Your investment update

Q3 2024

Succession Model Portfolios
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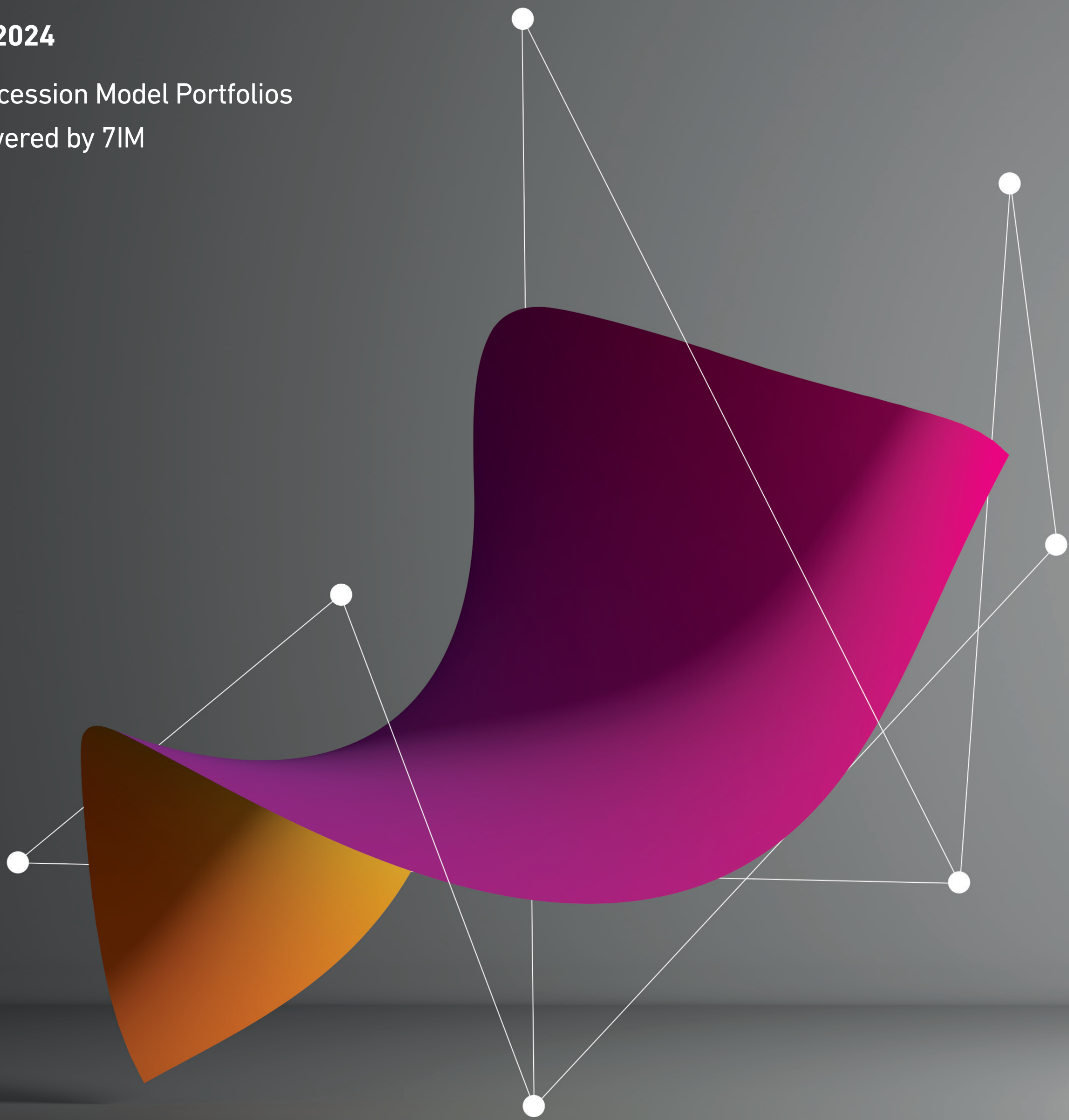

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Welcome

Sporting lessons

What a summer of fantastic sport we have! The football Euros, Wimbledon upon us, the Summer Olympics and Paralympics in Paris, the British Open at Royal Troon and the cricketers host the West Indies. Don't worry, you haven't stumbled across another advert for Sky Sports – but this avalanche of sport prompted me to think about the parallels between the world of elite sport and investment.

There are many moments of enormous stress in sport. When the golfer stands over a crucial putt, the athlete awaits the starting gun, the tennis player faces "break point", the opening batsman sets up to face the first ball, or the footballer steps up to take the decisive penalty. The key for them is to shut out the noise and trust the process that has enabled them to reach that point. Their training, their preparation and the mental resilience built up through the peaks and troughs of years of competition.

"Trust the process" is something that's heard a lot in sport. It's the process which really equips you in the heat of battle rather than relying on individual moments of brilliance. The same is true in investment. Success over the long term is built on the construction of a proper process. One that can withstand the challenges that financial markets set us. One that holds up well in moments of high stress. A long-term plan that works and fine-tuned to respond to shifts in market conditions.

Sticking to the plan, the process, is what takes investors to their long-term destination, not zigzagging emotionally to short-term news flow."

Ignoring the noise is crucial. Emotions seldom help in elite sport and never help in investment. There's so much noise at present – a changing government in the UK, Trump in the US, geopolitical horrors and tech stocks that seem to defy gravity. Some of the noise screams at us to retreat to the sidelines while, on the other hand, a fear of missing out tells us to take the plunge, buy technology and forget the lessons of history. Both are almost certainly bad pieces of advice. Sticking to the plan, the process, is what takes investors to their long-term destination, not zigzagging emotionally to short-term news flow.

Teamwork, too, is a crucial element of sport and investment. Of course, that's true for team-based sports but there's not a single elite sportsperson who hasn't reached the heights without armies of specialist coaches and support staff. The same is true in investment as every portfolio is a product of the work of the strategists, the investment selectors, the risk team and of course the process!

Looking ahead, it's our view that 2024 will very much prove to be "a game of two halves". The next six months should bring some long-awaited cuts to interest rates and yields, a broadening out of stock market performance away from the tech titans and a more balanced feel to global growth. That's how our portfolios are positioned – balanced across a range of assets, as Ahmer points out in his piece. Ben looks at the UK economy, before it all comes home with Wenqian's take on the environmental impact of sports tournaments.

If sport is your thing, have a great summer watching it. If not, I wish you the best of luck in avoiding it. Enjoy reading!

MARTYN SURGUY
Chief Investment Officer

Strategy

Talking tactics

Modern sports is *full* of numbers.

A couple of decades ago, the team of a marathon runner or cricketer or tennis player were likely to be a coach, an agent, and perhaps a physio. Most of those would be ex-athletes themselves. Now, almost all serious athletes – whether individuals or teams – have a data analyst on call.

After all, more than most things, succeeding at sport is about doing the exactly same thing, time and time again, better than anyone else. And data is *crucial*. The “marginal gains” from Sir David Brailsford’s British cyclist team is a great example of this. The ‘Moneyball’ success in US baseball is another. And even modern football analysis is in terms of ‘xGs’ and ‘progressive carries’.

Of course, it’s not just your own performance that’s worth collecting data on – it’s also your possible opponents’. Do they prefer to lead, or come from behind? Are they easily riled by a crowd? Do they tend to serve down the middle on big points?

Because although the usual advice is to “*play your own game*”, it’s important to know what you’re facing...

The investment “opponent”

Of course, investing has always attracted data nerds. For investors, even if we don’t *change* the way we invest, it’s important to have an idea of what might happen next. What kind of environment might we be heading into – as that can affect how our portfolios might perform. What’s the gameplan?

This is *always* challenging, but the last few years have proved particularly difficult. The Covid pandemic, the emergency stimulus, the inflation that followed, and the resulting interesting rate hikes all happened more quickly than any previous data analysis prepared us for. But now, four years on, the aftershocks may finally be fading.

Supply and demand imbalances have *mostly* been resolved, while the last gasps of stimulus cash are being spent. Spending has also moderated with retail sales in the US flatlining this year, with recent poor earnings results from consumer goods companies such as Nike, Levi’s and H&M, suggesting there’s less disposable income available.

Taking it all together, we can suggest that the next 12 months are very unlikely to see *higher* interest rates, but nor will they see rates fall sharply. The global economy is likely to grow sluggishly, without the same post-Covid confidence boom."

At the margins, the last few years of interest rate hikes are starting to weaken parts of the global economy – as they are designed to. The housing sector isn't firing on all cylinders and employment isn't growing as strongly as it was.

As a result, inflation across the world is settling down to a more tolerable level. That's essential for businesses looking to plan their future investment. For the past few years, they've not managed to get an accurate picture of the "true" level of demand for their product. Was it artificially supressed in Covid? Was it artificially boosted by stimulus? Those ripples are fading, and surveys of business and consumers point towards an expectation that the future will be calmer.

In terms of knowing the opponent, it looks like the next 12 months will be a tougher environment for companies to make strong profits. Ordinarily, that would mean an environment of lower interest rates, to try and pep things up.

However, with the wild card of inflation still very much in the public consciousness, central banks won't go wild with rate cuts. Reduce interest rates too early, spark growth too quickly and maybe inflation surges again. The lesson of history is that high inflation is a catastrophe – and it's better to be cautious rather than blasé (not that many central bankers are blasé people...).

Taking it all together, we can suggest that the next 12 months are very unlikely to see *higher* interest rates, but nor will they see rates fall sharply. The global economy is likely to grow sluggishly, without the same post-Covid confidence boom. And that's an outcome a central banker would be very happy with. Arguably, it's their gameplan... >>

AHMER TIRMIZI
Head of Fixed Income Strategy

Strategy
Continued

Investment tactics

There's only so much you can know about your opponents. They can always surprise you with a new player, an innovative tactic or a different style of play. When it comes to investing, uncertainties around the outlook remain. How far will central banks go? Will inflation return? And which way is economic growth heading?

Just like in sports, we never know the answer to these questions beforehand. And so, our gameplan will need to acknowledge that. At 7IM, our gameplan is to hold a diversified portfolio with some offbeat positioning that should help over the next 12 months:

Overweight bonds

Bonds are supposed to be the safe assets while equities are the 'higher risk' ones. However, in the last few years, this has flipped on its head. While equities have been up materially, we've seen government bonds – the safest assets of them all – fall by double digits.

Surging inflation and interest rates are the main culprits – bond prices and rates go in opposite directions. This is offering investors a historic opportunity to invest in *real yields* – income that is higher than inflation – at levels we haven't seen in over two decades (see chart). That's a free shot on goal, in our view.

Alternatives

Holding bonds will be key to delivering outperformance over the coming years. If the economy weakens, central banks are likely to dust off their old playbook of cutting interest rates. And those rates fall, bond prices will rise – hence our overweight above.

However, we shouldn't forget the experience of the last few years. Surprises can happen. And so, we look to 'diversify our diversifiers'. If the game changes, and bonds don't play the role they have done in the past, we own a portfolio of alternative strategies ready to deliver diversifying returns, much like they did in 2022-23.

Healthcare

The global healthcare sector remains one of our favourite long-term investments. Earnings stability helps to weather economic downturns, valuations are attractive and it's coming off one of the worst periods of performance in decades. As always in sports, form is temporary, but class is permanent. And at the same time, if there's one area where AI really can make a *difference*, it's likely to be here.

Metals and mining

Metals and mining stocks are as solid as it gets – net debt is close to zero, profit margins remain elevated and dividend yields are higher than the markets. Add on to that, these companies will be at the centre of the climate transition. The long-term tailwind is clear. And we're paid handsomely to wait.

Japanese Yen

As US interest rates have risen, Japanese interest rates have stayed low – and so Japanese investors have naturally moved some of their money out of Japan, weakening the currency in the process.

But this won't last forever. If a currency gets too cheap, exports will soar, which eventually pushes the currency back up. Timing is tricky, but this is why holding on to cheap currencies pays off in the long run.

At the time of writing, the Japanese Yen is the cheapest it has *ever* been – ~40% below fair value estimates. At the same time, US inflation is easing, which should lead to falling rates. This will lead to some Japanese investors to repatriate their money, boosting the currency.

And of course, in a world in which the US economy starts to struggle, the Yen would benefit even further as its safe haven status becomes in demand – so the position can play a little bit of a defensive role too.

This is offering investors a historic opportunity to invest in real yields… a free shot on goal."

US 10-year real yields (Bond yield minus inflation)

Source: Macrobond/7IM

Special feature

United Kingdom vs. Low Growth: a match we can win!

You've heard us say it a million times.
Do not worry about UK politics.

And that's absolutely true... as an investor. Over the long term, with a portfolio which invests around the world, it doesn't matter who's behind the door at No. 10 Downing Street.

But look, as a *citizen* of the UK, there's a lot to be interested in.

So I thought I'd give a quick take on the challenge/opportunity facing the new government. After all, we do live and vote here – even if our investments don't!

And hey, who am I to abandon the sports theme... ?

Coaching a country

Get the fans cheering!

That's your *only* goal as a new coach of a sports team. Naturally, you'll set about doing things *your* way. Changing training patterns to work on certain areas, buying in new equipment and expertise, and shifting the psychology to a winning one.

Now, of course you don't have an unlimited budget. You can't upgrade the training facilities, and the medical team, and buy a new defence all at once. So instead, it's all about focus – choosing where and what to spend, to get the biggest impact as quickly as possible.

Being a new *government* is similar. Here in the UK, the Labour Party has been chosen to do things a different way, with different people – but ultimately it needs to keep the fans happy.

Even more than in sport, focus is *everything*. Keir Starmer and his cabinet can't solve all the problems at once. They need to work out where to direct their resources – what needs to be faced first, and what can be booted out into the next ~~transfer window~~ parliament.

So what's the goal, and how do we get people cheering for it?

Like most things in the world, your inputs dictate your outputs. Better ingredients mean a better meal. Regular rehearsals result in good opening nights. And *proper* investment leads to growing economies."

Growth is the goal

The big *economic* problem that any new UK government is going to have to address is: Lack. Of. Growth.

In the UK, economic wealth per person[1] has been basically *flat* for nearly 20 years. People don't feel like they're getting particularly richer or better off, largely because, on average, they haven't been. In the US, GDP per capita is up by a third in the last two decades...

It's not just the sluggish bounce-back from Covid. Nor is it all to do with Brexit. And actually, it isn't even about the 2008 financial crisis (although it didn't help either).

The big problem has been brewing since before the millennium. Lack. Of. Investment.

Like most things in the world, your inputs dictate your outputs. Better ingredients mean a better meal. Regular rehearsals result in good opening nights. And *proper* investment leads to growing economies.

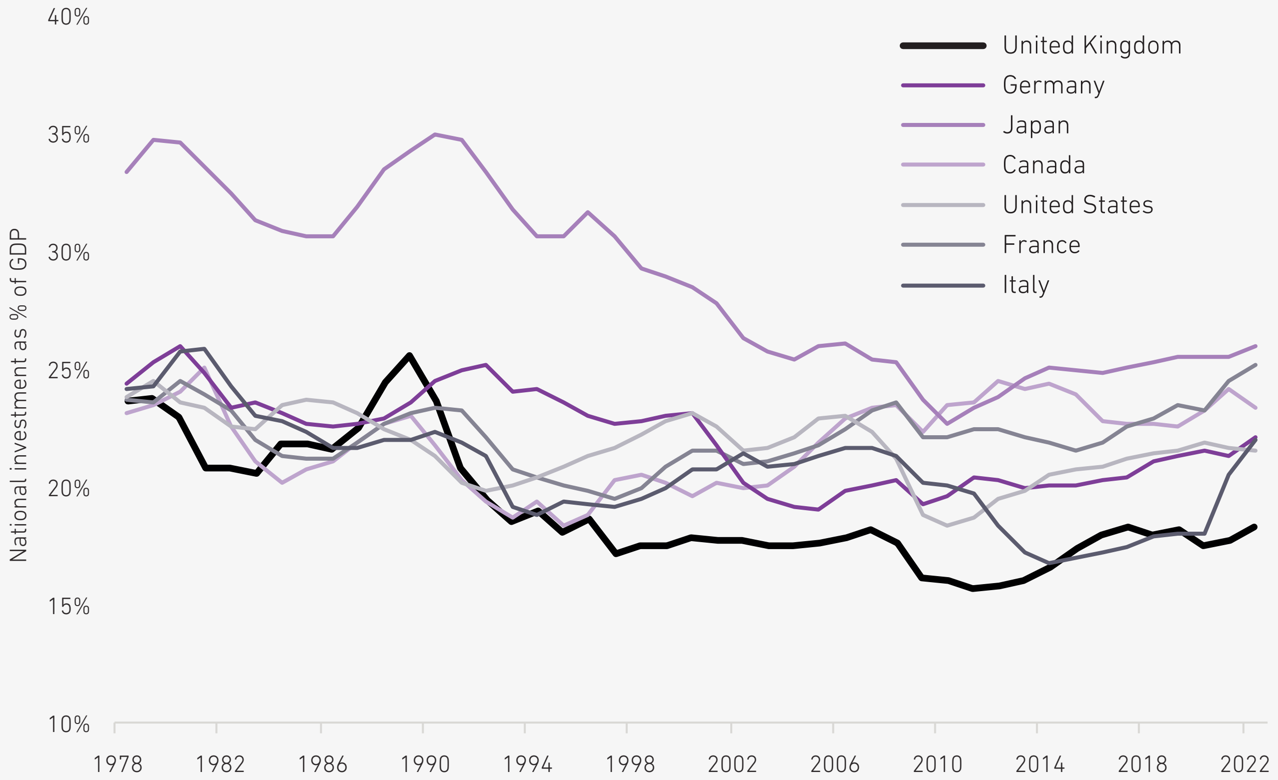
Since the mid-1990s, the UK hasn't been investing anywhere near enough in the basics that lead to growth. >>

BEN KUMAR
Head of Equity Strategy

[1] Technically, *GDP per capita*. There are no perfect economic statistics, but GDP per capita is a pretty good way of comparing how wealthy the average person in a country is.

Special feature
Continued

Investment as % of GDP



Source: OECD / 7IM

Some of it is obvious, everyday stuff (not even high-tech). Yes, it's fibre optic cables, but it's also fixing potholes. But much of it is longer term. The lesson from the chart above is that if you don't invest **now**, the effects stick around for three decades.

So the incoming government needs to put in place a system which allows planning, financing and building infrastructure for the next 20 or 30 years.

The problem, of course, is that politicians tend not to like investing in things which they might not be around to take credit for.

Take Nick Clegg's now infamous 2010 dismissal of new nuclear power because it wouldn't be around until 2021... Or look at planning reform, or tax legislation, or social care.

> The key thing is confidence. Regardless of the project – potholes or power stations – the government's storytelling has to be confident and personal."

Anything that needs a time-horizon longer than the next election gets sidelined. As Henry Hazlitt, a keen critic of US politicians in the 20th century, said, "*Today is already the tomorrow which the bad politician yesterday urged us to ignore*."

So the goal is to put the foundations for growth in place.

Getting the crowd on side

Personally, I think this bad politician, short-term approach doesn't give enough credit to the UK electorate. More people have patience and tolerance for **big** projects than we think; just watch any episode of Grand Designs. As long as we support the team, we don't stop watching when they lose a match – even after all of the years of grief, there's a majority of popular support in *favour* of HS2[2]!

The key thing is confidence. Regardless of the project – potholes or power stations – the government's storytelling has to be *confident* and *personal*.

Communication is everything.

Talk about the benefits as well as the costs – and make the updates exciting, modern and honest. Get an engineer to talk through how to build a bridge. Ask a town planner why they picked a roundabout, not traffic lights. A CEO to explain their plans for the new factory. A county councillor to explain how much of your tax bill goes on a specific project.

Above all, the effort needs to be on local, not national. As in any sport, the most loyal fans are the ones around the corner. The local network effects of our populations are huge. Negativity in a few streets spreads to the whole town – but so does positivity!

We might not ever get to matchday levels of excitement over local roadworks, but that should be the aim!

[2] https://yougov.co.uk/topics/politics/trackers/support-for-high-speed-rail-hs2

Culture & Sustainability

Scoring net-zero

Heatwave. Pints. Euros. Now that's what I call summer.

The Euros in full swing, beer gardens packed, and the England team routinely torturing the entire nation for 95 minutes!

While I'm not a die-hard football fan, I do love the passion, joy, and excitement that the Euros bring. And what makes this European Championships a little more special (for me!) is UEFA's bold statement: "*The most sustainable European Championship of all time.*"

We don't tend to associate climate change with sports, but they sure do impact each other. Remember when athletes fainted and running events were moved to different locations due to the heat and humidity in the 2021 Tokyo Olympics? Or when tennis matches were disrupted by bushfires in the 2020 Australian Open?

At the same time, large sporting events have huge carbon footprints; mostly from travelling. UEFA's EURO 2024 Environmental, Social and Governance (ESG) strategy focuses on 11 areas of actions ranging from renewable energy and circular economy to local public transport incentives for ticket holders and a climate fund. Whether this is "*the most sustainable European Championship of all time*" remains a question mark. I suspect that Euro 1976, held in then-Yugoslavia, with just four teams (Czechoslovakia, Netherlands, West Germany, plus the hosts) was quite a lot lower than today's 24-team event!

Europe is taking the centre stage this summer with Olympics scheduled following Euros, and Paris braces for a big test as Météo-France, the national weather service, warns of extreme heat expected this summer.

And in the UK, football faces its own climate challenges. The increasingly extreme and unpredictable weather patterns, such as flooding and drought induced by a changing climate, pose significant risks to stadiums and grassroot games. A study by Rapid Transition Alliance reported that a quarter of UK football grounds will be flooded by 2050...

We don’t tend to associate climate change with sports, but they sure do impact each other. Remember when athletes fainted and running events were moved to different locations due to the heat and humidity in the 2021 Tokyo Olympics?”

However, football is adapting. Six Premier League clubs have net-zero targets and efforts such as on-site clean energy generation, rainwater drainage and harvesting systems, as well as serving plant-based food to reflect a growing commitment to sustainability. And let’s not forget Tottenham Hotspur Game Zero day back in 2021, the world’s first net-zero-carbon elite football match.

International sporting events are a calendar highlight we’ve become used to – but there’s a lot of work to do to make sure they can still go ahead over the next century.

WENQIAN ZENG

Junior ESG Investment Analyst

Meet the teams

Investment Management Team

Martyn Surguy
Chief Investment Officer

ACA Chartered Accountant, MCSI, CISI Level 4, 37 years of industry experience.

Matthew Yeates
Deputy Chief Investment Officer

CFA, FRM, BA Economics, 13 years of industry experience.

Uwe Ketelsen
Head of Portfolio Management

MEcon, CFA, 28 years of industry experience.

Duncan Blyth
Head of Private Client Portfolio Management

BSc Actuarial Mathematics & Statistics, CFA, 28 years of industry experience.

Hugo Brown
Investment Analyst – Alternatives

BEng, CFA level 3 Candidate, 6 years of industry experience.

Ross Brydon
Investment Implementation Manager

BA in Finance, 6 years of industry experience.

Sam Hannon
Investment Associate

IMC and IAD. 6 years of Industry experience.

Tiziano Hu
Quantitative Investment Strategist – Multi Asset

MSc in Financial Technology, 4 years of industry experience.

Ben Kumar
Head of Equity Strategy

CFA, MSc Behavioural Economics, 12 years of industry experience.

Tony Lawrence
Head of Model Solutions

CFA and CAIA, 23 years of industry experience.

Stephen Penfold
Senior Investment Manager

BSc in Economics & Computing, 38 years of industry experience.

Ahmer Tirmizi
Head of Fixed Income Strategy

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Jack Turner
Head of ESG Portfolio Management

CFA, 16 years of industry experience.

Fiammetta Valentini
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Wenqian Zeng
Junior ESG Investment Analyst

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Adam Bloss
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MSci Theoretical Physics, 1 year of industry experience.

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Loic Yegba
Investment Risk Developer

MSc Mechanical Engineering, FRM, CFA level 3 candidate, 2 years of industry experience.

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