

SEI UK Strategic Portfolios

Quarterly investment review.

Q4 2021

For use by advisers of regulated intermediaries in
accordance with all applicable laws and regulations.

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Summary

Market overview

- Sky-high COVID-19 cases, a volatile equity-market rally, and worry over rising interest rates can describe both the first and last weeks of 2021. An obvious is that the prospect of widespread vaccination became reality, with 9 billion vaccine doses administered worldwide through the end of 2021, rendering roughly 49% of the global population fully vaccinated.
- In financial markets, the fourth quarter began in the shadow of September’s selloff, which was the most extended shakeout of 2021. After recovering in October, equities vaulted higher through mid-November before unrestrained inflation, tightening central bank policy, and the emergence of the omicron variant combined for a choppy climb to finish the year.
- Across the UK, eurozone, and US, short-to-medium-term government bond rates increased during the fourth quarter, while long-term rates declined, resulting in flatter yield curves. Fourth-quarter fixed-income performance mirrored the full year: inflation-indexed bonds were the top performers, followed by high yield. Most other sectors were mildly negative given the impact of rising rates, but global bonds were down by more due to currency effects. Local-currency emerging-market debt had the steepest losses for the quarter and year.

Stability-Focused Funds

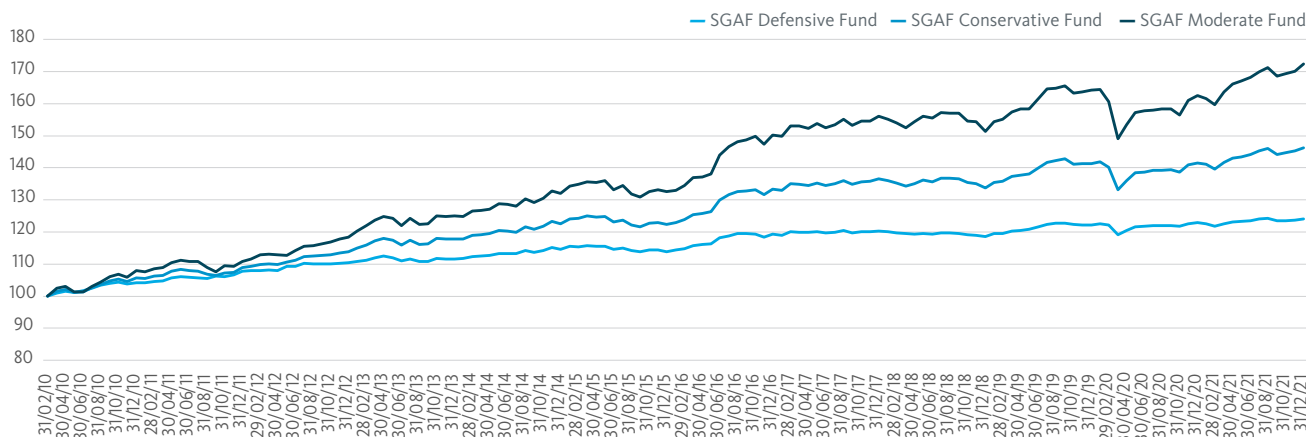
Performance

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	0.40%	0.85%	0.85%	0.75%	1.50%	0.77%	0.77%
SEI Conservative Fund	1.38%	3.25%	3.25%	1.69%	3.02%	1.73%	1.85%
SEI Moderate Fund	2.34%	6.12%	6.12%	2.49%	4.46%	2.52%	2.80%

Source: SEI, as at 31 December 2021. 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 31 December 2021. 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

Q4 Performance drivers	Positioning	Key asset class(es)	Key manager(s)
<p>+ (Absolute)</p>	Equity exposure	<ul style="list-style-type: none"> • Global managed volatility • UK equity (moderate only) 	
	Inflation-sensitive assets	<ul style="list-style-type: none"> • Commodities, UK inflation-linked bonds 	
<p>- (Absolute)</p>	High-grade bonds	<ul style="list-style-type: none"> • UK core fixed income 	
	Diversifying fixed-income exposure into emerging markets	<ul style="list-style-type: none"> • Emerging-market debt, global multi-asset income 	
Active management			
<p>+ (Active)</p>	Credit manager benefitted from benign spread environment and positive carry portfolio, while underweight duration in H1 and preference for longer duration securities in H2 aided performance.	<ul style="list-style-type: none"> • UK core fixed income 	<ul style="list-style-type: none"> • Wellington Management Co (until July 2021) • M&G Investments Management Ltd (from July 2021) • PIMCO Europe
	<p>Positive stock selection (notably in the consumer discretionary sector) and a tilt to cheaper value stocks enjoying positive earnings momentum.</p> <p>Overweight to bank loans and basic industry and positive selection within basic industry, services and energy sectors of the high yield market.</p>	<ul style="list-style-type: none"> • UK equity (moderate only) • High yield 	<ul style="list-style-type: none"> • Jupiter Asset Management • Invesco Asset Management • Brigade Capital Management • JP Morgan Asset Management • Ares Asset Management

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

Theme	Active positioning	Rationale/adjustment
Relative value in development market sovereign bonds	<p>Underweight duration in most core markets (UK, US, Core Europe) but with select overweights (Australia)</p> <p>Overweight select local currency emerging markets (Mexico, Colombia)</p>	<p>Developed-market real yields remain deeply negative. Inflation likely to remain structurally higher than in recent decades, even after supply chain issues recede.</p> <p>Emerging-market yields remain attractive versus developed markets. Many EM central banks took a proactive stance on inflation and are therefore much further ahead than developed countries in their hiking cycles. Emerging-market currencies generally remain undervalued.</p>
Environment remains supportive for credit assets	<p>Modest overweight credit risk, with a lower quality and shorter maturity bias. Favouring sectors likely to benefit from a reflationary environment.</p>	<p>Preference for higher-yielding, shorter-dated credit as it provides a yield pickup with less interest rate risk. Underweight UK government in favour of securitised and corporate sectors. Preference for financials within corporate debt and overweight to mortgage credit risk transfer securities as an attractive source of credit risk with lower interest rate sensitivity.</p>

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Growth-Focused Funds

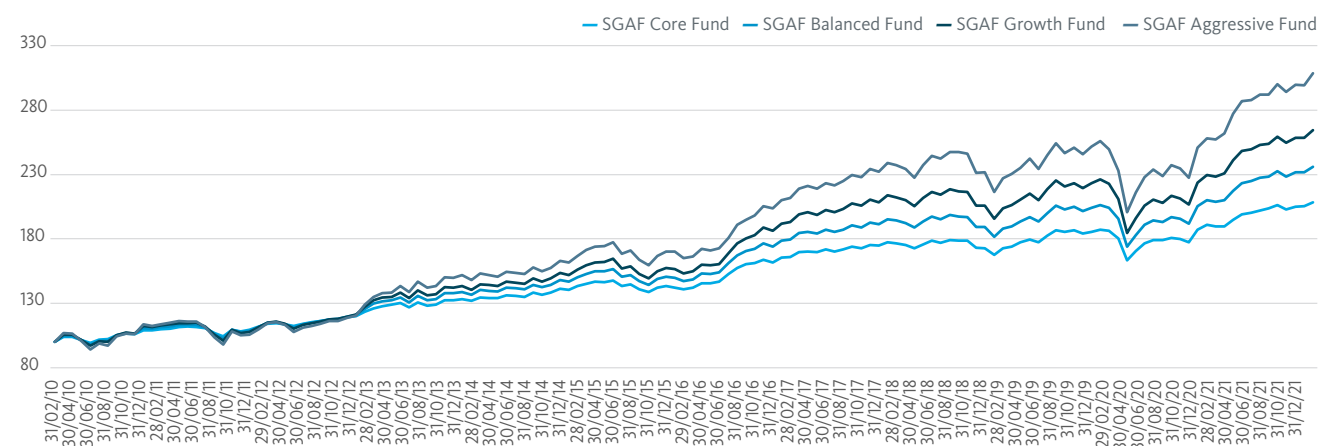
Performance

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	2.66%	9.14%	9.14%	5.44%	7.50%	4.07%	4.67%
SEI Balanced Fund	3.30%	12.37%	12.37%	6.93%	9.14%	4.83%	5.71%
SEI Growth Fund	3.83%	15.28%	15.28%	8.12%	10.58%	5.47%	6.63%
SEI Aggressive Fund	4.88%	19.56%	19.56%	9.85%	12.51%	6.62%	7.98%

Source: SEI, as at 31 December 2021. 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 31 December 2021. 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

Q4 Performance drivers	Positioning	Key asset class(es)	Key manager(s)
+ (Strategic)	Inflation-sensitive assets (core, balanced, growth)	<ul style="list-style-type: none"> UK inflation-linked bonds, commodities 	
- (Strategic)	<p>Small-cap equity exposure</p> <p>Diversifying fixed-income exposure through emerging-market debt (core, balanced, growth)</p>	<ul style="list-style-type: none"> US small companies Emerging-market debt High yield Global multi-asset income 	
Active management			
	Exposure to cheaper companies but with higher quality in the US	<ul style="list-style-type: none"> US factor allocation 	<ul style="list-style-type: none"> SEI
	Owning cheaper companies with higher quality. Companies with solid cash flow generation, reasonable valuations, and high profitability outperformed	<ul style="list-style-type: none"> US small companies 	<ul style="list-style-type: none"> Hillsdale Investment Management LSV Asset Management Copeland Capital Management
+ (Active)	Positive stock selection (notably in the consumer discretionary sector) and a tilt to cheaper value stocks enjoying positive earnings momentum	<ul style="list-style-type: none"> UK equity 	<ul style="list-style-type: none"> Jupiter Asset Management Invesco Asset Management
	Exposure to global equity factors (value, momentum, quality) and positive selection from managers within those factors	<ul style="list-style-type: none"> Global equity 	<ul style="list-style-type: none"> Lazard Asset Management Poplar Forest Capital Fiera Capital Corporation
	Tactical overweight to commodities and equities	<ul style="list-style-type: none"> Dynamic asset allocation 	<ul style="list-style-type: none"> SEI

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

Theme	Active positioning	Rationale/adjustment
Tactically positioned for reflation and higher interest	Positioned to benefit from a rise in both longer-term and short-term US interest rates, US inflation expectations, commodities and equity markets.	Policy dynamics create a favourable environment for more economically sensitive areas of the capital markets to outperform in 2022. Significant risks to the upside in terms of the duration and intensity of the current inflationary pressures could see a more aggressive tightening cycle from Federal Reserve.
Environment remains supportive for credit assets	Modest overweight credit risk, with a lower quality and shorter maturity bias. Favouring sectors likely to benefit from a reflationary environment.	Preference for higher-yielding, shorter-dated credit as it provides a yield pickup with less interest rate risk. Underweight UK government in favour of securitised and corporate sectors. Preference for financials within corporate debt and overweight to mortgage credit risk transfer securities as an attractive source of credit risk with lower interest rate sensitivity.
Outlook for value remains strong	Preference for value	<p>Elevated valuation dispersions have a long way to normalise. Consumers remain in a strong position. Undervalued energy stocks bolstered by growing energy demand and limited supply as a result of underinvestment.</p> <p>Undervalued banks boosted by steepening yield curves and rising loan demand.</p> <p>Japanese exporters increasingly attractive given undervalued yen.</p> <p>Highly rated growth stocks face headwinds from elevated multiples.</p>

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Market commentary

The final quarter of 2021 began in the shadow of September's selloff, which was the most extended shakeout of 2021. After recovering in October, equity markets continued to move higher through mid-November before higher inflation releases, which brought with them the increasing prospect of tightening central bank policy, and the emergence of the omicron variant combined to make for a more volatile end to the year.

Against this backdrop, the MSCI All Countries World Index returned 6.2% in GBP terms for the fourth quarter, ending the year 19.6% higher. The US was the top-performing major equity market for the quarter and the calendar year, the European & UK markets both performed well, and Japan lagged its developed-market counterparts. Emerging markets lost ground over the quarter and year, with China delivering the deepest loss among the major markets in 2021 following a slowing Chinese economy and government regulations.

Faced with increased uncertainty over the quarter, investors shifted towards perceived safety—namely lower risk, mega cap, and higher-quality stocks across both traditional defensive sectors, such as utilities, consumer staples, and healthcare, and more cyclical growth sectors, such as luxury goods and specialty industrials. The result, from a style perspective, was that quality and low-volatility factors outperformed over the quarter. Returns from momentum were neutral in US large cap but positive outside of this segment. And results from value were mixed but generally faced headwinds due to higher exposures to energy, consumer discretionary, and financials, all of which tend to struggle during periods of rising COVID-19 concerns and a general flight to safety.

For 2021 as a whole, the environment was generally good for all three of the Portfolio's primary equity factors. The year saw clear outperformance from those higher-quality stocks whose earnings continued to beat expectations and exhibited strong positive momentum. Cyclical stocks that recovered as economies came out of COVID lockdowns also performed strongly—IT, financials, energy, and industrials all led the way—while utilities staples, and discretionary lagged.

Across fixed-income markets, short-to-medium-term government bond rates in the UK, eurozone, and US increased, while long-term rates declined, resulting in flatter yield curves over the quarter. The performance of bond markets over the fourth quarter mirrored the full year: inflation-indexed bonds were the top performers, followed by high-yield corporate bonds. Most other

segments were mildly negative given the impact of rising rates. Local-currency emerging-market debt experienced the steepest losses for the quarter and year.

Stability-Focused Funds

The SEI Defensive, Conservative, and Moderate Funds returned between 0.4% and 2.3% for the final quarter of 2021, with gains of between 0.9% and 6.1% for the calendar year.

The Portfolios' strategic positioning was broadly neutral for the quarter and positive for the year. Diversifying fixed-income exposure across high-yield and emerging-market debt worked against the Portfolios over both the quarter and the year, particularly on the back of the headwinds faced by emerging markets. However the Portfolios' allocation to lower-volatility stocks and inflation-linked bonds were able to offset this over the quarter, and those allocations along with the commodities exposure were beneficial over the year.

Active management decisions were rewarded across the quarter and the year, thanks to positioning with UK equities, UK core fixed income, and high yields.

Within UK equities, the combination of positive stock selection (notably in the consumer discretionary sector) and a tilt to cheaper value stocks enjoying positive earnings momentum benefitted the Portfolios. At the manager level, Invesco was the strongest performer over both the quarter and the year. The manager follows a quantitative investment approach that favours higher-quality value stocks enjoying positive momentum. With the ability to take short positions in lowly rated stocks, their approach came to the fore this year. The Portfolios' UK value manager, Jupiter, also performed strongly over the year due primarily to favourable style tailwinds, although these were mitigated in the final quarter by stock selection in financials.

UK core fixed income benefitted from a benign spread environment and positive carry portfolio provided by PIMCO (UK credit mandate), while being underweight duration in the first half of the year (through Wellington) and preference for longer duration securities in the second half of the year (M&G, who replaced Wellington in July) aided performance.

Finally the Portfolios benefitted from an overweight to bank loans and basic industry and positive selection within the basic industry, services, and energy sectors of the high-yield market. The high-yield mandates managed by Brigade, JP Morgan and Ares all performed well over year.

Growth-Focused Funds

The SEI Core, Balanced, Growth, and the equity-only Aggressive Fund returned between 2.7% and 4.9% for the fourth quarter, and between 9.1% and 19.6% for 2021.

The Portfolios' strategic positioning proved to be a mild headwind to performance over both the quarter and the year. Exposure to small-cap companies was not rewarded as smaller companies lagged their larger counterparts over both periods. With the exception of the Aggressive Portfolio, diversifying fixed-income exposure across high-yield and emerging-market debt worked against the Portfolios, particularly on the back of the headwinds faced by emerging markets. However, this was somewhat offset by exposure to inflation-linked bonds and commodities.

From an active management perspective, the Portfolios' various equity components outperformed over the fourth quarter and the year as a whole. Within UK equities, the combination of positive stock selection (notably in the consumer discretionary sector) and a tilt to cheaper value stocks enjoying positive earnings momentum benefitted the Portfolios. At the manager level, Invesco was the strongest performer over both the quarter and the year. The manager follows a quantitative investment approach that favours higher-quality value stocks enjoying positive momentum. With the ability to take short positions in lowly rated stocks, their approach came to the fore this year. The Portfolios' UK value manager, Jupiter, also performed strongly over the year due primarily to favourable style tailwinds, although these were mitigated in the final quarter by stock selection in financials.

The Portfolios' allocation to US equity factors, through the SEI US Factor Allocation Fund, was also strongly beneficial over the year. Exposure to cheaper companies but with higher quality on average was the dominant driver within this component. The Portfolios also benefitted from significant outperformance within smaller-cap stocks. As market participants became more discerning, higher-risk and lower-quality stocks—those with poor earnings momentum, speculative revenue growth, or that looked very overvalued—underperformed markedly. The net result was strong outperformance from the Portfolios' selected US and Pan European small-cap managers for both the fourth quarter and the year as a whole.

Within emerging-equity markets, concerns over a slowing Chinese economy and uncertainties surrounding its e-commerce regulations saw quality and momentum

outperform over the quarter, and mildly positive results from value. While all of the Funds' underlying emerging-market equity managers outperformed over the period, emerging Asia drove the bulk of outperformance, where positive results in IT and an underweight to the region's healthcare stocks contributed strongly.

Across the fixed-income segments, performance was positive, largely thanks to good performance from the Portfolios' core fixed-income and high-yield managers. Within high yield, the Portfolios benefitted from an overweight to bank loans and basic industry and positive selection within the basic industry, services and energy sectors. Brigade, JP Morgan and Ares all performed well over year.

Tactical asset allocation

The contribution from the Growth-Focused Portfolios' tactical asset allocation positions were broadly neutral over the quarter, and strongly positive for the year as a whole. Over the fourth quarter, our tactical overweight to equities and 10-year US inflation expectations were marginally positive, commodities were neutral, and positions designed to benefit from higher yields in the US were a headwind. For the 2021, the Portfolios' commodities exposure was the largest contributor to overall results, followed by the equity and US inflation positions.

In terms of our overall positioning, we continue to express a diversified 'reflation' theme in the Portfolios. During the quarter, we initiated a position that allows the fund to express a view on the terminal federal funds (i.e., the rate that will be reached by the end of the next hiking cycle), which we believe may be underpriced in the current market and still reflective of a transitory view of the current inflationary pressures. We see significant risks to the upside in terms of the duration and intensity of the current inflationary pressures, and therefore to the speed and magnitude of the expected Federal Reserve tightening cycle, given easy financial conditions, the potential for additional fiscal stimulus, and a still tight labour market.

During the quarter, we also trimmed the tactical overweight to commodities. While we continue to maintain a favourable view on commodities, given the strong performance in 2021, we decided to take some profits.

Outlook and positioning

Equity markets stumbled in late 2021, owing to nervousness over the latest COVID-19 surge. This wave, too, shall pass. We remain optimistic that global growth will accelerate as the omicron wave fades. Although there have been pockets of speculative behaviour in some areas of the financial world, we do not see the sort of widespread frenzy that would point to a serious equity correction in 2022. The economy would have to slow precipitously for reasons other than the temporary impact stemming from COVID-19 mobility restrictions; the trend in earnings would need to flat-line or turn negative.

We expect a gain in overall US economic activity of around 4% in 2022—appreciably above the economy’s long-term growth potential of 2%. We also expect other countries to continue to post above-average growth as they recover from the past two years’ worth of lockdowns and shortages. With the major exception of China, which continues to pursue a zero-COVID-19 policy, most countries are unlikely to shut down their economies as fiercely or for as long as they did in 2020.

We remain optimistic that growth in the major economies will be buoyed by the strong position of households. In the US, household cash and bank deposits were still almost \$2.5 trillion above the pre-pandemic trend as of the end of September. This total is equivalent to almost 14% of disposable personal income. Excess savings in the UK, meanwhile, has reached 10.6% of annual personal disposable income. Euro-area bank balances aren’t quite as high, but still amount to 5% of after-tax income.

The year ahead promises to be another one of extremely tight labour markets. We think more people will return to the workforce as COVID-19 fears fade, but there likely will still be a tremendous mismatch of demand and supply.

In our view, inflation continues to be a risk due to labour market shortages and higher raw materials cost. While central bank stimulus is set to slow down, corporate profits have remained strong, and it appears equity markets have support going into 2022. Where we depart from the crowd on inflation is in the years beyond 2022. We are sceptical that the US Fed will be sufficiently proactive as it struggles to balance full and inclusive employment against inflation pressures that are starting to look more entrenched. We believe this will be the central bank’s biggest challenge in 2022 and beyond.

In terms of Portfolio positioning, we do believe we are moving into a more supportive environment for active management in general, for a number of reasons:

- The end of easy money, brought on by policy tightening and falling liquidity in response to rising inflation
- A return to focusing on fundamentals, with unprofitable, speculative growth stocks lagging proven cash flow generators
- Headwinds to mega-cap technology stocks should see increased market breadth
- And in general, the need to be more selective

Within equities, the Portfolios target strategic allocations to value, momentum, and quality, as our key alpha sources while maintaining a tilt towards value. Elevated valuation dispersions still have a long way to normalise, and have the fundamental support to do so. From a sector perspective, consumers remain in a strong position to increase spending on discretionary items such as travel, leisure and autos, and we expect these areas of the market to recover. Undervalued energy stocks are also expected to be bolstered by growing energy demand and limited supply resulting from underinvestment, and undervalued financials should be boosted by steepening yield curves and rising demand for loans. Rising interest rates and inflation should provide a further boost to the outperformance of value and a headwind to highly rated growth stocks trading at elevated multiples.

Across the Portfolios’ fixed-income exposures, our positioning remains fairly consistent. We continue to hold a modest overweight credit risk, with a lower-quality and shorter-maturity bias, and favour sectors likely to benefit from a reflationary environment. Within government bonds markets, we remain underweight duration in the core markets (US, core Europe and UK). Within corporate credit, we have a preference for lower-quality and shorter-maturity issues, which limits our sensitivity to interest rate moves.

Manager changes

- None in the reporting period.

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 ACWI (Net) (GBP)	6.2%	19.6%	19.6%	16.1%	17.9%	12.1%	12.3%
FTSE UK Series All Share Index (TR) (GBP)	4.2%	18.3%	18.3%	3.3%	8.3%	3.6%	5.4%
Russell 1000 Index (Net 30%) (USD)	9.7%	25.9%	25.9%	23.1%	25.6%	17.0%	17.8%
MSCI Europe ex UK Index (Net) (EUR)	7.7%	24.4%	24.4%	12.5%	17.2%	9.4%	9.8%
MSCI Pacific ex-Japan Index (Net) (USD)	-0.1%	4.7%	4.7%	5.6%	9.7%	4.3%	8.3%
Tokyo Stock Exchange TOPIX (JPY)	-1.7%	12.7%	12.7%	10.0%	12.7%	4.7%	8.0%
MSCI Emerging Markets Index (Net) (GBP)	-1.8%	-1.6%	-1.6%	6.2%	8.7%	3.9%	7.9%

Fixed income	3 month	YTD	1 year	2 year*	3 year*	4 year*	5 year*
ICE BofA UK Gilts All Stocks Index (GBP)	2.4%	-5.2%	-5.2%	1.3%	3.2%	2.5%	2.4%
Bloomberg Global Treasury Index (GBP Hedged)	0.1%	-2.0%	-2.0%	1.3%	2.7%	2.3%	2.0%
Bloomberg Global Aggregate Index (GBP Hedged)	0.0%	-1.5%	-1.5%	1.7%	3.2%	2.4%	2.3%
Bloomberg Global Aggregate ex-Treasury Index (GBP Hedged)	-0.1%	-1.0%	-1.0%	2.1%	3.9%	2.6%	2.7%
ICE BofA US High Yield Constrained Index, Hedged (GBP)	0.5%	5.1%	5.1%	4.8%	7.2%	4.3%	4.7%
50/50 JPM EMBI Glob Div (H) & GBI EM Glob Div(GBP)	-1.8%	-5.0%	-5.0%	-1.7%	2.4%	1.0%	2.2%

Cash	3 month	YTD	1 year	2 year*	3 year*	4 year*	5 year*
ICE LIBOR 3 Month GBP (TR) (GBP)	0.0%	0.1%	0.1%	0.2%	0.4%	0.5%	0.5%

Commodities	3 month	YTD	1 year	2 year*	3 year*	4 year*	5 year*
Oil (ICE Brent Crude)	2.3%	54.3%	54.3%	16.1%	10.4%	7.8%	5.7%
Gold (\$/oz)	4.1%	-3.6%	-3.6%	9.8%	12.6%	8.9%	9.8%
Bloomberg Commodity Index (USD)	-1.6%	27.1%	27.1%	11.0%	9.9%	4.2%	3.7%

Commodities	12/31/21	9/30/21	12/31/20	12/31/20	12/31/19	12/31/18	12/31/17	12/31/16
Oil (ICE Brent Crude)	\$77.78	\$76.06	\$50.41	\$50.41	\$57.70	\$57.83	\$57.67	\$58.88
Gold (\$/oz)	\$1,829.20	\$1,756.95	\$1,898.36	\$1,898.36	\$1,517.27	\$1,282.49	\$1,302.80	\$1,147.50
Bloomberg Commodity Index (USD)	211.8033	215.1673	166.631	166.631	172.0042	159.7202	179.9572	176.9417

Source: IMU Data Portal, Bloomberg. Data to 31 December 2021.

*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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Past performance is not a reliable indicator of future results. Standardised performance is available upon request. All data is as at 31 December 2021.

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Asset class performance discussed is based on the majority SEI fund underlying the asset class. This does not include analysis of the manager pools, hedged share class investments within SEI Funds, additional SEI funds or any third-party funds within the Strategic Portfolios.

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- The risks described below may apply to the underlying assets of the products into which the Strategic Portfolios invest.
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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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