Q2 2020

UBAM – EUROPE SMALL CAP EQUITY

Quarterly Comment

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

Market Comment

- As the previous quarter ended with the global economy on idle, the slow reopening of countries allowed by a relative containment of the virus propagation led to a strong second quarter for both the equities and credit markets. This was also supported by central banks around the globe which ensured that they would continue to provide the necessary firepower to keep government and corporate borrowing costs low.

- Reflective of the sharp rebound, equities display strong positive performance across the board. It is important to note that this was supported by normalizing levels of volatility throughout the quarter as the VIX indicator remained in the 25-35 region compared to the 70+ highs observed during Q1.

- The S&P500 index returned +20.5% during the quarter despite still high levels of unemployment, while the MSCI Europe ex-UK index returned +15.1%. Emerging markets recovered strongly too, with the MSCI EM index displaying 18.2% returns while the UK shows lower double-digit returns of +10.2%. The MSCI Europe Small Cap Index returned 18.7%, outperforming the MSCI Europe Index as investor risk appetite improved.

- It must be noted that underneath the index performance numbers, the sector returns are more differentiated. Unsurprisingly, the areas most affected by the virus such as hotels, airlines and banks have lagged the rally since late March. Similarly, while food retailers and supermarkets are the best performing sectors year-to-date, they have also lagged for most of the rally. Overall, value stocks are down -17% while growth stocks are up +6%.

- Positive performance was also seen on the credit market too. On the corporate side the Euro high yield rallied by 11.2% during the quarter, followed by US high yield which was up nearly +10%. More broadly, the Global Investment Grade instruments returned +8.6% during the period. In some way, this reflects that a liquidity crunch was avoided, thanks to the central bank stimulus of providing liquidity were necessary. In contrast, UK Gilts returned +2.6%, followed by Euro Government bonds with +1.7% and the US Treasuries at +0.5%.

All performance figures are given net of fees. Past performance is not a guide to current or future returns. See full disclaimer at the end of the document.

Performance Review

- During the second quarter of 2020, the UBAM - Europe Small Cap Equity Fund returned 23.83%, strongly outperforming the MSCI Europe Small Cap Index which returned 18.66% (performance is shown net of fees, IC EUR share class).

- Despite extreme levels of volatility, particularly during the first half of the quarter, stock selection and the fund's focus on strongly financed, well managed, competitively advantaged quality growth companies proved extremely positive. Amongst the top contributors to relative returns were our holdings of video gaming companies Stillfront Group AB and Codemasters Group Holdings PLC, online retailer Boohoo Group PLC, online financial services companies Avanza Bank Holdong AB and FinecoBank SpA, healthcare companies Diasorin SpA and Gerresheimer AG, and consumer goods companies Dometic Group AB, Thule Group AB and PIERER Mobility AG.

- During the quarter, it became apparent that lockdown would be beneficial for the video gaming industry as a whole with strong growth in player engagement, and our holdings in this space were no exception to this trend. Stillfront announced very strong first quarter earnings and provided positive updates on its recent earnings enhancing acquisitions. Codemasters also reported positive results with player engagement further enhanced by its involvement in rapidly developing esports activities. Codemasters has a strong programme of games launches in the coming months and remains one of the most attractively valued video gaming companies in Europe.

- Online financial services and brokerage businesses also benefited strongly from lockdown as consumers were able to spend more time assessing their savings. Strong brokerage revenues for Avanza Bank and FinecoBank as well as market share gains facilitated by the strong platform investment that both companies have made in recent years drove high levels of investor interest in these businesses.

- Similarly, online retailers benefited from lockdown as consumers shopped for essential and non-essential items from the relative safety of their own homes. Following initial share price declines during March, our holding of Boohoo recovered during the second quarter following the announcement of strong results and an opportunistic capital raise to provide additional firepower to acquire ailing retail fashion brands.

- Our holdings of healthcare related companies Diasorin and Gerresheimer continued to benefit from strong investor interest in the sector. Diasorin has managed to offset declines in revenues for standard diagnostic testing with its highly regarded Covid tests, leading to a significant rerating of the shares during Q2. Gerresheimer benefited as it's glass vials will be used extensively by Covid vaccine manufacturers, as well as a realisation by the market that the new management team are doing a good job of implementing a programme of operational excellence and investments in future growth.

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- Finally, a number of our holdings of consumer-oriented companies performed exceptionally strongly, driven by improved investor sentiment and a realisation that early estimates of the impact of lockdowns would prove to be overly negative. Our holdings of Dometic, Thule and PIERER Mobility also benefited from the fact that they sell outdoor leisure products which will continue to be in demand as consumers look to spend their holidays closer to home.

Portfolio Activity

- During the quarter we took advantage of the extreme levels of market volatility to adjust the weightings of some of our existing holdings as well as to add to introduce a number of new holdings to the fund.

- Following very strong relative performance during the early stages of the quarter in particular, we trimmed a number of our holdings of more defensive growth companies such as distribution company DCC PLC, healthy food producer Raisio OYJ, pharmaceutical packaging company Gerresheimer, diagnostic equipment company Diasorin, and healthcare services company UDG Healthcare PLC. We also trimmed holdings of digital platform companies such as Boohoo and Avanza following very strong share price performance.

- We took advantage of share price weakness to top up holdings of quality companies which had fallen in line with or by more than the market despite continue solid longer-term prospects. These included additions to leisure equipment company Dometic, holding company D'leteren, hotel company Dalata, visualisation technology company Barco NV, recycling company Befesa SA, building matertials company Volution Group, and travel retailer WH Smith PLC.

- Elsewhere on the fund we introduced new holdings in semiconductor equipment manufacturer ASM International NV and insurance company Lancashire Holdings Limited. We also participated a capital raise for leisure company JD Weatherspoon PLC. ASM International is the world leader in the attractive niche market of atomic layer deposition equipment. The highly innovative company stands to benefit as increasing levels of precision are required as semiconductor geometries shrink further.

- ASM International also has an exceptionally strong balance sheet and we were able to add the stock to the portfolio at an attractive valuation. Lancashire is one of the leading speciality insurance underwriters in the UK market and stands to benefit strongly from a hardening market cycle following its recent capital raise. JD Weatherspoon is the leading pub operator in the UK, focused on delivering a quality product to its customers at reasonable prices. Management has focused on operational excellence and continual improvements to the pub estate. The company stands to benefit from a gradual reopening of the UK economy including pubs and restaurants in the coming months.

Outlook

- The second quarter of 2020 witnessed a strong recovery in equity markets following extreme volatility at the end of March and into the month of April. Despite continued high prevalence of coronavirus in a number of geographies, early signs of improvement in macroeconomic data and business surveys from the very low levels witness in April, coupled with record levels of monetary and fiscal support from central banks and governments around the world, have provided some hope that corporate earnings might find a base level in the coming quarters. However, until further progress is made in discovering effective coronavirus treatments or vaccines, we believe that the market is likely to remain range bound and prone to bouts of heightened volatility.

- Against this continued challenging backdrop, we maintain a well-balanced portfolio from a country, sector and market capitalization perspective. We believe that effective stock picking will remain crucial to investment returns in the remainder of 2020, and our focus on well financed, competitively advantaged businesses with strong returns should stand the fund in good stead.

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