

# Alpha Beta

PARTNERS



## Investment Update

May 2021

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Central banks kept their foot hard down on the accelerator pedal during May as developed economies vigorously rebounded from the pandemic. There is little fear of the larger central banks running out of fuel anytime soon – they simply print their own. Rather the fear of economies being driven too fast and thus provoking an accident that sends markets spiralling is more of a concern. We would expect to see some more cautious driving in the not-too-distant future in the guise of tapering down the massive liquidity programmes and/or a gradual increase in rates to slow economies to a safer speed.

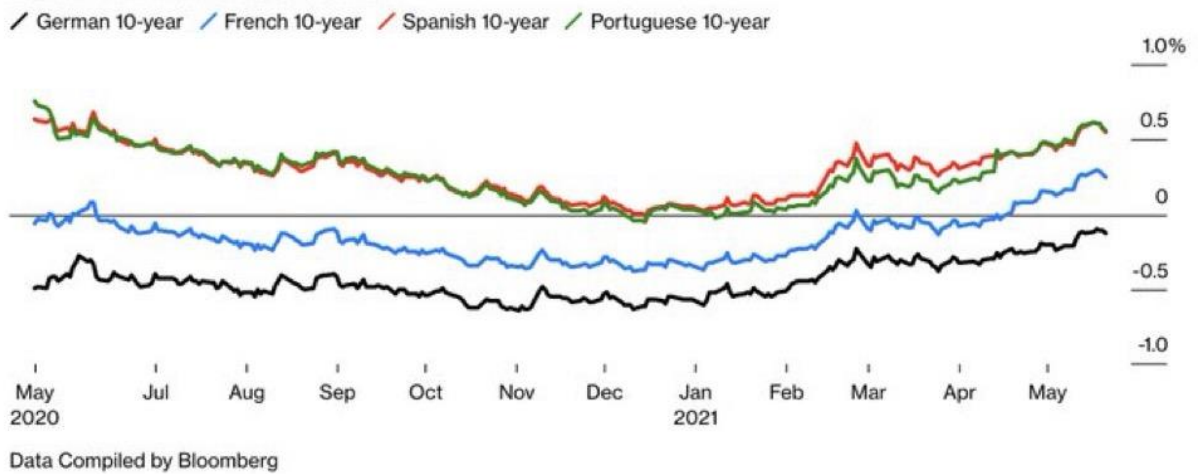
The all-important Q1 earnings season in the United States produced very strong results where companies' earnings surpassed levels recorded pre-pandemic. The jump upwards was magnified by a base effect from the previous quarter where earnings had been badly suppressed by the pandemic. This same base effect will apply to Q2 earnings which will be reported later this summer, with more of a flattening off only starting later this year as we head into the autumn. With earnings at a decade high point, you may have been surprised to see equity momentum tailing off and markets falling back from previous highs.

As we have stated in previous updates, markets, particularly in the US, have become expensive. As such the likelihood for stocks to rise significantly pushed by robust Q1 earnings were somewhat unrealistic. The potential for inflation to hike a company's input prices are real with shipping costs ballooning and basic commodities also rising – this could feed into lower profits as the year plays out. By contrast the Federal Reserve has so far insisted that a higher inflationary figure, which spooked markets mid-month, is transitory. There were certainly more base effects driving the inflationary data higher. One year ago, as you will recall, oil prices fell to a record low, so an increase to around \$60 a barrel was a major contributor to the higher US inflationary data, as were car rental costs and hotel and leisure costs. Nevertheless, there are some real price increases in our midst, and we wait to see whether they push the new average inflationary yardstick north of 2% and trigger a rate rise. We also keep a vigilant eye upon real wage increases as unemployment falls back. Economic theory states that usually wages begin to rise as unemployment falls [the Phillips Curve] and in turn this stokes further inflationary pressure. Despite record low unemployment real wages did not rise pre-pandemic which proved a major surprise and fuelled equity markets for longer.

US growth remains attractive and well supported by monetary and fiscal policies and an accelerating vaccine roll-out, though earnings must avoid slipping back. The Federal Reserve has consistently rebuffed concerns over inflation but has notably offered some clues about likely liquidity tapering in coming months. European equities have pushed forwards notably in Germany where all-time highs have been recorded. The vaccine roll-out continues to be impressive in the UK and is gathering momentum quickly across Europe. The upside-down world of negative bond yields, particularly in Europe has begun to see signs of normalising. The UK market remains attractively priced and is buoyed by strong commodity price increases and a more conventionally shaped yield curve which is beneficial for banks. Companies are reporting strong demand in their Purchasing Managers reports and sterling is also performing well. Japan is improving too, based upon greater availability of vaccines and an associated economic rebound. The emerging world and China are supported by a lower Dollar Index, and we expect

a pick-up in equity performance from the region as the impact of Covid-19 begins to recede and vaccines are more widely available.

### Government Bond Yields



The chart shows the steady normalisation of bond yields across Europe.

For the month we are pleased to report performance remains encouraging and ahead of the peer group comparator benchmark for all Core and Core Plus portfolios for periods of 2 years or more\*. Our proprietary AB Momentum Indicator points to further global equity growth potential. Our decision to take some profits from US equities and to reallocate to UK and Europe is so far paying off. We are pleased to see gold back above the important \$1900 level. May has seen periods where growth-oriented companies such as technology stocks and value stocks such as cyclicals have both performed well although value has been the stronger over the full month.

We were delighted to launch a new range of Sustainable portfolios during May. The Sustainable range is designed to appeal to a broad church of modern investors who will similarly benefit from our Dynamic Asset Allocation and Risk First approach to portfolio management. Click to find out more [Sustainable Range | Alpha Beta Partners](#)

If you have any questions or feedback, please get in touch – as ever we would be very pleased to hear from you.

\* As at 31 May 2021.

## Featured Fund

### Brown Advisory US Sustainable Growth Fund

The Brown Advisory US Sustainable Growth Fund is an active fund within the Sustainable portfolio range. It provides US exposure whilst maintaining a goal of contributing to the UN Sustainable Development Goals and minimising ESG risks.

The Fund slightly underperformed its benchmark, the Russell1000®Growth Index in the first quarter. In its technology allocation, retraction in some of the fast-growing stocks were offset by strong performance from Dynatrace, Analog Devices, and Microsoft. Brown Advisory view this retraction in some of its technology stocks as temporary.

The health care sector, which has been a reasonably consistent contributor to the fund over the last few years, was an area of underperformance this quarter. In the fourth quarter of 2020, Brown Advisory reported that they trimmed many of their healthcare names in the understanding that organic growth will slow. This quarter, they resourcefully added to some healthcare names, where they believe that outlooks have been realistically re-evaluated. These additions include Edwards Lifesciences, who develop innovative technologies in the areas of structural heart disease and critical care monitoring to help patients live longer, healthier, and more productive lives. Brown Advisory predict that heart valve replacement surgery should start to pick up on the other side of the healthcare crisis. Brown Advisory also see another of their healthcare investments, Bio-Rad as being on a multi-year journey toward greater profitability. Bio-Rad develop and manufacture a range of innovative products for the life science research and clinical diagnostic markets. Their products advance the discovery process and improve healthcare.

We had a call with Katherine Kroll, Investment Specialist for the Brown Advisory US Sustainable Growth fund on 12th May 2021. Drivers behind the fund include looking for companies that are helping to solve environmental or social challenges, with solutions that are 'cheaper, cleaner, and greener'. They are also seeking out companies with an 'edge', which are doing something different and so not easily replaced.

Over the 3 years and since inception the fund has outperformed its benchmark. It provides our Sustainable portfolios with US exposure and unlike many of its US peers, the fund allows us to avoid certain big US stocks that we do not feel belong in a responsible portfolio, e.g., Facebook. We subscribe to the full liquidity, and value pricing of this fund. However, the strategy is not designed for private investors to access and offers no downside protection when and if markets fall. This is a strategy best selected by professional investors who fully appreciate the benefits and pitfalls and manage the portfolio in line with the mandate description and in sympathy with the prevailing economic and market driving forces.



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