SEI UK Strategic Portfolios

Quarterly Investment Review

Q3 2020

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Summary

Market Overview

- It was another positive quarter for most risk assets on the back of continued, although still partial, reopening of economies, ongoing fiscal and monetary support and an encouraging rebound in economic activity.
- The best economic and stock market performance came from the major Asian economies – China, Taiwan and South Korea. Heavy tilts towards technology and advanced industrial sectors were a benefit in the current environment.
- UK equities continued to struggle, driven to a large extent by its sector composition. The underperformance of energy and financials weighed heavily on the overall fortunes of the UK stock market over Q3.
- A modest increase in UK bond yields, and a short lived rebound in inflation expectations, saw the value of UK core fixed assets decline over the quarter. US high yield debt performed well, thanks in part to a continued improvement in default expectations.
- Commodities had a strong quarter, though remain meaningfully down on a year-on-year basis. Gains were broad based with Silver, industrial metals and agricultural goods leading the way. Only Brent crude and heating oil were lower over the quarter.

Market Outlook

- Most countries exhibited some form of a V-shaped recovery during the third quarter, moving sharply off their low points in May and June. While the recent rise in infection rates across parts of the developed world has unnerved investors, we assume that future lockdowns to contain COVID-19 outbreaks will be far more limited in scope. For developed countries, treatments have improved, vulnerable populations appear to be better-protected, and younger, generally healthier people are accounting for a much larger share of confirmed new cases.
- A return to normal economic behaviour appears, to us, to ultimately depend on the distribution of one or more safe and effective vaccines. On that front, the news is mostly positive with a number of vaccines currently in clinical trials.
- In the meanwhile, consumer and business sentiment remains depressed, and the danger exists that the lack of additional income support in the US will drag down consumer spending into year end.
- On the political front, key concerns dominating investors' minds have been around which form Brexit will take, in essence whether a trade deal can be struck between the UK and EU, and the outcome of the US presidential elections. We expect clarity on both fronts over the course of the fourth quarter.
- The US presidential election will likely have a major impact on the US economy and financial markets. However we firmly believe that basing an investment decision around not only predicting the outcome of the election, but also the policies that would be proposed, how these policies will ultimately be modified by Congress and finally forecasting their impact on the economy and financial markets is unwise.
- It has been an unsettling year to date, and the next few months could prove critical to the future course of the global economy and financial markets. In uncertain times, we believe it is important to maintain a risk aware approach to wealth management through prudent planning that focusses on companies with strong fundamentals and reasonable valuations.

Stability Focused Funds

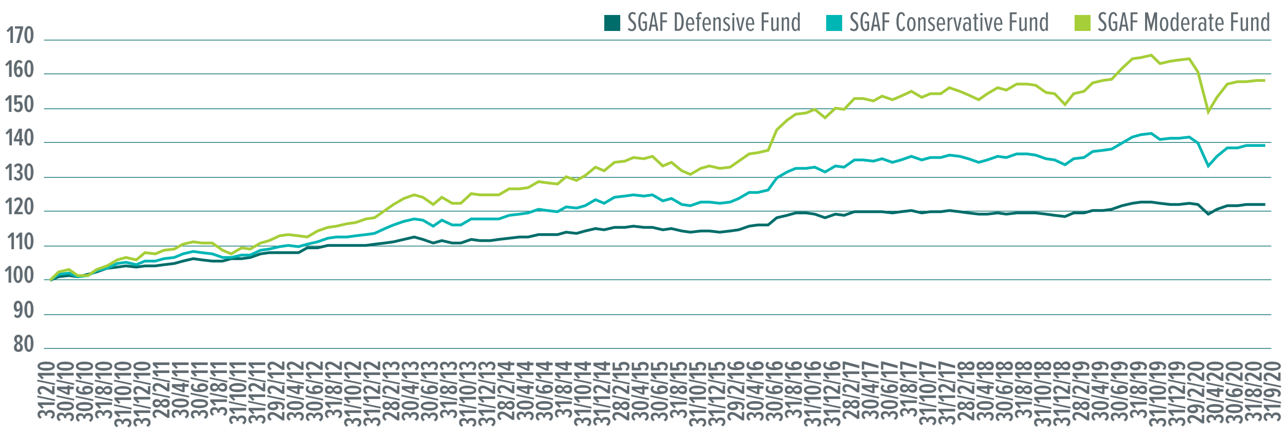
Performance

Figure 1 – Annualised performance of the Stability-Focused Strategic Portfolios

	3 month	Year-to-date	1 year	2 year*	3 year*	4 year*	5 year*
SEI Defensive Fund	0.21%	-0.08%	-0.61%	1.04%	0.64%	0.54%	1.40%
SEI Conservative Fund	0.43%	-1.44%	-2.39%	0.99%	1.07%	1.22%	2.75%
SEI Moderate Fund	0.27%	-3.58%	-4.41%	0.42%	1.08%	1.58%	3.87%

Source: SEI, as at 30 September 2020. Net of fees, Sterling Wealth A Distributing share class. Past performance is not a reliable indicator of future results.
*Indicates annualised data.

Figure 2 – Long-term performance of the Stability-Focused Strategic Portfolios



Source: SEI, as at 30 September 2020. Net of fees, Sterling Wealth A Distributing share class. Net Asset Values rebased to 100 at start of period. Past performance is not a reliable indicator of future results.

Portfolio Contributions

Figure 3 – Portfolio performance drivers within the Stability-Focused Strategic Portfolios

Q3 Performance Drivers	Positioning	Key Asset Class(es)	Key Manager(s)
– (Absolute)	Equity exposures	• Global Managed Volatility • UK Equity	
+ (Absolute)	Credit Commodities	• Global Opportunistic • High Yield • Commodities	
+ (Relative)	Overweight off-index credit, select emerging markets, overweight Italian Sovereign bonds Underweight and positive selection within Energy. Overweight CCC rated bonds Overweight higher yielding countries and hard currency corporate debt	• Global Fixed Income • High Yield • Emerging Market Debt	• Brandywine, Colchester, Insight • Brigade, Benefit Street Partners • Stoneharbour, Marathon, Neuberger Berman

Figure 4 – Portfolio themes within the Stability-Focused Strategic Portfolios

Theme	Active Positioning	Rationale / Adjustment
Relative value in sovereign markets	Overweight select local currency emerging markets (Mexico, Colombia, Indonesia) Overweight Italy	Emerging market yields remain attractive versus developed markets as do emerging market currencies. European Central Bank ("ECB") asset purchase programmes will continue to support peripheral European debt.
Inflation linked securities remain attractive	Modest overweight to US inflation linked securities	Market implied inflation expectations remain below 2% while the US Federal Reserve's new framework could tolerate higher inflation for a period of time. Fiscal stimulus, pent-up demand and the trend to localise supply chains could add to inflationary pressure over the medium term.
Environment remains supportive for credit assets	Modest overweight credit risk	Credit should continue to benefit from favourable technical support, including low or negative yields on government bonds and central bank asset purchase programmes.

These are the views and opinions of SEI which are subject to change. They should not be construed as investment advice.

Growth Focused Funds

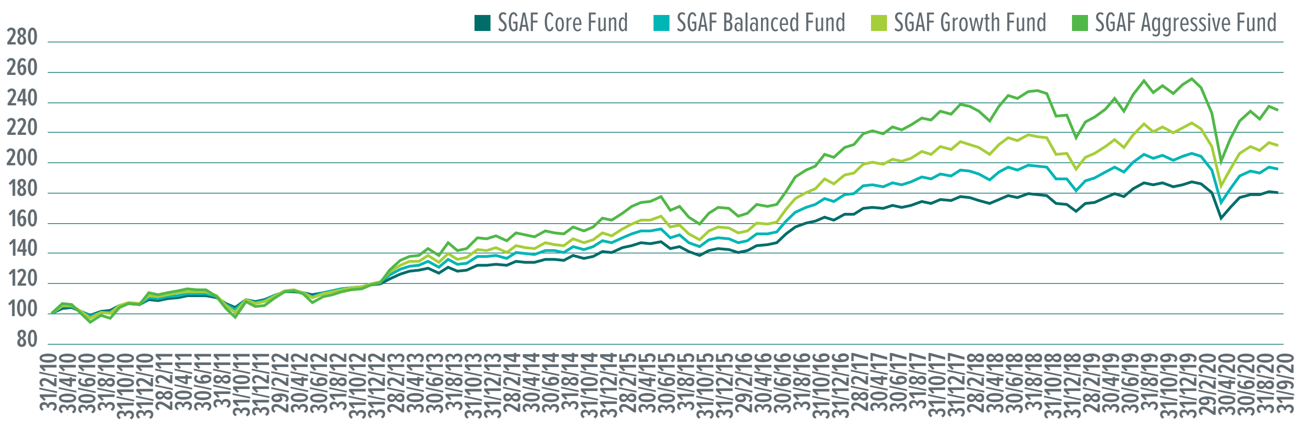
Performance

Figure 5 – Annualised performance of the Growth-Focused Strategic Portfolios

	3 month	Year-to-date	1 year	2 year*	3 year*	4 year*	5 year*
SEI Core Fund	0.50%	-3.81%	-3.57%	0.45%	1.38%	2.80%	5.35%
SEI Balanced Fund	0.61%	-5.21%	-4.51%	-0.37%	1.15%	3.20%	6.28%
SEI Growth Fund	0.47%	-6.5%	-5.32%	-1.11%	0.92%	3.71%	7.23%
SEI Aggressive Fund	0.31%	-8.27%	-6.48%	-2.35%	0.94%	4.32%	8.02%

Source: SEI, as at 30 September 2020. Net of fees, Sterling Wealth A Distributing share class. Past performance is not a reliable indicator of future results.
*Indicates annualised data.

Figure 6 – Long-term performance of the Growth-Focused Strategic Portfolios



Source: SEI, as at 30 September 2020. Net of fees, Sterling Wealth A Distributing share class. Net Asset Values rebased to 100 at start of period. Past performance is not a reliable indicator of future results.

Portfolio Contributions

Figure 7 – Portfolio performance drivers within the Growth-Focused Strategic Portfolios

Q3 Performance Drivers	Positioning	Key Asset Class(es)	Key Manager(s)
– (Strategic)	Low volatility equities (Core, Balanced)	• Global Managed Volatility	• LSV
+ (Strategic)	Commodities (Core, Balanced)	• Commodities	• Threadneedle
+ (Active)	Tactical Asset Allocation	• Gold	•SEI
+ (Active)	Active management within Fixed Income (Core, Balanced, Growth)	• UK and Global Fixed Income • High Yield • Emerging Market Debt	• PIMCO (UK), Brandywine, Colchester (Global) • Brigade, Benefit Street • Stoneharbour, Marathon, Neuberger Berman
– (Active)	Underweight Momentum, overweight Value (Underweight megacaps and technology, overweight financials)	• Global Equity • US Large Companies • US Factor Allocation	• LSV, SNAM • Shafer Cullen, LSV • SEI

Figure 8 – Portfolio themes within the Growth-Focused Strategic Portfolios

Theme	Active Positioning	Rationale / Adjustment
Rebound in global economic activity	Overweight Valuation focused managers, underweight Momentum	Large dispersions between cheap and expensive stocks point towards a positive outlook for Value
Risks remain	Gold	Gold is a potential store of value and portfolio diversifier

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Portfolio Commentary

Portfolio Positioning

Financial markets continued to recover over the third quarter as the panic around COVID-19 eased and the prospect of ongoing policy support became entrenched in investors' minds. Despite a reversal in fortunes during September, the established trend of large technology and growth stocks leading returns remained in place for the third quarter.

While risks assets in general fared well over the quarter, UK equities did not, with the FTSE All Share Index almost 3% lower. Index heavyweights in the energy sector fell sharply due to the ongoing challenges of a painful transition towards cleaner energy, while UK banks continued to face headwinds. With short term interest rates anchored amid speculation that the Bank of England may be considering negative interest rates, a modest move up in longer term rates meant that UK government bonds also ended the quarter lower.

For the quarter as a whole, returns across the range were remarkably similar. The Stability Focused funds returned between 0.2% and 0.4%, while the Growth Focused funds generated between 0.3% and 0.6%.

Stability Focused Portfolios

The SEI Defensive, Conservative and Moderate, with a focus on wealth preservation, have a significant exposure to defensive, lower volatility equities. The current risk-on environment coupled with strong performance from the more volatile mega-cap technology companies meant that low volatility equities lagged the broad market this quarter. Of the three active managers employed within the Global Managed Volatility strategy, LSV Asset Management struggled given their value orientation, while Wells Fargo proved more resilient due to their preference for higher quality, more profitable businesses within the low-volatility space.

With strong gains from commodities and continued outperformance of many areas of credit, exposure to these asset classes buoyed overall returns for the Stability Focused funds into positive territory for the quarter.

From an active management perspective, the funds' fixed income strategies all performed well against their respective market benchmarks. Our global fixed income component benefitted from select positions in emerging markets, an overweight to Italian government debt and an off-index position in US inflation linked bonds. Brandywine, Colchester and Insight all added meaningfully to performance over the quarter.

Within High Yield, Brigade and Benefit Street Partners were strong contributors. Overall, a persistent overweight to CCC rated bonds contributed as the ongoing rebound in economic activity and supportive policies fostered a broadening credit recovery. The energy sector struggled over the quarter and our underweight to this part of the market, and good security selection within energy, further boosted returns.

In Emerging Market Debt, our allocation to hard currency corporate bonds contributed positively to performance. Beyond that, key overweights to Mexico (on expectations of a continued recovery), Argentina and Ecuador (having reached restructuring deals with bondholders) as well as an underweight to Turkey were rewarded. Our two hard currency specialist managers, Stone Harbor and Marathon, were top contributors over the quarter.

Growth Focused Portfolios

For the SEI Core, Balanced, Growth and Aggressive funds, exposure to equities outside of the UK, as well as exposure to credit and commodities for all except the SEI Aggressive portfolio, drove overall performance for the quarter.

With continued strong performance from the largest companies, and growth companies for the most past outpacing value stocks, the performance of our regional and global equity exposures fell short of overall market returns over the quarter. Relative performance continues to be driven by our value bias, and underweights to the largest information technology names in the US.

Within Global Equities, strong performance from INTECH and Lazard, both Momentum managers, helped partially mitigate the underperformance as did Rhicon, our currency manager, who benefitted from elevated levels of volatility in currency markets and recorded another strong quarter. While value generally disappointed, Towle & Co, a US small cap deep value manager, defied the trend to post a positive outcome over the quarter, benefitting from a cyclical value rebound in US small caps as well a good stock selection.

Active Asset Allocation

A new tactical asset allocation position, a 3 year option that will benefit from a rise in 30 year US interest rate swaps, was entered into over the quarter.

Along with the swift and aggressive monetary and fiscal response to the COVID-19 crisis, US policymakers announced a major shift in interest-rate policy. Rather than taking pre-emptive action against inflation when the US unemployment rate reaches a very low level that might cause inflation to rise, the US central bank will now wait for an actual worsening of inflation pressures before responding.

Given the sheer amount of stimulus that has been poured into the US economy, with more stimulus likely, we find the market's inflation expectations and implied path for long-term interest rates to be overly pessimistic. While our base case scenario is not for a sharp increase in US rates, we view the market as not fully appreciating the possibility of such a move, making an options implementation an attractive and inexpensive route through which to provide protection against possibly higher long term US rates.

Our most significant position continues to be our positon in gold, which was unchanged over the quarter. We continue to view gold as a safe haven asset during periods of market volatility, a portfolio diversifier and, with soaring global debt levels, increasingly likely to be seen as a store of value.

Positioning

Within the funds' fixed income components, we have not significantly changed our positioning. We do though believe the environment remains supportive for credit and as such we retain a modest credit overweight in our higher grade fixed income strategies.

While forward looking, absolute returns on government and investment grade positions are likely to be muted, we do believe that fixed income continues to play an important role in the portfolios as it remains one of the few asset classes that has a somewhat persistent negative correlation to equities over time.

Within equities, we maintain conviction in our positioning. Our portfolios are positioned for a rotation out of the favoured few, into those sectors and industries that have lagged sharply over the year. The exact timing of, and catalyst for, that rotation is difficult to say, but should coincide with increased investor confidence that the world is returning to some form of normality. Expectations for subsiding COVID-19 infection rates following the introduction of one or more vaccines could well be a trigger. Ultimately, valuations matter and with dispersions between expensive and cheap stocks at or near all-time highs, we continue to hold an exceptionally favourable outlook for our positioning.

Global Market Performance

Representative market indices

Figure 9 – Major Market Data

Equity Indices	3 month	YTD	1 year	2 year*	3 year*	4 year*	5 year*
MSCI World Index *(Net) (Hedged) (GBP)*	6.2%	-0.3%	6.8%	4.0%	6.4%	9.0%	9.1%
FTSE UK Series All Share Index *(GBP)*	-2.9%	-19.9%	-16.6%	-7.5%	-3.2%	0.4%	3.5%
Russell 1000 Index *(Net 30%) (USD)*	9.3%	6.0%	15.4%	9.2%	11.7%	13.2%	13.4%
MSCI Europe ex UK Index *(Net) (EUR)*	1.4%	-7.9%	-3.0%	1.7%	1.2%	5.5%	4.8%
MSCI Pacific ex Japan Index *(Net) (USD)*	2.0%	-11.3%	-6.1%	-1.7%	0.3%	3.6%	6.7%
Tokyo Stock Exchange TOPIX *(JPY)*	5.2%	-3.4%	4.9%	-3.1%	1.4%	7.7%	5.2%
MSCI Emerging Markets Index *(Net) (GBP)*	4.7%	1.3%	5.4%	4.5%	3.7%	7.2%	12.5%

Fixed Income	3 month	YTD	1 year	2 year*	3 year*	4 year*	5 year*
Bank of America Merrill Lynch UK Gilts All Stocks Index *(GBP)*	-1.2%	7.6%	3.5%	8.3%	5.7%	3.3%	5.1%
Bloomberg Barclays Global Treasury Index *(Hedged) (GBP)*	0.4%	4.4%	2.8%	6.0%	3.8%	2.3%	3.2%
Bloomberg Barclays Global Aggregate Index, Hedged *(GBP)*	0.6%	4.2%	3.3%	6.0%	3.7%	2.5%	3.3%
Bloomberg Barclays Global Aggregate ex-Treasury Index *(Hedged) (GBP)*	0.9%	3.8%	3.8%	6.0%	3.5%	2.7%	3.4%
Bank of America Merrill Lynch US High Yield Constrained Index, Hedged *(GBP)*	4.3%	-1.5%	0.6%	2.4%	2.0%	3.5%	5.2%
50/50 JP Morgan EMBI Global Dividend & JP Morgan GBI-EM Global Dividend *(GBP)*	-0.9%	-2.7%	-3.0%	4.7%	1.7%	2.2%	6.6%

Cash	3 month	YTD	1 year	2 year*	3 year*	4 year*	5 year*
LIBOR 3 Month GBP *(TR) (GBP)*	0.0%	0.3%	0.5%	0.7%	0.6%	0.6%	0.6%

Commodities	3 month	YTD	1 year	2 year*	3 year*	4 year*	5 year*
Oil *(ICE Brent Crude)*	1.3%	-30.9%	-24.4%	-24.3%	-8.4%	-8.1%	-7.6%
Gold *($/oz)*	5.9%	24.3%	28.1%	25.8%	13.8%	9.4%	11.1%
Bloomberg Commodity Index *(USD)*	9.1%	-12.1%	-8.2%	-7.4%	-4.2%	-3.2%	-3.1%

Commodities	9/30/20	6/30/20	12/31/19	9/30/19	9/30/18	9/30/17	9/30/16	9/30/15
Oil *(ICE Brent Crude)*	$42.30	$41.76	$61.22	$55.93	$73.88	$55.01	$59.28	$62.80
Gold *($/oz)*	$1,885.82	$1,780.96	$1,517.27	$1,472.49	$1,190.88	$1,279.75	$1,315.87	$1,115.09
Bloomberg Commodity Index *(USD)*	151.2189	138.6382	172.0042	164.7214	176.3125	171.8648	172.3635	176.9206

Source: Bloomberg. Data to 30 September 2020.
*Periods greater than 1 year are annualised.
Data refers to past performance. Past performance is not a reliable indicator of future results.

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To speak with an SEI specialist, contact:

sei_intermediaries@seic.com
+44 (0)20 3810 8001

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- *Fixed Income securities are subject to credit risk and may also be subject to price volatility and may be sensitive to interest rate fluctuations.*
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