

UBAM - EURO CORPORATE IG SOLUTION

Quarterly Comment

For Professional Investors in Switzerland or Professional Investors as defined by the relevant laws.

Market Comment

- The positive sentiment towards risk markets continued in July, buoyed by reports of progress made on several Covid-19 vaccine trials, as well as Q2 earnings beginning on a strong footing. On the Covid-19 case growth front, by the end of the month we also saw the first signs that the lockdown measures put back in place in several US states were helping to slow the pace of case growth.
- The economic consequence of reversing several reopening plans is beginning to have an impact on the data in the US however, which appears to have lost some of its momentum. For example the US economic data surprise index has fallen off historical highs, with high frequency labour market indicators such as initial jobless claims showing two consecutive weeks of deterioration, which is the first time we have seen such a trend since the beginning of the pandemic.
- In contrast in Europe, the more effective management of Covid-19 thus far has allowed for economies to largely remain open. As such, the economic data in the region has continued to improve, with the Euro Area economic surprise index reaching historical highs in July, and the composite PMI reading beating consensus expectations, driven by the service sector.
- Credit spreads managed to continue to tighten amid these developments, with US investment grade spreads tightening by 19 bps during the month and European IG spreads by 21 bps. The marginal outperformance of European spreads was driven by both the data as well as the July Eurogroup meeting in which they agreed on an EU Recovery Fund worth a significant EUR 750 bn. Italy is set to be one of the main beneficiaries of this fund, with 10-year BTP spreads tightening by 17 bps as result.
- Despite the positive risk sentiment, interest rate markets continued to rally in July, given that the key central banks of the Fed and ECB emphasised that monetary accommodation is set to remain intact. US rates outperformed with the curve flattening as negotiations on a new fiscal package did not begin well, which meant that the enhanced unemployment benefit scheme expired at the end of July without an extension in place. As such, 10-year US yields declined by 13 bps during the month, outperforming the equivalent German Bund yield which fell by 7 bps.
- August saw risk markets continue to perform well with the S&P 500 index breaking through pre-Covid-19 levels as the US infection rate, as well as hospitalisations declined following a second wave peak.
- Positive risk sentiment here allowed for credit markets to strengthen further, with US Investment Grade spreads tightening by 7 bps in August, whilst European Investment Grade spreads tightened by 13 bps during the month.
- Despite the number of Covid-19 cases accelerating within the Euro Area, mortality rates remained very low which allowed for economies to largely continue on their reopening paths and for the economic recovery to remain intact. Economic data released for August was also encouraging as the Global Manufacturing PMI rose to 51.8 from 50.6 in July, in a move that was driven by the new orders component.

- The US labour market normalised further as the unemployment rate declined to 10% from 11% the previous month as payroll job gains were larger than consensus. Markets also took comfort from the positive trend of headlines around progress made on a potential vaccine for Coronavirus ahead of year-end.
- From a central bank perspective, the main event during the month was the much-anticipated annual Jackson Hole symposium in which Fed Chair Powell revealed the conclusions of the Fed's framework review, as well as their revised statement of long run goals. In his speech, Powell highlighted the committee's new aim of seeking to achieve inflation that averages 2% over time, as well as the Fed now looking to cover shortfalls in employment, rather than just deviations.
- This dovish communication confirmed for markets that central bank accommodation is here to stay, although interest rate markets still managed to sell-off during the month as safe haven hedges were unwound with the risk backdrop improving and as heavy US Treasury supply, particularly at the long end, weighed on US rates. US 10-year yields for example ended the month 18 bps higher, whilst German 10-year yields rose by 13 bps, with the US 5s30s curve steepening by 22 bps in August alone.
- September saw risk sentiment turn less positive as markets took caution from rising Covid-19 cases in Europe and the UK, as well as reduced hopes of a fiscal package in the US ahead of the November Presidential elections.
- Developments herein allowed for the momentum behind the recent credit spread tightening to take a pause, with US investment Grade spreads widening by 9 bps in September and European spreads by 4 bps. Despite this widening observed, 10-year Italian BTP spreads managed to tighten by 10 bps after regional election results reduced the chances of a snap election being called, supporting political stability.
- In contrast, politics in the US became increasingly focused on in light of the first Presidential debate, in which Trump did not rule out contesting the election result were he not to win, adding to investor uncertainty. Meanwhile in the UK, with the number of Covid-19 cases accelerating to new highs, the government announced the reintroduction of various social distancing measures which led to fears that the global growth recovery may stall if such restrictions were to be implemented in other countries.
- For now though, economic data releases remain encouraging, as highlighted by the Global Manufacturing PMI rising for another month to 53 from 52.4 in August, whilst high frequency mobility indicators have continued to normalise despite the rising Covid-19 case growth observed.
- From the central bank perspective, the Fed at its September meeting released its updated summary of economic projections in which its new dot plot suggests unchanged interest rates for the forecast period, out until the end of 2023, given that inflation is only expected to get back to 2% at this time. The Fed also adjusted its forward guidance at this meeting in which it now aims to achieve inflation moderately above 2% for some time, so that inflation averages 2% over time.
- Such dovish guidance is in line with current market pricing which does not see the first rate hike until 2025, and as such US 10-year yields only moved modestly lower during the month, by 2 bps, whilst German 10y Bunds yields declined by 12 bps.



Performance Review

- YTD, UBAM - Euro Corporate IG Solution returned +0.55% net of fees (I Share class).
- YTD, credit generated -42bps whereas interest rates and cash +124bp, before fees

Portfolio Activity

- At the end of the quarter, the carry and roll-down of the fund was 0.8% which compared to the carry and roll-down for the ICE BofA Euro Large Cap Corporate Index at 0.9%.
- Portfolio allocation:
 - ▶ Interest rate: 5.3 years in EUR rates vs. 5.3 years for the ICE BofA Euro Large Cap Corporate Index
 - ▶ Credit: 5.5 years vs. 5.3 years for the ICE BofA Euro Large Cap Corporate Index implemented 5.4 years via the European CDS index and 0.1 years via the US CDS index
- In July, we made no active changes to the portfolio.
- In August, we added 0.1 year spread duration through CDX US investment grade index with the virus getting under control and central bank accommodation remaining intact through the summer. In particular, Covid-19 case growth trend in the US continues to improve, with hospitalisation levels significantly off the July peak with improvements in all of the key hotspot states.
- In September, we left our positioning unchanged.

Outlook

- The third quarter of 2020 saw risk markets recover further with the S&P 500 index reaching new highs as economic data continued to indicate a sharp bounce back in global growth. Although the quarter saw a resurgence in Covid-19 cases across Europe and the US, this second wave was very different to the first as both hospitalisation and mortality rates remained at low levels, which allowed economies to continue on their reopening paths. From a policy perspective, whilst significant stimulus had been provided by the major central banks immediately after the pandemic spread globally, key developments still took place in Q3 including the Fed's conclusion of its framework review, which resulted in a shift towards an average inflation rate targeting regime. The quarter ended on a softer tone as investors looked ahead to an event-filled final quarter of the year, which includes the US elections, the deadline for a UK-EU trade deal, and the results of the Phase III Covid-19 Vaccine trials.
- Having already brought interest rates to the zero lower bound earlier this year, the focus for the Fed in the third quarter was its framework review that resulted in a revised statement of long run goals, as well as enhanced forward guidance. Specifically, in Fed Chair Powell's speech at the annual Jackson Hole symposium, he highlighted the committee's new aim of seeking to achieve inflation that averages 2% over time, as well as the Fed now looking to cover what they describe as shortfalls in employment, rather than just deviations. This dovish shift was further emphasised at the September FOMC meeting, where the summary of economic projections included the new dot plot, which showed unchanged interest rates for the forecast period, out until the end of 2023, given that inflation is expected to only return to 2% at this time. The Fed also adjusted its forward guidance at this meeting in which it now aims to achieve inflation moderately above 2% for some time, so that inflation averages 2% over time. Such dovish guidance is in line with current market pricing which does not see the first rate hike until 2025 and as such, US rates markets observed little volatility during the quarter and largely traded within a 25 bp range in light of this clear communication from the Fed.
- Looking ahead, we do not expect inflation to move above 2% for some time given the amount of slack still in the labour market due to the pandemic and as the disinflationary forces of technology change and demographics are still at work. We therefore expect the Fed to leave rates at current levels for the foreseeable future, standing ready to ease financial conditions further through either larger asset purchases or extending the duration of these purchases, were the outlook to warrant such action. This is especially the case at a time when the current US administration is struggling to push through another fiscal stimulus package ahead of the Presidential elections. Although high frequency data such as retail sales, ISM survey data and initial claims highlight a sharp improvement in growth from the pandemic lows, the final quarter of the year will be crucial in seeing how the economy performs without the help of stimulus cheques and the now expired enhanced unemployment benefits.



- In Europe, the ECB appeared satisfied enough with low Bund yields and the tightening of peripheral spreads observed to not make any major changes to its policy in Q3, especially given that the PEPP program had been expanded in June by EUR 600bn, to a total of EUR 1.35trn. Asset purchases from the ECB actually slowed during the quarter given the positive sentiment towards the Euro area, which was not only driven by the data, but also by the outcome of the July Eurogroup meeting. At this meeting, the group managed to agree on an EU Recovery Fund worth EUR 750bn, in a move that should finally take some pressure off the monetary authorities to be the only provider of policy support in the bloc. Despite these developments, the ECB has clearly stated that risks to the growth outlook remain to the downside, where inflation moved worryingly lower during the quarter as well, with Core inflation declining to just 0.2% YoY from 1.2% at the start of the quarter. With several furlough schemes that had been supporting economies in the region also potentially coming to an end this year, we see a high possibility that the ECB will increase the size and duration of its PEPP package before year-end, in a bid to continue supporting the recovery.
- Increasing the size of the asset purchase programme is an announcement that we also expect to be made by the Bank of England in Q4 as the UK furlough scheme ends in October and with Brexit uncertainty still weighing on the outlook. We do expect for a trade deal to ultimately be made with the EU, however negotiations leading up to a deal will likely be volatile, which will leave the market pricing in a small chance of interest rates going negative next year, given that unlike the Fed, the BoE has not ruled this possibility out. Instead, at the last MPC meeting the bank said that they would explore how a negative bank rate could be implemented effectively, should the outlook for inflation and output warrant it at some point.
- With the crisis stage of Covid-19 having passed, the end of the year will focus on various risk events, as well as the growth outlook. We take comfort from the fact that whilst the coronavirus has not gone away, its consequences appear to be fading as highlighted by the latest hospitalisation and mortality rates. As such, we think that as long as we do not return to severe national lockdowns, economies will continue to grow, albeit at a slower pace than observed in Q3, with the trough in global growth now well behind us. Although some sectors of the economy will take longer to fully bounce back, this should be somewhat offset by the accommodation from monetary and fiscal authorities which we expect to remain intact for years after this crisis has passed. In addition, despite the US Presidential elections looming, it is unlikely that either candidate will look to implement restrictive growth policies given where we are in the growth cycle.
- Given this backdrop, we think it makes sense to have exposure to credit markets, where spreads are still well above levels seen pre-virus, and with risks skewed to further stimulus coming through from policy makers. A potential Covid-19 vaccine approval coming through before year-end would also further support risky assets. However with uncertainties still clouding the outlook given the possibility of a contested Presidential election and with Covid-19 still present, we believe that the focus should remain on high quality credit and segments of the market that are benefitting from direct central bank support.



This would include US investment grade credit, where the Fed has plenty of room to increase its corporate purchases if needed. We are also still positive on the financial sector where capital ratios are higher than during the GFC and where importantly, banks are part of the solution to this crisis and not the cause as in 2008. On interest rate duration, given the lack of inflation globally, we are ultimately buyers of duration on significant yield spikes, as we expect the low rates environment to continue. That said in the near term, we think that risks of a potential Democratic sweep at the elections in both the House and Senate could fuel some bear steepening pressures on the curve.

This is a marketing document and is intended for informational and/or marketing purposes only. It is confidential and is intended to be used only by the person(s) to whom it was delivered. It may not be reproduced (in whole or in part) or delivered, given, sent or in any other way made accessible, to any other person without the prior written approval of Union Bancaire Privée, UBP SA or any entity of the UBP Group (UBP). This document reflects the opinion of UBP as of the date of issue. This document is for distribution only to persons who are Professional clients in Switzerland or Professional Clients or an equivalent category of investor as defined by the relevant laws (all such persons together being referred to as "Relevant Persons"). This document is directed only at Relevant Persons and must not be acted on or relied on by persons who are not Relevant Persons. It is not intended for distribution, publication, or use, in whole or in part, in any jurisdiction where such distribution, publication, or use would be unlawful, nor is it directed at any person or entity at which it would be unlawful to direct such a document. In particular, this document may not be distributed in the United States of America and/or to US persons (including US citizens residing outside the United States of America). This document has not been produced by UBP's financial analysts and is not to be considered financial research. It is not subject to any guidelines on financial research and independence of financial analysis. Reasonable efforts have been made to ensure that the content of this document is based on information and data obtained from reliable sources. However, UBP has not verified the information from third sources in this document and does not guarantee its accuracy or completeness. UBP makes no representations, provides no warranty and gives no undertaking, express or implied, regarding any of the information, projections or opinions contained herein, nor does it accept any liability whatsoever for any errors, omissions or misstatements. The information contained herein is subject to change without prior notice. UBP gives no undertaking to update this document or to correct any inaccuracies in it which may become apparent. This document may refer to the past performance of investment interests. **Past performance is not a guide to current or future results.** The value of investment interests can fall as well as rise. Any capital invested may be at risk and investors may not get back some or all of their original capital. Any performance data included in this document does not take into account fees, commissions, and expenses charged on issuance and redemption of securities, nor any taxes that may be levied. Changes in exchange rates may cause increases or decreases in investors' returns. All statements other than statements of historical fact in this document are "forward-looking statements". Forward-looking statements do not guarantee future performances. The financial projections included in this document do not constitute forecasts or budgets; they are purely illustrative examples based on a series of current expectations and assumptions which may not eventuate. The actual performance, results, financial condition and prospects of an investment interest may differ materially from those expressed or implied by the forward-looking statements in this document as the projected or targeted returns are inherently subject to significant economic, market and other uncertainties that may adversely affect performance. UBP also disclaims any obligation to update forward-looking statements, as a result of new information, future events or otherwise. The contents of this document should not be construed as any form of advice or recommendation to purchase or sell any security or funds. It does not replace a prospectus or any other legal documents, which can be obtained free of charge from the registered office of a fund or from UBP. The opinions herein do not take into account individual investors' circumstances, objectives, or needs. Each investor must make their own independent decision regarding any securities or financial instruments mentioned herein and should independently determine the merits or suitability of any investment. In addition, the tax treatment of any investment in the fund(s) mentioned herein depends on each individual investor's circumstances. Investors are invited to carefully read the risk warnings and the regulations set out in the prospectus or other legal documents and are advised to seek professional counsel from their financial, legal and tax advisors. The tax treatment of any investment in the Fund depends on the investor's individual circumstances and may be subject to change in the future. This document should not be deemed an offer nor a solicitation to buy, subscribe to, or sell any currency, funds, products, or financial instruments, to make any investment, or to participate in any particular trading strategy in any jurisdiction where such an offer or solicitation would not be authorised, or to any person to whom it would be unlawful to make such an offer or solicitation. Telephone calls to the telephone number stated in this presentation may be recorded. UBP will assume that, by calling this number, you consent to this recording.

Any subscriptions not based on the funds' latest prospectuses, KIIDs, annual or semi-annual reports or other relevant legal documents (the "Funds' Legal Documents") shall not be acceptable. The Funds' Legal Documents may be obtained free of charge from Union Bancaire Privée, UBP SA, 96-98 rue du Rhône, P.O. Box 1320, 1211 Geneva 1, Switzerland (UBP), from UBP Asset Management (Europe) S.A., 287-289 route d'Arlon, 1150 Luxembourg, Grand Duchy of Luxembourg, and from Union Bancaire Gestion Institutionnelle (France) SAS, 116 avenue des Champs-Élysées, 75008 Paris, France. The Swiss representative and paying agent of the foreign funds mentioned herein is UBP. The Funds' Legal Documents may be obtained free of charge from UBP, as indicated above.

This content is being made available in the following countries:

Switzerland: UBP is authorised and regulated in Switzerland by the Swiss Financial Market Supervisory Authority (FINMA). The head office is Union Bancaire Privée, UBP SA, 96-98 rue du Rhône, P.O. Box 1320, 1211 Geneva 1, Switzerland. ubp@ubp.com | www.ubp.com

United Kingdom: UBP is authorised in the United Kingdom by the Prudential Regulation Authority (PRA) and is subject to regulation by the Financial Conduct Authority (FCA) and limited regulation by the PRA.

France: Sales and distribution are carried out by Union Bancaire Gestion Institutionnelle (France) SAS, a management company licensed with the French Autorité des Marchés Financiers, - licence n° AMF GP98041 ; 116, av. des Champs Elysées | 75008 Paris, France T +33 1 75 77 80 80 Fax +33 1 44 50 16 19 www.ubpamfrance.com.

Hong Kong: UBP Asset Management Asia Limited (CE No.: AOB278) is licensed with the Securities and Futures Commission to carry on Type 1 – Dealing in Securities, Type 4 – Advising on Securities and Type 9 – Asset Management regulated activities. The document is intended only for Institutional or Corporate Professional Investor and not for public distribution. The contents of this document have not been reviewed by the Securities and Futures Commission in Hong Kong. Investment involves risks. Past performance is not indicative of future performance. Investors should refer to the fund prospectus for further details, including the product features and risk factors. The document is intended only for **Institutional Professional Investor** and not for public distribution. The contents of this document and any attachments/links contained in this document are for general information only and are not advice. The information does not take into account your specific investment objectives, financial situation and investment needs and is not designed as a substitute for professional advice. You should seek independent professional advice regarding the suitability of an investment product, taking into account your specific investment objectives, financial situation and investment needs before making an investment. The contents of this document and any attachments/links contained in this document have been prepared in good faith. UBP Asset Management Asia Limited (UBP AM Asia) and all of its affiliates accept no liability for any errors or omissions. Please note that the information may also have become outdated since its publication. UBP AM Asia makes no representation that such information is accurate, reliable or complete. In particular, any information sourced from third parties is not necessarily endorsed by **UBP AM Asia**, and **UBP AM Asia** has not checked the accuracy or completeness of such third party information.

Singapore: This document is intended only for accredited investors and institutional investors as defined under the Securities and Futures Act (Cap. 289 of Singapore) ("SFA"). Persons other than accredited investors or institutional investors (as defined in the SFA) are not the intended recipients of this document and must not act upon or rely upon any of the information in this document. The financial products or services to which this material relates will only be made available to clients who are accredited investors or institutional investors under the SFA. This document has not been registered as a prospectus with the MAS. Accordingly, this document and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of this product may not be circulated or distributed, nor may the product be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (i) to institutional investors under Section 274 or 304 of the Securities and Futures Act (Cap. 289) of Singapore ("SFA"), (ii) to relevant persons pursuant to Section 275(1) or 305(1), or any person pursuant to Section 275(1A) or 305(2) of the SFA, and in accordance with the conditions specified in Section 275 or 305 of the SFA, or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA. This advertisement has not been reviewed by the Monetary Authority of Singapore.

MSCI : Although Union Bancaire Privée, UBP SA information providers, including without limitation, MSCI ESG Research LLC and its affiliates (the "ESG Parties"), obtain information from sources they consider reliable, none of the ESG Parties warrants or guarantees the originality, accuracy and/or completeness of any data herein. None of the ESG Parties makes any express or implied warranties of any kind, and the ESG Parties hereby expressly disclaim all warranties of merchantability and fitness for a particular purpose, with respect to any data herein. None of the ESG Parties shall have any liability for any errors or omissions in connection with any data herein. Further, without limiting any of the foregoing, in no event shall any of the ESG Parties have any liability for any direct, indirect, special, punitive, consequential or any other damages (including lost profits) even if notified of the possibility of such damages.