Baillie Gifford™

Multi Asset
Q3 investment update

October 2024

Investment manager James Squires and investment specialist Steven Milne give an update on the Multi Asset, Diversified Growth, Sustainable Multi Asset and Diversified Return strategies covering Q3 2024.

Your capital is at risk. Past performance is not a guide to future returns.

Steven Milne (SM): Hi and welcome to this Multi Asset quarterly strategy update. I'm Steven Milne and I'm an investment specialist with the Multi Asset client team.

Just as a brief reminder, the Multi Asset strategy seeks to achieve 3.5 per cent over the relevant base rate, looking to keep those volatility of returns below 10 per cent, and provide that all-important portfolio diversification.

Today we're going to be discussing asset allocation. We're also going to be talking about diversification during volatile markets. And we're also going to be asking, what next for the strategy?

I'm delighted to say that I'm joined today by James Squires, who's the head of Multi Asset and also a partner of the firm. And he's going to be doing most of the heavy lifting today by answering all my questions. James, welcome.

James Squires (JS): Thank you, Steven. Good day.

SM: I think sticking with the topic of market volatility would be a good place to start. We obviously saw equity markets sell off quite considerably over the end of July and August and obviously bounce back. But with diversification really being a central tenet of multi asset, how did the portfolio perform over that time?

JS: Yeah, you're right. There's quite a lot went on this quarter, even though we ended up in quite a good place across most asset classes. And as you say, end of July, start of August, there were concerns about rates, about growth, politics, global conflicts. We had a period where the S&P 500 fell by the best part of 10 per cent.

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And as you allude to in the question, our portfolios fell by maybe 1 per cent. So generally it was very robust during that period, which obviously is really important, very pleasing to see in a diversified strategy.

So what went on there? We had some really good performance from our infrastructure and real assets more broadly. We also saw the alternatives, the insurance linked securities, the structured finance contribute well. So they balanced out the asset classes that were weaker and led to an overall robust portfolio performance, which is what we're looking for.

SM: Good. So... did what we had expected it to do, what we had hoped for it to do, over that volatile period. But perhaps thinking of performance that you'd mentioned just there as well, another strong quarter of returns that has really carried on from the end of last year. Perhaps you can talk about what really drove that in terms of asset classes and perhaps stocks as well.

JS: Yeah, it was a strong quarter. It's been a strong 12-month period. Look, several asset classes contributed over the quarter, which again is something that I look to see. You want to see a number of different asset classes contributing for different reasons.

It's not always the case, but it's something you look for, and it very much was the case in the last three months. Infrastructure led that. US utilities in particular were really strong performers. We went into the quarter with them being pretty cheap, we thought. That was why we were adding. And we saw them re-rate. In P/ E ratio terms, we went from 17 (which is below average) up to sort of 20 (which is closer to average). So that was the re-rating that drove the performance.

And that came partly because we were in an environment of falling yields. We've started very clearly now a global rate-cutting cycle. And that does make a difference to asset classes like that.

But it wasn't just utilities. We also saw some really strong performance from the rare earths within our commodities allocation, different reasons sitting behind that, including the Chinese stimulus towards the end of the quarter.

We saw good performance from property, particularly some of the digital communications properties, or sort of the data centres and communications towers. And we also saw things like emerging market hard currency do very well.

SM: I think after a period of good performance, there's sometimes the logic to take some profits and reinvest them elsewhere. In terms of asset allocation decisions, when we were talking last quarter, it was relatively modest changes to the asset allocation. Maybe you can talk to this quarter and if there's been any changes and any changes of view that's been driving any of the transactions.

JS: Yeah, I mean, changes in asset allocation often aren't modest unless there have been dramatic changes to valuations or in the world. So it was again, say, this quarter, we did make some additions at the start of the quarter to infrastructure and to emerging market hard currency, both of which went on to do very well over the three months. But it was a few percentage points into each.

But most of the changes were within asset classes. And exactly as you say, in a period like this, you'll see some investments perform very, very well, perhaps get a little bit ahead of themselves, and you want to take some money away from those to fund opportunities elsewhere.

So we took money out of CLO funds in structured finance. We sold our Ukrainian bond position. We reduced our exposure to the cable companies within economic infrastructure and to some logistics property.

Out of those, Ukraine's probably quite interesting. We've held that for a while. And a combination of a debt restructuring that the country went through and a bit more of a positive tone to its conflict with Russia, particularly that point where Ukrainian forces were entering Russian territory. That just gave everyone a little bit more confidence on what the outcome is for Ukraine here. That's where the bond prices step up meaningfully, gave us a great opportunity to come out of there.

So, those are the sorts of things we were taking profits in. And we were finding opportunities in a number of different places. We added to copper in the commodities area. We bought some Bright Line bonds within high yields. So, that's financing a US railroad project that we thought was a really attractive yield on. And we bought some European utilities.

Copper is one that actually, again, it had a good quarter overall. But just after that period of volatility, we saw prices dip down below $9,000 a tonne. That, for us, was an opportunity to get in, to add to our position. We did so. It's finished the quarter closer to $10,000. So lots of things that we did within asset classes rather than big allocation decisions.

I guess the one other thing that's kind of more in the asset allocation area would be portfolio protection, and we added some portfolio protection this quarter.

SM: Okay, so similar again to the previous quarter in terms of modest changes, but I am intrigued about the portfolio protection point as well. That kind of alludes to having some shorter term concerns. Perhaps you can just cover why you've added that to the portfolio and some of the reasons for that.

JS: Yeah. A few concerns, but I don't want to overplay the concerns. It's more of the opportunity to add some cheap insurance whilst there are some concerns lingering. So, what did we actually do?

We went long equity volatility. That means we bought December VIX futures and we bought some protection on European high yields through CDS. So we judged both of those to be cheap. So the levels were 17 on VIX, just under 300 on CDS.

Now, those are below average levels for those indices, and particularly at this time of year. So that translates to a low cost of protection for the portfolio.

Now, when we look out at the world, actually our base case is positive. We think a soft landing is very likely. We think even that notwithstanding, the portfolio has more than enough diversification to ride through minor wobbles, just as we saw in July, just as we saw in the start of August.

So we're not sitting here massively concerned about the world, but there are things that we're thinking about. Valuations do look stretched to us in some parts of the market. There are threats to growth if you look at the path of unemployment, if you look at some of the earnings that have come out of the bigger companies in the US in the last few months.

And we're seeing some vulnerabilities in the private credit model, which have just got us thinking. So you take those things. You also think about the end of the year coming up. We've got a really polarised US election, which is bound to bring some kind of volatility. We've got an escalating conflict in the Middle East.

So there's definitely things that can go wrong. And there's an opportunity to protect the portfolio with some very cheap insurance. So why would you not do that, given that confluence? That's our thinking.

SM: Fair enough. It's OK, my final question won't be about the US election, so I'll leave that one just now. But I think after a period of good performance, it is only natural to sort of re-evaluate the portfolio and look at it again. So what's really next for the strategy, and where does it go from here?

JS: Yeah, look, I mean, we do what we always do, which is seeking opportunities in as many places as we can find them. And actually having put that kind of that backstop to the portfolio with the protection puts us in a better place to step forward and do that.

So we've been looking at opportunities in different property sectors. We've been looking at commodities like uranium. We've spent lots of time looking at insurance linked securities. That's an asset class we've actually done a lot more in the last year, we see as being much more attractive.

So premiums there are high, higher than they have been for a long time. Many of the investors who'd come into the asset class as sort of tourists in the last 5, 10 years have stepped away. And we've had a period where actually we haven't had many losses.

We had a couple of hurricanes in the quarter, Hurricane Beryl that hit Jamaica at the start, and Helene that hit Florida and the Southeast US towards the end. But neither of those have been loss-triggering events. So it's been a good period for insurance linked securities, and that's one that we like as a diversifying, return-generating asset class. It's the sort of thing we're seeking.

Just more broadly, what are we doing? We're keeping an eye on those threats, but we're seeking to find those opportunities always, and we think there's lots out there that our clients can benefit from.

SM: Brilliant. Well, thank you very much. Sadly, we have run out of time for today. Just to recap, we have had a strong period of performance over the quarter. The portfolio has remained resilient in spite of some severely volatile equity markets.

But we do believe that we are at the start of a global interest rate cutting cycle. Inflation will continue to moderate. And that has led us to make some asset allocation changes to the portfolio, add a little bit of portfolio protection, but really have a broad range of diverse asset classes and stocks within that that can drive those portfolio returns in future.

And with that, I thank you for joining us today.

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Diversified Growth (representative of Multi Asset, Multi Asset Growth, Diversified Return, Sustainable Multi Asset)

Annual past performance to 30 September each year (net%)

	2020	2021	2022	2023	2024
Diversified Growth Composite	-1.0	10.3	-13.2	-1.3	15.1
Base rate +3.5%	3.9	3.6	4.3	7.6	8.8

Annualised returns to 30 September 2024 (net%)

	1 year	5 years	10 years
Diversified Growth Composite	15.1	1.5	2.8
Base rate +3.5%	8.8	5.6	4.8

Base rate: UK Bank of England.

Source: Revolution. Sterling. Returns have been calculated by reducing the gross return by the highest annual management fee for the composite. 1 year figures are not annualised.

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