Alpha Beta
PARTNERS

Quarterly Review

December 2020

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	Q4 2020	Return	Level
Equity	MSCI AW Index	14.68%	646
	S&P 500 Index	12.15%	3756
	MSCI EM Index	19.70%	1291
	MSCI CH Index	10.66%	108
	FTSE 100 Index	10.86%	6461
Debt	BBARC GA Index	3.28%	559
	US G2Y Index*	0.06%	0.13%
	US G10Y Index*	-0.32%	0.93%
	US G30Y Index*	-0.34%	1.65%
Infrastructure	S&P GI Index	15.03%	2545

(Source: Morningstar)

The final quarter of 2020 saw the fantastic news of not one but three Covid-19 vaccines. The whole world simultaneously breathed a sigh of relief. However, for now the World Stringency Index which tracks population mobility clearly shows the increased severity of lockdowns around the world. Covid-19 variants are a concern too of course, although we anticipate the vaccines are able or are adaptable to tackle the issues at hand. Mass roll-outs and vaccination of millions of people will bring new life experiences for us all.

The US election concluded with a Democrat win and after some time and some wrangling it now appears the Democrat "blue wave" controls both Houses. This is a more one-sided outcome than we anticipated. Markets have celebrated this win during early January, although there are some implications to spending and down-stream inflation, plus potential of tax hikes and "Giant Tech" control measures which we must keep under close observation.

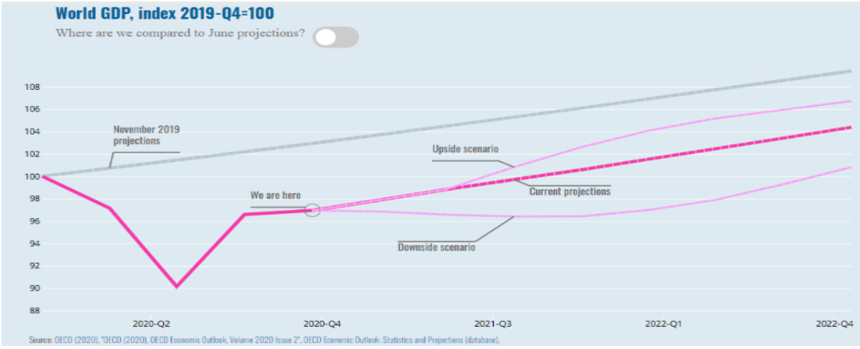
The interminably tedious Brexit saga reached a climax and as expected produced a last minute deal between the EU and Great Britain. The deal resembling more of a Canada type structure than anyone thought probable. In reality the deal is "thin", does not as yet support the GDP-significant Financial Services sector but is certainly somewhere positive to start. We are encouraged and UK markets have sparkled as a result, with our increased UK weightings offering pleasing inputs to portfolios. Sterling rallied quickly, damaging non-UK performance but has since settled back within a narrow range, where we expect it to trade for a period of time.

The past 8 months or so have proven beyond anyone's doubt that markets and risk asset prices reflect the future and not the past or present. The real economy just about everywhere entering a slowdown or recession yet equity prices rallying and in some cases driving hard into overbought territory. Central banks have been largely responsible for the rally although technology giants and others deemed to be beneficiaries of the "new normal" post pandemic have seen genuine earnings growth. Set against the awful economic backdrop, markets have rewarded these companies with super-normal share price growth.

Oil prices and the leading indicator commodity copper have shown stability and growth, which is positive indeed. The dollar, as forecast, continues weakening in absolute and trade weighted terms which has in turn stimulated gold and Bitcoin to new highs. Mainstream

central banks, including the ECB and Bank of England are conducting feasibility studies around the potential for digital currency deployment in the future.

Whilst economic data points to strong forward momentum, in absolute terms output remains lower than pre-Covid levels. The new wave of lockdowns will impact Q1 and Q2 results this year, depending of course on how long the lockdowns last. The chart below shows world GDP forecast by OECD for 2021 and 2022.



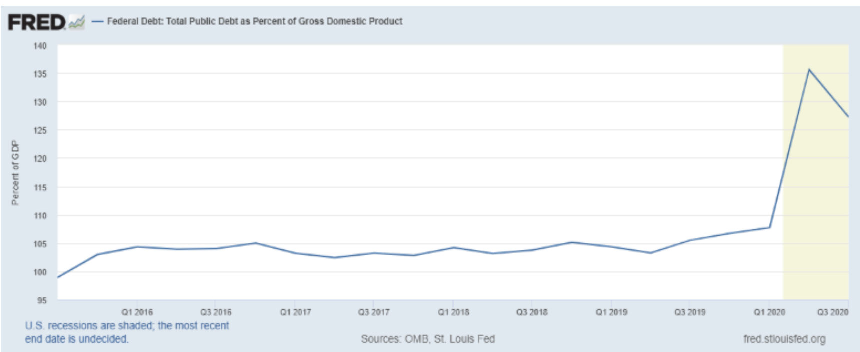
According to the OECD's forecast, the world's GDP is expected to recover to 2019 levels during Q3 2021. The developed economies are expected to recover by the end of 2021. The expected growth rate for the UK economy is 4.2% for 2021/22. The market-implied growth rate for the UK is around 5%. The US is expected to rebound with a relatively modest 3.2% growth whilst the Emerging Markets look to grow the most, especially China with an expected 8% in 2021. A far rosier picture than a year ago!

We should remember that a recovery in developed markets will invite other headwinds such as fiscal tightening, inflation and possible monetary policy changes. We remember 1994 – not all investment managers controlling client money today do! Solid experience and quality information helps us make better decisions.

We maintain our stance on inflation, and we expect central banks to allow it to "run hot" in a post-Covid world.

The Democrats plan to add another trillion dollars of stimulus debt in short order. This is likely to push risk asset prices further. Modern Monetary Theory relies on the careful monitoring of inflationary pressure whilst stimulus is poured into the economy. Balancing output and demand is the key to avoiding inflation – or "Capacity Utilisation" to use the modern vernacular. We remain vigilant and monitor signs of positive and negative outputs from this Modern Monetary Theory policy currently in play. Weaning markets off this debt-financed liquidity will not be easy. That is something to worry about later…

The chart shows US debt to GDP which has spiked upwards in recent times.



Equity markets, especially the US, appear overpriced. Fundamental ratios such as the Cyclically Adjusted Price Earnings ratio point to a slower growth period ahead and relatively lower returns for the US. As discussed in previous updates, our near-term price target for the S&P 500 was around 3700. There is the possibility of a slowdown in US and linked markets in the short term, but medium and longer term we remain in a positive mindset. We are equally aware of the power of stimulus and that “free money” may nudge markets further north. For now, in the US risk/reward ratios have begun to appear stretched.

By contrast, we observe UK, Europe, and Emerging Markets are set to benefit possibly more from this excess liquidity post-Covid. These markets are attractively priced on a relative basis and have a higher growth trajectory for the next 2 to 3 years. We have marginally reduced our exposure to US equities and expect to increase our exposure to higher growth markets when prudent to do so. Alpha Beta portfolios have performed well during the period. Thank you for your support and please do get in touch if you have feedback or questions. As ever, we would like to hear from you.

Our portfolio returns:

Performance %	Year to Date	Quarter to Date	Month to Date
AB1	5.33	3.59	1.21
AB2	5.98	4.69	1.40
AB3	6.30	5.58	1.48
AB4	6.92	6.83	1.52
AB5	7.59	7.84	2.04
AB6	7.41	8.70	2.49

(Source: ABP and Morningstar, for Indexed funds solution, Data 31/12/2020)

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