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Quarterly Review

December 2021

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	Q4 2021	Return	Level
Equity	MSCI AW Index	6.39%	754.83
	S&P 500 Index	10.62%	4,766.18
	MSCI EM Index	-1.68%	1,232.01
	MSCI CH Index	-6.24%	612.93
	FTSE 100 Index	4.60%	7,384.54
Debt	BBARC GA Index	-0.67%	532.43
	US G2Y Index*	-0.71%	0.73%
	US G10Y Index*	-0.87%	1.51%
	US G30Y Index*	0.77%	1.91%
Infrastructure	S&P GI Index	4.13%	6,096.56

* TR on TSY futures

(Source: Morningstar 31/12/2021)

Our favoured markets ended the year at an all-time high, delivering further seasonal cheer to investors, and particularly those in Alpha Beta portfolios. Market capitalisation stands at a record high, significantly higher than global GDP, marking equities as expensive. This was the first pandemic with a hashtag, causing fear to spread faster and farther than before. Populations adapted quickly leveraging technology and new working practices. Consequently, corporate earnings proved robust, and valuations remained intact. Last year was about the consequences of the biggest demand shock for goods in 75 years—overwhelming the supply surge and awakening the inflationary beast from a multiple decade slumber. This year is likely to be about demand normalising, and how that impacts disinflation, relative demand, and employment.

Our anticipation of returning inflation stood out against more tranquil investment industry mood music last year and our forecast of inflation trending "higher for longer" was proven accurate and will remain so into 2022. In UK there will be a cost-of-living squeeze throughout the first part of 2022 where a confluence of events led by energy prices will impact us domestically. Globally we see disinflation coming through later in 2022 but it is unlikely central bank 2% inflation targets will be met in absolute terms.

As we enter 2022, the economic recovery remains firmly on track across developed markets. Less so, at this point, in the emerging world, especially China. We remain mindful of the possible impacts tightening monetary policy in US can bring and coupled with China's apparent crack down on media and ecommerce firms on the mainland and in Hong Kong. The unresolved defaults in the important property sector weigh on sentiment. Growth has been slower in China over the past quarter. However, we do anticipate the People's Bank of China maintaining accommodative interest rates and a supportive policy. Recovery is likely later into 2022.

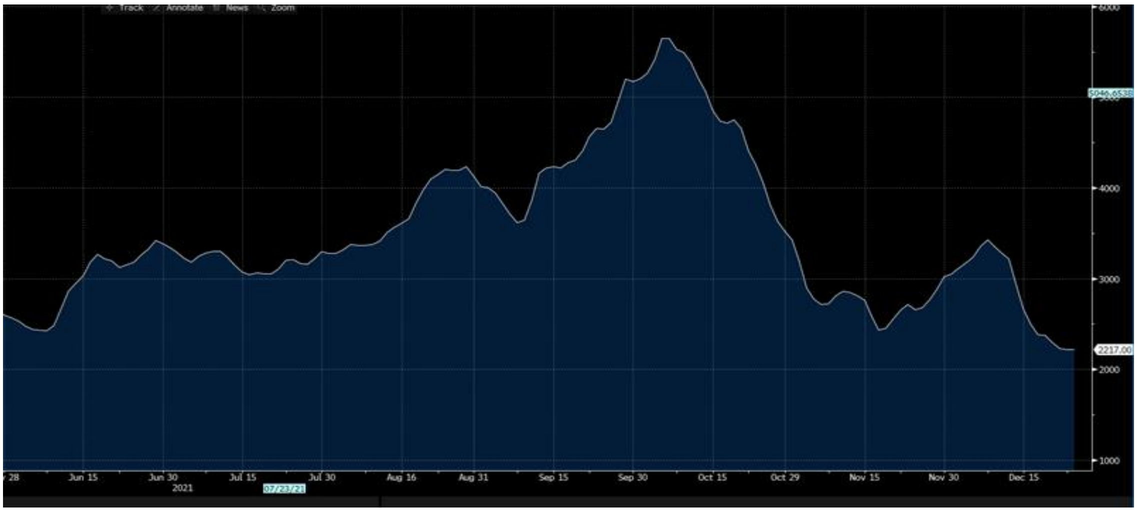
Equity markets, led by the US, have been relatively quick, this time, to shrug off news of the Omicron variant as data provided renewed confidence the strain, whilst highly contagious, would prove to be milder than many feared. Vaccinated populations continued life with only modest restrictions to personal freedoms.

The final quarter of 2021 was an interesting one, littered with event and political risks, as forecast in our Q3 Quarterly Update. In the United States the "debt ceiling" issue and monetary policy clarity were resolved whilst the Biden Administration's spending package was not passed. President Biden's approval rating has slumped following the botched Afghanistan exit and with the onset of inflation. The mid-term elections later this year will prove an interesting event, although for now several months distant.

The Federal Reserve meeting during December set a clear course for higher rates in 2022 but an ongoing commitment to support markets if conditions turn weaker. This central bank strategy is likely to be adopted more widely. The Bank of England after what can only be described as a pregnant pause cautiously raised rates 0.15% from a record low-point. Forward visibility is helpful to equity investors, at least for now.

The major central banks in developed markets led by the Federal Reserve gave notice that liquidity will be withdrawn steadily as economic conditions allow. Markets had already penciled-in a reduction in bond purchasing by the Federal Reserve and some uplift in the interest rates, so this was not much of a surprise. Nonetheless, the tapering decision did bring some volatility to equities.

As the global economy makes its transition into a post-covid era, we envisage a normalisation of monetary and fiscal policies. Inflation has been and remains the major concern with US CPI registering 6.8% in November. Indices which track some of these inflationary catalysts now show a sign of moderation and point towards a drop in costs in the coming years. One such index is the Baltic Dry Index which tracks the cost of bulk shipping around the world as shown in the chart below:



(Source: Bloomberg 04/01/2022)

Whilst the broader inflation number (CPI) is expected to moderate as we move towards normalisation, we expect the wage and rent pressure to remain persistent.

The US central bank expects long term inflation to be at or near its 2% target. Bond markets are currently pricing a breakeven inflation number of 2.64% for a 10-year treasury. The market breakeven inflation rates for the US treasury are shown below:

Largest Breakevens	
1) US Breakeven 2 Year	3.30
2) US Breakeven 3 Year	3.07
3) US Breakeven 4 Year	3.00
4) US Breakeven 5 Year	2.99
5) US Breakeven 6 Year	2.97
6) US Breakeven 7 Year	2.85
7) US Breakeven 8 Year	2.74
8) US Breakeven 9 Year	2.69
9) US Breakeven 10 Year	2.64
10) US Breakeven 20 Year	2.46
11) US Breakeven 30 Year	2.41

(Source: Bloomberg 04/01/2022)

Whilst the latest US CPI inflation figure is a whopping 6.8%, the bond market reaction remains muted. The US treasury yield curve remains in flattening mode and there was no material shift during the quarter. It seems for now at least that the market either believes 1) the Federal Reserve's projections will be delivered and inflation will ebb away, or 2) the central bank's tightening interest rates into slower economic growth ahead represent policy error and may trigger the next recession. Either way, it will be interesting to see the impact on longer dated yields as quantitative easing is finally withdrawn. Given the sharply negative real yields on offer, scope must remain for longer dated yields to rise, perhaps 50-100 basis points, over the next 12 months, from current levels.

Both UK and European equities (STOXX 50) registered a positive quarter despite the new wave of Covid-19 infections in Germany, France, and the UK. We remain of the view that current labour shortages in the UK are not expected to have a material impact on GDP growth, which is once again likely to lead the G7 growth rates for another year. Possible unfolding wage rises ahead of long-term inflation remain a concern and if manifested could unseat progress at home.

Our in-house proprietary technical indicators pointed to a positive change in momentum since the Omicron emergence at the end of November and suggest some further upside in US equities is achievable in the near term. We marginally increased our US equity exposure in late December. We expect equities to perform strongly in the first quarter with earnings momentum from 2021 still likely to provide a supportive tail wind. Central bank policies and bond market reactions will remain our areas of greatest short-term interest. We look forward to 2022 with enthusiasm and hope to see a normalisation of activity and policy which should provide support for a decent year if forward corporate earnings growth can be preserved.

Written by the Alpha Beta Investment Team.

Our Portfolio Returns:

AB Core Performance %	Year to Date	Quarter to Date	Month to Date
Alpha Beta AB1 Core	4.55	1.69	0.37
Alpha Beta AB2 Core	6.66	2.10	0.71
Alpha Beta AB3 Core	9.16	2.60	1.17
Alpha Beta AB4 Core	12.95	3.56	1.74
Alpha Beta AB5 Core	12.89	3.52	2.06
Alpha Beta AB6 Core	12.27	3.54	2.14

AB Core Plus Performance %			
AB Core Plus Cautious	5.55	1.95	0.78
AB Core Plus Cautious Balanced	7.34	2.19	1.18
AB Core Plus Balanced	10.60	3.01	1.36
AB Core Plus Balanced Growth	13.69	3.68	1.88
AB Core Plus Growth	10.80	3.22	1.92
AB Core Plus Adventurous	10.08	3.32	1.84

SRI & Ethical Portfolios Performance %			
AB SRI Defensive	3.45	1.54	0.25
AB SRI Balanced Income	9.56	2.48	2.26
AB SRI Balanced Growth	16.22	3.47	1.04
AB SRI Adventurous	14.83	2.56	1.51
AB Ethical Balanced Income	8.35	1.28	1.78
AB Ethical Balanced Growth	17.27	3.73	0.81

(Source: ABP and Morningstar, Date: 31/12/2021)

Written by the Alpha Beta Investment Team.

Contact: **Andrew Thompson**
Tel: 07968 934127
Email: at@alphabetapartners.co.uk

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Alpha Beta Partners Ltd.
Northgate House, Upper Borough Walls, Bath
BA1 1RG
info@alphabetapartners.co.uk I 020 8059 0250

www.alphabetapartners.co.uk