

UBAM - EUROPE MARKET NEUTRAL

Quarterly Comment

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

Market Comment

- Following the regional disparities observed in Q3, the fourth and final quarter of 2020 displays more homogenous developments, in terms of both performance and Covid-19 evolution. Combined with a busy political agenda made up of unfolding US elections, the finalisation of Brexit negotiations, and widespread continuation of monetary and recovery stimulus, this was an eventful ending to the year.
- On one hand, the pandemic took a turn for the worse as autumn materialised and winter approached, with rapidly rising infection rates in Europe and the US surpassing the previous highs. As the capacity of intensive care units filled up, governments were forced to implement new lockdowns with the hope of slowing down the spread of the virus. This temporarily supported continued outperformance of pandemic winners such as online retail and healthcare.
- Nonetheless, pharmaceutical companies announced early November that they had been successful at developing vaccines which effectively reduce Covid-19 symptoms by helping individuals build antibodies prior to getting infected. This caused a sharp change of momentum on the equity markets in favour of value sectors such as hotels, airlines, energy and traditional retail which had their best quarter since 2009, rising nearly 16%. Although underperforming for the quarter, their growth counterparts still rose by 13%, allowing them to maintain a significant lead for the year overall (34.2% versus -0.4%).
- Overall, equities were up in all regions during the quarter. The UK FTSE All-Share is the leading index with +12.6% return, followed by the US S&P500 returning 12.2% and the MSCI Europe ex-UK index displaying 10.2% returns. The MSCI Europe Small Cap index rose by 16.6% during the quarter. This is not representative of the full year numbers which reflect the regional disparities a lot more: +18.4% for the US S&P500, +2.1% for the MSCI Europe ex-UK and -9.8% for the UK FTSE All-Share. European Smaller companies outperformed their large cap counterparts during 2020 with a return of 4.6% from the MSCI Europe Small Cap Index.
- The US growth stocks which had been important contributors to the country's performance throughout the year were affected by the vaccine news but following a peak of uncertainty the market found comfort in the election results and the prospect of a less confrontational president allowed a strong Q4.
- Good news also came from the UK a few days before the end of the year, as a Brexit deal was finally agreed with the EU which supported a +5% appreciation of the GBP. On the emerging markets side, strong performance this quarter again due to hopes of increased global trade and a cyclical recovery. This was fuelled by high demand for medical supplies and technological equipment which boosted Chinese activity, leading to +20% returns of the MSCI EM index (and 18.7% for the full year).

*All indices are total return in local currency, except global ones in US Dollars

Performance Review

- In the fourth quarter of 2020, UBAM - Europe Market Neutral returned +0.65% (Class I EUR), lagging the HFRX Equity Market Neutral Index (hedged in EUR) and the EuroStoxx 50 Index (total return) that returned +2.9% and +11.4% in Q4 respectively.
 - ▶ In terms of quarterly contribution, our Long bucket contributed positively +10.9% (gross of fees) to the overall portfolio, generating a positive alpha of +0.7% versus the beta-adjusted Eurostoxx 50 TR (SX5T) reference. The Short bucket detracted +0.5% (gross of fees) on an absolute basis, but generated an alpha of +0.1%.
- On a YTD basis through September, UBAM - Europe Market Neutral returned +11.2% (Class I EUR), comparing very favorably with the HFRX Equity Market Neutral Index (hedged in EUR) and the EuroStoxx 50 Index (total return) that returned -10.1% and -3.2% in 2020 respectively.
 - ▶ In terms of YTD contribution, our Long bucket contributed positively +12.0% (gross of fees) to the overall portfolio, generating a positive alpha of +10.3% versus the beta-adjusted Eurostoxx 50 TR (SX5T) reference. The Short bucket contributed +0.7% (gross of fees) on an absolute basis, but generated an alpha of +2.4%.
- Within the Long book:
 - ▶ The quarterly alpha of the long book was largely a result of very strong stock picking within the Information Technology and the Consumer Discretionary sectors; on the other hand, the underweight in Financials detracted alongside challenging stock picking within Industrials and Materials.
 - ▶ In terms of specific stocks positions, significant positive outperformance was recorded in SAP (IT), Moncler (Consumer Discretionary), ASM (Information Technology), Ryanair (Industrials), Sanofi (Health Care). On the other hand, ASML (IT), LVMH (Consumer), Santander (Financials), Airbus (Industrials), Teleperformance (Industrials) underperformed the main Eurostoxx reference on a relative basis.
 - ▶ Overall, our Long book outperformed the EuroStoxx 50 on a beta-adjusted basis.
- Within the Short book:
 - ▶ Short Bias, which represents 85% of the overlay allocation and is implemented via both futures and options on the Eurostoxx 50 Index most liquid contract, slightly underperformed during the quarter. The allocation was positioned defensively on average during the quarter, which translated into a cost when the market rallied in November before recovering in December 2020.
 - ▶ Tail Risk represents the remaining 15% of the overlay allocation and is implemented via front-contract Vstoxx volatility futures. The strategy initially suffered as the market dropped before the elections but volatility did not react as much as expected. However, the strategy brought some positive alpha over the quarter and compensated the loss of the Short Bias Strategy as quantitative signals reset the allocation to volatility futures to the minimum as equity market rallied post US election.
 - ▶ Overall, our Short book was in line with its reference.

*Index provided for comparison and information purposes only. The fund has no official benchmark.

Portfolio Activity

- UBAM – Europe Market Neutral combines two alpha generating engines in a single systematic investment process. The long leg is invested in the AM League Euro 50A© Index, which is based on best ideas from top-performing buy-side managers and is rebalanced on a quarterly basis and weighted according to conviction. The short leg is comprised of a dynamically managed short index overlay, which uses ultra-liquid index futures and options and volatility futures. UBAM has partnered with AM League to launch this innovative investment solution to capture this alpha.
- Overall, our long book positioning during the quarter was much more defensive than the market, with a beta of the long book of approximately 0.76, a one-way quarter-on-quarter turnover of 57% and estimated active share of 70% vs the EuroStoxx 50.
 - ▶ In terms of sectors, the largest allocations were in Industrials and Consumer Discretionary, with the former representing significant overweight versus the EuroStoxx 50 at the expense of underweights in sectors such as Financials and Consumer Staples.
 - ▶ In terms of countries, the largest active bets were notable underweights in Germany and France with a corresponding overweight in Italy and Spain.
 - ▶ The portfolio is relatively skewed towards large rather than mid-caps, with an average market cap of 19bn vs 90bn for the EuroStoxx 50.
 - ▶ Looking at single stocks, the top 5 positions were Teleperformance (IT), Iberdrola (Utilities), Intesa SanPaolo (Financials), Moncler (Consumer) and Covestro (Materials), nearly all representing significant overweight versus the EuroStoxx 50 and some with membership in the wider EuroStoxx 300 only.
- Within the Risk Management Overlay bucket:
 - ▶ Within the Risk Management Overlay bucket, trend signals used in the Short Bias strategy began the quarter with a slightly bearish positioning. Signals turned slightly bullish in late November and until the end of the quarter.
 - ▶ Within the Tail Risk bucket, the exposure to volatility futures was low at the beginning of the quarter. It remained stable with an under-protection until the end of the quarter. In terms of currency exposure, the portfolio remains 100% invested in EUR.

Outlook

Given where we are in the cycle, an equity market neutral product should appeal to many investors, with very low correlation to traditional assets and absolute returns. UBAM – Europe Market Neutral combines two complementary systematic strategies that may generate value both on the long side and the short side in a single daily liquid UCITS EUR-based fund.

The AM League methodology is fully transparent, but their underlying database is proprietary, with alpha capture mainly driven by their capability to access portfolios of best ideas in a way that isn't available to other players. For example, European carve-outs of global unconstrained (buy-side) portfolios with high active share.

On January 5th 2021, the long book quarterly rebalancing triggered a significant sectorial reduction in Consumer, Health Care and Communication Services in favour of Financials, Energy, Industrial and IT. New top stock picks are ASML, Schneider, Allianz, Adidas and Nestle.

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