TAM ETHICAL PORTFOLIOS

QUARTERLY COMMENTARY: Q1 2019

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MARKET Review

Equity markets across the board had a strong start to the year, with US stocks rebounding off December lows to have their best start to a year since 1987. Market volatility came down sharply as robust US jobs data, the possibility of a trade truce between the world's two largest economies and the Fed's signal of a slower path of rate rises, contributed to the bounce back in global stocks.

In general, riskier assets outperformed in Q1, including small-cap stocks, economically sensitive stocks such as those in the energy and industrials sectors and emerging market (EM) equities, helped by a slowdown in the strengthening of the US dollar.

Brexit continued to drive volatility in UK equity and currency markets. The British Parliament did not manage to agree on the kind of Brexit it wants when "indicative" votes were held, offering 8 different options on how the UK should break up with the European Union, after MPs twice rejected Prime Minister Theresa May's Brexit deal. This was despite May's announcement that she would resign if Parliament backed her Brexit plan.

The Fed took a surprisingly dovish stance, signalling that it did not expect to raise rates this year due to concerns about a weaker US economy. This led to a key measure of the US yield curve inverting for the first time in over a decade, a move widely seen as indicator of a coming recession. Concerning manufacturing data from Germany also led to a rally in safe investments and contributed to the nervous sentiment in stock markets at the end of the quarter.

PERFORMANCE REVIEW

The performance data below relates to the period 1st January 2019 – 31st March 2019.

	PORTFOLIO	BENCHMARK	RELATIVE
Defensive	1.92	1.38[1]	0.54
Cautious	3.03	2.98[2]	0.05
Balanced	4.51	4.18[3]	0.33
Growth	6.08	5.82[4]	0.26
Adventurous	7.31	7.06[5]	0.25

Notes on Benchmarks: FTSE All-Share Index + Cash (1 Month Libor) in the following proportions: 1) 15% + 85% 2) 35% + 65% 3) 50% + 50% 4) 70% + 30% 5) 85% + 15%
Source: TAM Asset Management Ltd.

Most UK equity funds outperformed the benchmark given their large exposure to FTSE 250 companies which generally outperformed FTSE 100 companies in Q1. Our US and EM equity positions benefited from stronger risk appetite over the quarter, driven by improved global trade sentiment.

The largest detractor came from exposure to Japanese equities which continued to get caught up in global trade volatility. A portion of our global equity exposure also failed to keep up with the strong UK benchmark, while our European equity fund underperformed due to the impact from weak European economic data.

PORTFOLIO ACTIVITY

There were few changes to portfolios over the quarter. On the equity side, we made a small increase to our UK exposure to take advantage of attractive valuations, as it became more likely that we would get a soft Brexit. We also took the decision to reduce our exposure to Japanese equities, as our conviction in Japan as an export-orientated economy to remain resilient during a period of slowing global growth, has moderated.

There were no changes on the non-equity side of the portfolios over the quarter.

OUTLOOK AND STRATEGY

While markets have had a robust start to the year, there remains a fair amount of geopolitical risk that could hamper the progress that's been made repairing last year's losses. We believe it is prudent to remain cautious this year given the extent of Q1's rally which will undoubtedly be hard to replicate. We expect intermittent volatility to persist until some clarity is reached on geopolitical issues such as Brexit and trade, but also as a result of investors taking profits and keeping cash on the sidelines.

We feel there is a strong possibility of a breakthrough in Brexit and trade talks in Q2 which could provide another boost to investor sentiment and, given the amount of cash on the sidelines, result in a significant amount of capital returning to the market, spelling the next leg of the recovery from 2018.

We favour domestically-focused companies in the UK over the more internationally exposed businesses as we anticipate a soft Brexit, while we have become less positive on European equities due to weak economic data and continued political troubles. We remain constructive on EM assets, particularly as the Fed is now looking increasingly dovish, which should put a ceiling on the US dollar's ascent and help EMs to sustain their strength into the second quarter.

We hope to be as surprised with markets in Q2 as we were in Q1 as we anticipate global headwinds beginning to abate, however it will undoubtedly be another quarter of "hold your breath" and keep one finger on the sell button, whilst electively taking risk in certain areas and maintaining enough cash to deploy should markets take a lurch lower.

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