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Lonsec CFS FirstChoice Portfolio Update

Years of accommodative monetary policy combined with ample liquidity from central banks, remnants of the global financial crisis of 2008 may be coming to a gradual end. We are arguably entering a period transition in the economic environment from one of low inflation, low interest rates backed by unconventional monetary policy (quantitative easing) to one of higher inflation and higher interest rates.

Adding fuel to inflationary pressures has been a global pandemic where supply chains have been disrupted like never before, heightened geopolitical risks with the Russian invasion of Ukraine, known as the breadbasket of Europe putting additional price pressures on everything from crude oil, wheat to sunflower oil and where globalization, the accepted mantra for economic growth for decades under increased scrutiny with talk of a deglobalized world.

Periods of transition from a market perspective are always challenging. They are characterised by increased uncertainty and subsequently increased market volatility. In such environments it is a balancing act between defence and offence. In recent years and offensive game has been a clear winner, however defence has become increasingly important. While we do not have a crystal ball on how high inflation will be and by how much interest rates may rise the likely trend is up. Considering assets that can assist in navigating a higher inflation environment is important. While there is no perfect hedge for inflation there are assets that can benefit from a higher inflation environment. Some of these include real assets such as infrastructure and property and commodities.

The Lonsec suite of portfolios on the CFS FirstChoice platform have not been immune from the market volatility. There have been very few places to hide from the volatility with few sectors generating positive returns, notably those sectors that have benefited from the higher inflation such as commodities and resources. The market selling has been indiscriminate with quality companies with strong balance sheets being sold down alongside companies with high debt and poor earnings. From a portfolio perspective manager performance has been mixed over the short term. For the Lonsec CFS FC Active and Core Plus portfolios Australian equity managers with a value bias such as IML performed strongly on a relative basis, whereas growth focused managers and manager investing further down the market capitalisation spectrum lagged the market e.g. Bennelong ex-20. On the global equity side MFS and Acadian have outperformed in this market environment benefitting from their regional, sector and stock positioning. Growth managers such as T.Rowe Price lagged as their exposure to the US and notably exposure to technology continued to drag on performance. On the fixed income side while rising bond yields made it a difficult environment for bonds our active manager generally performed better than the market. The portfolio bias to active managers within fixed income with the ability to actively manager duration assisted performance.

We remain comfortable with the overall quality of the portfolio. While some of the growth managers have suffered in terms of performance the overall quality of their investments remain intact and we don't believe crystallising losses at this point is prudent. We believe that the coming six months will be volatile as the market digests inflation. We believe rates will likely rise in the short term however may ease further afield given the fine balance between managing inflation and not impacting economic growth.

Want to find out more?

Call us on 1300 826 395 or email info@lonsec.com.au

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Lonsec Investment Solutions Pty Ltd ACN: 608 837 583, a corporate authorised representative
(CAR number: 1236821) of Lonsec Research Pty Ltd ABN: 11 151 658 561 AFSL: 421 445