Dynamic Portfolios
A solution from **Foster Denovo**

Quarterly Investment Review

Quarter 3 2022

Dynamic Portfolios
Sustainable
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Introduction – Q3 2022

The Dynamic Portfolios (DPs) and the Sustainable Dynamic Portfolios (SDPs) benefit from a responsive approach which means that they reflect up-to-date markets and continue to match a level of risk that you, the investor, are comfortable with.

To help manage and spread risk, we select assets from a wide variety of classes and funds to sit inside the DPs. This enables us to build diversified portfolios that spread investment risk. This includes adjusting the balance between active and passive investment strategies to align with where we believe we are in the market cycle.

This rebalancing is reviewed on a quarterly basis and is linked to your risk tolerance.

This quarterly investment review contains information from the most recent investment committee held on 20th October 2022 and governance oversight committee meeting on 21st October 2022, with the subsequent rebalances occurring on 28th October 2022.

There was no pause in the degree of geopolitical, economic and market uncertainty in the third quarter of 2022. The quarter started with a rally in major asset classes in July spurred on by hopes of a more moderate interest rate environment and avoiding recession via a controlled slowdown in economic activity, aka ‘a soft landing’. However, by September renewed worries caused further volatility and losses in all major asset classes for the quarter as a whole. In particular, the central banks of the US, UK and Eurozone reiterated that ‘higher for longer’ interest rates are here to stay.

Against the backdrop of higher interest rates across major economies, the duration (interest rate) risk of bonds and equities, were again a marked feature. This was particularly evident in bonds, a traditional ‘defensive’ asset class that exhibited volatility and falls in value more akin to equities. Global equity style growth to value rotation remained a distinct feature with the performance difference staying in the mid teen percentages for the year to date, although Q3 saw growth lose less than value, narrowing the gap. UK fixed income (bonds) was impacted by a radical and unanticipated change in government fiscal policy in late September, spooking markets and impacting sterling and UK government gilt yields which spiked up substantially. Core UK government gilts were down almost 13% for the quarter. Index linked (inflation protected) gilts were down over almost 10%.

September accounted for a large portion of the significant losses in Q3 for both the US and the UK stock markets. Large cap UK equities were partially cushioned from the worst of the volatility although still returned negative numbers. Small cap equities including those of the UK continued to be adversely affected with developed markets seeing drawdowns persist irrespective of the quality of the underlying holdings.

US equities rose from the end of June through August; however, they fell sharply in the final month of the quarter after the US Federal Reserve signalled further rate hikes would occur this year and possibly into 2023. This is the third successive quarter that the S&P 500 has fallen; the first-time investors have seen this since 2009 following the Global Financial Crisis.

Although European countries continue to be impacted by the over reliance on Russian energy, companies and economies are adapting and are gradually acclimatising to the new normal. However, the onset of Winter in the coming months may bring fresh challenges.

China continued to be hampered by the ongoing consequences of the housing bubble collapse, weak domestic demand, and their hard line ‘zero covid’ policy. Against a backdrop of the notably US $ strength, emerging markets suffered further falls. Commodities, although down slightly in the quarter were relatively one of the best performers in context with other asset classes.

This document summarises what was discussed at the Q3 2022 FD Dynamic Portfolios Investment Committee.

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A full quarterly review of the Plus, Lite and Core variants was carried out with the following outcomes.

FD Dynamic Portfolios Plus Risk Grades 4 to 8 and 10

NO CHANGE

The bespoke nature of two new Sequel Real Assets and World Sector Equity funds have been built to our asset diversification specification. It is our intention to 'reengineer' the DP Plus range using these 'asset building blocks' at the earliest possible opportunity; likely at the next quarterly meeting in Q1 2023. Given the near-term nature of the proposed changes together with the continued elevated level of market volatility, asset class uncertainty and very recent UK governmental policy risk, making changes for the very short term are clearly counterintuitive to the longer-term financial planning objectives of our clients.

The changes in the next quarterly review cycle will further consider use of uncorrelated/real assets and further diversification of active funds. A decision on all the existing underlying holdings exposure will also be part of this process.

FD Dynamic Portfolios Lite Risk Grades 4 to 8 and 10

NO CHANGE

Continue to monitor the degree of exposure to L&G Multi Index to enhance diversification and reduce exposure to one fund manager. Will likely seek to trim going forward to allow scope for more concentrated diversifying assets like real assets such as energy, raw materials, and real estate. We have paused any proposed changes again due to current market and asset class uncertainties.

"Active management doesn't mean doing something all the time; but rather means systematically reviewing whether something should be done or not."

FD Dynamic Portfolios Investment Team, March 2020

FD Dynamic Portfolios Core Risk Grades 3 to 7

NO CHANGE

Correct equity risk alignment was delivered in Q2 2022. However, duration risk has developed in the underlying bond allocation; most prominent in Risk Grade 3 via Vanguard LifeStrategy 40% Equity.

Duration risk means that interest rates and bond prices move in opposite directions. When interest rates rise, as they have recently, prices of traditional bonds fall, and vice versa. For example, a bond paying a 3% interest rate (or yield) will look less attractive when interest rates rise. Recent events, particularly in UK, have meant that the longer the timeframe of a bond, the more its price will drop as interest rates rise. Investors will need to wait longer to receive income payments (known as coupons), and the return of the original investment (known as the principal). Because of duration risk, future consideration will include replacing Vanguard's LifeStrategy fixed asset allocation with L&G Multi Index and the new Sequel Real Assets and World Sector Equity funds.

Highlights and changes

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A full quarterly review of the Active and Passive Sustainable Dynamic Portfolios (SDP) variants was carried out with the following outcomes.

FD Sustainable Dynamic Portfolios Active Risk Grades 4 to 8 and 10

NO CHANGE

Consideration given to reducing the duration exposure in the bond element, by reducing exposure to bonds with longer timeframes. However, this could result in a less positive impact as a direct result.

We will continue to monitor increasing diversifying assets for potential future inclusion.

FD Sustainable Dynamic Portfolios Passive Risk Grades 4 to 8 and 10

NO CHANGE

Limited opportunity set for new additions due to constraints of sustainable passive investing.

Will review including other asset types beyond equity and bonds (such as infrastructure) where possible in the future.

FD Sustainable Dynamic Portfolio Climate Impact Risk Grade 10

NO CHANGE

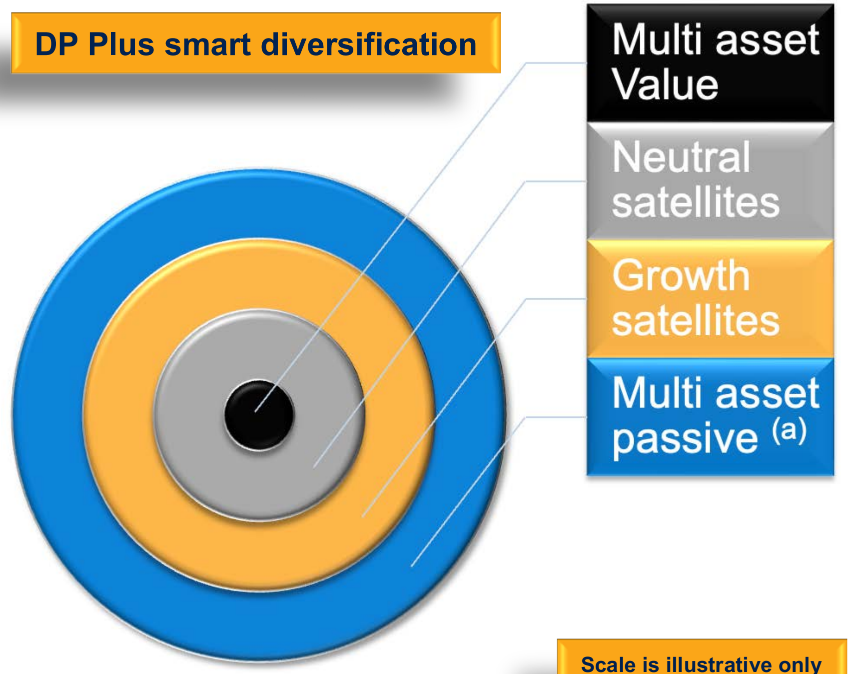
Smart diversification

To help manage and spread investment risk, assets are selected from a wide variety of classes and funds to sit inside the Dynamic Portfolios. Without knowledge of investment and asset classes, as well as sufficient resources, it may be difficult for you to create a diversified portfolio. To help with this, the Dynamic Portfolios benefit from 'smart diversification'.

What is smart diversification?

Diversification works best when assets are uncorrelated or negatively correlated with one another, in other words, as some parts of a portfolio fall, others potentially rise.

DP Plus smart diversification

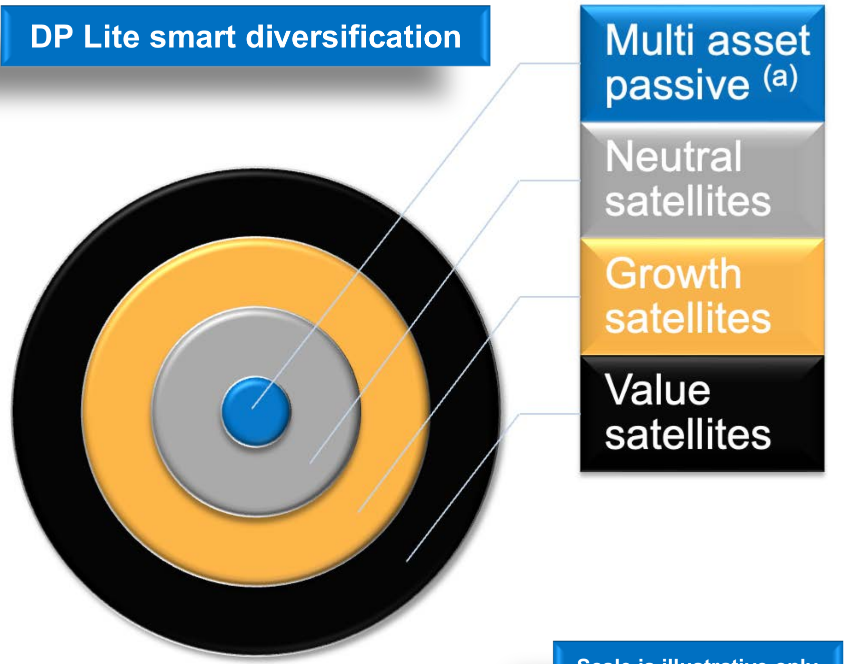


Scale is illustrative only

'Smart diversification', where possible, involves investing across different asset types (i.e., bonds as well as equities, etc.), different investment styles (i.e., active management and passive investing) and different investment philosophies (i.e., growth, value, and neutral bias).

It is also important to note that a fund's stated philosophy (i.e., value, growth etc.) will likely change over time due to valuation criteria; for example, a fund that was once a growth philosophy may now be neutral following sell offs in the growth philosophy.

DP Lite smart diversification



Scale is illustrative only

While individual stocks and markets will continue to go up and down, smart diversification across assets, styles and philosophies can help investors minimise their risks. Although it does not guarantee against loss, smart diversification is one of the most important component of reaching long-range financial goals while minimising risk.

[a] Although passive funds are used, the asset allocation benefits from being fully actively managed.

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Cash Plus benchmarks

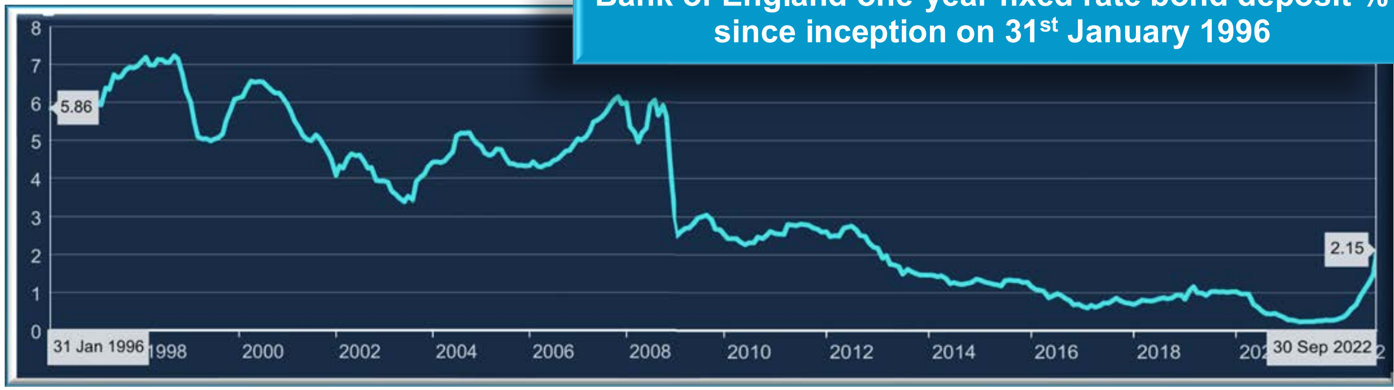
The idea behind a benchmarked investment at Foster Denovo is simple and attractive:
- it has a clearly defined target return; and
- it provides a gauge so that your financial adviser can check the progress of your Dynamic Portfolio.

Most of the Dynamic Portfolios have their own benchmark, known as Cash+ (*), providing a precise benchmarked investment goal – to beat the value of cash in a bank over the medium to long term. This allows you to check that your portfolio is performing as it should and allows you to see if your investments are on track and how your expectations align with your goals.

The Cash+ benchmark is designed to encourage each Dynamic Portfolio to produce returns that are above those you would expect from putting money into a long-term cash deposit. For example, let's say an investment into a Dynamic Portfolio was made, with a target of Cash+ 3.5%. And the calculated Bank of England benchmark interest rate (*) at the time was 1% per year. Then the overall target return would be 4.5% a year over the medium term

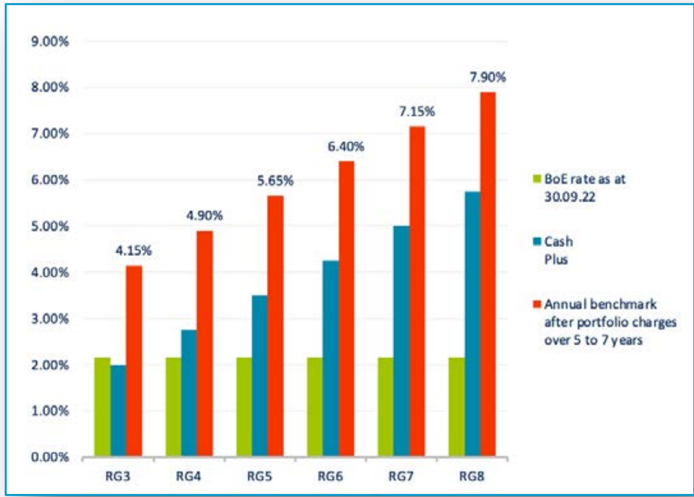
The Cash+ benchmark assigned to each Dynamic Portfolio reflects the amount of risk the investments are designed to take and can help you see which Dynamic Portfolio is right for you and offers transparency and clarity on return expectations.

Bank of England one-year fixed rate bond deposit % since inception on 31st January 1996



Source: Bank of England monthly interest rate of UK MFIs (excl Central Bank) sterling one-year fixed rate bond deposit - IUMWTFA

As can been seen in the above graph, the rate published on 30th September 2022 was 2.15%. This is up from 1.03% on 31st December 2021 and is the highest for nearly a decade. As the graph also shows the rate has been historically low since 2008 (the Global Financial Crisis caused by the 'credit crunch') and will likely increase materially in the coming months due to Bank of England interest rate policy to tackle inflation and recent government fiscal policy meaning the respective benchmarks used will increase.



Source: Bank of England

Risk Grade	BoE rate as at 30.09.22	Cash Plus	Annual benchmark after portfolio charges over 5 to 7 years
RG3	2.15%	2.00%	4.15%
RG4	2.15%	2.75%	4.90%
RG5	2.15%	3.50%	5.65%
RG6	2.15%	4.25%	6.40%
RG7	2.15%	5.00%	7.15%
RG8	2.15%	5.75%	7.90%

Source: Bank of England

*Cash+ (also known as Cash Plus) is an ongoing calculation based on statistics provided by the Bank of England. It's based on the Bank of England monthly interest rate of UK monetary financial institutions (excluding Central Bank) sterling fixed rate bond deposits from households (in percent) not seasonally adjusted. It is used to represent the return that could be expected from long-term (at least five years) cash deposits.

Key indicators

The 'Key Indicators' shown in the table to the right are designed to provide an overview analysis of different asset types, different geographical jurisdictions, and industrial sectors.

They also include statistics that show the changes in inflation, property – both residential and commercial – together with how UK base interest rate and 'high street' interest rates change.

The comparison period is over 1 year and compares the difference on a monthly basis over that 1-year period.

For example, this version compares the statistics for all key indicators between 31st August 2021 and 31st August 2022 against 30th September 2021 and 30th September 2022 (the end of Quarter 3 2022).

When available Gross Domestic Product (GDP) and unemployment figures for the UK and overseas geographical jurisdictions will be included.

The source of this data is FE Fundinfo.

Sector	31.08.21 to 31.08.22	30.09.21 to 30.09.22	Movement
Asia excluding Japan	-7.43	-13.94	-6.51
Emerging Markets	-7.51	-13.17	-5.66
Euro Stoxx	-13.85	-15.28	-1.43
Europe excluding UK	-11.72	-12.81	-1.09
France CAC	-4.71	-7.01	-2.30
German DAX	-19.83	-20.78	-0.95
Hong Kong Hang Seng	-6.83	-13.21	-6.38
Japan Equities	-4.15	-14.60	-10.45
Japan Nikkei 225	-6.26	-18.01	-11.75
Nasdaq 100	-6.13	-9.07	-2.94
UK	9.21	3.78	-5.43
UK 100 Leading Companies	6.22	0.90	-5.32
UK 250 Leading Companies	-18.92	-23.50	-4.58
UK Base Rate	0.63	0.78	0.15
UK Commercial Property	10.77	6.93	-3.84
UK Consumer Price Index	9.81	9.52	-0.29
UK Direct Property	9.89	5.95	-3.94
UK Gilts 10 to 15 years	-14.55	-20.57	-6.02
UK Growth Philosophy	-1.18	-6.87	-5.69
UK Moneyfacts 90 Notice (£10k)	0.52	0.58	0.06
UK Moneyfacts Instant Access (£10k)	0.28	0.58	0.30
UK Value Philosophy	15.60	10.49	-5.11
US S&P 500	5.00	2.10	-2.90
USA Equities	2.35	-0.47	-2.82
World Equities	0.45	-2.93	-3.38
World Commodities	58.14	44.51	-13.63
World Global Aggregate	-2.55	-3.89	-1.34
World Growth Philosophy	-8.79	-11.69	-2.90
World Precious Metals	-8.97	-7.40	1.57
World Property	3.81	-1.95	-5.76
World Small Cap	-4.24	-9.43	-5.19
World Value Philosophy	9.47	5.49	-3.98

Based on data from FE Fundinfo

What are the FD Dynamic Portfolios?

The FD Dynamic Portfolios (DPs) are investment portfolios that have been carefully designed to balance investment risk with returns to help investors achieve their financial goals, considering their attitude to risk, time frame and capacity for loss.

They are spread across distinct offerings, enabling the selection of the option that best matches an investor's goals. Each of these portfolios can be further tailored with risk levels ranging from a low-risk tolerance to a high-risk tolerance.

Our responsive approach means that the DPs reflect up-to-date markets and continue to match a level of risk within the given targeted range. This includes adjusting the balance between active and passive investment strategies to align with where we believe we are in the market cycle. This rebalancing is reviewed on a quarterly basis and is linked to an investor's risk tolerance.

To help manage and spread risk, we select assets from a wide variety of classes and funds to sit inside the DPs. This enables us to build diversified portfolios that spread investment risk. All the funds that sit inside the DPs are selected following a comprehensive quantitative and qualitative screening process that brings together both hard and soft facts.

Each of the DPs undergoes rigorous quarterly reviews that involve both internal and external investment experts. The review process is a core part of our dynamic offering, giving investors' confidence that their portfolio is frequently reviewed with their risk tolerance and wider market and economic factors in mind.

Contact us

If you'd like further information about the Dynamic Portfolios or the Sustainable Dynamic Portfolios, please contact your Foster Denovo Partner. Or, if you are new to Foster Denovo:

call: **0330 332 7866**,

email: **info@FDdynamicportfolios.com**; or

visit **fosterdenovo.com/investment-solutions/sustainable-investing/**

Calls are charged at your standard landline rate.

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If a client wishes to obtain financial advice as to whether an investment is suitable for their needs, they should consult their Foster Denovo Partner. Clients should make sure they have understood the contents of their Foster Denovo Partner’s suitability report before proceeding with any proposed investment.

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