Q2 2020

UBAM – EUROPE 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 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%.All indices are total return in local currency, except MSCI EM in US Dollars.

- 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 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 indices are total return in local currency, except global ones in US Dollars.

- Despite the positive picture painted above through the market recovery and central bank help, it must not be forgotten that to date, the virus has still not been fully contained and no vaccine has been approved. While some economies are reopening thanks to low levels of new infections, the US, Latin America and some emerging countries have been unable to control its spread.

- Moreover, a long duration of the current environment would lead to new risks. Indeed, some central banks have indicated that they are lending rather than spending, meaning that they address liquidity over solvency. Similarly, governments have issued stimulus cheques and generous unemployment benefits, but these are supposed to expire in July for the US and in October for the UK. This could lead to lower incomes for many people and have an impact on consumption.

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.

- Finally, political risks still exist as the Brexit situation remains unsolved, tensions between China and the rest of the world continue, and the US elections are fast approaching.

- Overall, an undeniably strong quarter across markets stimulated by an improving global environment and renewed investor optimism. Nonetheless, the second half of the year remains uncertain and infection rates will continue to be closely monitored.

Performance Review

- The fund delivered a net return of +14.01% in Q2 2020 versus a return of +12.60% from the MSCI Europe benchmark, an outperformance of 1.41%. (performance shown net of fees, IC EUR share class)

- Geographically, the strongest performance came from our overweight position in the UK and our underweight position in Denmark, although the former was by far and away the more significant effect. The UK outperformance can be attributed to a couple of positions in the UK retail sector, Boohoo Group PLC and JD Sports Fashion PLC. Underweight in large caps HSBC Holdings PLC, BP PLC, Royal Dutch Shell PLC and Glaxosmithkline PLC also contributed significantly. Generally, our bias to UK domestic stocks and away from the large multi-nationals stood us in good stead during. The Danish outperformance can be entirely attribute to one stock, pharma company Genmab A/S which continued to deliver good news on both existing and pipeline drugs.

- The largest negative contributors to the fund were our underweight positions in Germany and our neutral position in Switzerland. The German underperformance can be attributed to zero weightings in index heavyweights Siemens AG and SAP SE. Generally speaking German cyclicals performed well during the quarter, reflective of their value attributes. In Switzerland, our overweight in Zurich Insurance Group AG had a large negative effect as the sector moved out of favour with investors.

- At a sector level, an overweight stance in the healthcare sector and an underweight stance in Energy both positively contributed to performance. Amongst the healthcare names it was our holding in Genmab and zero weightings in Novartis AG and Glaxosmithkline that added the most value. A heavy underweight in the energy sector also contributed positively with zero weightings in Royal Dutch Shell PLC and BP PLC having the most notable effect.

- In terms of detractors, our overweight positions in consumer staples and our underweight in materials that were the largest negatives. Domestic staples stocks were the main culprits with Sainsbury PLC, Cranswick PLC and Kerry Group PLC detracting the most. Unusually, materials stocks and energy stocks moved in opposite directions during the quarter. Fortunately, the negative effect of the former was outweighed by our underweight in the oil names.

Portfolio Activity

- We entered the current crisis with a strong exposure to high quality stocks with strong balance sheets. This served the portfolio well in Q1 2020. As we entered the second quarter, we recognized that many value/cyclical stocks had been hard hit and that selectively there may be some opportunities. We therefore took the decision to selectively build up positions in these to protect the portfolio from the "bounce back" effect of economies re-opening.

- We focused our attention on those names where we felt either the company would emerge from the crisis in a stronger position or where we identified a high quality company with a strong balance sheets and great long term franchise which had been punished too hard on valuation in our opinion.

- In terms of purchases we added French auto component company Valeo SA, UK based testing company Intertek Group PLC, Irish budget airline Ryaniar Holdings PLC, French concession and construction company Vinci SA and UK pub operator JD Wetherspoon PLC. We also continued to build on some of our important themes, particularly those focused on sustainability, healthcare and the technology revolution. We added internet financial service companies Avanza Bank Holding AB in Sweden and Finecobank SpA in Italy to the portfolio. We also purchased holdings in Italian diagnostics company DiaSorin SpA and German healthcare packaging company Gerresheimer AG. Elsewhere we purchased holdings in French Energy company Total SA and German utility RWE AG.

- On the sell side, we predominantly financed the purchases through the reduction in position size of some of our large defensive stocks. We took profits in UK pharmaceutical stock AstraZeneca PLC and Swiss pharmaceutical stock Roche Holding AG. We reduced our position size in Swiss consumer gods stock Nestle SA and UK beverage company Diageo PLC. We reduced our position size in UK electricity distributor National Grid PLC and German utility Eon SE.

Outlook

- The current pandemic and the consequent socio-economic effects continues to dominate the narrative regarding the market outlook. We still have little visibility as to how and when economies normalise. The short-term impact is well understood but the longer-term implications are difficult to fathom. At this point in time we seek to retain some balance in the fund between higher quality value/cyclical stocks which will benefit from continued economic recovery and growth/defensive companies who will fare well in a low interest rate environment. However, if a vaccine is not forthcoming and the duration of this crisis turns out to be extended then a shift in exposure to the latter style may well be the next move.

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