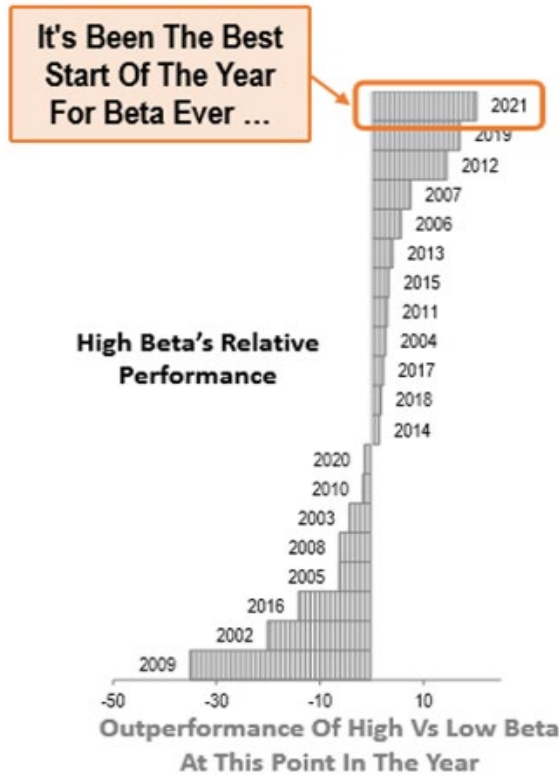


Beta in Focus



Source: Cornerstone Macro

We have several fans of the Atlantic Coast Conference basketball teams in our office, and ahead of this week's tournament, it tends to be helpful to keep an eye on which team is playing well coming into the tournament. In terms of this year's stock market, high beta is one characteristic that is playing well. Higher-beta stocks can be described as those with higher volatility and, from an academic perspective, higher systematic, or stock-specific, risk.

In the chart above, Cornerstone Macro highlights the remarkable start for high-beta stocks in 2021. While several characteristics are performing well year-to-date, we'd like to focus on high beta, as Cornerstone Macro states that, "the recent outperformance of high beta and lower-quality fundamentals (i.e., negative earnings, most shorted, etc.) has coincided with the significant reacceleration we've seen in economic data (i.e., PMIs, NAHB Housing data, etc.) as well as the easing of financial conditions." Their observations appear to be

confirmed in the data from Bank of America below, showing that, over the past three months, lower-quality stocks (C&D rated, according to BofA) outperformed A+ stocks by ninefold.

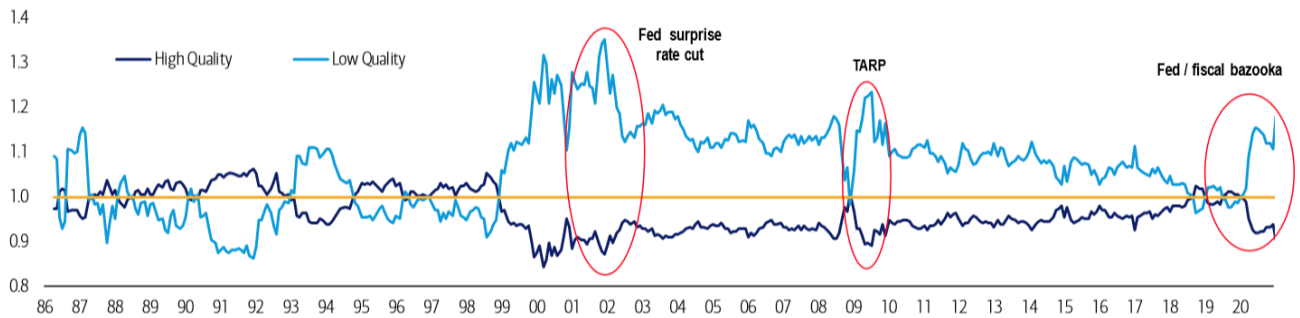
Quality Indices (1)	1 M	3 M	6 M	12 M	YTD
A+	4.11%	3.19%	10.92%	24.99%	0.85%
A	3.53%	2.73%	11.09%	22.49%	0.11%
A-	6.71%	9.85%	23.46%	27.32%	5.72%
B+	6.74%	12.60%	27.90%	35.87%	7.66%
B	6.93%	15.26%	31.71%	38.19%	9.85%
B-	11.61%	39.37%	63.01%	69.16%	30.05%
C&D	1.72%	27.68%	56.79%	56.52%	16.91%

Source: BofA Global Research

How long could this trend last with the ample fiscal and monetary stimulus employed to support the U.S. economy and reduce unemployment closer to 4%? We are not economists. However, we would note that Cornerstone Macro believes that "the beta trade is likely to be flat/range bound in the year ahead." Cornerstone bases their assessment in large part on economic data that is nearing all-time highs across a number of metrics.



**Exhibit 14: Fiscal and monetary stimulus has buoyed risk assets but with diminish returns**  
 B+ or Better vs. B or Worse Fwd. P/E relative to BofA Universe (1986 – present)



Note: TARP stands for Troubled Asset Relief Program  
 Source: BofA Global Research, FactSet, BofA US Equity & US Quantitative Strategy

BofA notes that economic and fiscal stimulus appears to be peaking, but also highlights the increasing valuation disparity between high- and low-quality stocks in the market. As seen in the chart above, lower-quality stocks tend to benefit from government stimulus, where “a rising tide lifts all boats.” While we are bottom-up managers, we are constantly on the lookout for market anomalies that can increase the chance of success for our investment strategies. In addition, by employing our consistent investment approach of identifying

investment opportunities with quality characteristics, in terms of return on capital and strong balance sheets, coupled with compelling valuations, the combination should help us take advantage of opportunities presented in this unique start to the New Year.

As always, thank you for your interest and trust in managing your investments.

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