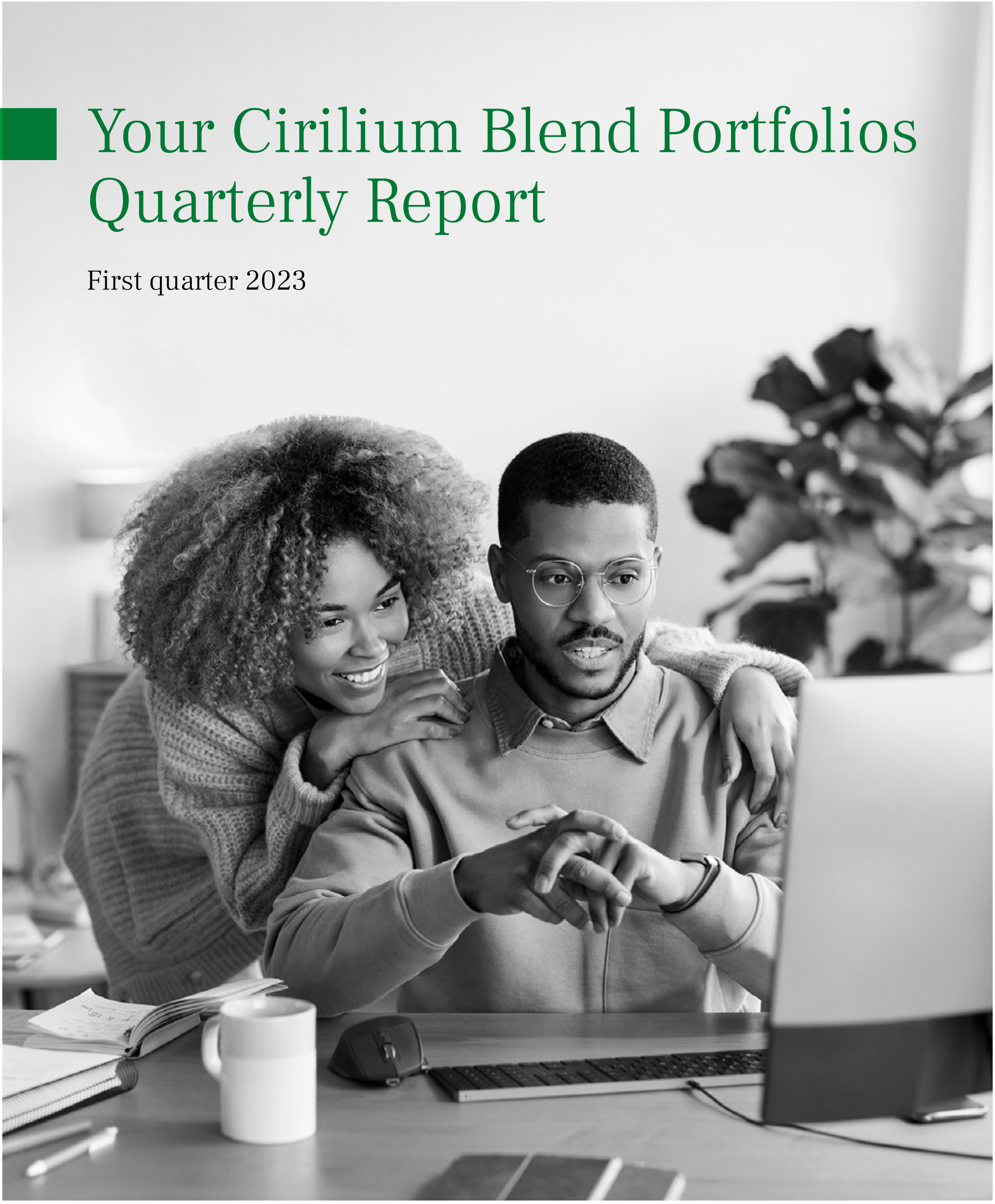
UK: Suitable for retail and professional clients.

Quilter Investors

Your Cirilium Blend Portfolios Quarterly Report

First quarter 2023



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Marcus Brookes
Chief Investment Officer

Our market summary

The collapse of Silicon Valley Bank (SVB) Contingent convertible capital in the US, alongside the 'shotgun' merger of Credit Suisse and UBS in Europe, momentarily spooked investors with echoes of the 2007-08 financial crisis. Despite the subsequent increase in market volatility, global equities delivered worthwhile gains over the quarter. Inflation remained a key topic among analysts, with central banks in developed economies such as the US, UK, Europe and Switzerland each electing to raise interest rates over the period.

Equity markets

US stock markets delivered a return of 4.8% over the period. With the exception of the SVB situation, which prompted a brief but sharp fall in markets in March, US stocks made gains thanks largely to renewed optimism over the slowdown in US inflation. Even so, the US Federal Reserve raised interest rates twice in the quarter. However, the slower rate of increases may signpost the nearing end of this rate-hiking cycle.

The first quarter was a strong period for European stock markets which gained 9.1%. Even the continent's financials sector, which was impacted by the troubles of Credit Suisse and the subsequent merger with UBS (a deal brokered by the Swiss government), ended the period in positive territory. The European Central Bank opted to raise interest rates twice during the quarter, each time by 0.5%, while inflation in the region dipped to a one-year low in March.

UK stock markets were buoyed by expectations that the Bank of England would ease its cycle of interest-rate increases later in the year, although the bank remained committed to fighting inflation. Positive data from the Office for National Statistics showed that the UK had avoided a technical recession in the fourth quarter of 2022, although analysts still anticipate an economic decline later in 2023. Over the quarter, UK equities were up 3.1%.

Emerging market stocks began the quarter with a strong tailwind thanks to China's economic re-opening following the dismantling of its failed 'zero-covid' regime. However, political tensions between the US and China subsequently cooled investor sentiment with Chinese stock markets delivering a modest 1.9% return over the quarter. Meanwhile, the MSCI Emerging Market Index gained just 1.2%, with local news impacting returns from Brazil and India.

Fixed-income

Government bond prices rose across the quarter, driven in part by an improving inflationary backdrop but also by the demise of SVB, which sparked a rally in bond markets as investors sought safe havens. Against this backdrop, US Treasuries (US government bonds) gained 2.7% in sterling terms. Meanwhile, UK gilts (UK government bonds) gained 2.3% while sterling-denominated corporate bonds (issued by companies) added 2.4%.

Total return, percentage growth in pounds sterling except where shown, rounded to one decimal place. Global equities are represented by the MSCI World Index; US equities by the MSCI US Index; European (excluding UK) equities by the MSCI Europe ex UK Index; UK equities by the FTSE All-Share Index, emerging market equities by the MSCI EM (Emerging Markets) Index; Chinese equities by the MSCI China Index; UK corporate bonds by the ICE BofA Sterling Corporate Index; gilts by the ICE BofA UK Gilt Index; and US Treasuries by the ICE BofA US Treasury (GBP hedged) Index.

Your performance review

Ian Jensen-Humphreys
Portfolio Manager

Sacha Chorley
Portfolio Manager

The Cirilium Blend Portfolios delivered strong relative returns with returns ranging from 1.8% to 3.6%, with the higher-risk portfolios generating the highest returns against a backdrop of rising equity and bond markets as investors forecast the imminent end of central bank interest-rate hikes due to inflation showing tentative signs of normalising. A key contributor to returns was our equity manager selection with those managers able to avoid the turmoil in the banking sector, whether due to a bias in their investment style or their market-cap focus, doing especially well. Meanwhile, our fixed-income holdings delivered positive returns, despite the challenges presented by the failure of Credit Suisse and its impact on the contingent convertibles market.

Contingent convertibles (CoCos) are bonds mainly issued by European banks. The issuing bank has the option to convert them from bonds into equity to help improve their capital buffers in times of stress, which makes them more risky for holders but leads to a higher yield. They are also referred to as alternative tier 1 capital notes (AT1s).

How our equity holdings performed

US markets shrug off banking concerns

US-centric markets ended the first quarter as one of the top performers with the MSCI North America Index up 4.5%, slightly ahead of the MSCI AC World Index. However, concerns arising from the failure of SVB in the US impacted a number of areas. The Granahan US SMID Select Fund was among the worst hit; its direct exposure to SVB helped to deliver a 1.5% decline for the fund over the quarter.

Europe outperforms

Both our UK and European holdings were significant contributors to returns. While our European exposures delivered the strongest returns, our UK holdings led the way in terms of benchmark outperformance. Despite tilting towards smaller company stocks, the Quilter Investors Equity 2 Fund (NinetyOne) outperformed by over 3.5% while the Montanaro European Income Fund outperformed by 2.5%.

Growth allocations rebound

The first quarter saw growth stocks outperform strongly, partly as they had little to do with concerns as to a potential banking crisis. Investors showed a renewed focus on larger-cap technology and communications stocks like Nvidia, Microsoft and Amazon, all of which were up over 10% during the quarter. This was especially beneficial to funds such as Sands Capital US Select Growth, which outperformed the broader market by over 9% in the first quarter.

How our fixed-income holdings performed

Strong returns despite volatility

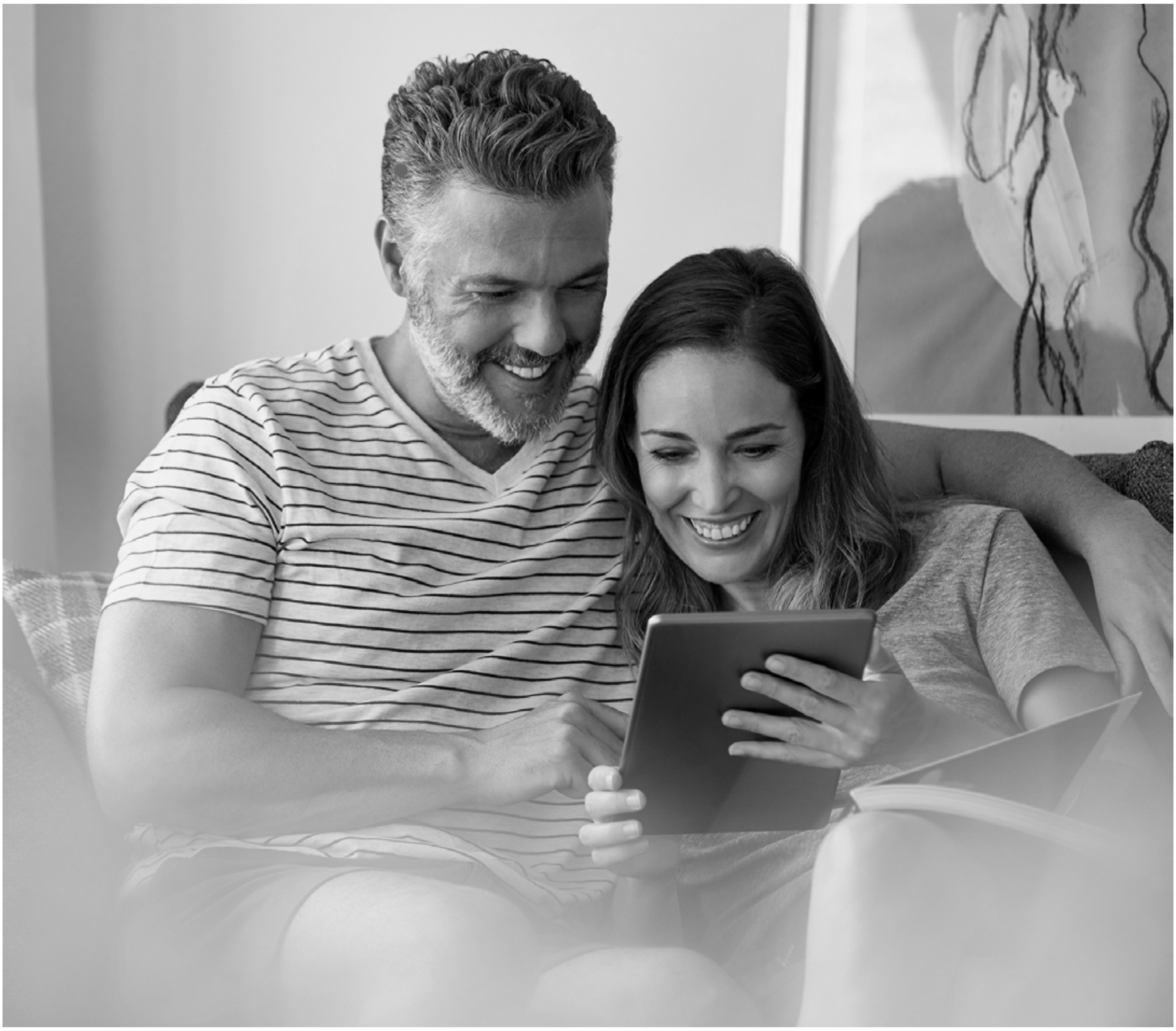
Fixed-income markets were again volatile over the quarter as investors aggressively re-priced the path of likely interest-rate moves. Overall, however, yields fell (meaning prices rose) and this led to positive returns for the Cirilium Portfolios. Even so, overall manager performance was relatively weak with losses arising in the high-yield segment of the fixed-income holdings. These arose as a result of the Credit Suisse failure and its requisite impact on the contingent convertible bond market. The Premier Miton Financials Capital Securities Fund was our core position here; it declined 5.5% over the quarter.

How our alternative holdings performed

Mixed performance in volatile markets

Overall, returns from our alternatives holdings were flat over the quarter. Some managers were able to take advantage of the volatility – particularly those in the equity markets. The Cooper Creek North America Long Short Equity Fund was a highlight here, delivering more than 2%. Our carry strategies also performed well, with the UBS Commodity Carry ETF delivering a 7% return. Unfortunately, our inflation-linked exposures declined with the likes of the WisdomTree Enhanced Commodity ETF falling 3.5%.

Carry strategies seek regular, low-risk returns regardless of market direction. 'Carry trades' try to exploit differences in future pricing points, interest rates or currencies.



Portfolio changes

We reviewed our equity exposure in early February and, as a result, we reduced our overweight position, reflecting our increased concerns as to the likely earnings trajectory of the stock market. Within this, we removed our existing underweight to the European equity market. Elsewhere, we increased our exposure to high-yield bonds, which should fare well in the 'muddle through' economic outcome we expect to see. In mid-March we also reviewed our government exposure and increased the size of our underweight here, reflecting our view that high inflation is likely to be more persistent than investors currently hope and expect, and hence will demand further interest-rate increases from central banks.

When a fund is 'underweight', it holds a smaller position in a particular stock, sector or region than the stock market index or strategic asset allocation (SAA) model against which it's benchmarked. 'Overweight' means the opposite.

New and increased holdings

Brandes US Value Fund

We initiated a small new position in the Brandes US Value Fund. The fund is from a manager focused on larger-cap value investing and will sit well alongside existing value exposures, adding explicit active management alongside our 'smart beta' holdings. This position will gradually be scaled up over the coming quarter.

Jupiter Strategic Absolute Return Bond Fund

We initiated a small new position in this fund which is an alpha and carry-focused alternatives holding. It generates returns by expressing macro views in fixed-income markets while not relying on corporate bond holdings to boost returns. Following the removal of the QMS Multi Strategy Fund (below) we will be adding to this position as it complements our existing holdings.

Federated Hermes Unconstrained Credit Fund

We increased the size of our holding here as part of our moves to increase our high-yield bond exposure.

Removed and reduced holdings

QMS Multi Strategy Fund

We removed this holding as, despite a good performance track record over the three years since its launch, the strategy had failed to attract sufficient investors and was scheduled to close.

Premier Miton Financial Capital Securities Fund

Following the Credit Suisse collapse, we reviewed the risk assumptions we had made regarding the CoCo market. Although we had assumed a level of risk similar to high-yield bonds, the Credit Suisse collapse suggested that risks are more in line with equity markets. We therefore reduced the position size accordingly.

Investment outlook

Our shift towards a more cautious stance through the quarter was heavily influenced by the decline in corporate earnings (when measured on a year-on-year basis) over the period. Looking ahead, we need to confirm whether this decline was temporary or the start of a more persistent fall. Although we will continue to seek specific sectoral or structural opportunities, the three key factors we're focused on are economic growth, what this means for earnings and, the key risk for us, the chances of a central bank policy mistake.

1. More signs of a slowdown in growth but no deep recession

Economic activity has certainly slowed. For example, activity levels in the consumer and industrial sectors have softened of late while the banks are generally tightening lending standards – and the recent SVB and Credit Suisse issues are likely to exacerbate this in the near term. However, we believe a 'soft' landing is still possible – the US labour market remains particularly robust, but unemployment rates are low globally. Consumer confidence levels have started to pick up and this has fed through to increases in GDP growth estimates.

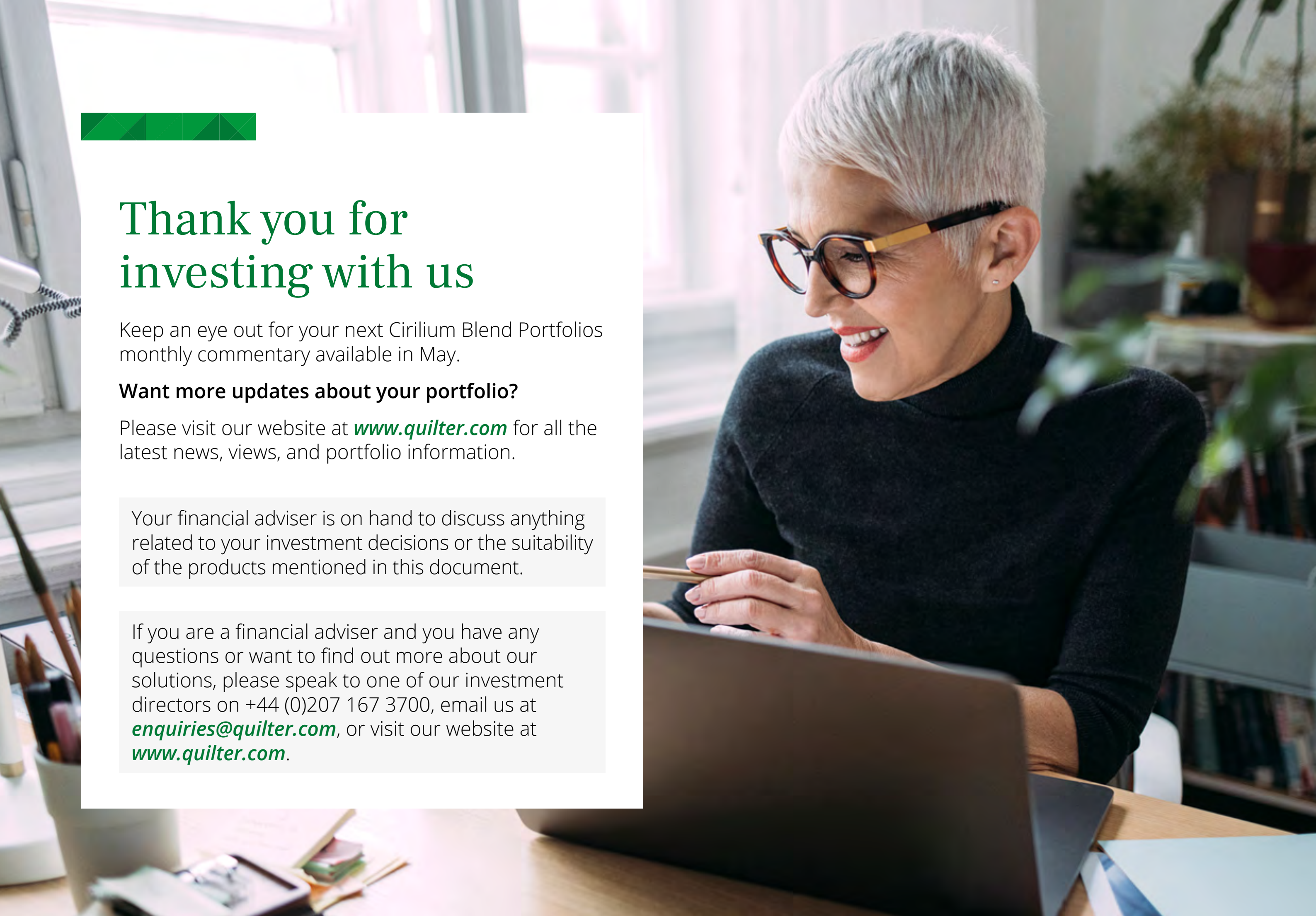
2. Earnings still crucial

With slowing economic activity, there's an increased risk of a contraction in company earnings. Company valuations are not yet cheap enough to be our only guide, consequently we need to hold companies that demonstrate the ability to continue growing their profits. We saw a decline in company earnings last quarter as well as the first major decline in profit margins, but the upcoming earnings season will give us another raft of information to help us determine whether companies have managed to turn the corner or not.

3. Central bank policy missteps remain the key risk

In an environment of generally sound economic activity, we would expect central banks to act in an appropriately benign manner. The surprising persistence of inflation had put pressure on central banks to continue to raise interest rates at the risk of disrupting the economic momentum. We have started to see some signs that the US Federal Reserve is stepping back from this stance, which helps to reduce the risk of further rate increases.

Earnings seasons are quarterly. They are the periods when listed companies release their financial data including information on company revenues, sales, profits and margins as well as more granular details of the underlying business, its liabilities and its forecasts for future revenue growth.



Thank you for investing with us

Keep an eye out for your next Cirilium Blend Portfolios monthly commentary available in May.

Want more updates about your portfolio?

Please visit our website at ***www.quilter.com*** for all the latest news, views, and portfolio information.

Your financial adviser is on hand to discuss anything related to your investment decisions or the suitability of the products mentioned in this document.

If you are a financial adviser and you have any questions or want to find out more about our solutions, please speak to one of our investment directors on +44 (0)207 167 3700, email us at ***enquiries@quilter.com***, or visit our website at ***www.quilter.com***.

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