

INNOVA
ASSET MANAGEMENT

QUARTER FOUR 2023 | RISK DEFINED
MARKET OUTLOOK REPORT



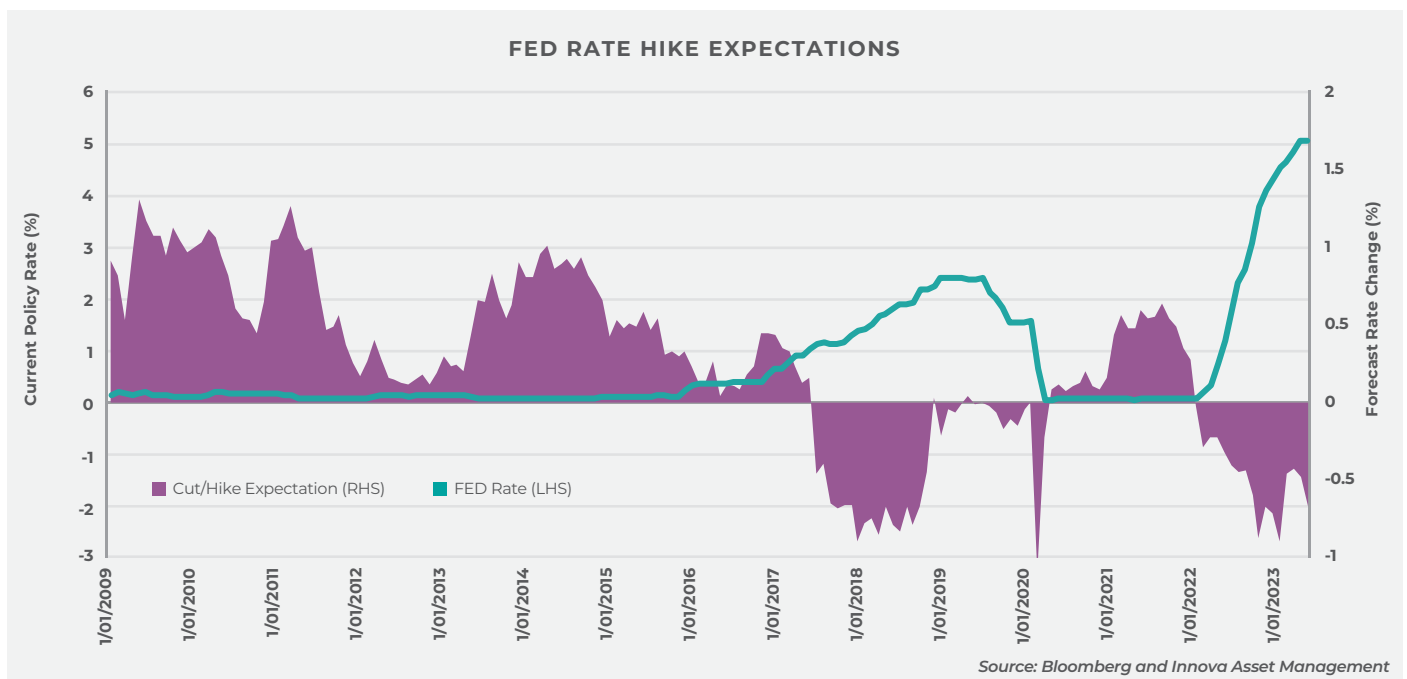
KEY TAKEAWAYS

- In the first half of the CY, markets rallied on strong economic trends. In the September quarter however, markets traded lower. If inflation continued to recede and the US economy remained strong, there would be little impetus for the Fed to cut rates and stimulate the economy.
- This rhetoric started playing out in the September quarter, as rising bond yields have detracted performance of interest rate sensitive sectors and long duration assets such as large cap tech stocks.
- Cautious of US fiscal position, increasing debt levels outside of quantitative easing periods can raise supply more than demand, leading to higher yields.
- Discrepancies between market behaviour and Innova’s leading economic indicators raise concerns and call for a cautious approach. This consequently leads to slower economic trends, market volatility and therefore defensive positioning.
- There has been a clear separation between US large cap and the rest of the equity universe valuations. Unlike US large caps, many equity markets globally are trading close to or slightly below fair value.

WHAT’S HAPPENED IN MARKETS

In the recent quarter major market indices such as the MSCI ACWI fell roughly 4% for the month and are down moderately for the quarter. Overall, 2023 has been driven by narratives including strong economic trends, normalising inflation and AI driven sentiment. If GDP and employment remains robust, there would be little impetus for the Fed to cut rates.

Given the market is pricing for rate cuts, in contrary action, rising bond yields meant interest rate sensitive sectors came under pressure. We’re cautious of the dynamics behind US budget deficits, which is also causing the US government to push supply to fund their interest expenses and budget deficits. Whilst this is not the sole cause of rising yields, it is a factor that should be monitored closely given they are no longer engaging in QE and letting these bonds roll-off.

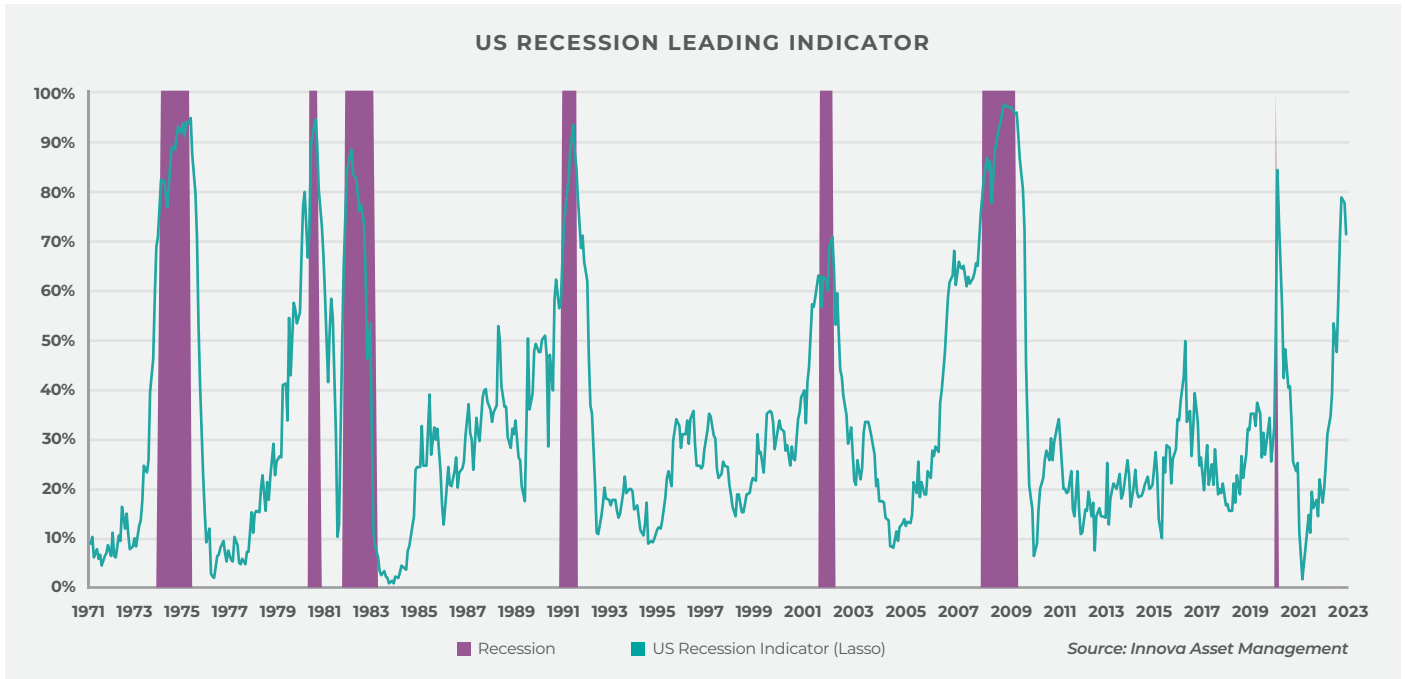


INNOVA HOUSE VIEW

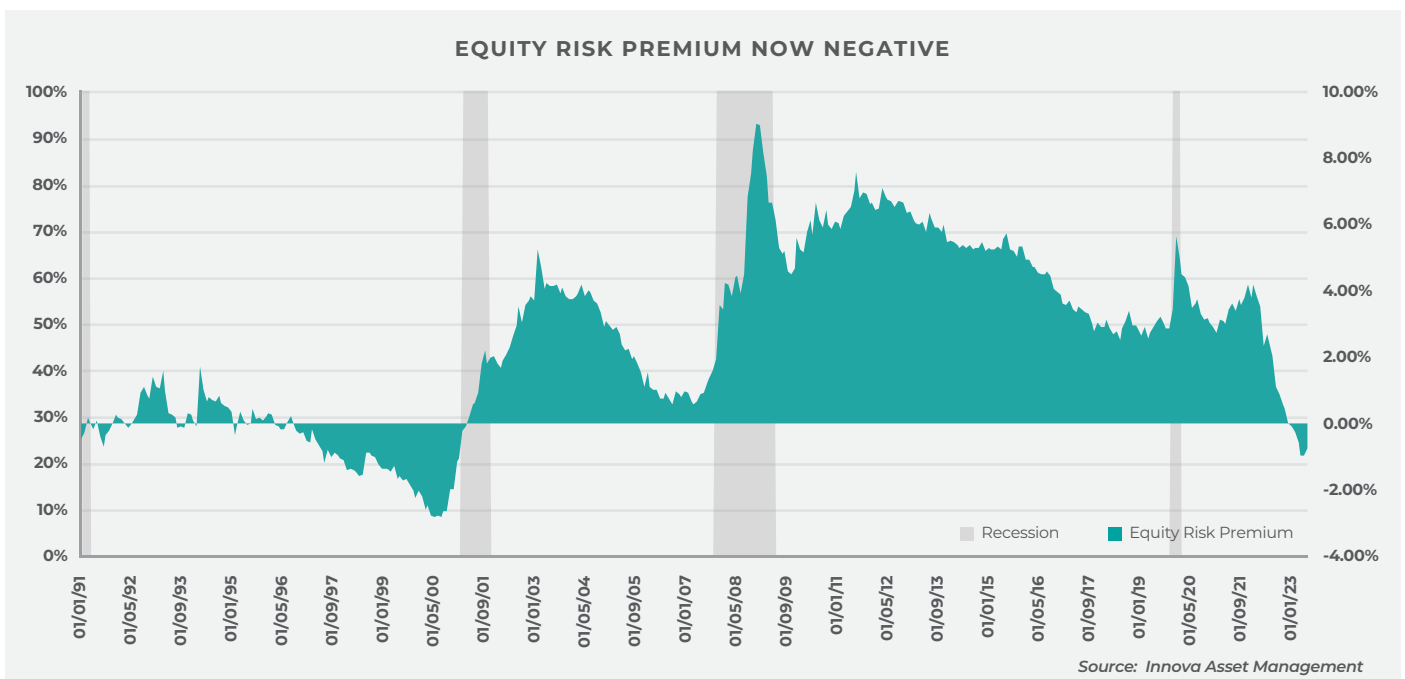
Innova's Leading Economic Indicators (LEI's) continue to suggest that the economic backdrop is less resilient than headline numbers indicate. Whilst these are not a driver of our portfolio positioning, they are a 'sensitivity check' for our return and risk forecasts.

In terms of valuations, there is a large dispersion between US large cap and the rest of the equity universe. Many equity markets globally are trading close to or slightly below fair value (e.g., Australia, the UK, emerging markets).

We believe this dispersion in valuations has created an interesting opportunity to allocate to equity markets that should provide some level of downside protection if markets continue to fall, or greater upside participation if equity markets rebound from here.



The Equity Risk Premium measures the difference between the yield on short term government debt and earnings yield on US equities. This has now turned negative, meaning T-Bills (short term debt) have a greater expected return than US equities.. Generally, risk premiums predict subsequent 5-7-year returns and show a significant positive relationship between the two.



HOW WE'RE POSITIONING OUR PORTFOLIOS

Given our view on equity valuations, we remain underweight US equities based on valuations, particularly growth style equities. However, we maintain a key overweight in value equities and relative value equity positions. These include positions in UK equities, via the FTSE100 ETF, which continues to demonstrate outsized forecast returns from our systematic outputs, as do South Korean equities via the IKO ETF, and Emerging markets in general. We remain divested from A-REITs and underweight Infrastructure, as well as underweight Real Assets more generally.

Within fixed income we now have a more balanced position between long duration fixed rate Government bonds and floating rate credit. Our duration positions are diversified across US Treasuries (via USTB), retain some Aus 10y exposure (via VGB) and have added the Western Asset Australian Bond Fund. In the credit space, Domestic 'A' rated floating rate credit still looks attractive on a relative and absolute basis, though is unlikely to act as a positively performing equity-hedge in the event of equity market weakness.

We remain largely unhedged in our global asset positioning. We believe defensiveness is warranted based on our poor outlook for corporate earnings and the global economy, so we retain active positioning across the board. However, as mentioned above in our "House View" these same defensive allocations should provide outsized upside if we are wrong, and new bull market resumes.

RECENT PORTFOLIO CHANGES

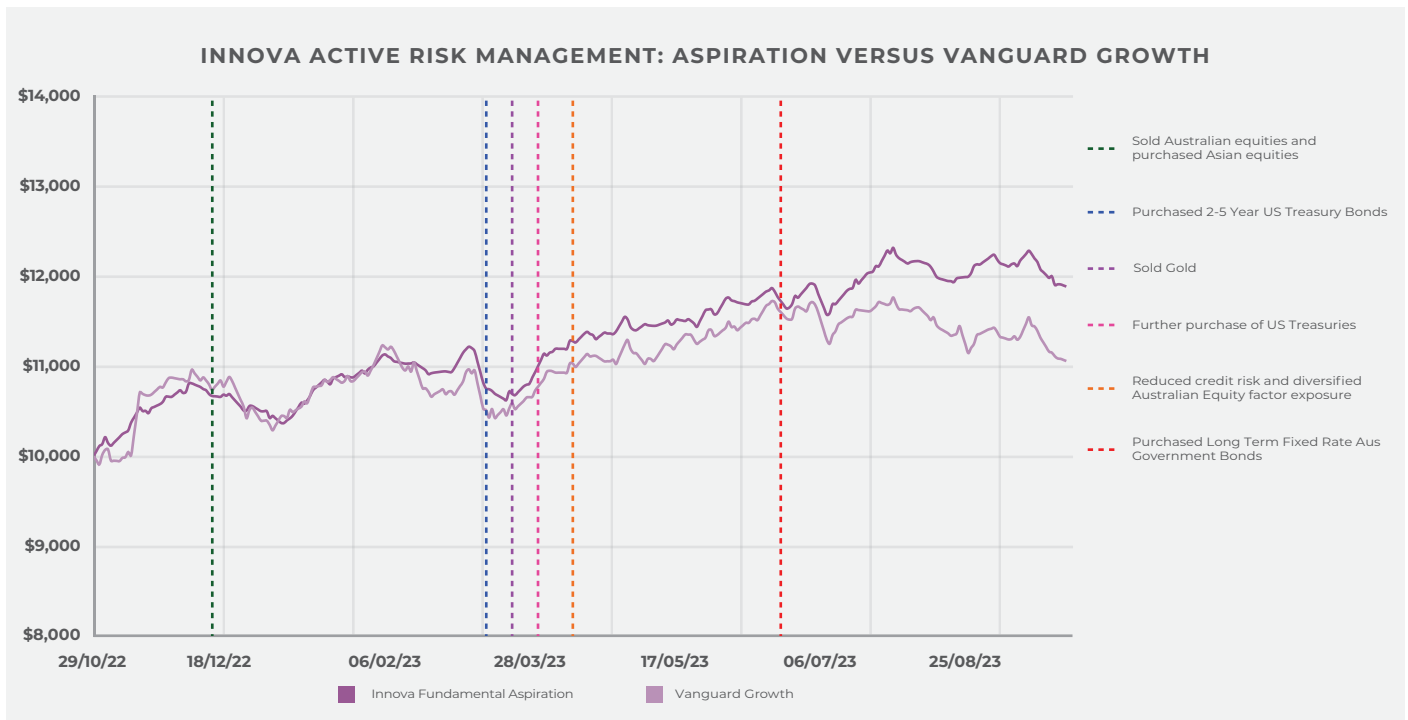
No recent portfolio changes made over the quarter.

PERFORMANCE

PERFORMANCE TO SEPTEMBER 30TH

	1 MTH	3 MTH	6 MTH	1 YR	3YR	5YR
CONSERVATIVE/ LOW RISK BUCKET						
Innova Lifestyle Preservation Portfolio - Fundamental	-0.95%	-0.27%	-0.16%	4.44%	1.28%	1.60%
Innova Lifestyle Preservation Portfolio - Flagship	-0.96%	-0.41%	0.08%	4.29%	1.89%	1.52%
Target Cash Rate +1.5%	0.46%	1.43%	2.80%	5.18%	2.96%	2.75%
BALANCED/MEDIUM RISK BUCKET						
Innova Wealth Creation Portfolio - Fundamental	-1.75%	-0.34%	0.94%	9.48%	5.04%	4.09%
Innova Wealth Creation Portfolio - Flagship	-1.96%	-0.48%	1.31%	9.09%	6.28%	4.05%
Target Cash Rate +3%	0.59%	1.81%	3.56%	6.73%	4.48%	4.27%
GROWTH/ HIGH RISK BUCKET						
Innova Aspiration Portfolio - Fundamental	-2.15%	-0.33%	1.39%	11.96%	7.07%	5.63%
Innova Aspiration Portfolio - Flagship	-2.32%	-0.49%	1.75%	11.08%	8.29%	5.33%
Target Cash Rate +5%	0.75%	2.30%	4.56%	8.81%	6.51%	6.30%

PORTFOLIO CHANGES (PREVIOUS 12 MONTHS)



23/06/2023

Long term fixed rate Aus Government Bonds (Buy) & Global Equities & credit (Sell)

Amid a worsening economic outlook, we held reservations about the pricing of equities, which did not adequately account for the elevated risk level of potential future earnings. In light of this, we made the decision to decrease our global equity exposure and instead allocate to long-term fixed-rate Australian Government Bonds. These bonds had reached more appealing levels, offering an opportunity to strengthen our hedge against potential equity market risks. Additionally, we opted to further reduce our credit exposure. Although this position was attractively priced, we recognised that it was unlikely to generate gains in the event of equity market declines.

12/04/2023

US Treasuries (Buy) & Subordinated Debt (Sell) / Momentum Aus Equities (Buy) & Value Aus Equities (Sell)

Our modelling was continuing to present an uncomfortable likelihood of recession, leading us to take steps to reduce credit risk and enhance the defensive nature of our client portfolios. To achieve this, we opted to further increase our allocation to US Treasuries, which serve as a reliable hedge against the expected economic slowdown in the US. Additionally, we decided to capitalise on the strong performance of value equities by taking some profits and diversifying our factor exposure within Australian Equities. We achieved this by allocating to a momentum-based strategy that had not performed as robustly during the period.

31/03/2023

US Treasuries (Buy) & Relative Value (Sell) / South Korea (Buy) & Japan (Sell)

The bond market has been unstable lately and other investment options are now offering higher returns, making less traditional fixed income options less attractive. As a result, we plan to invest more in US Government bonds and less in other fixed income strategies. We also believe that South Korea presents a better opportunity for growth than Japan, so we'll be selling our Japan exposure to focus on South Korea's promising risk/return profile.

22/03/2023

Cash (Buy) & Gold (Sell)

Gold prices had reached record highs in Australian Dollars and had successfully protected portfolios during periods of equity market volatility, which was its intended purpose. However, at the price it was trading at, we believed the upside potential for gold was limited, and the downside risk significant. Therefore, we decided to sell some of our gold holdings to take profits. We allocated the proceeds to cash as we anticipate continued volatility in equity and bond markets.

13/03/2023

2-5 Year US Treasury Bonds (Buy) & Australian Government Bonds (Sell)

Our economic indicators suggested a high likelihood of a global economic slowdown or recession, which was concerning. To hedge our equity market exposure, we found the most attractive option to be 2-5 year US Treasury bonds. These bonds offered an attractive inflation premium, yielding around 5%, and have the potential for significant capital gains in the event of a stock market decline. To fund this investment, we sold Australian Government Bonds as we believe a US-centric allocation will offer a better return profile in the future.

08/12/2022

Asian Equities (Buy) & Australian Equities (Sell)

We decided to decrease our investment in Australian Equities because it had performed well, and we expected lower returns in the future. Additionally, we had concerns about the domestic economic landscape in 2023. Instead, we chose to invest the money in Asian equities because our short-term forecasts for this region were among the highest compared to other asset classes. After thorough research and analysis, we also felt comfortable with the risks associated with investing in Asia that we were previously concerned about.

15/08/2022

Floating rate credit (Buy) & Infrastructure (Sell)

We decided to decrease our investment in Infrastructure because it had performed exceptionally well over the year, making it expensive. Instead, we invested the money in diversified floating rate credit because it provided a better yield, had a lower price, and was more secure. Additionally, we diversified our credit exposure by bringing in another credit manager.

Important Information

This document has been prepared by Innova Asset Management Pty Ltd (Innova), ABN 99 141 597 104, Corporate Authorised Representative of Innova Investment Management, AFSL 509578 for provision to Australian financial services (AFS) licensees and their representatives, and for other persons who are wholesale clients under section 761G of the Corporations Act.

To the extent that this document may contain financial product advice, it is general advice only as it does not take into account the objectives, financial situation or needs of any particular person. Further, any such general advice does not relate to any particular financial product and is not intended to influence any person in making a decision in relation to a particular financial product. No remuneration (including a commission) or other benefit is received by Innova or its associates in relation to any advice in this document apart from that which it would receive without giving such advice. No recommendation, opinion, offer, solicitation or advertisement to buy or sell any financial products or acquire any services of the type referred to or to adopt any particular investment strategy is made in this document to any person.

All investment involves risks, including possible delays in repayments and loss of income and principal invested. Any discussion of risks contained in this document with respect to any type of product or service should not be considered to be a disclosure of all risks or a complete discussion of the risks involved. Past performance information provided in this document is not indicative of future results and the illustrations are not intended to project or predict future investment returns.

Although non-Fund specific information has been prepared from sources believed to be reliable, we offer no guarantees as to its accuracy or completeness. Any performance figures are not promises of future performance and are not guaranteed. Opinions expressed are valid at the date this document was published and may change. All dollars are Australian dollars unless otherwise specified.