Close Brothers Asset Management

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Close Portfolio Funds

Monthly fund manager update

JANUARY 2021

RIITTA HUJANEN
Managing Director

MONTH IN REVIEW

The Close Portfolio Funds all delivered marginally negative returns in January as investors paused to consider what 2021 might bring. The Conservative Fund returned -0.16%, Balanced fell -0.18% and Growth dropped -0.38%. Their relevant IA Sectors returned -0.36%, -0.28% and -0.11% respectively (see below).

EARLY THOUGHTS ON 2021

We are pretty happy with how the year has started for the funds. There have been no major disappointments and quite a few strong performers, especially in equities. Shares in **Applied Materials** (a semiconductor machine producer which we bought at the end of December) got off to an impressive start adding +18%, followed by +15% for **eBay** (another relatively new investment from 2020), and the long-held technology giant **Alphabet**, which has advanced nearly +10% (all year-to-date). Not bad for the first few weeks' work.

In addition, the full-year 2020 reporting season is off to a pretty convincing start. Roughly 80% of US companies which have reported so far have met or exceeded earnings expectations. The Funds' holdings rarely disappoint on this front (thanks to our quality bias) and traditionally deliver as expected or better, so we feel 'no fear' as earnings season kicks in fully in February.

Looking at the current market, we make three observations:

COVID-19 TUG-OF-WAR

This refers to the on-going investment debate between Value/Cyclical and Growth/Quality stocks. The former are associated with 'risk-on', back to work, 'vaccines will helps us through'; while the latter are linked with 'risk-off', stay-at-home, 'lockdown for longer scenarios. The pendulum swings wildly between these two camps. We have been leaning slightly on the more cautious side with a preference for less cyclical, more Quality/Growth style investments. The three aforementioned star performers represent that category. However, as time passes, we can see a path towards a more cyclical recovery, which has already partially started in Asia. Therefore, we are currently focusing our research efforts on several new ideas and preparing to add some more Cyclical/Value exposure, when the time is right. There is no rush on this front however - in any case, it is important to keep a balanced approach.

INFLATION SCARES

The hope for a cyclical recovery could bring inflation into the picture. Could the prevailing loose financial conditions combined with already very low interest rates mean that inflation risks are rising? Price stability has persisted for years due to competitive pressures globally, low economic growth, the use of technology and aging populations. Our research in this area has led to the following findings: inflation in services has been higher, less volatile and in-line with the growth in wages. Inflation in goods has historically been lower, although more volatile, and correlated with commodity prices. In the pandemic, services have been impacted by mobility restrictions, with pent-up demand likely building. This could cause demand-pull inflation once restrictions have eased. Demand for goods, on the other hand, has been 'V-shaped', but with deflationary pressures still persisting.

In the short-term, increases in inflation will be driven by commodity prices, which will likely occur once March 2020 lows become comparators. But in the current environment, sustained inflationary pressures are unlikely with core inflation forecast to remain muted. Significant disruption to global supply chains and de-globalisation, however, could cause longer-term inflationary pressures. This has negative implications for fixed income securities and we therefore intend to keep our underweight position and maintain low duration to control interest rate risks in the Funds.

POSITIVE OUTLOOK FOR EQUITIES

We continue to like innovative quality growth companies for the long-term. Technology companies – the likes of **Microsoft**, **Accenture**, **Checkpoint Software** and **Cerner** - and selected Financial Services companies, such as Stock Exchanges and Asset Managers (**3i plc**, **Schroders**, **Partners Group**) drive profitable structural growth in the portfolio. At the same time, we will keep an eye on the near-term economic recovery. There could be much pent-up demand for goods and services after the lockdowns end. In the most positive scenario it is possible that the global economy experiences another 'roaring twenties'. That is what happened after the previous pandemic, a century ago. It may feel distant at the moment but this outcome cannot be excluded. To a certain extent, we are already seeing higher demand and increasing prices in raw materials, for example. This is why we also hold cyclical base material producers, such as **Rio Tinto** and **Anglo American** in the Funds, alongside precious metals like gold, silver and platinum in physical ETF holdings. In order to strike a balance between Growth and Value, we also hold consumer-oriented stocks such as **Asahi** for beer, **Mowi** for salmon and **eBay** for online retail. We remain optimistic; based on our quantitative valuation framework, positive returns are expected in all major markets. We are confident that 2021 will provide the opportunity to increase both prosperity and charity, so let's keep on keeping on.

CLOSE PORTFOLIO FUNDS DISCRETE PERFORMANCE AS AT 31 JANUARY 2021

	YTD	2020	2019	2018	2017	2016
Close Conservative Portfolio Fund	**-0.2%**	**3.0%**	**12.5%**	**-2.7%**	**9.0%**	**5.4%**
IA 20-60	-0.4%	3.5%	11.8%	-5.1%	7.2%	10.3%
Close Balanced Portfolio Fund	**-0.2%**	**2.4%**	**17.1%**	**-2.9%**	**11.8%**	**6.3%**
IA 40-85	-0.3%	5.3%	15.8%	-6.1%	10.0%	12.9%
Close Growth Portfolio Fund	**-0.4%**	**5.4%**	**21.9%**	**-3.4%**	**12.5%**	**6.8%**
IA Flexible Investment	-0.1%	6.7%	15.7%	-6.7%	11.2%	13.8%

SOURCE:
FE Analytics 03.02.2021; 2021 (YTD) data as at 31.01.2021; fund performance is total return net of fees with dividends reinvested for X Acc share class.