Investment Managers

For professional clients only
June 2019
Monthly Perspectives
Optimal Income Range

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Central Bank Put supports investors' sentiment

- Global equity markets rebound in June as central banks reinforce their dovish stance
- G20 summit merely a truce in the "Trade war"; We maintain a lower risk portfolio
- We expect more central bank support going forward and more Chinese stimulus

Serge Pizem
Portfolio Manager

What's happening?

Most equity markets rebounded over the month. By adopting a much more accommodative stance, Central Banks opened the door to rate cuts in the United States as early as 2019 and raised the possibility of a return of asset purchase programmes in the euro zone and Japan if economic data were to disappoint.

In the United States, the June economic data remained relatively positive. In the euro zone, economic data was slightly disappointing, as reflected in the results of the European Commission's surveys. The good news is that the job market continued to improve. In the United Kingdom, Brexit concerns focused on the election of the new Conservative Prime Minister. In Asia, the latest Japanese domestic data point to a slight increase in activity despite exports continuing to suffer from trade war uncertainty. In China, the latest publications report a slowdown in activity, impacted both by the trade war uncertainties and by a slowdown in domestic demand.

Bond markets continued their recent gains. In the credit market, spreads narrowed on investment grade and even more so on high yield in both the United States and Europe.

Portfolio positioning and performance

	GLOBAL OPTIMAL INCOME				OPTIMAL INCOME				DEFENSIVE OPTIMAL INCOME			
	Dec-18	May-19	Jun-19	Δ	*Dec-18*	May-19	Jun-19	Δ	*Dec-18*	May-19	Jun-19	Δ
Equity	*40,1%*	43,0%	43,0%		*47,9%*	40,3%	43,2%		*13,9%*	17,9%	17,6%	
Equities	*37,3%*	44,7%	44,1%	↓	*51,2%*	49,6%	50,3%	↑	*11,1%*	17,4%	17,1%	↓
Equity Derivatives	*2,8%*	-1,7%	-1,1%	↓	*-3,3%*	-9,3%	-7,1%	↓	*2,8%*	0,5%	0,5%	
Fixed Income	*49,4%*	41,0%	39,7%		*40,3%*	31,2%	31,9%		*75,3%*	62,3%	60,2%	
Govies	*27,1%*	15,8%	14,9%	↓	*24,7%*	10,4%	10,3%		*38,4%*	20,9%	19,7%	↓
Bond Derivatives	*-16,5%*	*-3,4%*	*-3,2%*		*-21,6%*	*-0,4%*	*-0,4%*		*-13,9%*	*-5,3%*	*-5,1%*	
High Yield Credit	*5,3%*	5,8%	5,5%		*5,2%*	6,4%	6,5%		*6,0%*	6,5%	6,2%	
Investment Grade	*17,0%*	14,6%	14,7%		*10,4%*	10,9%	11,7%	↑	*30,9%*	29,7%	29,4%	
Emerging Debt	*0,0%*	4,8%	4,5%		*0,0%*	3,5%	3,4%		*0,0%*	5,2%	4,9%	
Risk Mitigation Strategies	*0,1%*	-0,6%	-1,5%		*0,0%*	-1,1%	-1,5%		*0,0%*	0,0%	0,0%	
Diversification	*2,6%*	2,3%	2,2%		*4,4%*	4,2%	4,2%		*0,6%*	0,5%	0,8%	
Cash & Money Market	*7,7%*	14,3%	14,8%	↑	*7,4%*	25,3%	22,2%	↓	*10,2%*	19,3%	21,4%	↑

↑ ↓ Major changes

MONTHLY PERFORMANCE CONTRIBUTORS

Global Optimal Income	Optimal Income	Defensive Optimal Income
Contributers	**Contributers**	**Contributers**
Equities	Equities	Equities
Corporate Bonds	Corporate Bonds	Corporate Bonds
Mutual Funds	Mutual Funds	Mutual Funds
Emerging Debt *(Long)*	Emerging Debt *(Long)*	Emerging Debt *(Long)*
Detractors	**Detractors**	**Detractors**
Equity alpha strategies	Equity alpha strategies	Equity alpha strategies
Short US and Europe; Long EM	*Short US and Europe; Long EM*	*Short US and Europe; Long EM*

In terms of performance, all three strategies (Global Optimal Income, Optimal Income and Defensive Optimal Income) were up in June after the May downturn. Equities were the main contributor for all three strategies but our fixed income strategies also contributed. Our equity replacement strategy (taken to have exposure to long term Eurozone volatility) and our long positions in EMU banks were close to flat.

In terms of positioning for the whole range of strategies, we maintained our overall positioning. We have done a small increase in our credit exposure. We got out of a stock in the defence sector on all three funds for ESG purposes. We increased our exposure to Global Small caps by adding to our existing position. We also reduced our exposure to the European auto industry. In Global Optimal Income specifically, we added to a few existing holdings of our quality growth companies in the US, Europe and Japan and sold some small remaining positions in REITS (Real Estate Investment Trusts) and telecom sectors.

Outlook

US monetary policy outlook appears increasingly dependent on the outlook for US trade policy. Markets currently expect the Fed to cut interest rates as soon as July. History suggests that the reaction of financial markets will depend on the reason for cutting rates. If the reason is weakening growth then this would not a good environment for equities overall (e.g. Jan 2001 or Sep 2007). If the reason is to provide insurance against future downside risks despite a resilient growth backdrop (e.g. in July 1995 or Sep 1998), then these rate cuts would most likely bolster equity markets.

In US, against a backdrop of weaker global activity, rising trade concerns and a spillover to US industrial activity we lower our GDP forecasts to 2.4% for 2019 and 1.6% for 2020. In Eurozone, Business manufacturing surveys merely stabilized around their 6 year lows, while disappointing forward looking indicators suggest that manufacturing weakness should remain in place. There is thus downside risk to our GDP growth of 1.1% in 2019 and 1.2% for 2020. We remain prudent on developed equities given the ongoing risks related to trade tensions between China and the US amidst soggy economic data.

In Investment Grade Credit, Year to date returns remain excellent but that does somewhat limit the outlook for further performance in the short term. The 12 month return outlook would be improved should the dovish commentary from Central Banks evolve into concrete steps which might include the reopening of asset purchase programs. A more dovish Fed is also supportive for carry positions, which would cushion the negative impact, should a modest correction occur in underlying bond markets. We continue to favour Euro Zone markets over the US as the currency hedging drives US yields below those available in the Euro Zone.