Setanta Managed Fund
Q4 2022

Fund Description

The **Managed Fund** ("the Fund"), managed by Setanta Asset Management Limited ("Setanta"), is a unit-linked offering of Irish Life Assurance.

The Managed Fund is an actively managed multi-asset portfolio, which holds a combination of equities, fixed income, property, commodities, cash and absolute value. The Fund holds between 50-80% of its assets in equities, reflecting the breadth of the market and Setanta's expertise in the area. The portfolio is managed in accordance with the Setanta investment philosophy. That is, the managers seek to own good assets for the long-term at prices below what they think they're worth, carefully considering each investment's risk profile.

The investment objective of the Fund is to outperform the median of competitor Managed Fund offerings over the long term.

Fund Commentary

The Managed Fund was up 4.2% over the fourth quarter, bringing the year-to-date return to -9.0%. It was comforting to see a positive quarter after a historically tough year for markets.

While bonds in general struggled, equities finally started to move higher. There was a positive catalyst with inflation figures falling, though this was offset somewhat by central banks stalling a year-end rally in December on continued hawkish resolve.

(Fund Commentary continued on Page 3)

Portfolio Managers

Kieran Dempsey & David Ryan CFA, CAIA, FRM

Our Investment Principles

We do not believe markets are efficient

We invest below our estimate of intrinsic value

We invest in businesses rather than buying stocks

Preservation of our clients' capital is key

Investing is a marathon, not a sprint

We are not afraid to swim against the tide

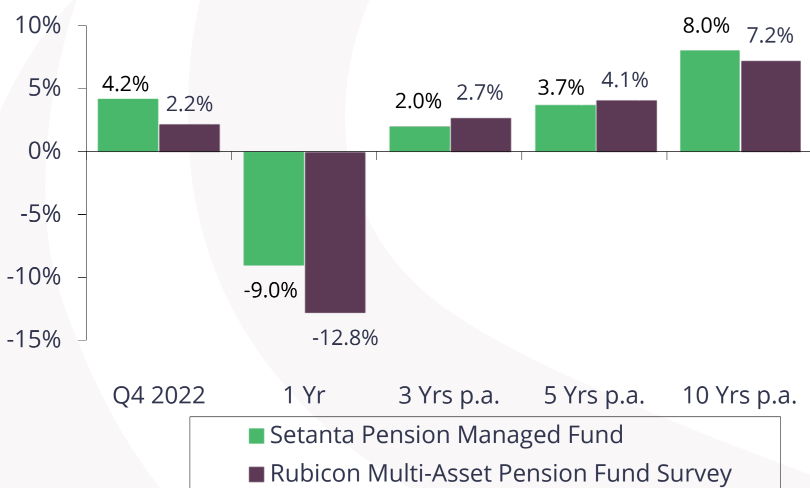
We consider scenarios rather than making forecasts

Businesses we own must have strong balance sheets

We make mistakes and always endeavour to learn from them

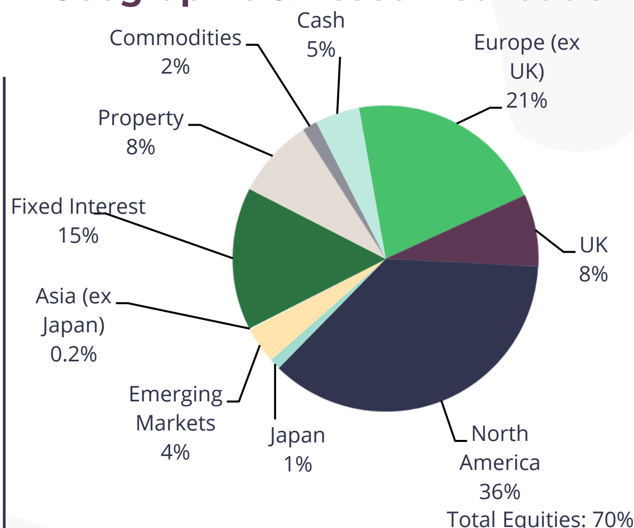
We will act with integrity in everything we do

Fund Performance – 31.12.22 (EUR)

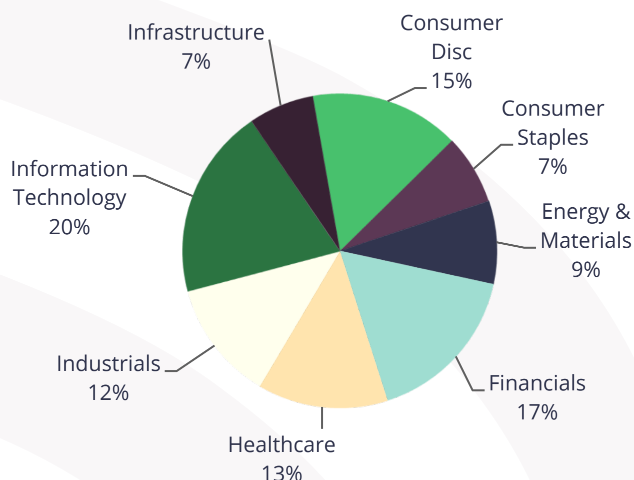


Performance Source: Setanta Asset Management Limited. The actual Fund returns stated are based on the movements in the unit prices of an institutional series of the Fund (ILA/CLI Setanta Managed Fund [H012]) and are net of management fees. Benchmark: Rubicon Multi-Asset Pension Fund Survey. **Holdings Source:** Setanta. Sector allocations based on invested portfolio only (excludes cash). **Credit Rating Source:** S&P.

Geographic & Asset Distribution



Equity Sector Distribution



Top 10 Equity Holdings

COMPANY	SECTOR	% OF FUND
MICROSOFT CORP	INFORMATION TECHNOLOGY	2.8%
BERKSHIRE HATHAWAY	FINANCIALS	2.6%
ORACLE CORP	INFORMATION TECHNOLOGY	2.1%
JOHNSON & JOHNSON	HEALTHCARE	1.9%
MCDONALD'S CORP	CONSUMER DISCRETIONARY	1.9%
NIKE INC	CONSUMER DISCRETIONARY	1.8%
COSTCO WHOLESALE	CONSUMER DISCRETIONARY	1.7%
JOHNSON CONTROLS	INDUSTRIALS	1.7%
SAMSUNG ELECTRONIC	INFORMATION TECHNOLOGY	1.6%
KEYSIGHT TECHNOLOGIES	INFORMATION TECHNOLOGY	1.6%

Fixed Interest Portfolio

CREDIT RATING WEIGHTING		
CREDIT RATING TYPE	**ASSET TYPE WEIGHTING**	**BENCHMARK WEIGHTING**
AAA	19.7%	23.1%
AA	51.6%	38.4%
A	10.5%	15.7%
BBB	18.2%	22.8%
	100.0%	**100.0%**

Yearly Performance

Year %	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Fund	-29.6	22.9	9.5	0.5	14.2	18.5	17.8	7.9	12.2	6.8	-2.7	16.1	-3.1	20.4	-9.0
Benchmark	-35.6	22.0	11.3	-3.6	14.3	16.6	15.6	9.5	5.9	7.3	-5.2	20.6	6.2	17.6	-12.8

Commentary

Global equities significantly outperformed the benchmark, with all sectors posting positive returns. Energy (+12.1%) and Industrial and Materials (+9.74%) were the leaders, while Healthcare (1.9%) and Consumer Staples (2.3%) were the laggards, albeit positive.

While European Government bonds struggled (-2.7%) with higher interest rates and reduced central banks buying, Emerging Market debt managed to post positive returns (+0.4%), having started their rate hiking cycle earlier, and local currencies strengthening on stronger commodities and a lull in dollar strength, helping them perform in Euro terms.

Property was weak (-2.2%), however, in inflationary environments, real assets like property have proved their worth. With lease cashflows linked to inflation and higher replacement values, protecting real returns. The move higher in interest rates, while quicker than normal was expected, allowing time to term out debt longer term and fix funding at attractive levels historically.

The fund remains well diversified across asset classes and will look to take advantage of opportunities where valuations look appealing over a medium to long term horizon.

Key Contributors

- Global Equities
- Energy Sector
- Industrials & Materials Sector

Key Detractors

- Government bonds
- Property

Market Commentary

"Over the course of the year, we have taken forceful actions to tighten the stance of monetary policy. We have covered a lot of ground, and the full effects of our rapid tightening so far are yet to be felt."

Jerome Powell, Chair of the US Federal Reserve, 14 December 2022

2022: a turbulent year for markets

In aviation, turbulence is an unpredictable weather phenomenon: an irregular motion of air, which may be insignificant, causing a few slight bumps, or may be extreme, forcing an airplane out of control. With the speed and magnitude of recent moves in interest rates, it is still not clear whether we will see bumps, or further extreme moves, in 2023, or which way markets will go from here.

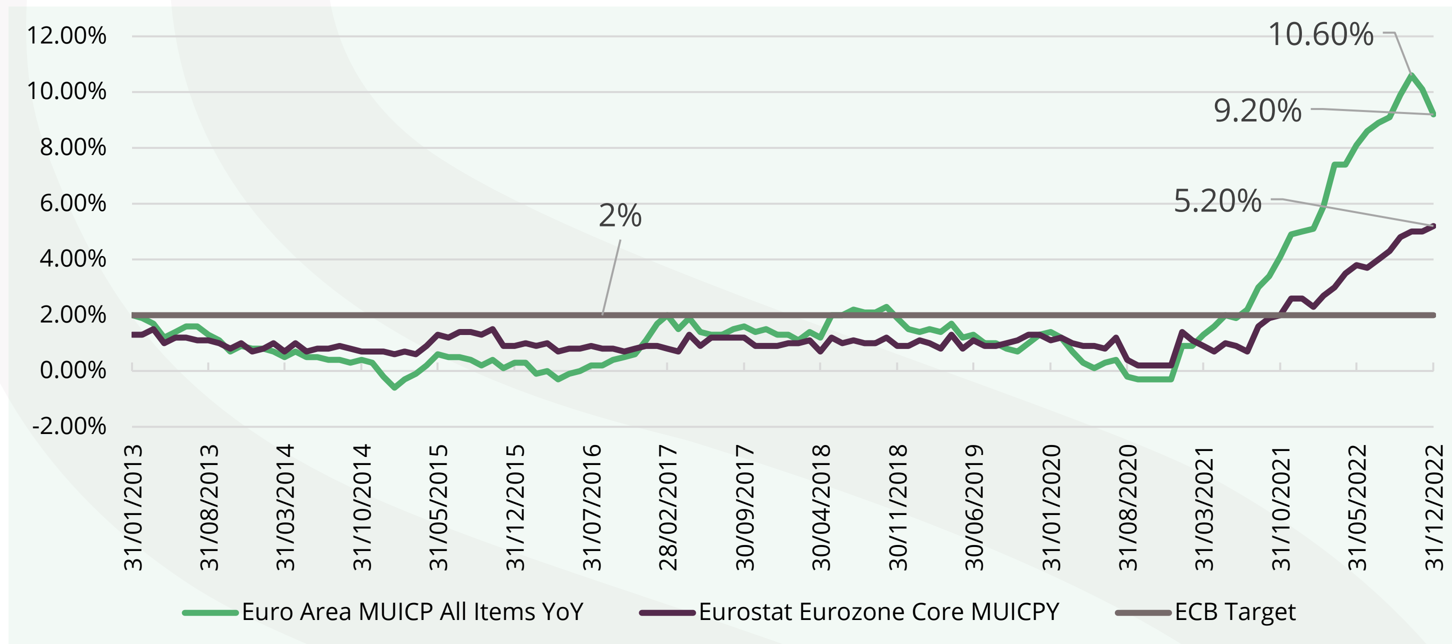
2022 was a year in which equities and bonds were simultaneously weak, and cash and commodities were some of the strongest performing financial assets. The low-to-negative correlation that we have come to expect from equities and bonds in recent years was non-existent, as rising interest rates hit both asset classes.

The year ended with a positive fourth quarter for equities, even with markets weakening in December on growing fears of recession. However, markets remain volatile, seemingly challenged by a 'perfect storm' of events, resulting in high inflation, rising interest rates and slower growth. It remains to be seen whether central bankers can pull off a 'soft landing'.

Euro area: macro outlook

While headline inflation fell over the quarter in Europe, from a 10.6% high to 9.2%, it should stay above the European Central Bank (ECB) target of 2% in 2023.

Euro area headline and core inflation



Source: Setanta / Bloomberg

The ECB will want core inflation – which excludes food and energy prices – to trend lower, before any change in policy. Stubbornly high core inflation could limit the central bank's ability to ease interest rates, even in a recession.

"In particular, the Governing Council judges that interest rates will still have to rise significantly at a steady pace to reach levels that are sufficiently restrictive to ensure a timely return of inflation to the 2% medium-term target."

European Central Bank, Press release, 15 December 2022

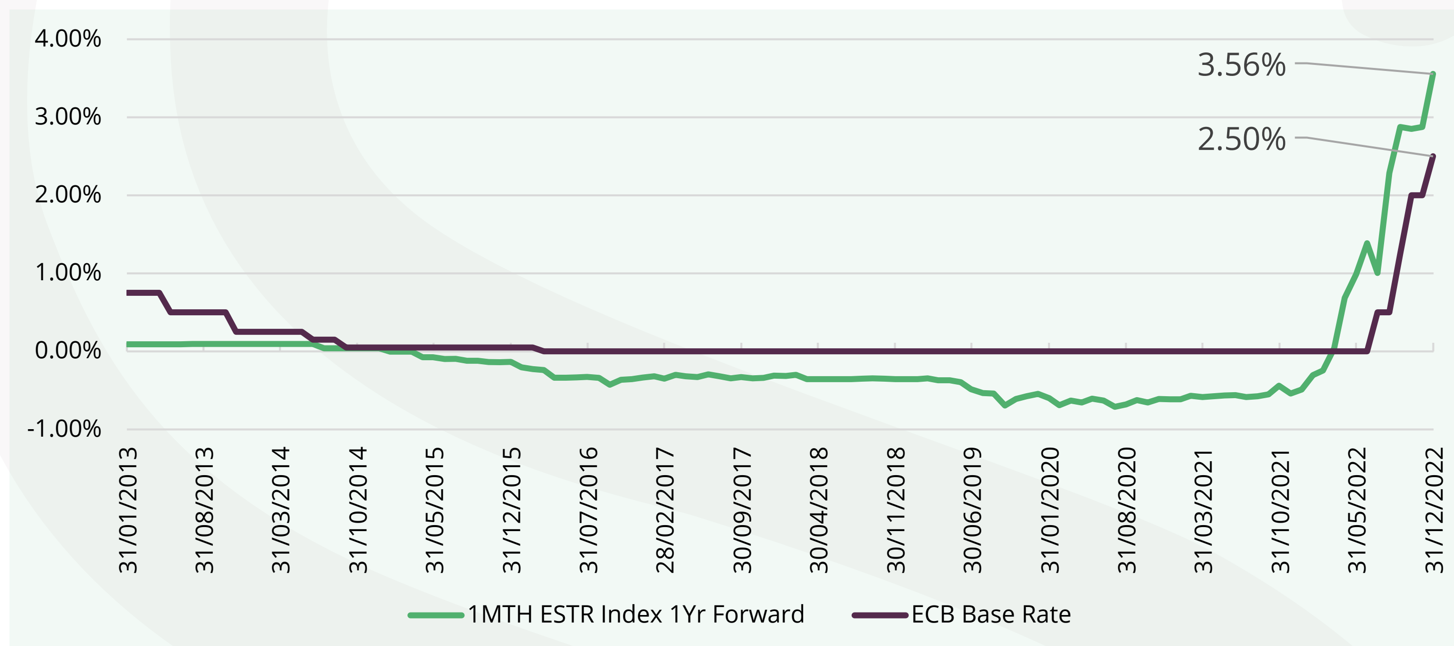
Interest rate changes, both increases and decreases, tend to have a lagged impact on the economy. It takes time to adjust to them, and we may not yet have felt the full effect of the recent moves as the ECB base rate has increased from 0% to 2.50% over the last year, with +1.25% in quarter four alone.

The ECB plans to continue to raise rates "significantly, at a steady pace" this year and indicated two more half-point hikes in early 2023 to try to tame inflation. Markets currently agree, pricing further hikes of somewhere around +1.50%. This could prove overly pessimistic if we are to see inflation turn meaningfully lower.

Along with rate increases, there will be a significant drain of liquidity. Bonds purchased during quantitative easing will roll off the ECB balance sheet and banks will see the expiration of longer-term loans. Both remove liquidity from the financial system, increasing the risk of volatility.

Overhanging this is slowing growth, which could develop into rolling recessions across the various economies.

ECB base rate and expected rate in 1Yr



Source: Setanta / Bloomberg

However, there is reason for hope in recent data – with German GDP, for example, coming in higher than expected, at +1.9% in 2022.

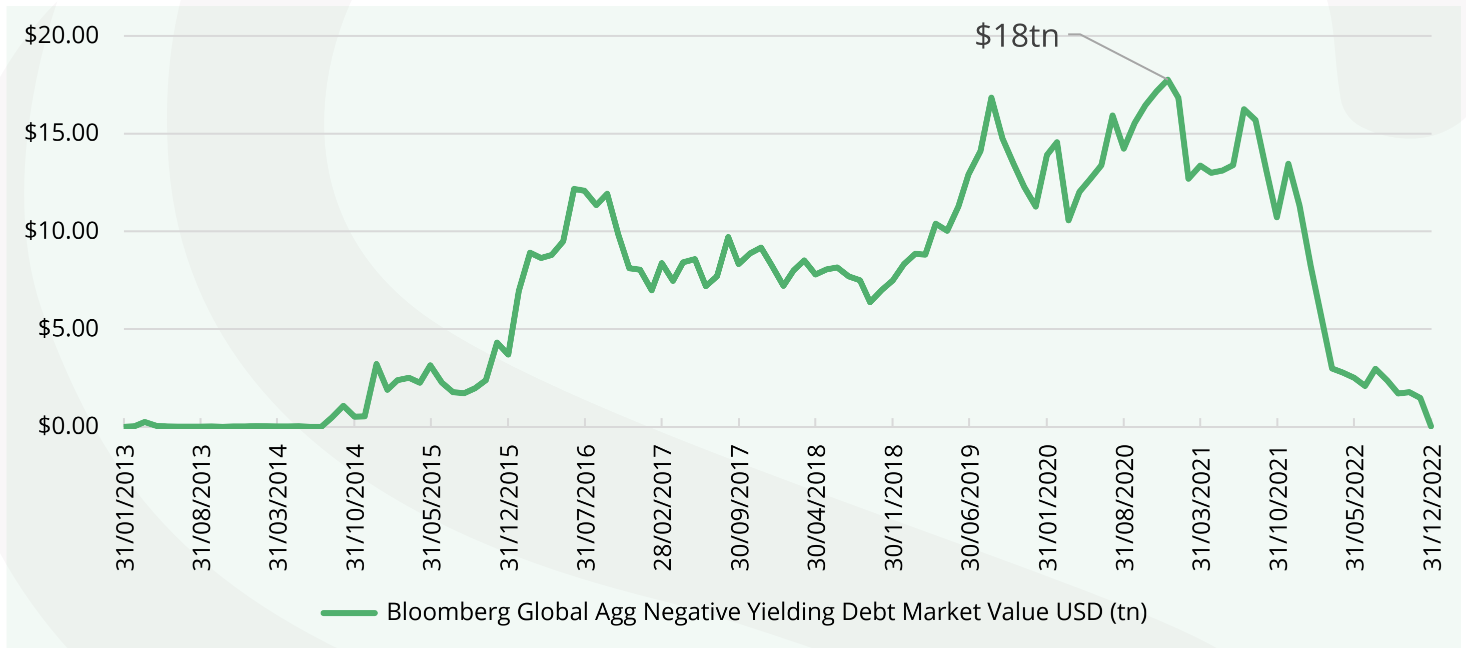
Equity versus bond positioning

For equities to offer decent long-term expected returns, stability in core inflation and interest rates is probably needed, alongside downward revisions to corporate earnings guidance, which is still too high given deteriorating fundamentals and the rising risk of recession.

Bonds, unlike equities, are easier to forecast, with the starting yield a good predictor of future returns. As yields have risen significantly, to the highest in decades in some instances, you can have more comfort investing for the longer term with the added benefit of them likely resuming their role as a reliable diversifier against equities.

The collapse in the quantity of negative yielding bonds – from $18 trillion worth, globally, to practically zero – marks a broad change in global bond regimes. In December, the Bank of Japan unexpectedly increased the range it would allow the 10-year Japanese government bond yield to trade at, from +/- 0.25% to +/- 0.50%.

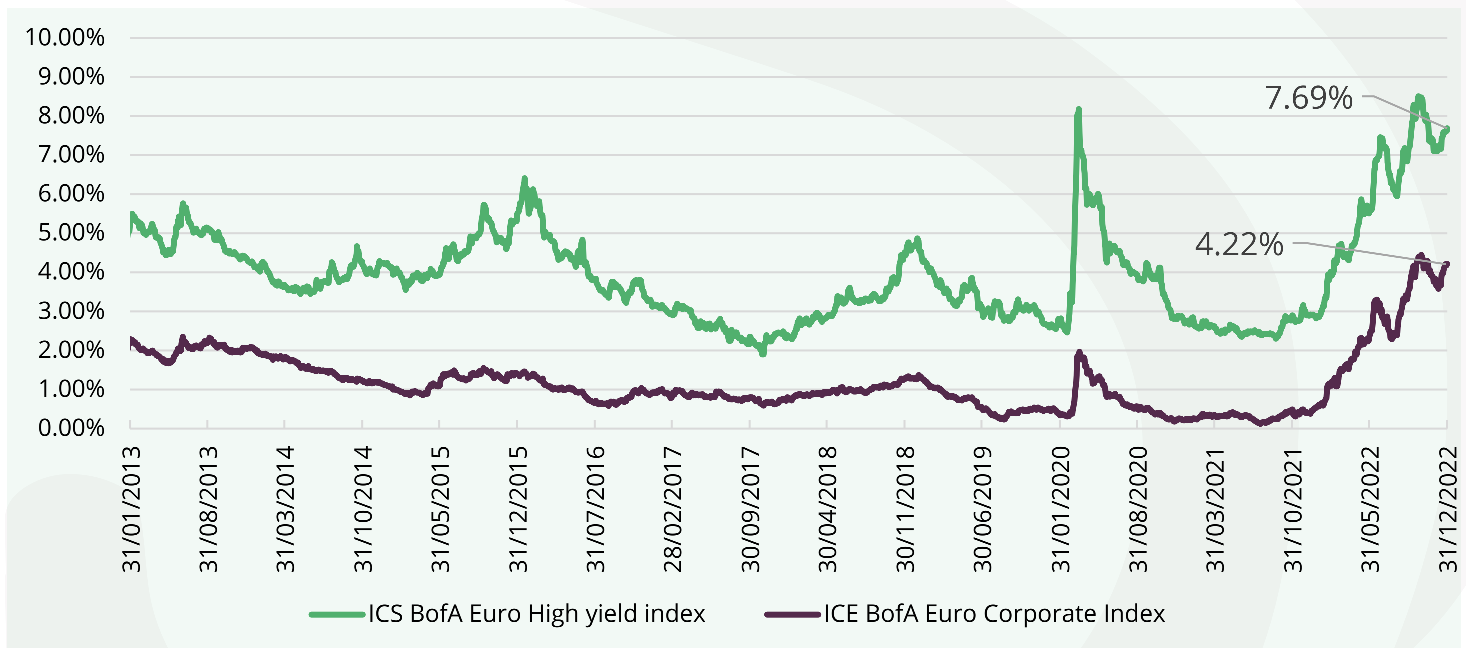
Negative yielding debt: market value



Source: Setanta / Bloomberg

In Europe, investment grade corporate bonds especially, and high yield somewhat, look attractive, with yields reaching 4% and 8% respectively over the quarter. Implied default rates from the spread offer considerable compensation, even in an economic downturn.

European yields: investment grade and high yield



Source: Setanta / Bloomberg

Opportunities

If a recession does become evident, equity weakness becomes more of a problem than bond weakness. High quality duration can protect multi-asset portfolios. Meanwhile, in equities, investing in quality at decent valuations – through strong balance sheets, steady cashflows and sound management – allows for more portfolio resilience.

Investors should look at the recent repricing of certain financial assets – bonds especially – as an opportunity to gain exposure at levels not seen in decades.

Meanwhile, if the economy manages to navigate away from a recession scenario – possibly through a combination of China reopening, a warmer winter resulting in lower gas prices in Europe and falling inflation in the US – there is ample exposure in the portfolio to risk assets to drive long-term expected returns.

David Ryan, CFA

Head of Multi-Asset Funds

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IMPORTANT INFORMATION

The Managed Fund is managed by Setanta Asset Management Limited and is a representative account of the Managed strategy. The performance shown is the performance of a representative account (ILA/CLI Setanta Managed Fund [H012]). For this life assurance product, investors should refer to the relevant policy conditions available through Irish Life and via www.irishlife.ie. The strategy is available on a separate account basis to institutional investors however current and prospective clients should not assume identical performance results to those shown would have been achieved for their account if it was invested in the strategy during the period. Clients of the firm may receive different performance than the representative account. Client performance may differ due to factors such as timing of investment(s), timing of withdrawal(s), client-mandated investment restrictions and the portfolio not being fully replicated for new accounts or new flows. Investors should consider the investment objectives, risks, charges and expenses carefully before investing. The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities. See 'WARNING' and IMPORTANT INFORMATION' below.

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