ARC RESEARCH

2023 IN REVIEW

January 2024

THE PURSUIT OF BETTER INVESTMENT PERFORMANCE

The year 2023 ended with a strongly positive quarter for financial markets and thus, for the twelve month period as a whole, nominal returns for private client investors were a little above average.

That was most welcome after the bond and equity market traumas of 2022 when the vast majority of private clients experienced significantly negative returns. But, generally, 2023 gains have not fully compensated for 2022 losses.

The table below sets out the estimated returns for private client portfolios across the five PCI currencies and four PCI risk categories.

RETURNS FOR 12 MONTHS TO DECEMBER 2023*

Risk Category	Risk Relative to World Equities	GBP	USD	EUR	CHF	CAD
ARC Cautious PCI	0 – 40%	4.4	7.0	5.1	2.9	7.1
ARC Balanced Asset PCI	40 – 60%	6.0	10.3	7.8	3.8	8.6
ARC Steady Growth PCI	60 – 80%	7.3	13.4	10.3	4.7	10.3
ARC Equity Risk PCI	80 – 110%	8.1	17.5	14.0	6.9	11.8

* Estimated returns for Q4 2023

Whilst the table above reveals that in local currency terms gains were highest for USD investors, when adjusted for currency moves, returns for private clients in the same risk category were similar regardless of reference currency.

After the painful normalisation of interest rates in 2022, bond markets seemed to offer reasonable value and, despite tighter monetary policy and the threat of recession, company profits proved resilient.

Yet, the breadth of equity market gains was extremely narrow, the rise in the world equity market index being driven by the 10 largest US listed "mega-cap" stocks (Alphabet, Amazon, Apple, Berkshire Hathaway, Broadcom, JP Morgan, Meta, Microsoft, Nvidia and Tesla).

In 2023, these stocks were up, on average, circa 90% and up around 85% on a market capitalisation-weighted basis, with the other 490 stocks making up the S&P 500 on average delivering a return of zero!

The Big 10

2023 average return

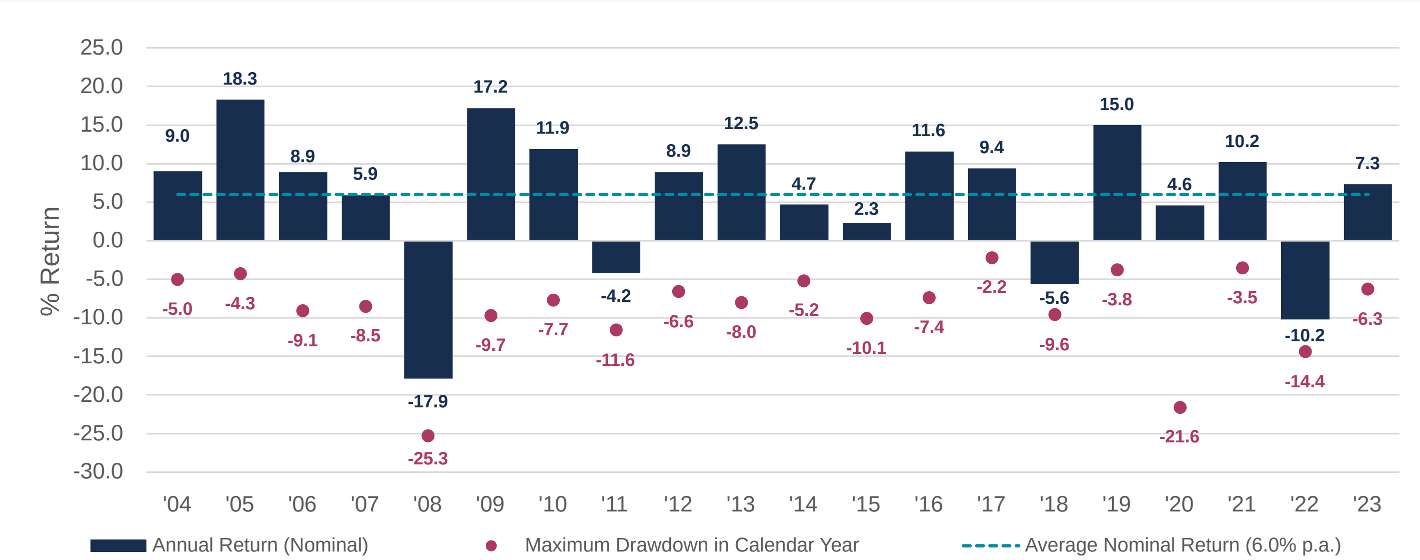
90%

THE LONGER-TERM PICTURE

So, how has the performance of a typical private client portfolio in 2023 compared to that experienced in previous years?

By way of illustration the chart below plots calendar year returns and maximum drawdown in each of the twenty calendar years since 2004 using the daily estimated series for the ARC Sterling Steady Growth Private Client Index, the PCI series with the greatest number of constituents.

CALENDAR YEAR NOMINAL RETURNS AND INTRA-YEAR DECLINES



In 2023, private clients following Sterling Steady Growth mandates recorded, on average, nominal returns of 7.3%, just above the historical average of 6.0% per annum.

The maximum drawdown during 2023 of -6.3% was unexceptional and less than the average of -9.0% over the 20-year history of the indices.

Average Return 2023
7.3%

Average Return 20 Years
6.0% p.a.

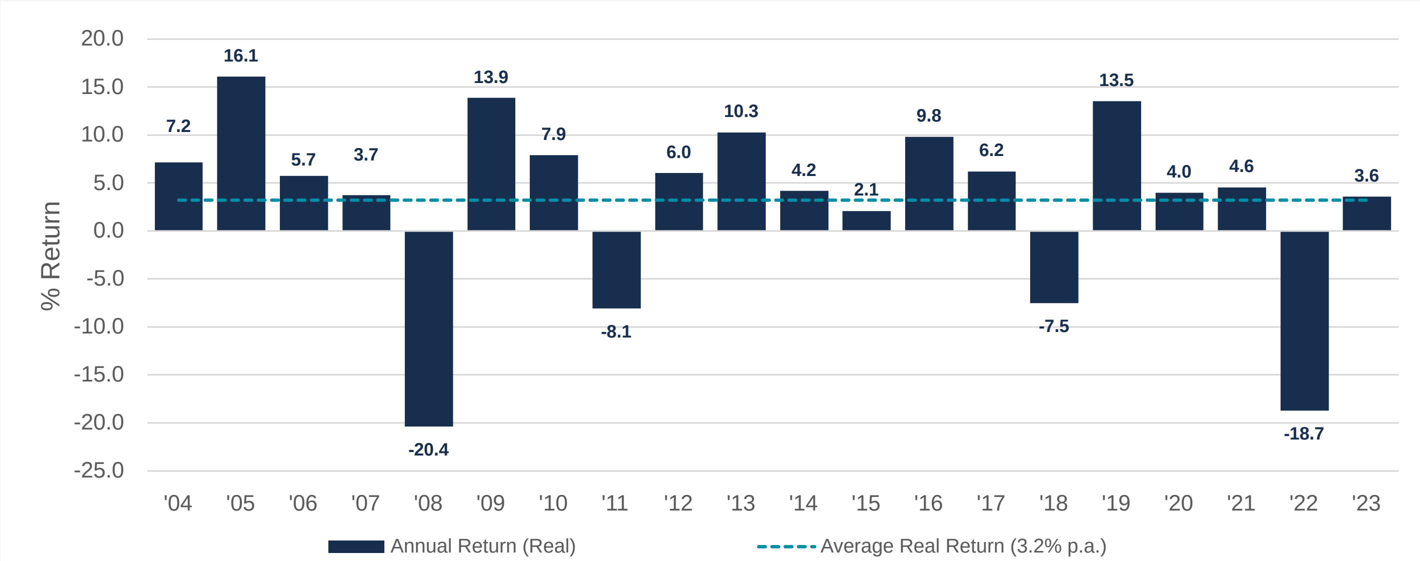
At first sight, results for 2023 look to be encouraging: a slightly above-average return achieved with typical return volatility during the year.

However, the picture is considerably less rosy once the impact of inflation is taken into account.

THE REAL LONGER-TERM PICTURE

The chart below plots the inflation-adjusted performance of a typical Sterling Steady Growth private client portfolio for the last 20 years.

CALENDAR YEAR REAL RETURNS



Whilst 2023 delivered a real return of 3.6% per annum for a Sterling Steady Growth investor, since 2021 real wealth has declined by around 15%.

After the Global Financial Crisis in 2008, it took six years for real wealth to recover despite extensive quantitative easing and negative real interest rates. Recovery from the impact of financial market normalisation in 2022 may well take longer.

In the 18 years to 2021, the average real return for a Steady Growth portfolio was 4.4% per annum. That has now dropped to an average real return of 3.2% per annum over the last 20 years. Looking forward, it feels reasonable to target a real return of 4% per annum for the next decade from a classic 60% equity: 40% bond asset allocation. But that is 4% per annum from now, not based on 2021 real wealth.

For those investors seeking to determine a sustainable withdrawal pattern from their portfolios, now feels like the right time to be rebasing to end 2023 values. It is time for investors to accept that 2022 was not an exceptional downturn but a year in which bond market yields and equity market valuations returned to “fair value” after a decade of being artificially pumped up by excessively loose monetary policy.

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