Macquarie Balanced Growth

Quarterly Investment Option Update

30 September 2022

Aim and Strategy

Aims to provide medium to long-term capital growth, together with some income, by investing in balanced level of growth and defensive assets.
The option provides exposure to a diversified portfolio of growth assets, including shares and alternative assets, with some exposure to cash and fixed interest. The investment manager aims to deliver above index returns through an active investment approach that identifies and pursues investment opportunities within set limits through a combination of active management within each asset class and tactical asset allocation across asset classes to meet the objectives of the portfolio. A varying portion of the foreign currency exposure is hedged through currency hedging solutions, whether passive or active.

Asset Allocation	Benchmark (%)	Actual (%)
Cash	1.5	11.5
Strategic Income*	9.0	10.2
Australian Fixed Interest	17.5	7.4
Global Fixed Interest	7.5	7.7
Inflation Linked Bonds	5.0	3.4
Australian Equities	26.0	24.3
Global Developed Markets	13.5	22.7
Global Emerging Markets Equities	12.0	2.7
Alternative Assets**	8.0	10.1

* Invests predominantly in high quality Australian and global credit securities
** May include investments in such asset classes as private equity, infrastructure or hedge funds

Investment Option Performance

To view the latest investment performances for each product please visit amp.com.au/performance

Investment Option Overview

Investment Category	Multi Sector (Balanced)
Suggested Investment timeframe	5 years
Relative risk rating	6/ High
Investment style	Active
Manager style	Single Manager

Investment Option Commentary

The Fund outperformed its strategic asset allocation benchmark, which was driven by the Fund's underweight position to growth assets.

In the third quarter, performance of hedged International and Australian equities was mixed with significant volatility, delivering -5.2% and +0.5%, respectively. With regard to fixed interest, the sector returned -0.6% domestically and -4.1% offshore. Finally, Macquarie's hedged international infrastructure performed negatively as well, detracting -8.4%. Market sentiment continued to dampen driven by heighten inflation and the aggressive monetary policy tightening trajectory. Throughout the third quarter the investment manager continued to observe significant volatility across different asset markets, with wide trading ranges for most.

During the third quarter, the investment manager maintained a close to maximum defensive allocation, with an overweight to defensive assets. This asset allocation helped buffer some of the market volatility.

Since the beginning of 2022, the investment manager has adopted a very cautious approach to asset allocation. The rapid deterioration in macro-economic conditions, exacerbated by unforeseeable geopolitical tension, extreme weather events such as the droughts in Europe and China, and the persistence of COVID-19 pandemic controls in China, have all brought forward the timeline and heightened the probability of a global economic recession. As such, the investment manager continues to expect elevated downside risks for growth assets to persist in the foreseeable future. In the short term, the investment manager also envisions elevated volatility and downside risks in fixed income markets. However, the investment manager expects fixed income to outperform should unemployment climb, and market participants begin to appropriately price the risk of a global recession. The investment manager expect that the Model Portfolio may experience heightened volatility given the current market conditions. In response, the Fund has maintained its asset allocation within the Model Portfolio to near-maximum defensiveness. It is important to note that Macquarie's defensive bias will likely persist for a significant period of time, unless the trajectory of global monetary tightening becomes notably less aggressive.

Market Commentary

The third quarter has witnessed central banks hardening their focus on inflation by delivering rapid and sizeable rate hikes. This is the fastest rate hiking cycle since the early 1980 and the guidance to financial markets is to expect further aggressive rate hikes in coming months. With short term rate expectations re-pricing rapidly, it was not a surprise for global bond yields to shift higher. Risk markets are waking up to the prospect of the unintended consequence of central banks efforts to bring inflation under control could be a recession, with equity major indices falling and credit spreads widening into the end of the quarter. However, risk markets remain vulnerable should a hard landing for economies become a reality.

Fiscal policy was again under the spotlight, with governments in Europe and UK in particular offering support to households and businesses to protect against the rapid rise in energy costs. In contrast to 2020-21, most fiscal action is not stimulatory but rather preventing a worst-case scenario unfolding. In fact, the markets quickly punished the new UK Prime Minister and Chancellor who unveiled a surprise by announcing significant unfunded tax cuts that are biased to benefit high income earners. The UK government bond market exploded higher, particularly the long end – which rippled around global markets and eventually prompted the Bank of England to intervene and buy bonds, reversing its intent to begin unwinding its balance sheet.

Outlook

In September, upon the release of the US Consumer Price Index (CPI), Fed Chairman Jerome Powell's press conference had important implications to Macquarie's outlook. With the US CPI climbing north of 8% YoY in September, it is reasonable to conclude that the Fed is not yet on track to achieve its price stability target of 2% - 3%. Importantly, with current US wage growth at 6%+, it is also fair to say that the federal reserve Will not achieve its' price stability target in the coming months. These observations offer us two important implications. First, the Fed will keep increasing the federal funds rate, or the rate will at least remain elevated for quite some time. Second, given elevated wage growth, the most likely means to curb inflation will be via a notable increase in unemployment. This is consistent with Macquarie's view that economic growth indicators are already weakening, and a continued, rapid upward movement of risk-free rates will inevitably lead to weaker labour market as well as a further deterioration in economic growth.

The investment manager expects this to be a painful experience for both businesses and households. Businesses will suffer from declining margins as costs inflate rapidly, and revenues fall from weakening demand. Households will need to endure a higher cost of living, higher mortgage repayments, and possible job losses.

Equity, fixed income and currency markets have started to price these scenarios. However, it will be some time before the pain is truly felt in the real economy. In Macquarie's view, when this scenario materialises in the real economy, central banks may pivot to more accommodative monetary policies. This may provide a catalyst for a shift in the manager's asset allocation strategy towards a more aggressive stance, meaning a completely turnaround from an underweight bias to growth asset to an overweight bias.

The investment manager continues to anticipate faster and sharper cash rate movements and have indicated previously that higher, faster increases in cash rates will elevate the probability of a global recession and speed up the pace at which it unfolds. With several major developed markets currencies having depreciated significantly against the US dollar in recent months, and weaker liquidity across global markets, the investment manager believes the likelihood of a possible negative tail risk event have increased significantly and will continue to increase as the rate rises. The investment manager portfolio's overweight bias towards fixed income asset in short term will increase portfolio volatility due to uncertainties associated with inflation. However, the investment manager expects losses generated by Australian fixed income asset is limited due to the size of household debt. In the medium term, fixed income offers attractive income and more importantly, in Macquarie's view, fixed income assets will act as a significant capital buffer should one of these unforeseeable events and/or global recession unfold.

The investment manager anticipates further market volatility ahead in the coming months, as each economic data print is likely to be closely watched for clues on how it may impact monetary policy decisions and trigger subsequent repricing of recession risk. The investment manager is maintaining a focus on protecting the downside. The investment manager also believes that this mentality is appropriate based on Macquarie's expectations for inflation, monetary policies, and economic growth.

Availability

Product name	APIR
SignatureSuper*	AMP0958AU

*Closed to new investors

Contact Details

Web: www.amp.com.au
Email: askamp@amp.com.au
Phone: 131 267