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UBAM – AJO US EQUITY VALUE

Quarterly Comment | Q1 2020

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

Market Comment

- The S&P 500 N.R. finished the quarter in negative territories with -19.72% performance at the end of March. Growth has been outperforming blend stocks this quarter with a performance of -14.18%. Value delivered a negative performance as well over the same period with -26.88%. Sector wise, Information Technology with -12.62%, Health Care with -12.92% and Consumer Staples with -13.62% have been outstanding. Energy delivered the worst sector performance with -49.44%, followed by Financials with -32.32% and Materials with -26.14%.

- January set the tone for the rest of the quarter: the fast spread of coronavirus infections quickly dampened the initial optimism among investors. Improving sentiment in services and firm consumer spending across almost all regions, as well as unexpectedly strong data in China, continued to support the scenario of gradual global recovery for 2020 – at least it did until the fears of a pandemic emerged.

- In February, the increase in the number of coronavirus cases outside China triggered massive sell-offs on equity markets at the end of the month. While the spread of the virus in China did not stop equity markets from hitting new highs up to mid-February, the highly rapid expansion of the number of cases on other continents caused a fall of around 10% in the last week of the month. Developed markets – with relatively little difference between regions – fell by around 8% over the month.

- In March, the headlines have been almost entirely dominated by the spread of the coronavirus around the world and governments' and central banks' responses to it. Equities suffered spectacular falls, with the US market shedding 20% in just sixteen trading days, compared with the previous record of forty-four days in 1929. The announcements of massive support programmes by governments and central banks then sparked a rally of some 18%, the biggest rise in three days since 1933. In the US, weekly jobless claims rocketed to 3.3 million. The Fed announced new currency swap agreements with other central banks. Budgetary responses have been rolled out more gradually and the sums involved increased during the month, with the United States and China leading the field, with their aid packages set to total more than 10% of GDP, making the amounts involved greater than those spent in 2008.

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

- Q1 2020 has been a difficult environment for value investors as the index (Russell 1000 Value NR) achieved -26.88% Vs -14.18% for the growth index (Russell 1000 Growth NR).
- In this context the strategy underperformed its benchmark lagging by 239 basis points net of fees (I share class) against the Russell 1000 Value NR.
- The biggest contributor in the quarter was the stock selection within Communication Services that added 0.97% of out-performance. Information Technology (+50bps) and Consumer Discretionary (+37bps) were also positive contributors to this quarter performance.
- The largest detractor in the quarter was the stock selection with financials that cost 205bps of underperformance. Stock picking in Industrials (-94bps) and in Utilities (-49bps) have been among the most challenging sectors.
- Within financials, Citizens Financial (-53.21%), MGIC Investment (-55%) and Ally Financial (-52.50%) were the main laggards throughout Q1.

Portfolio Activity

- The portfolio manager constructs the portfolio according to AJO's investment process relying on 4 pillars: Value, Management, Momentum and Sentiment. AJO focuses on well-managed companies with quality cash profits, relatively low market valuations, positive price and earnings momentum, and favourable market sentiment. The portfolio is optimised to diversify multi-faceted risks.

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Outlook

- A recession is expected in the US in Q2 due to quarantine and major disruptions to the supply chain and energy sectors. This recession is expected to be followed by a relative sustained recovery, thanks to the strong measures adopted by the Fed and the Congress.

- In the US, the downturn in activity should propel unemployment to above 10%, but measures adopted should prevent a sharp loss in income, support small and medium firms, and avoid a structural rise in unemployment and a depression.

- Bottom-up consensus earnings estimates have been significantly revised down already but many more adjustments will be needed over the coming weeks. Arguably, the visibility on earnings will remain extremely low for a long period of time. Many companies have already withdrawn previously issued guidance. They will probably abstain from providing an outlook when they start reporting Q1 results in the middle of April but may just shed some light on the economic damage.

- Given the nature of this shock and the fact that there is no historical precedent, predicting the impact of the coronavirus on earnings is somewhat hazardous. This will depend on the actual depth and duration of the economic downturn; there is no doubt that the containment and social distancing measures implemented will have a huge impact on earnings. Declines in the magnitude of those seen during the Global Financial Crisis (GFC) cannot be ruled out, but the most affected industries (financials at that time) will not be the same.

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