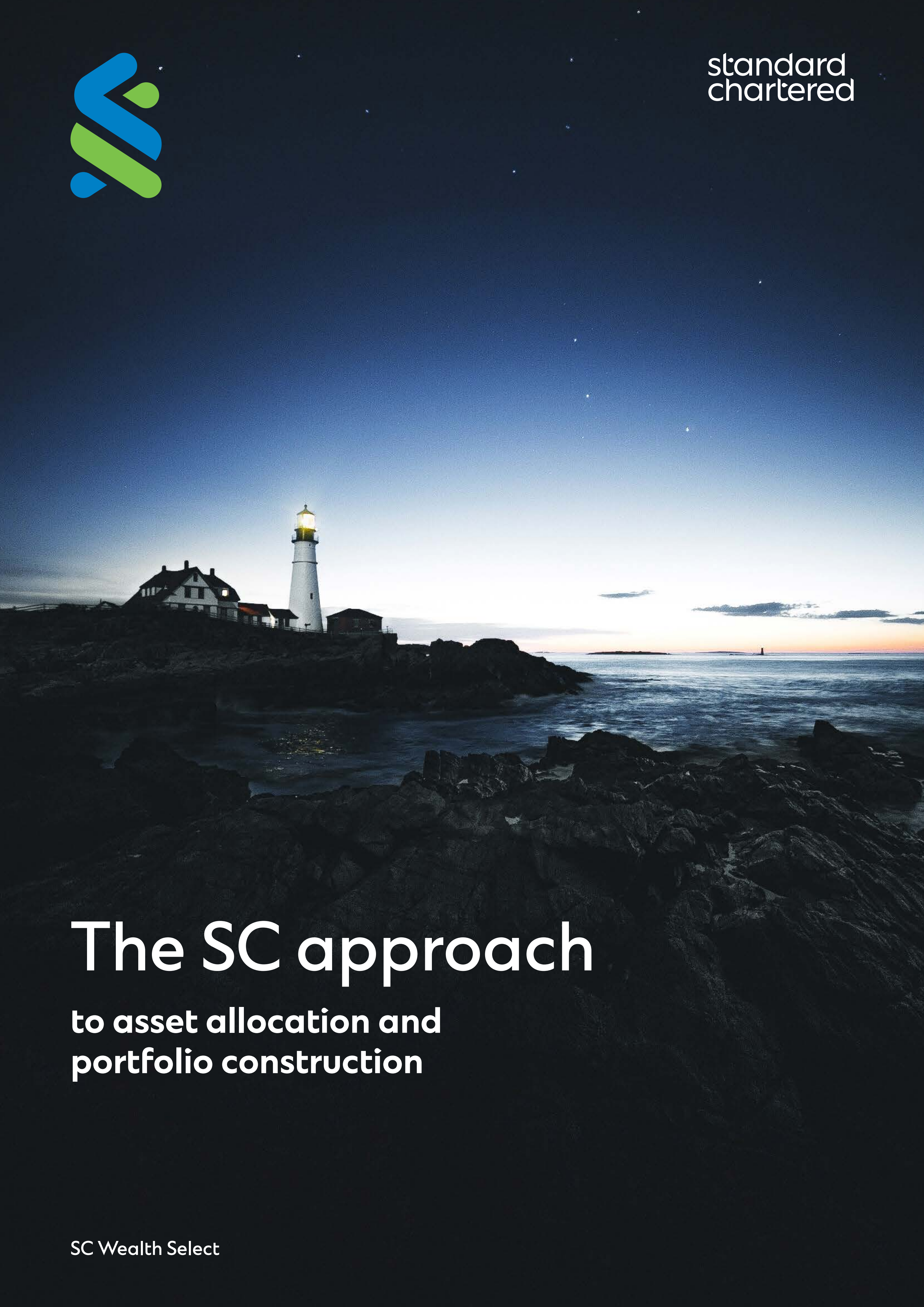
standard chartered



The SC approach

to asset allocation and portfolio construction

SC Wealth Select

If investing is a journey, asset allocation and portfolio construction is the guiding star.

How we advise you on building your investment portfolio is critical to your financial success. The following paper explains:

1. The importance of asset allocation
2. How we differentiate between Strategic Asset Allocation (SAA) and Tactical Asset Allocation (TAA);
3. Why building a firm Foundation is an important step in the portfolio construction process;
4. How we define Opportunistic investments and how they are used in a portfolio context; and
5. How different portfolio solutions suit different client types, which is why we retain flexibility in our advisory approach.

Portfolio Construction Glossary

There are a range of terms that we use in this paper, so for ease of understanding, we will briefly define these in the glossary below.

Capital Market Assumptions (CMA)	CMAs provide the expected returns, standard deviation, and correlation estimates that collectively represent the 7-year risk/return forecasts for a variety of asset classes. In Standard Chartered, CMAs are refreshed every 12 months and are a core input to deriving our Strategic Asset Allocation (SAA).
Strategic Asset Allocation (SAA) models	The SAA models provide allocations to asset classes which aim to maximise returns for different risk tolerances over a 7-year horizon. They establish an appropriate mix of assets in a portfolio, designed to achieve one's long-term goals and objectives. SAA models are updated annually.
Tactical Asset Allocation (TAA) models	The TAA models take tactical over- or under-weight tilts, relative to the Strategic Asset Allocation (SAA) baseline, to express our 6-12-month views on asset classes and geographies, and capitalise on opportunities based on near-term economic or market conditions. The TAA is the primary allocation model through which we express our house views.
Foundation Portfolio	We believe everyone should start with a strong Foundation Portfolio. This is a stable, diversified portfolio suitable for all clients that aims to deliver long term returns through investment cycles. In Standard Chartered, Foundation portfolios are built using Tactical Asset Allocation models as a guide.
Opportunistic Ideas	Opportunistic Ideas are an overlay to your Foundation Portfolio, allowing you to tailor your portfolio to include your preferences. Typically, they are short-term (0-12 months) investments, providing a way for you to generate absolute returns, enhance your portfolio income, or add additional exposure to supplement your Foundation Portfolio. Opportunistic ideas include themes or sectors you have high conviction on, FX, structured notes and high conviction equities and bonds.

Source: Standard Chartered.

Why is a portfolio approach important?

Instead of putting all your eggs in one basket, at Standard Chartered, we believe a portfolio approach improves your potential of achieving long-term financial success.

A portfolio allocates across a range of investments, each with varying characteristics and performance under different market conditions. Research has shown that asset allocation is an important driver of long-term portfolio returns.

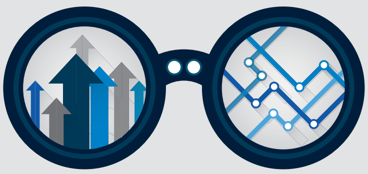
A portfolio approach also fosters discipline and avoids key behavioural biases, such as reacting excessively to short-term market moves, which can hurt investment returns.

At Standard Chartered, we believe investors should have a diversified portfolio as a starting point in their investment journey.

The importance of asset allocation

Getting your asset allocation right is an important first step to ensuring optimal portfolio performance over time. At Standard Chartered, asset allocation recommendations are delivered using our Strategic Asset Allocation (SAA) and Tactical Asset Allocation (TAA) models. Below we explain how our optimal asset allocations are determined.

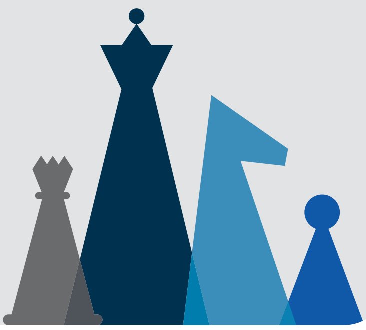
Capital Market Assumptions (CMAs)



At Standard Chartered, the starting point for determining optimal asset allocation is to derive the long term 7 year Capital Market Assumptions (CMAs), including expected returns, correlations, and standard deviation of a variety of asset classes. CMAs are updated on an annual basis.

Expected risk and returns of asset classes tend to be more predictable over the long-term. By using the long-term expected risk and returns of these asset classes in our models, we can formulate through-a-business-cycle strategic allocations.

Strategic Asset Allocation (SAA)



The next step is to build Strategic Asset Allocation models (SAA) incorporating our 7-year Capital Market Assumptions to derive the optimal allocations to each asset class.

Our Strategic Asset Allocation (SAA) models are built to provide an appropriate mix of allocations to asset classes over a 7-year horizon, with the aim of maximising returns for different risk tolerances.

Our SAA models are diversified, providing allocations to five broad asset classes and 15 sub-asset classes.

A well-diversified portfolio can lower the overall risk while enhancing realised returns.

Diversification is very important. Having a range of assets that perform differently from the rest of the portfolio can help reduce the overall portfolio volatility. While individual asset classes can be volatile, in a well-constructed portfolio there will be other asset classes that help offset that volatility, both on the upside and downside, producing a more stable return pattern.

By investing in a broad range of asset classes, it allows you to reduce risk while simultaneously enhancing realised returns, based on your risk tolerance and investment objectives. This is important to constructing an optimal portfolio allocation.

The below table illustrates that, in any given year, asset classes deliver varying returns, and no one asset class will always outperform. This demonstrates the importance of constructing a portfolio that invests in a variety of different asset classes.

Asset classes frequently and unpredictably change leadership. A diversified portfolio helps smooth out investment performance

'Periodic table' of asset class returns over the past 10 years

2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Asian Equity 22.4%	US Equity 31.8%	US Equity 12.7%	US Equity 0.7%	US High Yield 14.3%	Asian Equity 41.7%	Global Bonds 2.6%	US Equity 30.9%	Asian Equity 25.0%	Commodities 28.8%
US High Yield 19.6%	US High Yield 7.3%	Asian Equity 4.8%	US High Yield -2.7%	Commodities 11.8%	US Equity 21.2%	US High Yield -4.1%	Asian Equity 18.2%	US Equity 20.7%	US Equity 26.5%
US Equity 15.3%	EM Sov HC 17.4%	US High Yield 0.0%	Global Bonds -3.6%	US Equity 10.9%	Equal-Weight 16.1%	EM Debt -4.7%	Equal-Weight 14.6%	Equal-Weight 10.7%	Equal-Weight 6.0%
EM Debt 14.8%	Asian Equity 3.1%	Equal-Weight -0.4%	Equal-Weight -8.6%	Equal-Weight 8.8%	EM Debt 13.9%	US Equity -5.0%	US High Yield 12.6%	Global Bonds 10.1%	US High Yield 1.0%
Equal-Weight 12.1%	Global Bonds -4.0%	Global Bonds -0.5%	Asian Equity -9.2%	EM Debt 8.7%	US High Yield 10.4%	Equal-Weight -6.7%	EM Debt 12.2%	US High Yield 7.0%	Asian Equity -4.7%
Global Bonds 1.6%	EM Debt -7.3%	EM Debt -2.3%	EM Debt -12.0%	Asian Equity 5.4%	Global Bonds 7.5%	Commodities -11.2%	Commodities 7.7%	EM Debt 4.5%	Global Bonds -7.0%
Commodities -1.1%	Commodities -9.5%	Commodities -17.0%	Commodities -24.7%	Global Bonds 1.6%	Commodities 1.7%	Asian Equity -14.4%	Global Bonds 5.9%	Commodities -3.1%	EM Debt -7.1%

Source: Standard Chartered and Bloomberg.

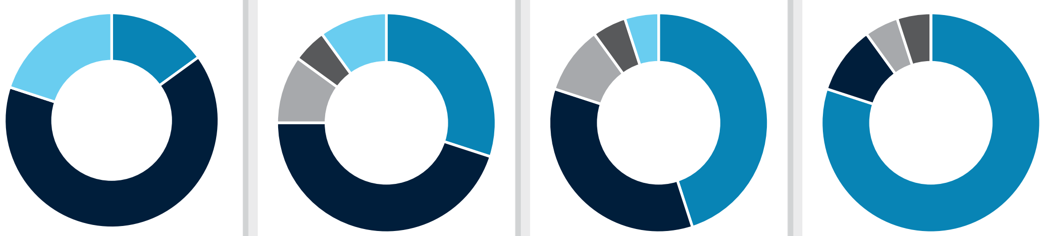
Why is Strategic Asset Allocation important?
Strategic asset allocations are an important determinant of long-term expected returns, especially in a long-only portfolio. Therefore, selecting the appropriate SAA model for you is a very important first step in the portfolio creation process.

Strategic asset allocations also offer a structured way to investing, guiding you on how you should allocate to each asset class. When allocations deviate significantly from the recommended exposure, the portfolio should be rebalanced back to its original targets, creating discipline around short-term market movements. This may also work as a disciplined form of profit taking, by adjusting your portfolio back to the intended allocations.

By having a structured guide to investing and allocating to each asset class, this can help to mitigate certain behavioural biases, such as over trading, excessive euphoria or pessimism, or an overreliance on market timing, which may have a disproportionately negative impact on returns. Investors often tend to chase the best performing assets and avoid the poor performing ones. Yet, it is extremely difficult to predict what will perform well next. Creating a disciplined, structured asset allocation approach can mitigate these biases.

Our strategic asset allocation models are diversified with the aim of producing a reasonable risk and return trade-off over a full business cycle. They are targeted to be efficient, to produce the highest estimated return per unit of risk assumed, based on the long-term CMA's risk and return assumptions.

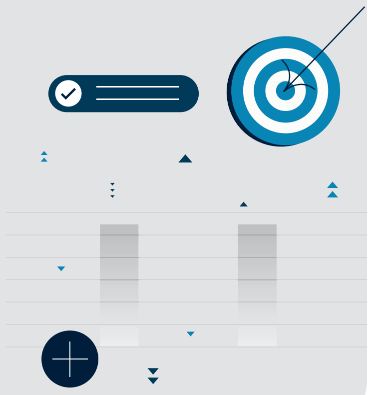
Sample: Standard Chartered Wealth Management CIO Office Strategic Asset Allocation models (Level 1)



	Conservative	Moderate	Moderately Aggressive	Aggressive
Equity	15%	30%	45%	80%
Fixed Income	65%	45%	35%	10%
Liquid Alternatives	0%	10%	10%	5%
Gold	0%	5%	5%	5%
Cash	20%	10%	5%	0%

Source: Standard Chartered CIO Office.

Tactical Asset Allocation (TAA)



Once the SAA is derived, we adjust these allocations to incorporate our house views. We actively adjust the asset class weightings relative to the long-term Strategic Asset Allocation model based on our Global Investment Committee's assessment of the potential for different asset classes to outperform or underperform other asset classes. This allows investors to refine their allocation to capitalise on expected economic conditions or financial market outcomes over the next 6-12 months.

For example, if we expect the outlook on the business cycle to improve substantially over the next 6-12 months, it may be sensible for an investor to increase their allocation to equities or higher yielding bonds as these are likely to outperform lower yielding bonds that generally outperform when the economic cycle deteriorates. Assuming a robust investment process, the underweighting and overweighting of asset classes relative to their strategic weights should add portfolio returns over the longer term.

The TAA is an overlay to the SAA and adjusts long-term target weights in the SAA for a short time, before reverting to the strategic asset allocation once the opportunities have played out. Tactical shifts can range from 5% to 10%, depending on the asset class, though in practice, it is unusual to adjust any asset class weight by more than 5% tactically.

Why is Tactical Asset Allocation important?

Strategic asset allocation provides a long-term framework to structure a balanced portfolio. However, tactical asset allocation can value-add to enhance returns or reduce portfolio volatility by providing an active overlay to adjust or fine-tune asset allocation, taking advantage of market trends expected to play out over the next 6-12 months.

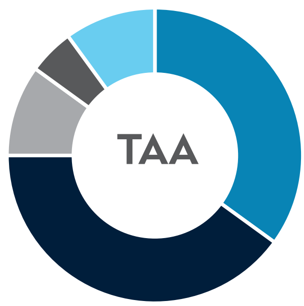
Market emotions affect asset prices, driving periods of overvaluation or undervaluation. Investors can take advantage of opportunities in assets which are experiencing extreme pessimism to tactically increase allocation, while taking profits during periods when assets are experiencing euphoria.

Tactical Asset Allocation in action

Below is an example of how our asset allocation team might implement tactical tilts based on our market views. The positions are sized based on expected returns, conviction levels as well as stand-alone risk and marginal contribution of risk to the overall portfolio.

The tactical overlays from the CIO Office help to ensure portfolios are responsive to market trends and conditions, allowing clients to capture opportunities across a much wider investment set.

Illustrative example when equities are expected to outperform: TAA equity allocation is increased, funded by a reduction in the allocation to bonds



	Strategic Asset Allocation		Tactical Asset Allocation	
	SAA	**VIEW**	**TAA**	**Tactical Tilts**
Equity	30%	Preferred	35%	+5% overweight
Fixed Income	45%	Less preferred	40%	-5% underweight
Alternatives	10%	Core	10%	Neutral
Gold	5%	Core	5%	Neutral
Cash	10%	Core	10%	Neutral

Source: Standard Chartered CIO Office.

The Standard Chartered approach to building client portfolios

At Standard Chartered, once the optimal asset allocation has been determined, we help guide you towards building a portfolio that is tailored for you. Our approach is to build a diversified Foundation Portfolio, which is like your portfolio ballast for stability and longer term returns, and then add in Opportunistic investments to tailor your portfolio to suit your unique needs and preferences.

Building a firm Foundation

We believe every investor, when building their portfolio, should start with a strong Foundation. A Foundation portfolio is a robust, stable, and diversified core portfolio, tailored to your unique circumstances and objectives which aims to deliver long term returns through investment cycles.

At Standard Chartered, we build Foundation portfolios using the TAA as a guide. We publish our TAA models for you to view – there are a variety to select from depending on your risk tolerance, your location, and your access to certain asset classes, such as liquid alternative strategies and/or private markets.

Whilst our TAA models provide a guide on asset classes and the recommended percentage allocation in your portfolio to each, the next step is to build your own Foundation portfolio consisting of investment products aligned to our TAA models.

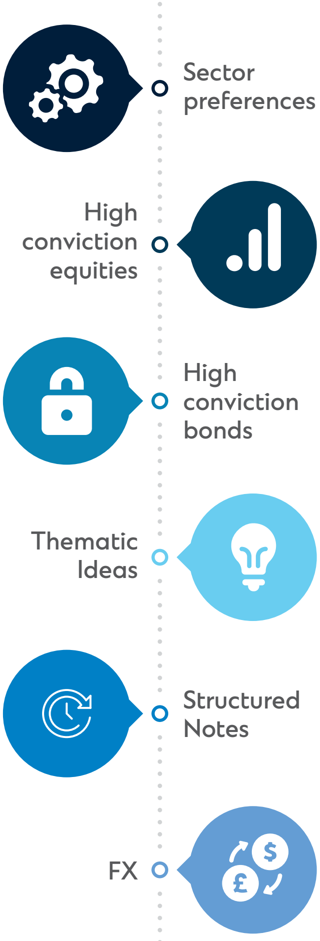
We have developed a range of model portfolios that can be used as a guide to help build your Foundation, depending on your risk profile and your goals.

Alternatively, you can customise your Foundation portfolio using a range of our recommended investments, aligned to the TAA.

For those clients who have little time or desire to be involved in building and managing their own Foundation portfolios and would prefer to outsource this to a professional portfolio manager, we also offer Discretionary Portfolio Management solutions.

Introducing Opportunistic investments

Example of Opportunistic ideas



Opportunistic investments are shorter term in nature (0-12 months) and are an overlay to the Foundation portfolio. They can be used to fulfil a specific need or preference – such as a desire to hold individual stocks or bonds or enhance income – or be used to be nimbler when it comes to taking advantage of short term moves in markets.

You may believe that you have an edge in certain investments, for example, given your knowledge of a particular sector or your ability to stomach greater volatility of short-term returns.

You may also use Opportunistic investments to add diversification, by adding investments that provide exposure to different markets, by adding FX trades, or by including structured products that have different pay-offs.

Examples of Opportunistic investments include sector or industry focused investments, single securities, currencies, commodities, structured solutions, and thematic ideas. They are shorter term in nature (up to 12 months). An example is when an investor sees a sharp sell-off in a particular sector as a great opportunity, such as the Technology sector. They may choose to opportunistically buy a Tech sector focused mutual fund or ETF to capitalise on this opportunity; buy shares in their favourite Tech stocks that are presenting value; or use structured products, such as Fixed Coupon Notes linked to Tech stocks or indices, to enhance their income profile.

Your allocation to Opportunistic investments is a very personal decision and can be linked to risk profile, investor sophistication and personal preferences. As rule of thumb, the higher the risk tolerance or investor experience/sophistication, the more you might want to allocate to Opportunistic investments.

Standard Chartered has a wide range of Opportunistic recommendations to select from – you simply need to discuss your requirements with your Relationship Manager.

How much do you allocate to Foundation versus Opportunistic?
While we believe that all investors should start with a diversified Foundation portfolio – as a guiding principle, we suggest you should have 70-100% allocated to a Foundation portfolio – we also acknowledge that some investors might a) want to supplement such an allocation with non-asset allocation-related investments, b) have a diversified allocation with another organisation, or c) want to pick each investment on its own merits without worrying about asset allocation.

We also acknowledge that at different life stages, your risk appetite and preference for certain asset allocations may change. Therefore, our advisory process needs to be flexible enough to incorporate these varying approaches.

The decision of how much to allocate to Foundation versus shorter term Opportunistic ideas is unique to everyone – as a guide, the table on the next page provides indicative allocations and depends on the type of investor you are, the level of activity you wish to undertake on your portfolio, your risk appetite, and your goals.

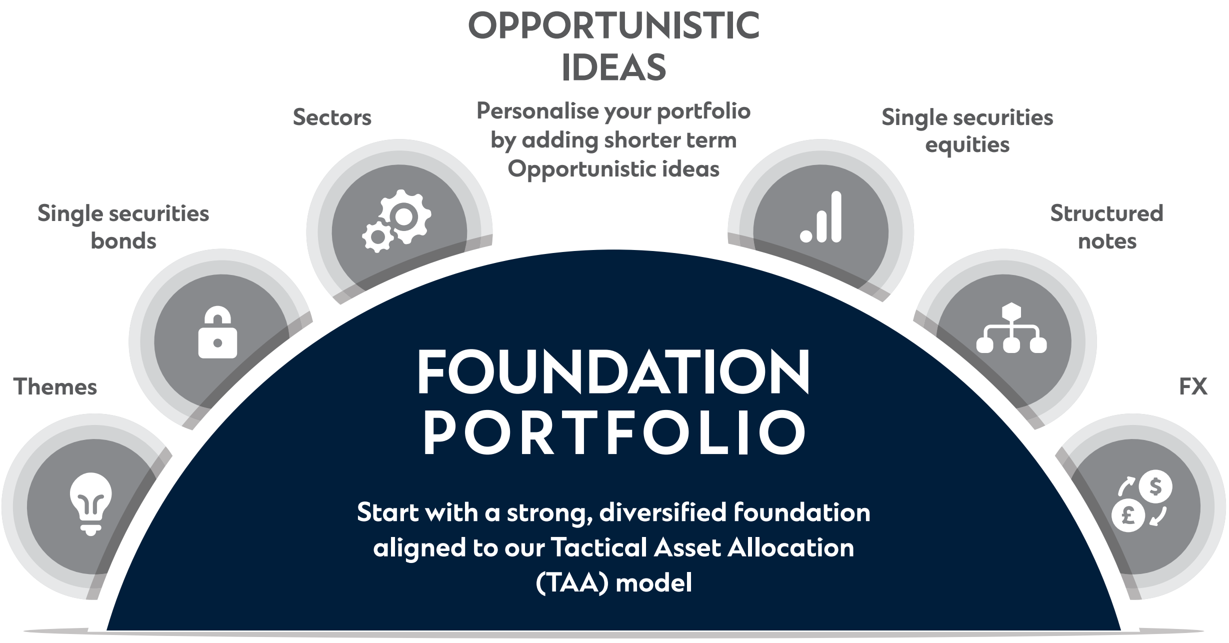
Different portfolio solutions to suit different client types

	New to wealth client	More sophisticated but time-poor client	Active sophisticated client	Highly active client
Who am I?	**I'm a** new to investing client and have basic knowledge of financial markets.	**I'm a** client who understands financial markets, but I'm busy and want a low-effort portfolio.	**I'm an** active client who understands financial markets and who values the SC house view.	**I'm a** client who is sophisticated and deeply involved in my investments.
What do I want?	**I want** a simple portfolio to improve my long term returns versus cash and build a nest egg for retirement.	**I want** to build a high quality, diversified portfolio aligned to the SC house view, that is low maintenance. I also want to build a nest egg for my retirement.	**I want** to build a robust portfolio, but also be opportunistic to trade in high conviction short term ideas. I also want to protect my family and I against unexpected events.	**I want** all my investments to be tactical and opportunistic. I also want to protect my family and I against unexpected events.
What am I recommended?	Start by building a simple Foundation Portfolio aligned to the TAA using our recommended Fund Select mutual funds. A regular insurance plan can also be implemented to maintain consistent investing for the long term	Build a Foundation Portfolio aligned to the TAA, or directly invest in a Discretionary Portfolio mandate. A regular insurance plan can also be implemented to maintain consistent investing for the long term	Build a Foundation Portfolio modelled on the TAA. Add some Opportunistic investments, such as bonds, equities, structured products or FX from the SC recommended lists, plus a Life Insurance plan	A wide range of Opportunistic investments from the SC recommended lists that are of interest to the client, and are aligned to the House View (securities, sectors and themes), plus a Life Insurance plan
How is this implemented?	**Foundation Portfolio (TAA)** **100%**  **+ Insurance / Protection** + Advisory or Discretionary Portfolio Management (DPM) + Insurance / Protection policies	**Foundation Portfolio (TAA)** **100%**  **+ Insurance / Protection** + Advisory or Discretionary Portfolio Management (DPM) + Insurance / Protection policies	**Foundation Portfolio (TAA)** **50-100%** **+ Opportunistic Investments** **up to 50%**  **+ Insurance / Protection** + Advisory or Discretionary Portfolio Management (DPM) + Security Convictions, Sectors, Themes, FX, structured products + Insurance / Protection policies	**Opportunistic Investments** **up to 100%**  **+ Insurance / Protection** + Security Convictions, Sectors, Themes, FX, structured products + Insurance / Protection policies

Start with a diversified Foundation and then overlay short-term Opportunistic ideas, as appropriate (based on your preferences and needs).

SC Wealth Select and portfolio construction

Lay a strong foundation before adding Opportunistic layers



Source: Standard Chartered.

Additional considerations when building your portfolio

Are you sufficiently protected?

Protecting the value of what you have, and what you will generate in the future, is important to help manage and grow your wealth. Protection should offer you the ability to overcome times of financial uncertainty and mitigate the long-term impact of unforeseen events on your wealth.

You can achieve this by having a well-designed plan that covers you and your loved ones in the future, therefore protecting your legacy from unexpected events.

A good protection plan should not only protect your wealth today, but also consider the value of your future earnings over your lifetime, in today's terms. It should provide a safety net, shielding both your wealth and future earnings capacity, ensuring that your financial goals are not side-tracked or delayed due to unforeseen life events. And it is also a great tool to ensure systematic planning for future needs, including leaving behind a legacy for your loved ones.

How does sustainability or ESG get incorporated?

Investor interest in sustainable investing and incorporating environmental, social and governance (ESG) considerations is growing, and another question we are frequently getting asked is how investors can incorporate this into portfolios.

ESG is not a separate asset class, rather it is a way of investing, which takes into consideration potential ESG risks and opportunities, alongside traditional financial analysis. The ESG lens can be applied in both the Foundation portfolio as well as Opportunistic investments. In terms of allocations in your Foundation, there are broad based ESG integrated funds which can be either multi-asset, equities or fixed income focused. These funds actively take into consideration material environmental, social and governance factors fully embedded in their investment process.

In terms of Opportunistic ESG investments, these fall under sustainable thematic ideas, such as climate change, water, electric vehicles, and we have a range of investment offerings available. There are also single securities available which have a high ESG score.

Taking your base currency into account

Investing in overseas assets generates diversification benefits, but also means investors become exposed to currency risks of their assets relative to their future liabilities. The impact of this exposure, via both expected returns and volatility, is already factored into the SAA construction process.

One question when it comes to investing overseas is whether to hedge the currency exposure or not. While this is a personal decision to some extent, it is important to understand the implications of doing so on the potential volatility of the holdings in local currency terms.

Our recommendation is that for bonds, absent a strong view on currency performance, we would generally hedge the currency exposure, where FX moves can easily dominate realised returns. However for equity holdings, we would generally leave the currency exposure unhedged.

The potential power of leverage

Another question we often get is when and how should clients employ leverage. Employing leverage has the potential to increase returns (or realised yields/income) on an asset or a portfolio if the return (or yield) is above the client's funding cost. However, leverage can magnify losses as well. If the value of the investment holdings declines, then leverage magnifies the portfolio loss. As such, employing leverage increases the overall volatility of the portfolio.

Given this backdrop, we believe there are 4 considerations when it comes to whether to employ leverage and, if so, to what extent. These relate to both the nature of the asset or portfolio being leveraged and the client's ability to tolerate different outcomes:

1. **Your risk tolerance** – Leverage increases the volatility of returns. Therefore, any use of leverage should be consistent with your ability to endure this volatility at both the financial and emotional level.

2. **The implications of a margin call** – The biggest fear for an investor should be the risk of permanent financial loss (rather than transitory losses which can be recouped over time). Using leverage introduces the risk of being forced to sell holdings regardless of the forward-looking outlook. Naturally, this means you would not be able to participate in any ensuing recovery. The less liquidity you can generate in a situation when there is a severe market dislocation, the less leverage should be used.

3. **The outlook for the asset or portfolio being leveraged** – If you have a high level of conviction that the investment will perform well, then more leverage may be justified.

4. **The volatility of the underlying asset** – The greater the volatility of the underlying asset, the less leverage should be employed.

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