RESPONSIBLE AND SUSTAINABLE GLOBAL EQUITY FUND

COMMENTARY FOR QUARTER TO END DECEMBER 2021

PERFORMANCE

	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Fund Performance (B Class)	2.57%	6.03%	19.29%	58.55%	63.54%	169.58%
FTSE World TR GBP	6.92%	9.06%	22.07%	69.01%	85.63%	282.22%
IA Global	4.67%	6.58%	17.55%	64.66%	76.79%	221.25%
Sector Quartile	4	3	2	3	3	4

Source: Morningstar. Figures compared on a Bid to Bid basis with Net Income Reinvested.

REVIEW

Global equities delivered a total return of 6.9% (in Sterling terms) in the fourth quarter as many equity indexes closed the year at or near all-time highs, with equally record breaking equity inflows. Despite the strong returns, the quarter had storm clouds aplenty with rising COVID-19 cases, spiking inflation and signals of less accommodative central bank policy for 2022. Volatility increased in November, as markets weighed the emergence of a new Covid-19 variant Omicron, leading to underperformance from the economically sensitive “opening-up” beneficiaries. More transmissible, the variant spread globally quickly, outcompeting previous forms of the virus. Despite the ballooning daily cases, optimism rose as data pointed to the strain being less severe and resulting in lower hospitalisation rates than prior waves. Supply chain dislocations and related inflationary pressures continued in Q4, leading to increasingly hawkish commentary from central banks and a slump for growth stocks at the end of the quarter. Even with these headwinds, corporate earnings, economic data and sentiment remained surprisingly resilient over the period.

From an environmental perspective, the major event was the UN Climate Change Conference (COP26) held in Glasgow following the relatively underwhelming G20 conference. The meeting was particularly timely against a backdrop of energy prices reaching record highs poignantly framing the security of supply, resiliency and transitional challenges. Headline announcements included more than 100 countries pledging to cut methane emissions by 30% and a goal to halt deforestation, both by 2030. Whilst we felt the overall progress fell short of the scale and urgency required, it illustrated the important role the private sector must play in order to transition to a just net zero within our current energy market.

Looking to equity market performance, US equities outperformed all other regions, returning 9.6% in Sterling terms as the S&P 500 reached new highs and rose 11% in dollar terms for the quarter. US markets were buoyed by a robust Q3 earnings season led by tech stocks, in addition to a strong economic backdrop with retail sales, non-farm payrolls and initial jobless claims all reported better than expected in November. The US CPI reached a staggering 6.8% in November, the highest in 39 years, building the narrative that inflation is less transitory than central banks had anticipated. As cases of COVID-19 rose across the US at the end of the year, the news that the new Omicron variant outcompeting Delta was less severe, bolstered hope of less economic disruption and also made the case for a more hawkish stance by the Federal Reserve. The Fed will start tapering asset purchases in January and forecasted three rate hikes for 2022. Possibly in sympathy with the hawkish pivot, the ambitious Build Back Better spending bill at c.$1.7trillion, with $550billion additional infrastructure spending, stalled in December after failing to garner a majority in the Senate.

Equity markets in continental Europe produced robust gains, the FTSE World Europe ex UK returned 7.5% in Euro terms with return reduced to 5.2% when translated into Sterling terms. Whilst several nations introduced new restrictions to slow the growth of Omicron, economic impact has been markedly lower compared to previous waves as a function of vaccination programs and the indicated lower severity of the variant. Instead inflation ranked higher on central banks list of concerns, with Europe hit by record gas prices driven by short supply. Generally resilient corporate performance outside of hospitality and travel allowed the market to overlook headwinds to an extent. In similar step with the US, the European Central Bank announced that they would end the pandemic emergency purchasing program in March, however retain the belief that inflationary remains transitory and will return to 2% target towards end of 2022.

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Within the UK, the FTSE All Share returned 4.2% over the period with defensive sectors outperforming the more economically sensitive despite some recovery towards the end of the quarter. In December, The Bank of England raised interest rates by 10bps to 0.25%, as high inflation and a tight labour market outweighed concerns from the growing COVID-19 infections.

Equity markets in Asia Pacific ex Japan delivered returns of 2.1% in Sterling terms underperforming global equities. Whilst other global economies experienced a relief rally on the news that the new Omicron variant was less severe, given the traditionally harder line taken by nations in Asia such as China's zero COVID-19 policy (focus on zero infections), significant economic disruption remains a distinct risk. Whilst other major markets tighten monetary policy to cope with inflationary pressures, the Peoples Bank of China took further dovish action which is expected to continue into 2022.

Japanese equities were the global laggard in Q4, previously the best performing region in Q3, returning -4.9% in Sterling terms. The depreciated Yen weighed on returns as the general election with the new Prime Minister drew most of the attention before fiscal stimulus discussions could occur. The economy also contended with rising input costs and supply chain dislocations which particularly hurt the production of big ticket items in Japan.

PERFORMANCE & ACTIVITY

The Edentree Responsible & Sustainable Global Fund rose 3.0% in Sterling terms for the fourth quarter, underperforming the FTSE World benchmark total return of 6.9%. Against the IA sector group, the fund is ranked fourth quartile on a three month basis. For the year, the fund finished second quartile, returning 19.3%.

From an allocation perspective, the underweight position in the US was challenging with US markets delivering a 9.6% total return, c. 5% ahead of most other markets. Leadership was relatively narrow, with technology shares and mega caps driving performance. More broadly, the Fund's underweight to global large caps was a headwind, as they significantly outperformed gaining 7.5% during fourth quarter, while global mid-cap and small-cap actually fell 1.1% and 2.3% respectively. Elsewhere, the overweight positions in Europe and UK dragged as the regions returned modestly below benchmark returns, which collectively with the US underweight summed to 0.8% headwind at fund level. Some of this was offset by Japan, which reversed its best performer status from Q3 to be by far the worst performer in Q4, falling c.5%, while our holdings only fell 3.3%.

Overall stock picking for the year has been strong with the Fund delivering relative outperformance in all regions except Europe ex UK where the Fund's holdings returned 15% relative to the benchmark's return of 17.4% during 2021. The final quarter of the year saw more mixed regional stock picking with the US, UK being more challenging. The Fund's US holdings gained 5.4%, c.4% less than benchmark with Everbridge, the leader in critical event management software falling over 50% on the unexpected news that CEO was leaving to join an upcoming IPO (Boomi), prompting investors to question the 2022 earnings outlook and future leadership. Not holding "mega-cap" US tech stocks Apple, Tesla and Nvidia which gained 25%, 36% and 41% respectively was a sizeable 1.1% headwind at portfolio level. That said, the Fund's tech holdings of Marvell Technology (45%), Lam Research (32%) were valuable contributors adding almost 1% at fund level. Our UK holdings fell 1.9% despite UK markets gaining 4.6%, led by IP Group which saw some profit taking (-11%) following the successful IPO of its largest holding Oxford Nanopore.

In terms of sectors, as highlighted above technology returns were buoyant gaining 12.2%, while the fund's holdings returned 8.8% despite the mega-cap and Everbridge headwinds. The healthcare sector saw mixed returns as the fund's medical equipment providers fell 9.6% led by Medtronic and Philips which are both battling against lower procedural volumes due to COVID-19 and product related issues. In contrast, our holding in Cerner, the provider of efficient electronic health record systems was subject to a $30bn bid by Oracle, famous for its databases, driving the stock up 32% for the quarter

In terms of investment activity, we exited Swedish speciality paper maker Billerudkorsnas following strong performance over the last three years as the company resolved its operational challenges and executed on its innovation opportunities. The stock's re-rating over this period was reflective of this progress, and as such valuation (prior to the Verso acquisition) was no longer attractive. In the US, we exited Cisco due to lower conviction in the fundamentals, and reduced our positions in Bruker and Boston Scientific following strong performance. Within Med-tech, we switched to favour Medtronic, which had meaningfully underperformed its peer, as well as adding to Lam Research in October. In the UK, we added to Biffa following an exaggerated reaction to quarterly earnings released in November. Further meetings with management supported our high conviction in their circular economy and broader sustainable initiatives, while the valuation remains at a material discount to global waste management peers. Additionally in the UK we added to DS Smith, for similar undervalued sustainable characteristics.

OUTLOOK

2021 was unquestionably a risk-on environment, 2022 is unlikely to provide equivalent returns. The extent of monetary and fiscal stimulus that entered the financial system created arguably more than a few anecdotal signs of excessive risk-taking behaviour which need to be addressed in 2022. Yet it has taken only a short-time for the US central bank's "transitory" outlook on inflation to evolve into a rapidly more hawkish assessment. As highlighted last quarter, this has partly been driven by the extent of inflationary pressures, with CPI in the US at c.7%, with "core" CPI over 5%, levels last seen in 1982. The primary factor driving this more hawkish outlook is the level of unemployment. The Fed's dual mandate of price stability and full employment has historically provided on numerous occasions for policy inertia, however with the December unemployment rate at 3.9% it appears there is much less justification for inaction. It's been apparent for some time that the rebounding economy has encountered numerous supply side constraints and bottlenecks, however the broader concern at this juncture is to what extent labour market constraints could trigger a similar feedback loop into wages. Evidence of any stagnation in labour participation will only add to these concerns.

The market's immediacy in pricing in three to four interest rate hikes in 2022, highlights the challenge the Fed faces in managing the pace of tightening. There remain several hurdles to clear in order to get back to more neutral monetary conditions, namely removing QE through faster tapering, raising rates (at least to 1.5%) and then, potentially, quantitative tightening. Historically, how negatively the equity markets have reacted to the arrival of tighter conditions has been a source of concern for the Fed, reflecting the equity market's prolonged conditioning to zero interest rates and Fed puts. Relative to previous taper false starts, the primary difference today is the inflation and employment backdrop, which may provide less latitude for such policy procrastination.

Stepping back, central bank liquidity has long been recognised as a key factor underpinning equity markets since 2008, and particularly supporting long duration assets such as high-growth equities, which have risen close to 600% since the end of 2008, outperforming value peers by over 310% since end of 2008. Given the material PE expansion witnessed since the end of the Global Financial Crisis, it would be imprudent to expect this trend to continue. As central banks look to wind down their asset purchase programmes, equity markets will need support from secular economic drivers, which include addressing the numerous sustainable challenges currently faced. Despite this incremental tightening backdrop, we continue to retain the view that the environment for sustainable investing has never been more supportive. From a fiscal stimulus perspective, several major economic powers have enacted stimulus directed to enabling a lower carbon economy. As significant incremental capital is channelled towards sustainable challenges, coupled with the reversal of highly accommodative monetary policy, we remain acutely aware that we must retain a healthy valuation discipline while recognising the scarcity context.

To obtain further information please speak to your normal EdenTree representative, visit **www.edentreeim.com or call** our support team on **0800 011 3821**

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