reducing the carry on offer.

All in all then, we see a window of opportunity over the coming months. The combination of benign economic conditions and increasingly supportive policy are supportive of risk assets. That said, valuations are more nuanced and inflation has not been completely quelled yet. Policy missteps such as overly aggressive rate cuts or excessive fiscal spending seeking political gain, could once more derail markets. An active approach is required to capture the opportunities and navigate the pitfalls.

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