MONTANARO
ASSET MANAGEMENT

# Montanaro Better World Fund

**Quarterly Commentary – Q1 2022**

## Market review

**After a difficult start to the year, the Fund stabilised in March, outperforming its benchmark. Clearly, this was not enough to offset the underperformance experienced in January, but it was a sign that investors' enthusiasm for Low-Quality Value stocks may be waning.**

It has been a painful quarter for Quality Growth managers like us. Our Funds recorded one of the worst months ever in relative terms in January. The reason for this was a dramatic style rotation from Growth to Value, one of the fastest that we have witnessed in over 30 years of managing Small & MidCap portfolios. The swift change in sentiment was due to a burst of global inflation, which stoked fears of interest rate rises and disproportionately hurt long duration assets, notably Growth Small & MidCap equities. To put things in context, the MSCI World Growth index underperformed its Value counterpart by a staggering 8.1% in January, the second largest such underperformance in almost 50 years (only topped by April 1999, when Value enjoyed a brief respite amidst the dot-com frenzy).

The outperformance of Value continued in February, albeit not with the same vigour as we had seen earlier in the year. While inflation remained a dominant theme, another far more serious moment of historical significance impacted markets on 24 February 2022. Russia launched the largest military attack in Europe since World War Two by invading Ukraine, further shaking the confidence of equity investors. None of our Funds has ever had (or will have) direct exposure to Russia or Eastern Europe.

## Portfolio

During the quarter, the NAV of the sterling share class declined by 17%, an underperformance of 13%. Much of this underperformance came in January and it was reassuring to see the NAV rise by over 4% in March and outperform the benchmark by 1.4%.

**The strongest contribution** during the quarter came from **SolarEdge**, the leading photovoltaic inverter supplier, which rose after reporting strong demand as the Russian invasion of Ukraine furthered interest in renewable energies. **Cognex**, the provider of machine vision systems enabling machines to "see", thereby increasing the efficiency and quality of manufacturing processes, performed well after posting strong results alongside a positive outlook. **Alfen**, the Dutch manufacturer and integrator of smart grid solutions, saw strong revenue growth and EBIT margin expansion, with strong underlying demand for energy storage and EV charging.

**The weakest contribution** came from **Trex**, the world's largest manufacturer of wood-alternative decking and railing products made from re-used plastic, which came under pressure as macroeconomic worries weighed on US consumer confidence. **Masimo**, the global leader in pulse oximetry sensors, saw its earnings multiple aggressively derate following investor uncertainty over its strategic move into consumer wearable technology through a surprising acquisition. **Tecan**, the Swiss manufacturer of specialised robotic instruments for use in medical research and diagnostics, experienced selling pressure after its 2022 guidance signalled headwinds from the loss of Covid-testing revenues.

**Outlook**

In times of market turbulence, it is easy to get distracted by the noise of headlines. There have been many such distractions over the quarter, from worries about inflation to sombre updates from Ukraine. Against such a backdrop, we have been focusing as always on our companies and understanding how they are impacted by the pressures impacting the global economy. On the whole, the message has been reassuring. Many companies have posted positive trading updates and some have come in ahead of consensus expectations. The environment has allowed us to invest in and add to companies whose valuations have fallen due to negative sentiment, rather than a deterioration in the underlying fundamentals.

The arguments – and the requirements – for sustainable investments continues to strengthen. The IPCC recently published its sixth assessment report and the conclusions were stark. While many of the impacts of global warming are now simply irreversible, a brief window of time remains to avoid the very worst consequences. Rapid action is needed and investors simply must allocate capital accordingly. Limiting global warming to 1.5C requires *“rapid and deep”* emissions reductions in *“all sectors”* of the global economy. Annual climate finance flows must increase by between three and six times to meet average annual needs until 2030. The report finds that *“there is sufficient global capital and liquidity to close investment gaps”,* but barriers remain, namely that Achilles’ heel of short-termism, which stalks financial markets. Sustainable investing is needed now more than ever.

**With this in mind, it is worth noting that the entire Montanaro team invested additional capital in our Funds in Q1. We are aligned with our clients and share the ups and downs of markets with you.**

*As well as the investment implications of the Ukraine conflict, MAM is acutely aware of the human suffering that is occurring. In response to this, our team has collectively made a contribution to the 'Disaster Emergency Committee – Ukraine Humanitarian Appeal'. This contribution has been matched by MAM, providing a significant donation to help people affected by this escalating conflict. More information about this appeal can be found here: https://www.dec.org.uk/appeal/ukraine-humanitarian-appeal*