


# UBAM - ABSOLUTE RETURN FIXED INCOME

## Quarterly Comment

For Professional Investors in Switzerland or Professional Investors as defined by the relevant laws. The classification of the fund(s) as per the Sustainable Finance Disclosure Regulation (SFDR) is available on [ubp.com](http://ubp.com) or in the latest prospectus.

### *Market Comment*

- Risk markets were supported in April as the vaccine rollout continued to pick up pace, particularly in Europe, which raised hopes that strict lockdown measures would soon be eased. High frequency data points were also impressive during the month, as the US ISM manufacturing survey for example rose to the highest level since the 1980's, whilst payroll growth also surprised on the upside, with almost 1 million new jobs being added and the unemployment rate declining to 6%. Although US growth data outperformed, buoyed by Biden's fiscal stimulus measures, the better sentiment was also observed elsewhere with the Global Manufacturing PMI rising to the strongest level since 2011, with global trade continuing to recover.
- As a result, credit spreads ended the month tighter with US investment grade spreads 4 bps tighter in April and European spreads 6 bps tighter. Moves herein were also helped by Fed and ECB meetings, in which both banks remained consistent with their prior dovish rhetoric, despite the recent strength in the data and at a time when the Bank of Canada decided to announce tapering. In contrast, Fed Chair Powell said in the press conference that now is not the time to talk about tapering, adding that the economy's improvement so far is not close to substantial further progress, which will take some time to be achieved.
- Similarly at the ECB, President Lagarde said that discussions to phase out PEPP was premature, where the economy has a long way to go until it has crossed the pandemic bridge. This allowed US 10-year yields to decline by 11 bps on the month, which was a significant outperformance when compared to German 10-year yields which rose by 9 bps in a curve steepening move. This underperformance of EUR rates in April could largely be put down to a catch-up to the rates sell-off that took place earlier in the year in the US, as well as significant progress on vaccinations in Europe during the month, paving the way for growth expectations in the region to be revised higher.
- With developed economies gradually reopening as the vaccine rollout progresses, the focus in May was on the data to see the impact that reduced lockdown measures were having on the real economy. From a global perspective, the data remained impressive, with the global manufacturing PMI for example reaching its highest level since 2010 at 55.8, with forward looking indicators such as new orders also at cycle highs. In the US however, despite the rise in mobility observed, the nonfarm payrolls report saw a significant miss to the downside, largely driven by a lack of incentives to return to work for low wage workers given the current enhanced unemployment benefits.

- 
- This allowed investors to push back their expectations for any imminent tapering announcement to be made by the Fed, where continued accommodation herein resulted in US Investment Grade spreads tightening by 4 bps in May. In contrast, European spreads were 2 bps wider on the month, as strong survey data released out of the region including consumer confidence and the ISM Services led to investors speculating whether the ECB would bring its PEPP purchases back towards a more normal level in Q3, following an accelerated pace in Q2.
  - Developments herein also allowed for German 10y Bund yields to rise during the month to a high of -10 bps, although this move was faded by month-end after several ECB officials made comments that reduced the likelihood that PEPP purchases would be tapered at the upcoming meeting. US 10y yields also ended the month with a modest move of just 4 bps lower despite the disappointing payrolls print, as inflationary pressures continued to support inflation breakevens. In particular, headline US CPI surprised significantly on the upside at 4.2% compared to the consensus of 3.6%, in what was the strongest reading since 2008, whilst the prices paid component within the ISM Manufacturing survey also surged to the highest level since 2008.
  - The hawkish shift taken by the Fed at its June meeting was the main focus this past month and led to significant moves in interest rate markets. The Fed surprised investors through its updated dot plot projection in particular, which now forecasts two rate hikes in 2023 compared to their prior dot plot which showed no hikes. In addition, 7 out of the 18 board members already see a hike as soon as 2022. Fed Chair Powell also confirmed that they began initial tapering discussions, although he added that they are still far from the “substantial further progress” required to actually begin to taper.
  - As a result, the rates curve saw a sharp flattening move as the front-end came under pressure given the move higher in the dots, whilst the longer end was supported by the possibility of a less patient Fed with regards to rising near-term inflation pressures. This led to the US 2-year vs 10-year curve flattening by 23 bps on the month, with the 10 year yield itself ending June 12 bps lower.
  - In contrast to the Fed, the ECB maintained its pledge to continue with its PEPP purchases at a “significantly higher” pace in Q3 compared to Q1, despite recent strength in the data as highlighted by both the manufacturing and service PMIs rising to new cycle highs in June. As a result of contrasting central bank communication, there was a significant divergence in USD and EUR rates during the month, with German 10-year yields ending June just 2 bps lower, whilst the German 2s10s rates curve was only 2 bps flatter. Despite the volatility in rates observed, risk markets were resilient in June with the S&P 500 reaching new highs, whilst credit spreads continued to tighten. US Investment Grade spreads for example were 4 bps tighter on the month, whilst European spreads were 1 bp tighter, as investors took confidence from the continued rebound in the growth data and reopening of economies ahead of the summer.

---

## Performance Review

- UBAM - Absolute Return Fixed Income delivered +0.25% net of fees QTD (I Share class). In relative terms, the strategy delivered +56 bps gross of fees above a reference index\*: the Eonia capitalization 7 days index.
- The excess returns for April were +26 bps, +2 bps for May and +28 bps for June.
- QTD, the main contributor to the excess returns was Senior Global IG Corporates: +40 bps. The main detractor was sovereign: -12 bps
- Volatility remained contained with a daily 12-month rolling volatility of 0.9%.

*\*Index provided for comparison and information purposes only.*

---

## Portfolio Activity

- At the end of the quarter, the yield of the portfolio in EUR was 0.5% and 1.3% in USD (hedged share class).
- The interest rate exposure was 0.3 year and the credit exposure was 4.4 years at the end of June.
- In April, we increased our credit positioning by adding 4% in High yield CDS indices, while maintaining the fund's short duration bias, as macro-economic data such as the global PMI's and payrolls continued to signal a strong recovery. This increased our confidence in the growth outlook, which we anticipate will accelerate further as economies continue to re-open and which should allow for interest rate markets to continue to normalise. As a result, we re-entered into a rates curve steepening position, in particular through EUR rates, on expectations that the vaccine rollout in Europe will pick up pace following a slow start, which should reduce some of the pessimism currently priced towards the region.
- In May, we left our interest rate and credit exposure levels unchanged. We continue holding above average historical levels of credit risk at 4.3 years of spread duration and 5.0 years of risk adjusted spread duration, while holding 0 interest rate duration. Our confidence in the growth outlook, which we anticipate will accelerate further as economies continue to re-open, should allow for interest rate markets to continue to normalize and credit spreads to gradually tighten. Additionally, we hold on to our EUR curve steepener positions, as the vaccine rollout in Europe is picking up pace following a slow start, which should allow for growth expectations towards the region to be revised higher given the current pessimism that is priced towards the region.
- In June, we left our interest rate and credit exposure levels unchanged. We continue holding above average historical levels of credit risk at 4.4 years of spread duration and 5.2 years of risk adjusted spread duration, given our belief that the growth recovery will continue as economies reopen further and labour markets recover. We still hold 0 interest rate duration given this growth backdrop and the hawkish shift from the Fed. We also maintained our EUR curve steepening position given improving high frequency indicators as observed by the latest PMI surveys, as well as the impressive vaccine rollout in the region, which should allow for growth expectations to be revised higher.

---

## Outlook

- Risk markets continued their strong run in Q2, with the S&P 500 for example closing the quarter at new highs as the vaccine rollout accelerated globally, which allowed domestic lockdown restrictions to ease further and for growth expectations to be revised higher. In contrast in rates markets, Q2 saw reflation trades lose momentum with US 10-year yields declining off the first quarter highs in a move that was driven by real rates, despite the hawkish shift taken by the Fed at the June meeting. Looking ahead, having passed the initial smooth “V” shaped part of the recovery from the pandemic, the attention for investors during the second half of the year will be on whether growth can continue to normalise and improve, despite potential Covid-19 variants posing a risk to the outlook. This will keep the data in focus, particularly the labour market in the US to see if the upcoming expiry of enhanced unemployment benefits results in a further pick-up in job gains, which will allow the Fed to adjust its forward guidance in the coming months to prepare for the eventual tapering announcement.
- The hawkish shift taken by the Fed at its June meeting was one of the main events for investors to digest during the second quarter. The Fed surprised markets through its updated dot plot projection in particular, which now forecasts two rate hikes in 2023 compared to their prior dot plot which showed no hikes. In addition, 7 out of the 18 board members already see a hike as soon as 2022. Fed Chair Powell also confirmed that they began initial tapering discussions, although he added that they are still far from the “substantial further progress” required to actually begin to taper. As a result, the rates curve saw a sharp flattening move as the front-end came under pressure given the move higher in the dots, whilst the longer end was supported by the possibility of a less patient Fed with regards to rising near-term inflation pressures.
- We believe this hawkish outcome was driven by the Fed’s increasing confidence in the economic growth outlook, as well as uncertainty with its inflation forecasts given the unprecedented nature of the economic reopening. The Fed is reacting to a strengthening consumer, in which low wage workers have continued to benefit from enhanced unemployment benefits which have supported incomes. Although labour market gains have been slower in recent months than had been anticipated, the Fed is confident that jobs growth will continue, specifically as these enhanced unemployment benefits which have already expired in many states this past month, will be fully expired by September and will force individuals to come back into the labour force and look for work. Whilst the Fed’s inflation forecasts for 2022 and 2023 were largely unchanged, the significant overshoot that is now expected for this year at 3% for core PCE seems to have also been behind the decision to shift the dots higher. Whilst the Fed expects current inflationary pressures to be transitory in nature, a more hawkish dot plot provides them with some room to manoeuvre if these pressures were to become more persistent.



- In contrast to the Fed, the ECB recently maintained its pledge to continue with its PEPP purchases at a “significantly higher” pace in Q3 compared to Q1, despite recent strength in the data as highlighted by both the manufacturing and service PMIs rising to new cycle highs in June. The Eurozone has also impressed with its vaccine rollout in Q2, having previously been a laggard in its distribution. This should provide resilience to the growth recovery, as it reduces the likelihood that we return to strict lockdown measures and it should allow for the crucial summer tourism season to be at least somewhat saved. We think that the ECB will take comfort from the Fed’s shift, which will also provide them with the opportunity to turn less dovish in the coming months. With the Fed moving first, the ECB will be able to bring PEPP purchases back towards a more normal pace in Q4 without fearing a significant tightening of financial conditions on such an announcement, which has been a clear focus for President Lagarde. With underlying growth and inflationary pressures in the Euro area less advanced than that in the US, any hawkish shift would be through tapering purchases only, rather than bringing forward guidance for rate hikes.
- From a positioning perspective, we remain comfortable with our short duration bias following the outcome of the Fed. We expect it to also limit the downside in US government bond yields, where we see room for rates to move back towards the top end of recent ranges, as the market prices in risks of a more hawkish Fed given the impressive growth data. This is likely to be driven by the front-end and belly of the curve, rather than the longer end, as the Fed acts to control inflationary pressures. In contrast in Europe, we continue to see room for the EUR curve to steepen given impressive growth trends and still elevated pessimism towards the region, where any hawkish shift from the ECB set to be focused on asset purchases, rather than rate hikes.
- For credit markets, we remain positive and see a Fed that is now no longer significantly behind the curve as reducing one of the major tail risks that investors have been concerned about. In particular, that of a persistent surge higher in inflation over the medium term, as the Fed’s guidance on rates indicates that they will not let inflation get out of hand, which also increases the likelihood that any inflationary pressures end up being transitory in nature. The other major tail risk being tracked is that of a more infectious and deadly Covid-19 variant resulting in a pause or reversal in the reopening process. Whilst the Delta variant has clearly been in focus given accelerating cases in the UK, hospitalisation and mortality data is more encouraging and indicates that the vaccine is preventing severe illness from this variant, which should allow for economies to continue to reopen.
- We expect for risk markets to focus back on the global economic growth path, which is now expected to exceed the pre-Covid trend. Our confidence in the recovery remains intact, not only due to the increasingly confident consumer, but also due to capex growth, which we expect to be helped from both the private and public sides as companies and governments get up to speed on the digital and green transformation taking place. This environment is one in which the higher beta segments of the market can outperform and where credit compression can take place.



High Yield spreads should benefit as the most severely impacted sectors from the pandemic begin to recover, whilst we also think that Subordinated Financial debt provides an attractive opportunity given strong fundamentals for the banking sector and resilient earnings throughout the pandemic.

**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 the fund(s) mentioned herein 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 a 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.

Pursuant to Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (the "Disclosures Regulation" or "SFDR"), funds are required to make certain disclosures. Funds falling under the scope of Article 6 of the SFDR are those which have been deemed not to pursue an investment approach that explicitly promotes environmental or social characteristics or has sustainable investment as their objective. Notwithstanding this classification, the Investment Managers may take account of certain sustainability risks as further described in the fund's prospectus. Funds falling under the scope of Articles 8 or 9 of the SFDR are those subject to sustainability risks within the meaning of the SFDR. The sustainability risks and principal adverse impacts as stipulated in the SFDR are described in the prospectus. In addition, unless otherwise specified, all funds apply the UBP Responsible Investment Policy, which is available on <https://www.ubp.com/en/investment-expertise/responsible-investment>.

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](mailto:ubp@ubp.com) | [www.ubp.com](http://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](http://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.

---