



# AB SUSTAINABLE US THEMATIC PORTFOLIO

## MARKET REVIEW

In the second quarter, US stocks were buoyed by optimism over US-China trade talks and hopes that the Fed would begin cutting interest rates. Despite sharp falls in May, equities rebounded in June as investors focused on potential monetary policy loosening from global central banks and prospects for improving international trade relations.

Although the Fed kept its benchmark interest rate on hold, officials signaled that further signs of an economic slowdown could spur the bank to begin cutting interest rates. On the trade front, tensions between the US and Mexico were resolved after President Trump put off scheduled tariffs on the country's goods indefinitely. Stocks rallied at the end of June ahead of the G20 summit, at which the US agreed to suspend additional tariffs on Chinese goods and China shared plans to buy certain US farm products.

During the quarter, the S&P 500 Index rose 4.30%. Financials posted the strongest gains. Energy was the worst-performing sector by a large margin, continuing its underperformance of the past few years. Across the market-cap spectrum, growth continued to beat value. Large-caps outperformed their smaller-cap counterparts as investors gravitated to safety and perceived stability.

## PORTFOLIO PERFORMANCE<sup>1</sup>

The Sustainable US Thematic Portfolio outperformed its benchmark, the S&P 500 Index, in the quarter. Stock selection contributed across most sectors, particularly in healthcare and utilities; technology and consumer discretionary names detracted. Sector selection was negative, as our cash holdings in a rising market offset the positive contribution of being underweight energy. From a theme perspective, ConsumerCare and Fortified Franchises were the top performers.

Contributors included Bruker, held in the ConsumerCare theme. Shares continued their strong returns after the company held an investor day in which it provided additional color on the drivers in each of its three business groups. Bruker also indicated its three-year revenue and earnings growth targets, which were perceived by investors as quite bullish.

MSCI, held in the Financial Security theme, also contributed. The global index operator advanced as global markets resumed their rally during the month of June. Investors continue to reward the company for its lack of interest-rate exposure and its steady release of innovative products, including a series of global environmental, social and corporate governance (ESG) fixed-income indices it has created for the Canadian market in a partnership with Bloomberg.

Bright Horizons Family Solutions, embedded in the Fortified Franchises theme, rose after announcing its quarterly earnings. Management upwardly revised its revenue and earnings expectations for the year, which were positively received by the market.

Detractors included SailPoint Technologies in the Digital Disruption theme. Shares fell as the company hit an air pocket of growth, driven by internal execution issues. Management lowered its annual revenue and earnings expectations after considering the weaker pipeline of new business. Despite the weaker guidance, changes to the company's key personnel and its updated go-to-market strategy look promising.

Shares of Charles Schwab, in the Financial Security theme, traded lower as expectations for a rate cut in the US increased in light of a setback in trade negotiations between the US and China. Lower rates are a headwind for the company, given its large asset base.

Shares of Alibaba Group, in the Digital Disruption theme, traded lower initially as trade discussions with China deteriorated. Shares later rebounded as talks resumed and investors viewed further US tariffs on Chinese goods as unlikely for the moment.

<sup>1</sup> Prior to 31 October 2018, the Portfolio was named AB US Thematic Research Portfolio. All data prior to 31 October 2018 relate to the AB US Thematic Research Portfolio.

## ESG ENGAGEMENTS

The Portfolio uses bottom-up research to assess a company's exposure to ESG risks, as well as its prospective earnings growth, valuation and quality of management.

In May, we engaged with Procter & Gamble (P&G) to discuss some of the company's key environmental risks, including how it promotes ethical sourcing of palm oil. P&G has enlisted the help of nongovernmental organizations, as well as researchers from the Massachusetts Institute of Technology, to train farmers on better agricultural practices, nutrient management and increasing oil yields sustainably.

We engaged with Bio-Rad Laboratories on the company's corporate governance practices, given the small size of its board.

Management noted that it is not typically asked about ESG issues by investors, and is looking to add another member with scientific expertise to its board.

## OUTLOOK

Equity markets rebounded in the first half of the year, although the increased volatility resulting from the escalation of the US-China trade war added to concerns about slower global growth. Trade uncertainty and declines in economic activities further increased the probability that central banks in Europe and the US will cut rates this year.

This backdrop bodes well for active management, as increased dispersion can lead to more opportunities for alpha generation while supporting a premium for companies that have their own growth drivers. Given the expected volatility, we

plan to take advantage of any price dislocations that are presented in the market.

We continue to maintain a balanced exposure to our long-term secular investment themes. Our top-down approach is complemented by attractive bottom-up fundamentals, with a focus on robust organic sales and earnings growth along with high returns on invested capital. We believe that this combination will continue to drive long-term alpha generation in the face of moderating economic growth and heightened market volatility.

Please refer to the following legal disclosures.

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