Cazenove Capital

Model Portfolio Service
Active/Passive Models

Q1 2021 Review

For financial advisers and their clients

Part of the Schroders Group

Cazenove Capital Model Portfolio Service, Q1 2021

Active/Passive Portfolio review

This review covers the Cazenove Capital Model Portfolio Service including asset allocation, performance and latest views from the investment team on markets and strategy.

If you have any questions about this report or your investment generally, please contact your local business development manager.

Contents

Availability

Awards

Risk mapping

Performance monitoring

What has happened in markets?

"Stock markets have continued to move higher, fuelled by an anticipated recovery in earnings and ongoing stimulus measures. While concern about inflation and rising interest rates could be a source of turbulence, the growth and earnings outlook continues to look favourable."

Caspar Rock
Chief Investment Officer
Cazenove Capital

When I wrote my review and outlook last spring, markets were in freefall and governments were imposing restrictions on their citizens that were unprecedented in peacetime. We are in a very different place today. While the UK is still subject to restrictions, and Covid-19 will not disappear, we can be reasonably optimistic that the virus will move from a public health crisis into a manageable threat.

Few would have expected it, but the tumult of the past year has created something of a sweet spot for equity investors. Companies which were anticipating a gradual shift towards digitalisation suddenly saw their growth turbo-charged. Lockdowns left many consumers with a significant increase in savings, providing fuel for a strong rebound in economic growth and corporate profits. Meanwhile, policy makers have provided huge levels of support – and continue to do so. With unemployment still at elevated levels in major economies, there is little prospect this will change in the near term.

The political backdrop is also less fraught than it has been for some time, which should give businesses and consumers more confidence in the post-pandemic recovery. In the UK, a Brexit trade deal was agreed at the very end of last year, removing the not insignificant risk of disruption in the flow of goods. In the US, Joe Biden took office smoothly and has now secured package for a near $2 trillion stimulus package.

Schroders' economists expect this extra fiscal spending to significantly boost global growth. It will have an impact this year, though some of the benefit will be offset by sluggish growth in Europe as a result of the slow vaccine roll-out. The bigger impact will come next year, which should be another year of growth much stronger than the tepid average of the last decade.

Some signs of excess in markets...

This economic recovery should continue to provide a tailwind for equity markets. While valuations are far from cheap, markets as a whole are not prohibitively expensive.

Having said this, there have been some clear signs of speculative excess. The combination of easy money and exciting new technologies are the classic ingredients of financial market bubbles. It may well turn out that some of the stratospheric valuations in today's market – with Tesla and Bitcoin the prime examples - prove to be wildly over-optimistic. Time will tell.

The wild moves we saw earlier this year in a handful of US stocks, notably video game retailer GameStop, were another kind of excess. This strange episode was not accompanied by any of the usual narratives that drive financial market manias, but it also depended on liquidity and technology. It was initiated by an army of retail investors flush with stimulus checks and easy access to option markets. The volatility caused meaningful losses for some prominent hedge funds, but otherwise seems to have had little consequence.

...but too early to worry about overheating in real economy

In the US, long-term inflation expectations are now back above 2% – the Federal Reserve's target – for the first since late 2018. This has taken a toll on government bond markets, which tend to be negatively correlated to inflation. Yields have risen significantly from their lows of the last year. In the US, the benchmark 10-year Treasury now yields 1.5%, compared to a low close to 0.5% last summer. The speed of the move has been uncomfortably fast. It has been exacerbated by concern that higher inflation may encourage central bankers to step back from their bond-buying programmes sooner than currently anticipated.

We do not think inflation is a worry yet. Higher commodity prices will certainly feed through into higher headline readings. But they will not impact the more important core measures of inflation, which strip out food and energy prices and are the focus of policy markers. A US unemployment rate of just over 6% suggests the economy has enough spare capacity to keep inflationary pressures at bay.

Inflation uncertainty: a longer-term worry

Even so, the unusual circumstances of the past twelve months mean the inflation outlook is particularly uncertain. There are likely to be some industries – such as air travel – where a rush of pent-up demand meets reduced capacity, resulting in price hikes. This may be a relatively short-lived phenomenon. The bigger worry is the huge increase in money supply we have seen over the past year. Incredibly, almost 20% of all US dollars currently in existence were created in 2020, thanks to the Federal Reserve' various support measures.

Of course, inflation hawks – as those who worry about inflation are known – have cried wolf before. It was widely feared that quantitative easing programmes after the financial crisis of 2008 would lead to runaway inflation. It didn't. There are good reasons to think this time may be different. The scale is much greater this time round and the banking system is not under the same pressure to shrink its balance sheet as it was a decade ago. This could mean more newly-created money makes its way into the real economy.

A period of somewhat higher Inflation would not in itself be a bad thing. It would help the world's major economies grow out of the debt burden they have taken on to deal with the pandemic. However, it could rattle markets along the way. If higher inflation brings higher interest rates too quickly, financing costs could become problematic for companies and governments. It could also undermine the rich valuation of equity markets, which depends on interest rates remaining low.

Note: Forecast is not a reliable indicator of future performance.

How are the portfolios positioned?

"Equity markets extended their rally whilst more defensive assets fell"

Steven Rooke
Portfolio Director,
Manager of Cazenove Capital
Model Portfolio Service

Global equity markets pushed higher, led by cyclical sectors

Energy and Financials rallied hard

Bond markets had a bruising quarter as fears grew over inflation

The first quarter can be broadly characterised as a risk on period, with global equity markets extending their rally from the March 2020 lows, whilst more defensive assets such as government bonds and gold fell. Within equities, the rotation away from defensive and 'growth' sectors towards more economically sensitive areas continued, driven by growing momentum in the vaccine rollout programmes, an improving earnings outlook and more attractive relative valuations. Energy and financials were the top performing sectors, returning 16.8% and 10.7% as a continuing recovery in the oil price and steepening yield curves benefitted these sectors.

As was the cas last quarter, smaller companies significantly outperformed their large cap peers in all major equity markets. This was once again of benefit for active managers who tend to be overweight this area versus their benchmarks. Stock dispersion also increased, with a wide range of stock returns providing an environment for active managers to add alpha. Having had a torrid 2020, the UK stock market followed up a strong Q4 with another good quarter of returns with the Vanguard UK FTSE All Share Index Fund our best performer in models. Our US equity exposure via the Vanguard US Equity Index did particularly well as did the HSBC Pacific Index Fund.

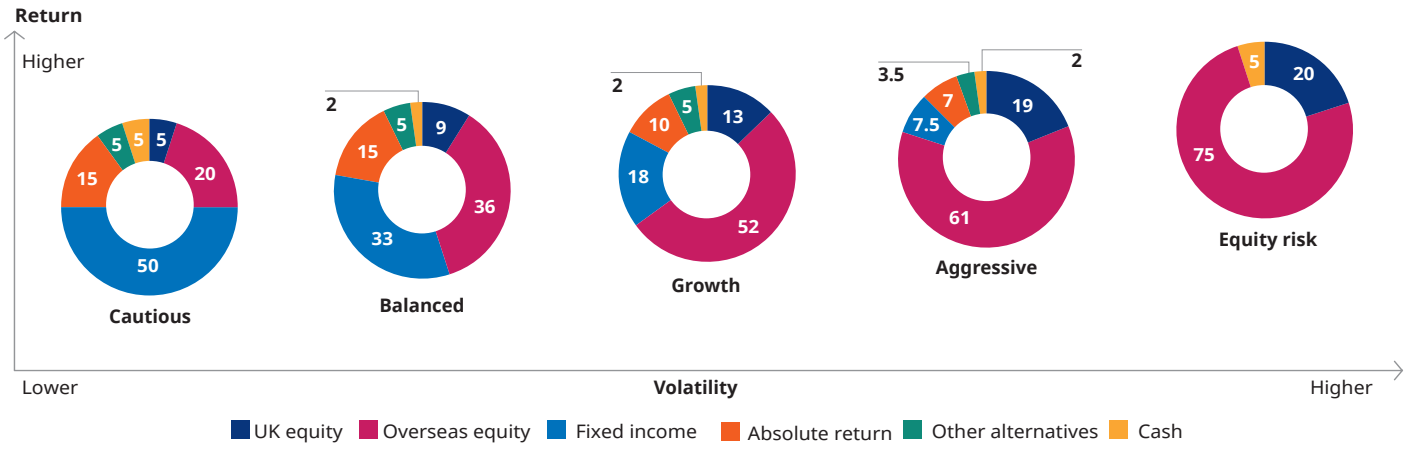
As Caspar noted in his economic update the moves seen in bond markets were dramatic. This had a big impact on our government bond positions (Vanguard UK Government Bond and Vanguard UK Inflation Linked Gilt Funds) with this the key reason for weaker performance seen in the lower risk models. Our short duration bond funds (Vontobel TwentyFour Absolute Return Credit and PIMCO Global Libor Plus) both held up well, delivering positive returns. Within alternatives the Atlantic House Defined Returns Fund had another good quarter, aided by the moves seen in the FTSE100, whilst the Janus Henderson UK Absolute Return Fund nudged higher.

Overall, we remain positive on the growth outlook for the rest of the year. In this environment, we might expect bond yields (both nominal and real) to move higher driven by expectations of a sustained economic recovery. Whilst this is a good reason for yields to continue to rise, it is likely to be a headwind to the performance of defensive assets such as government bonds and gold. Despite this we remain mindful of the potential for periods of elevated volatility and we feel it is appropriate to maintain our exposure to defensive assets which have historically offered diversification benefits and provided a degree of protection during equity market corrections.

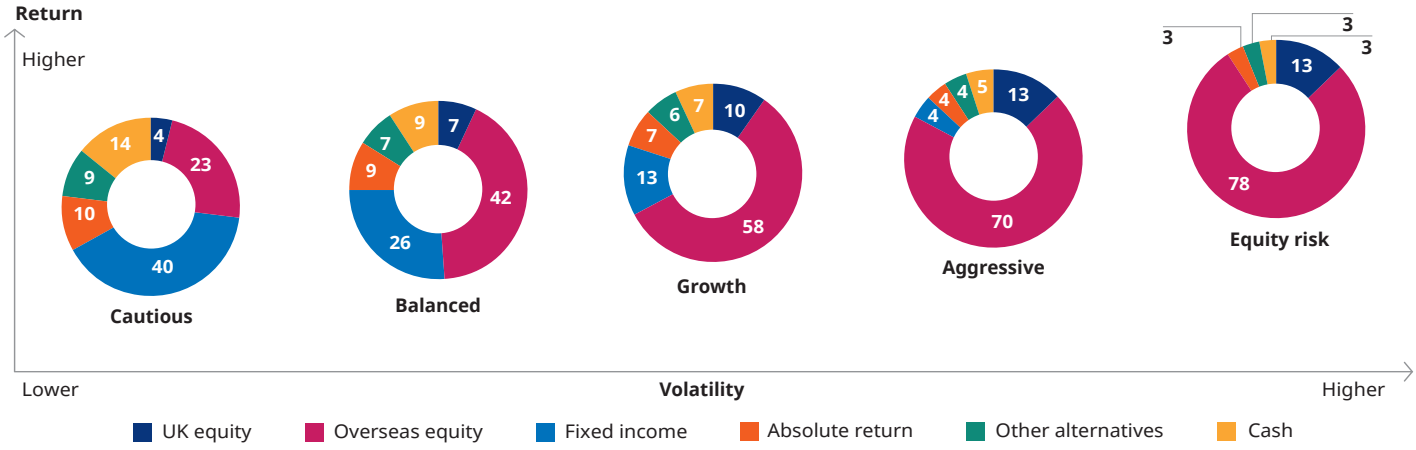
How are the portfolios invested?

The models adopt the Cazenove Capital multi-asset approach investing in a wide range of asset classes aiming to deliver strong risk-adjusted returns. The active/passive models invest in open-ended funds. The charts below illustrates the long-term (strategic) and current (tactical) asset allocation of the Active/Passive core models.

Long-term strategic asset allocation



Tactical asset allocations



Source: Cazenove Capital, as at 31 March 2021. Asset allocation is subject to change without notice.

How are the portfolios performing?

Active/Passive Portfolios	3 Months	1 Year	2 Years	3 Years	5 Years	Cumulative return since launch
Cautious	-0.1%	12.4%	7.7%	11.7%	-	**12.7%**
Balanced	1.2%	19.2%	12.9%	18.8%	-	**20.2%**
Growth	2.3%	25.1%	16.8%	24.3%	-	**25.8%**
Aggressive	3.2%	30.5%	19.3%	27.9%	-	**29.2%**
Equity risk	3.8%	34.6%	22.2%	31.8%	-	**33.5%**

Active/Passive Portfolios	Q1 2020 – Q1 2021	Q1 2019 – Q1 2020	Q1 2018 – Q1 2019
Cautious	12.4%	-4.2%	3.7%
Balanced	19.2%	-5.3%	5.2%
Growth	25.1%	-6.7%	6.4%
Aggressive	30.5%	-8.5%	7.2%
Equity Risk	34.6%	-9.1%	7.8%

Past performance is not a guide to future performance and may not be repeated. The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.

Source: Cazenove Capital, as at 31 March 2021. Performance is shown on a total return basis, net of underlying fund charges but gross of Cazenove Capital fees and any fees applied by the platform and professional adviser, deduction of these will have an impact on overall performance. Inception date 30 June 2017. Performance is calculated by Cazenove Capital and provided for illustrative purposes only and should not be viewed as the performance of a specific client portfolio.

The underlying portfolios in more detail

All holdings

Asset class	Security	MPS Cautious	MPS Balanced	MPS Growth	MPS Aggressive	MPS Equity Risk
Equities						
UK	Vanguard FTSE All Share Index	4.0%	7.2%	10.4%	12.6%	13.1%
	Total	**4.0%**	**7.2%**	**10.4%**	**12.6%**	**13.1%**
Europe ex UK	Vanguard FTSE Developed Europe ex UK Index	2.3%	3.3%	4.1%	4.9%	5.5%
	Total	**2.3%**	**3.3%**	**4.1%**	**4.9%**	**5.5%**
US	Vanguard US Equity Index	8.2%	15.1%	21.4%	26.3%	28.5%
	Total	**8.2%**	**15.1%**	**21.4%**	**26.3%**	**28.5%**
Japan	Vanguard Japan Stock Index	1.2%	1.5%	2.1%	3.0%	3.1%
	Total	**1.2%**	**1.5%**	**2.1%**	**3.0%**	**3.1%**
Asia ex Japan	HSBC Pacific Index	1.6%	4.0%	5.0%	5.9%	6.5%
	Total	**1.6%**	**4.0%**	**5.0%**	**5.9%**	**6.5%**
Emerging Markets	Vanguard Emerging Markets Stock Index	0.8%	3.9%	6.3%	8.6%	9.6%
	Total	**0.8%**	**3.9%**	**6.3%**	**8.6%**	**9.6%**
Global	L&G Global Healthcare & Pharmaceuticals Index	1.0%	3.4%	4.3%	6.9%	6.8%
	L&G Global Technology Index	0.0%	2.6%	3.2%	3.6%	3.6%
	L&G Global Equity Index	6.7%	7.4%	9.9%	9.5%	13.5%
	L&G Global Infrastructure Index	1.0%	0.9%	1.3%	1.3%	1.3%
	Total	**8.7%**	**14.2%**	**18.7%**	**21.4%**	**25.1%**
	Equities total	**26.8%**	**49.1%**	**68.0%**	**82.7%**	**91.4%**
Bonds						
UK	Vanguard UK Short-Term Inv Grade Bond Index	5.9%	2.5%	1.9%	0.0%	0.0%
	Vanguard UK Inflation-Linked Gilt Index	8.2%	5.2%	3.7%	0.9%	0.0%
	Schroder Sterling Corporate Bond Fund	6.9%	4.4%	0.0%	0.0%	0.0%
	Vanguard UK Government Bond Index	7.5%	5.6%	3.5%	2.3%	0.0%
	Vontobel 24 Absolute Return Fund	5.5%	3.8%	1.9%	0.9%	0.0%
	Total	**33.9%**	**21.5%**	**11.1%**	**4.1%**	**0.0%**
Global	PIMCO Global LIBOR Plus	3.8%	2.3%	0.0%	0.0%	0.0%
	Total	**3.8%**	**2.3%**	**0.0%**	**0.0%**	**0.0%**
Emerging markets	Schroder Emerging Market Absolute Return	2.7%	1.8%	1.8%	0.0%	0.0%
	Total	**2.7%**	**1.8%**	**1.8%**	**0.0%**	**0.0%**
	Bonds total	**40.4%**	**25.6%**	**12.8%**	**4.1%**	**0.0%**

Asset class	Security	MPS Cautious	MPS Balanced	MPS Growth	MPS Aggressive	MPS Equity Risk
Alternatives						
Hedge Funds	Janus Henderson UK Absolute Return	4.5%	3.6%	3.1%	2.4%	1.3%
	Total	**4.5%**	**3.6%**	**3.1%**	**2.4%**	**1.3%**
Other	Liontrust Diversified Real Assets	4.5%	3.6%	2.5%	1.3%	0.8%
	Total	**4.5%**	**3.6%**	**2.5%**	**1.3%**	**0.8%**
Multi asset	Trojan Fund	5.9%	5.0%	3.7%	2.0%	1.3%
	Total	**5.9%**	**5.0%**	**3.7%**	**2.0%**	**1.3%**
Structured Products	Atlantic House Defined Returns	4.1%	3.6%	3.1%	2.5%	2.0%
	Total	**4.1%**	**3.6%**	**3.1%**	**2.5%**	**2.0%**
	Alternatives total	**18.9%**	**15.9%**	**12.5%**	**8.2%**	**5.4%**
Cash – GBP		13.8%	9.4%	6.7%	5.0%	3.2%
	Cash total	**13.8%**	**9.4%**	**6.7%**	**5.0%**	**3.2%**
	Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Source: Cazenove Capital, as at 31 March 2021.

What are the costs?

Active/Passive	Active/Passive Cautious	Active/Passive Balanced	Active/Passive Growth	Active/Passive Aggressive	Active/Passive Equity Risk
Cazenove Capital (0.3%)	0.30%	0.30%	0.30%	0.30%	0.30%
Ongoing charges[1]	0.35%	0.31%	0.25%	0.20%	0.18%
Total	**0.65%**	**0.61%**	**0.55%**	**0.50%**	**0.48%**

Source: Cazenove Capital, as at 31 March 2021.
[1]Ongoing charge includes AMC, cost of investments but excludes any advice or platform charges. Fees and charges are indicative and may differ by platform.

Important information

Risk warnings

There is no guarantee that the objectives will be met. Past performance is not a guide to future performance. The value of investments and the income from them can go down as well as up and an investor may not get back the amount originally invested and investments may be affected by fluctuations in exchange rates. The levels and basis of tax assumptions may change. You should obtain professional advice on taxation where appropriate before proceeding with any investment.

Prior to making an investment decision, please consider the following risks:

Interest rate risk: For models investing in fixed income, changes in interest rates are likely to affect the fund's value. In general, as interest rates rise, the price of a fixed bond will fall and vice versa.

Credit risk: The value of the model may fall if the companies and governments who have issued the bonds deteriorate in quality, or in the worst case scenario become insolvent.

Liquidity risk: It may be difficult to sell some investments (or sell them without making a loss) due to an insufficient number of buyers in the market.

Currency risk: The model can hold some investments that are not denominated in UK Pound Sterling (£). These may be affected by changes in currency exchange rates.

Emerging market risk: The model invests in markets where economic, political and regulatory factors can be significant. This may affect the liquidity, settlement and asset values. Any such event can have a negative effect on the value of your investment. Investments in emerging markets can demonstrate significant declines in value over extended periods of time.

Counterparty risk: There is a risk that a counterparty may default or not comply with its contractual obligations resulting in financial loss.

Cazenove Capital
1 London Wall Place, London EC2Y 5AU
T +44 (0)20 7658 1000