MLC FirstChoice Managed Accounts

Portfolio Changes

Effective Date: 20th October 2023

What changes have we made?

At the headline level, we have reduced our Growth and increased our Defensive assets exposure across all seven risk profiles.

REDUCED* Australian Equities (High Growth 98)	**REDUCED** Global Equities	**INCREASED** Fixed Income Allocations

What is the rationale for these changes?

- **A sharp (and sustained) rise in long bond yields increases the risk of a near-term pullback in Global Equities**
- **We are leaning out of higher-valuation, 'longer duration' Growth equities a little more, along with an incremental increase to currency hedging**
- **Our preference for Australian over Global fixed income reflects our view that the RBA is likely to reverse course on rates sooner than global peers, particularly the US.**

The key development over the past few months is undoubtedly the ~100bps rise in US 10-year Treasury yields to 5% during October. Unlike the shorter-term Fed Funds rate, we view this as a more likely catalyst for a broader pullback in asset class valuations (including equities). It is important to understand why the yield curve has risen, because different answers have different implications for portfolio positioning. If the rise is due largely to inflation expectations, that is unequivocally negative for both equities and bonds.

Our reading is that only about a quarter of the rise can be attributed to inflation expectations, with the majority due to (i) the strong US economic growth outlook being belatedly priced into bond yields and (ii) the emergence of an oversupply in bonds, driven by central banks' retreat from Quantitative Easing (i.e. buying) while US fiscal deficits have remained higher than expected (i.e. the govt selling). Both factors are linked to the massive Bidenomics fiscal spending playing out in the US.

These changes, therefore, are more of a response to the risk of valuation impact from higher-for-longer bond yields (or perhaps a return to 'normal-for-longer' levels), than any major change in the macroeconomic fundamentals themselves. After all, other than a slight uptick in inflation, there has been little in the way of new macro data to explain a 100 bps increase in 10-year yields.

As we saw in 2022, Growth vastly underperformed Value in response to the Fed's rate increases. Accordingly, the decrease in Global Equity exposure is most concentrated on the higher-multiple, longer-duration equities held in Growth manager Intermede. These are supported by slight trims in fellow (hedged) Growth manager T. Rowe Price and Value manager Realindex. This configuration also effectively trims our unhedged exposure in response to the weaker Australian dollar.

On the other side of the ledger, we have increased our allocation to the Janus Henderson Tactical Income, Western Asset Australian Bond and Bentham Global Income strategies. Broadly, we have calibrated the relative allocation to these strategies to the risk profile (lower risk profiles skew to bonds, while the higher risk profiles include more Credit exposure). In addition, the resulting tilt toward domestic fixed income exposure aligns with our view that rate cuts will potentially arrive earlier in Australia than in the US (noting the more direct transmission mechanism of monetary policy here in Australia).

** The Australia Equities and Global Real Estate allocations were incrementally increased for the Moderate 40 portfolio, in conjunction with the decreases in the Global Shares and increases within the Fixed Income allocations of the other profiles. This additional portfolio reshaping was required to satisfy the CFS Investment Guidelines on aggregate Cash and Fixed Income exposure within the Moderate 40, specifically it not exceeding 60%, while still capturing the essence of the asset allocation driven portfolio rebalancing applied to the other portfolios.*

Summary of portfolio changes

This table outlines the changes to strategic portfolio weights vs the current published strategic allocation. Actual portfolio changes will differ slightly owing to portfolio movements between the effective trade date and the last rebalancing point.

Full portfolio allocations are available via the *Portfolio Holdings and Fees Summary Spreadsheet* located on the MLC CFS managed account microsite.

	Conservative 30	Moderate 40	Moderate 50	Moderate 60	Balanced 70	Growth 80	High Growth 98
Australian shares		**+1.00%**					
Solaris Core Australian Equity		+0.50%					
Ausbil Australian Active Equity		+0.50%					
First Sentier Small Companies							-1.00%
Global shares	-2.00%	-2.00%	-3.00%	-3.50%	-4.00%	-5.00%	-5.00%
Intermede Global Equities	-2.00%	-1.50%	-2.00%	-2.00%	-2.50%	-3.00%	-3.00%
T. Rowe Price Global Equity – Hedged		-0.50%	-0.50%	-1.00%	-1.00%	-1.00%	-1.00%
Realindex Global Share – Hedged			-0.50%	-0.50%	-0.50%	-1.00%	-1.00%
Real assets		**+1%**					
Resolution Capital Global Property		+1%					
Fixed income	+2.00%	+2.00%	+3.00%	+3.50%	+4.00%	+5.00%	+6.00%
Western Asset Australian Bond	+2.00%	+1.50%	+2.00%	+2.00%	+2.00%	+1.50%	
Bentham Global Income Fund						+1.25%	+1.00%
Janus Henderson Tactical Income		+0.50%	+1.00%	+1.50%	+2.00%	+2.25%	+5.00%
Cash		-2.00%					
First Sentier Strategic Cash		-2.00%					
Total Growth	+2.00%	–	+3.00%	+3.50%	+4.00%	+5.00%	+6.00%
Total Defensive	-2.00%	–	-3.00%	-3.50%	-4.00%	-5.00%	-6.00%

Portfolio fee impact

The changes are broadly cost neutral, with the net fee change most risk profiles being a decrease of 1-2 basis points. For the Moderate 40 portfolio the fee changes equate to a 1 basis point increase.

When were the changes made?

The relevant trades were processed by CFS on the 20th of October 2023.

Important Information

Portfolio changes outlined in this document are expected to be implemented by the client's platform, in due course.

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