THE DRIVE YOU DEMAND

SWISS EQUITIES

Investing in global growth

White Paper | November 2017

For Qualified Investors in Switzerland or Professional Investors
or Eligible Counterparties as defined by the relevant law.

UBP

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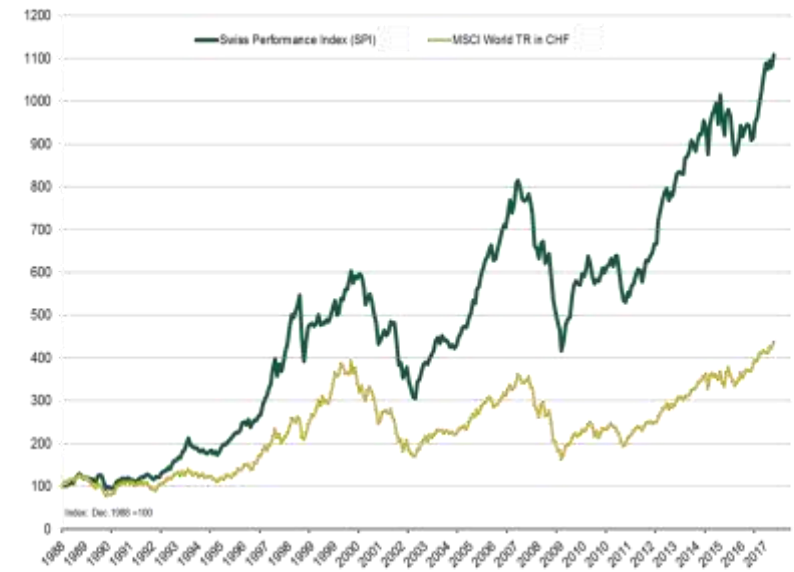
Key points

- The Swiss market relative to the MSCI World has delivered significantly higher returns with lower volatility and lower drawdowns.
- We believe this is thanks to the market's diversification, with a mix of high-quality defensive companies and niche, innovative players which both can deliver growth.
- The above average value creation, expressed by the very high level of CFROI (cash flow return on investment) generated by Swiss companies, is the main reason for the sustainable outperformance of the Swiss equity market.
- The headwind of the strong CHF, a consequence of the healthy Swiss economy and low level of indebtedness, is a discipline companies have learnt to overcome by generating higher value and exercising higher productivity in order to remain competitive.

Chart 1 | Historical performance: SPI Index vs. MSCI World TR Index in CHF



Past performance is not a guide to current or future results.

Last 10 years	SPI	MSCI World (in CHF)
Cumulative return	**43.9%**	21.2%
CAGR	**3.7%**	1.9%
Annualised volatility	**18.6%**	20.9%
Sharpe ratio	**0.19**	0.09
Maximum drawdown	**-52%**	-59%
Time to recover (months)	**77**	89
Tracking error	**10.0%**	*n.a.*
Beta	**0.78**	*n.a.*
Correlation	**88%**	*n.a.*
Upside capture ratio	**80%**	*n.a.*
Downside capture ratio	**76%**	*n.a.*

Source: UBP, Bloomberg Finance L.P. as of 31.10.2017

- In the near term, the appreciation of the EUR is likely to be helpful for Swiss company reported sales and, to a lesser extent, earnings.
- Any devaluation of the CHF against major currencies is helpful for sales growth expressed in CHF.
- Note however, that this is mostly a translation, less a transaction effect, as Swiss companies are well organized in terms of matching costs and sales where possible.

Chart 2 | EUR/CHF vs. USD/CHF

Source: UBP, Bloomberg Finance L.P., as of 31.10.2017.
Past performance is not a guide to current or future results.

- Switzerland is 3.4% of the MSCI World, the 7th-largest country weight and Swiss companies generate one of the highest returns on equity (ROE), illustrating their high efficiency and high value-add products and services.
- Swiss companies' industry leadership is a reflection of long-established global market presence, competitive advantages and high value-added products/services. Ultimately leadership and sustained innovation create strong pricing power.
- Swiss equities have delivered attractive risk-adjusted returns, compared to other developed markets.

Attractive Risk-Return for Swiss equities

Source : UBP, Bloomberg Finance L.P., 31.10.2017

Correlation table: Swiss Equities compared to Developed Markets

in USD	World	US	Japan	UK	France	Germany	Swiss	Average
World		0.96	0.71	0.73	0.76	0.79	0.79	0.79
US	0.96		0.58	0.65	0.60	0.65	0.71	0.74
Japan	0.71	0.58		0.30	0.54	0.59	0.57	0.61
UK	0.73	0.65	0.30		0.69	0.61	0.58	0.65
France	0.76	0.60	0.54	0.69		0.89	0.65	0.73
Germany	0.79	0.65	0.59	0.61	0.89		0.60	0.73
Swiss	0.79	0.71	0.57	0.58	0.65	0.60		0.70
Average	0.79	0.74	0.61	0.65	0.73	0.73	0.70	

Source : UBP, Bloomberg Finance L.P.

- The relatively high correlation to other developed countries and to the world is partly explained by the fact that mostly export oriented Swiss companies generate a large part of their sales internationally: more than 40% with Europe, 30% with the U.S. and 17% with Asia Pacific. Exposure across various geographies to the Emerging Markets therein is estimated at 34%. Bearing in mind the strong presence of suppliers quoted on the Swiss Market, the full exposure to geographies ex Western Europe is higher, if the final end product, to which the supplier has contributed, is taken into consideration.

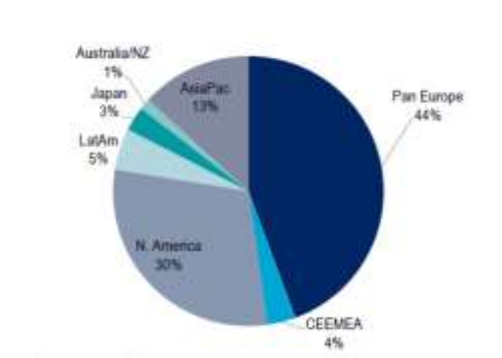
- The Swiss equity market is characterized by companies which are often global leaders in their respective segment and therefore exposed to global economic growth.

- In terms of valuations, Swiss equities are in line with their historical average. With the price earning (PE) ratio for the SPI at 17.5x earnings in 2017 and 15.9x earnings for 2018, Swiss equities are close to the US equity market valuations and a bit higher than global equities (PE = 15.7x 2017 and 14.3x 2018). Swiss equities trade at a justifiable premium to European and EM equities, due to their higher and more sustainable cash flow returns on investment (CFROIs).

Chart 3 - MSCI Switzerland – Cyclically Adjusted P/E

Source: DataStream Citi Research

Chart 4 - Switzerland – Geographic Revenue Exposure

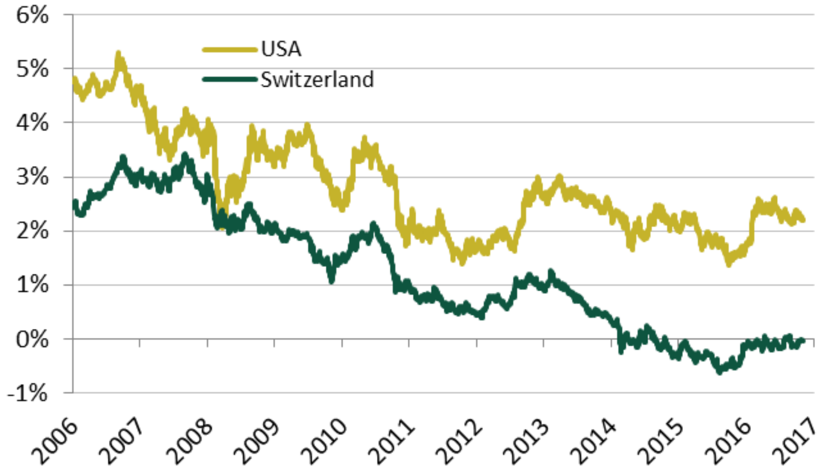


Source : DataStream, Citi Research

What could be the impact of a regime change on Swiss equities & on our funds?

- The U.S. 10-year Treasury rate is currently around 2.20%. The Swiss interest rates have been in negative territory since 2014 and the SNB is unlikely to raise interest rates in the near term in view of the current macroeconomic conditions in Switzerland. The SNB and the FINMA acted appropriately to avoid the property market overheating and the results from these measures are encouraging.

Chart 5 - U.S. 10-Treasury Yield & Swiss 10-year Government Bond Yield



Source: UBP, Bloomberg Finance LP. As of 31.10.2017

- The reversal of unprecedented monetary policy measures will be controlled. We are at the beginning of rate hike cycle and it should be supportive for global equities and therefore Swiss equities.

- Were interest rates hikes in the US to be sharper than currently expected, there could be a short term knock on negative effect on Emerging Markets stock exchanges and currencies. However, we would not expect a long term effect either on currency or economic activity. The pick-up in GDP growth in Emerging Markets is not slowed by US interest rate hikes and GDP growth in EM is supportive for Swiss and Global equity.

- Were there unexpectedly to be a regime change in 2018, and global GDP and company earnings growth to slow, the Swiss equity market may regain its safe haven status and be an interesting relative play against Global and regional markets. The high and stable CFROI generated by Swiss companies, the balanced geographic exposure, the market's large healthcare and staple sectors tend to attract investors in periods of uncertainty, leading to less downside risk.

Outlook - 2018 and beyond

- September Swiss PMI stands at 61.7, the highest level of the last seven years and Switzerland's key end markets in Europe, the US and Emerging Markets are healthy too. The depreciation of the Swiss franc against Euro, together with a lower appreciation of the Swiss franc against the USD, seems not to have been accounted for.
- The Swiss equity market should deliver mid-teens earnings growth for 2017 and low teens earnings growth potential for 2018. This should support high teens market performance in 2017 and low teens performance for 2018. The current dividend yield of around 3% is also achievable in 2018.
- Near-Term:
  Expect further solid growth, after global economic data has inflected higher, while inflation expectations have little reason to change after H1 setback. PMIs suggest elevated activity in the next 6 months.
- Intermediate-Term:
  During expansions, multiples tend to rise. The current recovery has been long, but shallow and came with a delay for Europe and Emerging Markets. Recessionary risk is low in the absence of excesses. The equity risk premium remains elevated and is above its long term average for Switzerland, leaving room for some further multiple expansions.
- Longer-Term:
  Reversal of unprecedented monetary policy measures will be controlled. Other end-of-cycle excesses (e.g. Capex overinvestment) are not apparent. Hence, expect low economic volatility and low market volatility as well as low inflation to continue, keeping pressure on discount rates up.

- In conclusion, the supportive factors of 2017, including low interest rates, modest but sustainable growth, underleveraged balance sheets, a stable macro-economic environment with sluggish growth in EU, a solid US economy and recovering EM should replicate in 2018.
- Potential lagging performances delivered by the three Swiss heavyweights, Nestlé, Novartis and Roche should not be a significant headwind for the market, with the cyclical components benefitting from high PMIs and ongoing synchronized global recovery.
- Typical cyclical sectors benefiting from expected growth drivers in 2018 include:
  - IT companies (ongoing strong demand, notably in the semi-conductor supply chain.
  - Luxury goods (short term recovery momentum further to Chinese and currency driven slowdown of 2015/2016).
  - Financials (potentially doing better on fading headwinds (Banks) plus ongoing gradual normalization of global interest rates (Banks and Insurance) plus undemanding valuations (Insurance).
  - Industrials and non-commoditized building materials (high PMIs, stabilized oil price, automation trends, solid European and US construction environment, and EM quality improvement drives.

Key takeaways

- Swiss companies' industry leadership is a reflection of long-established global market presence, competitive advantages and high value-added products and services.

- The investment strategy developed by our fund managers, which seeks to combine companies with high and sustainable CFROIs with those with growing or restructuring CFROIs, has benefitted from the market environment in 2017 and delivered significant absolute and relative outperformance should a similar framework be established in 2018, it should be supportive for our fund's investment process.

- The Swiss equity market is structurally exposed to global markets, due to a large proportion of its companies enjoying a well-established international franchise.

- Swiss equities have delivered attractive risk-adjusted returns, compared to other developed markets.

- Solid fundamentals and strong earnings' growth in Swiss equities this year have supported higher valuations, which make them in line with multiple expansions seen in global equities.

- Swiss equities trade at a justifiable premium to European and EM equities, due to their higher and more sustainable cash flow returns on investment (CFROIs).

- Ultimately leadership and sustained innovation create strong pricing power, which has been one of Swiss companies' trademarks.

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