UBAM – Multifunds flexible allocation

Quarterly Comment | Q2 2021

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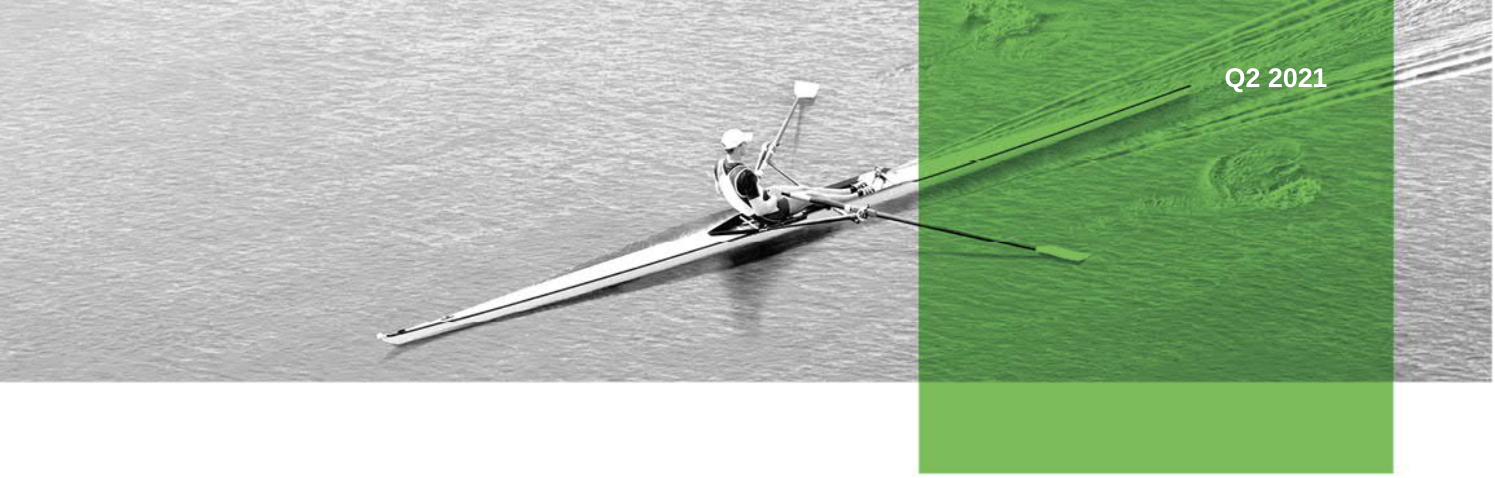
Market Comment

- 2021 has seen an uneven recovery in the world's economy, with variations driven to a large extent by the success of measures to stop the spread of Covid-19 and, particularly in the West, the speed of vaccine rollouts.
- However, the world's central banks, and increasingly fiscal policymakers as well, have stepped in to fill any gaps with stimulus measures of a kind not seen since the Second World War. This has driven a broad-based rally in risk assets around the world, while bond yields have risen, and the US dollar has weakened as a result.
- Global equities ended the quarter up 7.39% (MSCI ACWI*). In the US specifically, the S&P 500* index progressed by 8.44% during the second quarter with a noticeable outperformance of the Growth segment over the Value (11.9% q/q for the Russell 1000 Growth* and +5.06% q/q for the Russell 1000 Value*). Likewise, the MSCI North America Information Technology Index* progressed by 11.82% q/q, +3% above the broad S&P 500 index. In this context the MSCI Europe* delivered +6.46%, ahead of the MSCI Europe Small Cap* with + 5.30%. Finally, the Emerging markets delivered +5.05% but with a high dispersion. Brazil delivered +22.91% and on the other side, Chile was down – 14.19%.
- In April, investors were reassured by strong economic figures and the message sent by the Fed, which clearly stated its intention to continue supporting the US economy. The US economy grew at an annualized rate of 6.4% in the first quarter due to firm consumer spending, which was boosted by direct transfers to households as part of the stimulus plan adopted by the new Biden administration, along with an upturn in public-sector consumption and investment.
- Despite the Fed's slightly less accommodative message and the spread of the Delta variant, bonds and equities both posted positive returns in June. In the US, the ongoing economic recovery did not prevent some indicators falling short of expectations. While confidence in the manufacturing sector hit an all-time high, retail sales fell as direct support payments to households came to an end. Inflation continued to rise, with the annual figure reaching 5%. The FOMC surprised many observers in June, since most of its members are now expecting two rate hikes by the end of 2023. The Fed also increased its growth and inflation forecasts for 2021 fairly substantially.
- May 2021 will likely go down as a turning point in the fight against climate change, with three of the world's largest oil companies suffering defeats not only in the courts but also in their own boardrooms. Royal Dutch Shell became the first company to be ordered by a court to cut its carbon emissions – by 45% by 2030 – while the management teams of two of its American counterparts, Exxon and Chevron, saw their own shareholders vote against inadequate corporate climate targets.

Sources: UBP, Bloomberg Finance LP.



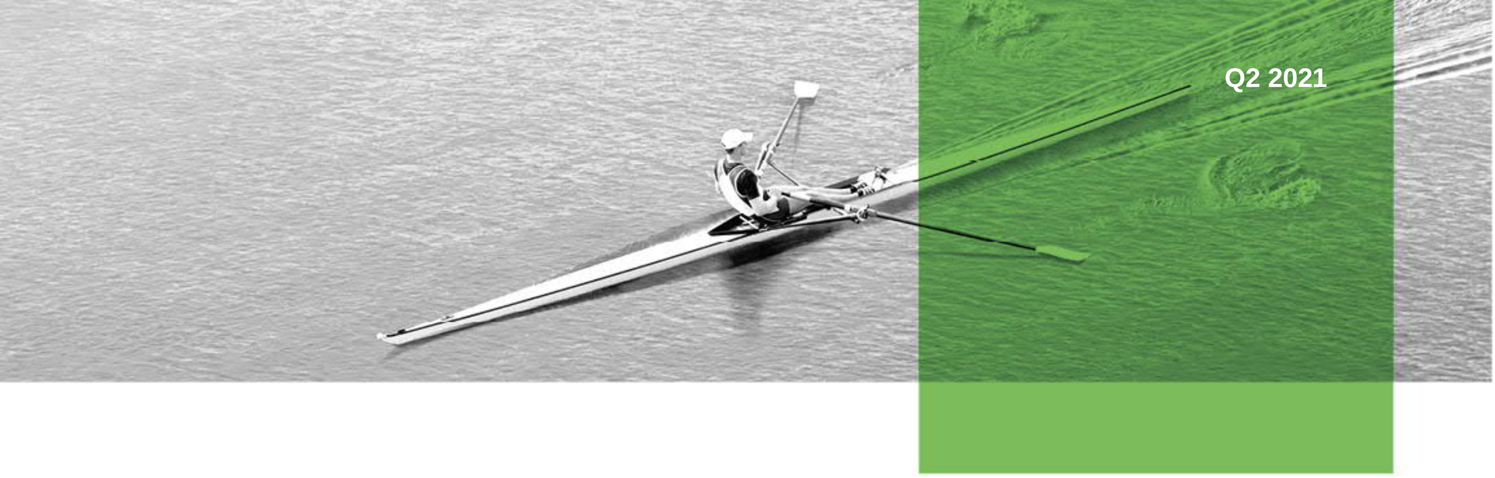
Performance Review

- A solid second quarter, delivering +4.6% in the USD Institutional class to leave the fund +8.6% for the first half of the year. Performance relative to the composite benchmark was broadly in line over the second quarter, however the fund remains +2.7% ahead of the composite benchmark on a year to date basis.
- Within the portfolio itself, most of the gains came from the bar-belled nature of the equity book, whilst the fixed income book was able to withstand a muted quarter for long duration fixed income overall. The rotations in markets caused by the COVID-related uncertainty and more hawkish Fed did modestly detract during the final month of the period. Of the twelve underlying active equity funds held in the portfolio, six finished above their respective benchmarks for the quarter, reflective perhaps of the gyrations seen during the final month of the quarter. Ten out of twelve of those funds remain ahead of respective benchmarks on a year to date basis however, and the core by a very wide margin. Of these, the more cyclically and operationally geared equity managers have experienced the strongest gains through 2021 as underlying portfolios have benefited by the strong rebound in global growth. Having begun the year at still relatively depressed valuation multiples, the majority are now back to mid cycle multiples and profitability measures. The best returns for these managers are arguably in the past for this cycle, however for now, they are still being buoyed by far stronger underlying earnings growth forecasts, particularly relative to their more defensive counterparts whilst the pent up operational gearing us further boosting profitability overall for this segment of the market.
- Within fixed income, solid gains came from the Flexible fund's skew towards Emerging Market hard currency debt via the Vontobel EMD Fund (+5.3%) and the Western Asset Macro Bond Opportunities Fund (+9.3%) which benefited from a flatter US yield curve during the latter part of the quarter, whilst spread compression across both the IG and HY areas of the corporate bond market was additionally incremental overall.

Portfolio Activity

- Portfolio activity was low during the quarter as preference was maintained to capitalise from this ongoing rebound in global growth and still ample liquidity environment. The only change which occurred was via the modest increase in the PIMCO Income Fund as a result of net inflows into the Flexible Fund.
- The fund finished the period with an equity weighting of 61%, very modestly ahead of the composite benchmark (60%), fixed income accounted for 26% of the portfolio (against the composite benchmark of 40%) and cash at 13%.

Sources: UBP, Bloomberg Finance LP.



Outlook

- Strong economic data and the momentum of the recovery have been a key driver of equity markets this quarter and with no doubt shall provide continued support. This was evident in the exceptionally strong March quarter reporting period, which saw the average earnings result beat expectations by over 20%. The stellar performance of the market since the drawdown in March 2020 has seen the MSCI World Index rally 93% in USD.
- The global economy is expected to rebound sharply this year thanks notably to the large support packages that many countries have pledged. The rebound in some EM countries may, however, be slower than initially planned due to the delayed deployment of vaccines and the appearance of new Covid-19 variants.
- A strong recovery is expected in Q3, but mainly driven by the rebound in domestic demand in developed countries. With the reopening of the economy, demand surged for goods and services after a long lockdown. US consumers spent the direct support delivered by the US Administration in Q1, but they still have large excess savings. In Europe, a similar rebound is underway from Q2 onwards, as governments prevented a large rise in unemployment and protected household incomes. Confidence is increasing further. GDP is expected to accelerate from the reopening phase thanks to a surge in domestic demand. US, UK and European growth should be close to double-digits in H2-21. Consumption and investment should benefit from deployment of the recovery plans adopted in the EU and discussed in the US, but emergency help to sectors and labour will end with reopening economies.
- Central banks will show more divergent strategies; some will shift their communication in favor of a more neutral stance, preparing markets to a tapering next year. Some central banks have mentioned their willingness to taper or adjust rates in the future: Canada, New-Zealand, Korea, Sweden and the UK's BoE have moderated their bond purchases. The Fed should explicitly talk about tapering in Q3 and prepare markets to reduce its purchases in 2022. To the contrary, the ECB should continue to purchase bonds in 2022 as inflation should be back below 2%.

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