UBAM - 30 EUROPEAN LEADERS EQUITY

Quarterly Comment

Marketing Communication
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Market Comment

- The last quarter of the year pushed global equity markets higher with another rally and +11% gains for the MSCI AC World. US equities rose +11.2% in Q4, Emerging Market equities +7.9%, Japanese equities +2.9% and Swiss equities +1.4%. The MSCI AC World delivered +22.2% over the full year with most regional markets finishing the year in the green despite limited market breadth and elevated bond yields (performances in local currencies). The MSCI Europe rose +6.4% in Q4 bringing its full year 2023 performance to +15.8%.

- As expected by the market, the Fed announced no change in its key rate policy in December, mentioning the pressure of financial conditions on global activity and alluding to potential interest rate cuts in 2024. The yearly trend in US headline inflation marginally declined from 3.2% to 3.1% as core inflation remained stable at 4.0% yoy. The US GDP growth projection for 2024 was revised slightly down from 1.5% to 1.4%, whereas Q3 2023 growth came in strong at 4.9%, lower than the 5.2% expected, but higher than the 2.1% for the prior print, reducing hard-landing fears.

- Q3 GDP growth for the Eurozone contracted -0.1% as expected, while the GDP growth projection for the Eurozone stands at 0.9% for 2024. Similarly to the Fed, the ECB held its key rates unchanged as the Eurozone's yearly inflation trend gradually eased to 2.4% yoy, slightly above the 2% target. 2024 earnings growth expectations for global equities remained stable at 10%, coupled with 16.6x forward PE ratio. After -3% contraction in 2023, the expected earnings growth rate for European equities for 2024 edged marginally lower to 5% overall, with 5% growth expected for the Eurozone and UK, but 9% for the Swiss market. This growth expectation reflects a broad recovery in corporate earnings which will probably, at least partly, depend on inflation and interest rate trajectories.

- The stock market has surprised investors over 2023, which had started with recessionary fears projecting more muted performances. The year also saw a large divergence in results between US IT mega cap names and the rest of the market, drawing a challenging environment for active fund managers. In Europe, performance sources were more diversified across names, sectors and countries.

- Over Q4, the majority of sectors of the MSCI Europe delivered positive performances. Industrials, Financials and IT were the largest contributors to the index' performance while Energy and Healthcare were the largest detractors. Top contributing names over the period were ASML, Siemens and Novo Nordisk, while the largest detractors were Sanofi, BP PLC and Bayer.

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Performance Review

- UBAM - 30 European Leaders Equity delivered +7.9% in gross performance over the fourth quarter of the year vs +6.4% for the MSCI Europe. Stock selection, particularly in Materials, Healthcare and IT, was the main contributor to relative performance. Sector allocation, especially the absence of exposure to Energy and the overweight in IT, as well as the currency effect, notably the overweight in CHF, also made positive contributions over the period. Since inception on the 12th of September 2023, the fund has accumulated +5.1% in gross absolute performance vs +5.3% for the MSCI Europe.
- Over Q4 2023, the biggest contributors to performance were the overweights in Hexagon, Atlas Copco and Givaudan (+75bps, +53bps and +44bps respectively). Hexagon rose +34% over Q4 after the company reported revenues above consensus and despite weaker free cash flow developments that were flagged as a temporary tie-up of NWC driven by strong organic growth. The company's capital markets day in early December, where they promised more detailed divisional disclosure allowing investors to build a better understanding of the business and its growth drivers, was also taken positively. Atlas Copco was up +23% over the period after reporting strong Q3 results across the board, despite a mixed macroeconomic backdrop. Givaudan's share price appreciated +21% over the period as the company reported a beat on Q3 results, with 4% organic sales growth stemming from continued strong pricing power.
- The main performance detractors over the period were the overweights in Julius Baer, Porsche and Merck (-84ps, -40bps and -39bps respectively). Julius Baer's share price lost around -16% after the bank warned that its full-year profit will probably decline after loan-loss provisions related to its CHF 606mn private debt exposure to the troubled real estate group Signa had to be markedly increased. Porsche dropped -10% as the company reported lower than expected margins in Q3. Despite robust demand and strong pricing, reported earnings and profits were negatively impacted by market weaknesses in China and the company's investments in innovation and marketing for its upcoming model launches. Merck was down -9% after its potential blockbuster drug Evobrutinib surprisingly failed Phase III clinical trials, negatively impacting the growth expectations of its pharma business.

Portfolio Activity and ESG

- No position switches were made over Q4. The position in Partners Group was slightly reinforced as the company confirmed markedly improved conditions for the second half of 2023.
- At the end of December 2023, UBAM - 30 European Leaders Equity had a AA ESG rating with an ESG quality score of 8.0, versus a A rating and 7.8 score for the MSCI Europe (ratings based on MSCI ESG Research). The portfolio's weighted average carbon intensity is lower than its benchmark's with 64.4 tons CO_2/$mn sales vs 93.4 tons for the MSCI Europe index.

Outlook

- Global equity markets finished 2023 on a strongly positive note, despite some signs of growth slowing, the banking sector fallouts, wars in the Middle East and Ukraine, and still elevated bond yields. US and European equities have regained all of their 2022 drawdown and are trading close to their respective end-2021 all-time market highs. Investors have factored in a soft-landing scenario for the US with possible interest rate cuts going into 2024. Moreover, with the Covid overhang now largely reflected in corporate results and the normalization of interest rates and inflation

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levels in sight, this should provide a supportive environment for equities in 2024, and more specifically for longer duration assets: quality companies with strong future cash flow streams.

- For global equities, valuation levels currently trade around long-term averages and earnings growth is expected to be the main market driver for 2024, after a low base of 0% growth in 2023. 2024 could thus offer a more favourable environment for active fund managers, as investors turn back towards fundamentally driven performance sources, which could lead to a catch-up of some of the lagging parts of the market. For European equities however, valuation levels are currently still below their 10-year historical range, offering continued re-rating potential for 2024. Coupled with an earnings growth recovery of 5% and a dividend yield of 3.8%, this could provide a relative performance advantage for European equities relative to global equities going into 2024.
- The 30 European Leaders Equity strategy should be well positioned to weather 2024 market conditions. The strategy continues to focus on high and stable value creation profiles, as well as strong fundamentals (visible and resilient earnings growth, pricing power, low debt levels and beneficiaries of structural growth trends). While there is limited re-rating potential for the portfolio, it is expected to deliver superior and visible 8.7% EPS growth in 2024 compared to 5% for the MSCI Europe, thus offering a fundamental catalyst relative to the overall market with little dependence on market timing or sector rotation.

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