Boubyan Multi Asset Holding Fund

Fund Licensed by the Kuwaiti CMA (F/2016/0003)

31 January 2019

Sub-Manager's Commentary:

Market Overview

Global equities rose in January, recovering from steep losses in the final quarter of 2018. Emerging markets led gains, in US-dollar terms, bolstered by double-digit growth in Latin America and emerging Europe. The advance in developed markets was led by North America, although all regions added value. The MSCI USA Index rose 8.22%, helping the MSCI World Index register a gain of 7.81% in January, while the MSCI Europe Index rose 6.61%, all in US dollar terms.

Growth stocks and value stocks both gained, as confidence returned to global markets, bolstered by hopes of a lessening in global trade tensions and a pause in interest rate hikes from the US Federal Reserve (Fed). The US dollar strengthened slightly against the euro.

Major European equity markets saw strong gains in January, following losses in December, although economic indicators continued to show weakness. Euro area consumer price index inflation eased from 1.9% year-on-year (y/y) in November to 1.6% y/y in December, while estimates for 2019 as a whole, were revised down to 1.5%. Euro area gross domestic product growth was also revised down to 1.5% for 2019, a reduction of 0.3% from the previous estimate.

Influenced by this, the European Central Bank (ECB) kept interest rates unchanged in January, suggesting that risks to euro area growth have increased due to softer external demand, protectionism and financial market volatility. The ECB stated that it will use forward guidance on key interest rates, reinforced by the reinvestment of acquired assets, to ensure that inflation moves back towards its 2% target. Ten-year German bund yields fell by 8 basis points (bps) to 0.16% on the gloomy outlook for growth.

US equities made significant gains in January, erasing most of December's losses. A more accommodative stance by the Fed, alongside hopes of progress in US-China trade talks, drove the shift in momentum. Concerns about global growth influenced the Federal Open Market Committee to keep US interest rates on hold at its January meeting, and it suggested it would exercise patience when considering any future rate hikes.

Perhaps more importantly, though, the Fed said it would reconsider its policy of quantitative tightening through balance sheet reduction, which has been blamed for amplifying recent equity-market losses. The Fed committed to use the 'full range of tools' to create more accommodative monetary policy, should economic conditions require it in future. Ten-year US Treasury yields fell 5 bps to 2.63%, while 10-year Japanese government bond yields turned negative, losing one bp to -0.01%. Both high-yield and investment-grade corporate bonds advanced in January.

Emerging-market (EM) stocks rose in January, as the MSCI EM Index gained 8.76%, in US dollar terms, aided by currency strength in Europe and Latin America. The MSCI EM Asia Index rose 7.33%, in US dollar terms, driven by double-digit gains from China, but held back somewhat by weakness in India. The MSCI India Index lost 1.93%, in US dollar terms, on weak corporate earnings, exacerbated by a weak Indian rupee. Latin America was the best-performing EM region, driven by Brazil, which rose 17.77%, as measured by the MSCI Brazil Index, helped by a strong Brazilian real. The MSCI EM Europe Index also saw a healthy return of 11.51%, in US dollar terms, thanks to strong performance from Russia and Turkey. Both local-currency EM bonds and hard-currency EM sovereign bonds rose sharply, in US-dollar terms, boosted by Fed policy.

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بـوبـيـان كـابـيـتـال
Boubyan Capital

Sub-Manager's Commentary:

Broad commodity prices rose in January, recovering somewhat from lows reached in late December. Brent crude moved back above US$60 per barrel, as an agreement within the Organization of Petroleum Exporting Countries to cut supply, alongside US sanctions on Venezuela, outweighed concerns about reduced demand due to slowing global growth. Gold extended recent gains into January, benefitting from the uncertain global outlook.

Outlook

The global economic outlook is more complex than has been the case for a long time, which is having an impact on the level of risk that investors are willing to sustain and causing some repositioning. Turbulence in the final quarter of 2018 and the rebound of stocks into the new year has highlighted the importance of actively managed portfolios. Markets are transitioning from a momentum-driven to a range-trading environment, meaning diversification will be key.

The highlights of our analysis include the following:

- A return to long-run levels of market volatility, rather than the lower levels seen for much of the past ten years, indicates a new volatility regime. Our current conviction remains tilted toward a more cautious outlook.

- Corporate fundamentals remain strong despite the moderation in global growth, but labour markets are tight in many leading economies. Wage growth appears to be picking up although the broad inflationary environment remains benign. This combination may start to weigh on profit margins and is likely to slow the pace of earnings growth.

- Despite geopolitical headlines and trade tensions, growth fundamentals in the US continue to be positive, with tax reforms still providing a tailwind for earnings and margins. With increased volatility and lower valuations, the market's attention will focus on both corporate earnings growth and Fed policy moves.

- We have adopted a balanced view on equities, taking a more defensive stance within global stocks and monitoring the potential for continued market volatility.

- Ongoing global growth leads us to prefer lower exposure to government Sukuk and duration. The economic environment remains more supportive of corporate Sukuk, particularly high-yield, where valuations remain attractive.

- We remain positive on the longer-term growth potential of emerging markets, as recent headwinds, linked to global trade tensions and an appreciating US dollar, have abated. EM stock valuations have become more attractive, so we have increased our conviction in both Sukuk and stocks in emerging markets.

- Continued fears over protectionism and geopolitics mean selective positioning in EM is important, in our view.