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PORTFOLIO UPDATE – DECEMBER 16, 2019

We find ourselves entering a season of great expectations as Alexander Boris de Pfeffel Johnson returns from what could easily have become the graveyard of his brief premiership with a decisive Tory win in his satchel. Whether one believes Brexit is a good thing or a bad thing for the UK or the broader European Union, the uncertainty around policy was preventing businesses, markets and economies from charting a way forward, and that uncertainty is now largely lifted. We have gone from a Brexit process as shambolic as Boris Johnson's hair to a clear path toward leaving the Union. All of the big issues do still remain, from a hard vs. soft Irish border to trade pacts between the UK and mainland Europe. Investors can at least envision what "after" looks like now, and can begin pricing structure and risk on that basis.

The immediate reaction from the investment community has been mixed. Some early enthusiasm carried stocks in the European sphere higher along with the Pound, only to be doused by renewed worries that the direction (out) is certain, but the method is not. A "no deal" Brexit appears to still be on the table according to Johnson, which may be reality and may just be a negotiating ploy. What we take away is that in the long term we know that the United Kingdom (we will assume that Scotland stays in the UK, which is increasingly debatable) will not be part of the EU, but in the short term there could be disarray. Markets are showing us a modest upgrade is valuation after a record low relative equity valuation vs the Eurozone and US, a currency re-valuation, and positive reactions to pro-growth policies likely to be implemented in the near/intermediate term.

A moment of short term uncertainty but long term clarity is usually when we seize the moment to make a tactical shift. After an extended period away from the UK and the GBP, in those portfolios with explicit levers we have modestly increased our exposure to UK equities and the Pound by purchasing an unhedged UK ETF funded by existing hedged UK equity and a small amount from US large cap equity. In portfolios such as our ESG series where we do not have a dedicated UK position, we have increased our allocation more broadly to international developed markets on the assumption that improving UK prospects will generally benefit all. This move was also funded from US large cap equity. Similarly, in our Disciplined Yield series the allocation was assigned to an international developed yield-emphasis ETF.

The long term is a relative proposition, and the time-value of money will dictate patience with this tactical shift. A hard Brexit vs. a more orderly exit, for instance, could mean that the stability that should come from knowing where we are headed would be pushed indefinitely out into the future and may sufficiently upset markets in the now that we would revisit the call and choose another (re)entry point down the line.

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