Monthly commentary / 30.06.2020
Vontobel Asset Management

Vontobel Fund - mtx Sustainable Asian Leaders (ex Japan)

Approved for institutional investors in: AT, CH, DE, ES, FI, FR, GB, IT, LI, LU, NL, NO, SE, SG (Professional Investors only)

Market developments
Asia ex-Japan rallied 8.4% in June, outperforming AC World (+3.0%) by 5.4%. June performance took the second-quarter gain to 16.7%, the best quarterly performance since the turn of the century. Over June, equities embarked on a risk-on session with the re-opening of broader markets, better-than-expected economic data, hopes for a fresh stimulus and calmed tensions between the US and China. However, broad sentiment remained subdued with re-emerging COVID-19 cases in the US and in some emerging markets. Defensives and IT took over broad market performance leadership from cyclicals.

Portfolio review
In June, we initiated new positions in Mahanagar Gas, Micro-Star, and Hong Kong Stock Exchanges and sold the remainder of Korea Zinc and PTT Public. We also decreased Indraprastha Gas. As a result, the number of portfolio holdings increased to 36. The largest positions were Tencent, Alibaba, TSMC, Samsung, and HDFC Bank.

Performance analysis
The fund underperformed its reference index in June, among other things due to negative stock selection in utilities and real estate. The biggest negative contribution came from China Gas.

Outlook
There are a number of uncertainties given the complex relationship between the spread of the virus, the effectiveness of virus containment, economic support policies, and the behavior of investors. This may remain the case for the next few months.

Operations – We expect industry leaders to weather the Covid-19 storm better and to emerge stronger. After a three-year period of growing returns on invested capital (ROIC) in Asian markets, we now expect ROIC to decline in 2020 before any recovery in 2021. The duration of lockdowns across the globe and the resumption of economic activity will determine whether the rebound will be in the form of a “V”, a “U”, or even a “W”. In our opinion, companies with leading business models will get even better and emerge from the crisis stronger, as they have done during other crises. They will widen the gap to companies with questionable business models and a weak track-record of operational performance. As always, we will remain focused on “leaders” generating the highest cash flow relative to peers (first-quartile ROIC) and boasting the strongest competitive position (first-quartile industry position), because this should enable them to take a larger share of the economic profit pools in which they operate. In addition, the companies in our fund have stronger balance sheets than the reference index in general and weaker competitors in particular (net debt/equity ratio of -18% vs +25% for the MSCI Asia ex-Japan Index), which will help them weather this storm better.

Valuation – Current valuation levels are attractive in historical context. Every time the valuation of the Asia ex-Japan Index was at the current level in 12-month-trailing price-to-book terms (in a recessionary environment, we prefer this measure to earnings-based metrics), the index was up within 12 months (100% hit rate) with an average performance of +44%. Typically, in the first phase of a snap-back rally, “value” outperforms “growth”. However, in the second phase of a potential recovery, we expect higher-quality, faster-growing and better-positioned companies to continue to outperform in a lower-growth recessionary environment. Many quality companies, for example in India, are now at more attractive valuation levels.

Momentum – Expect continued negative earnings revisions as consensus estimates are still too high. According to JPMorgan, 2020 earnings estimates for emerging market equities have fallen by 10% so far. It is difficult to estimate to what extent an economic recovery is already priced in. The first and second-quarter reporting season should bring more clarity on earnings estimates. Generally, a further setback for the stock market cannot be ruled out.

Growth – Industry leaders are better positioned in a low-growth world. We believe the better competitive position of the fund companies will enable them to grow at a faster pace than the emerging-market average. Moreover, loose monetary and fiscal policies resulting in low or sub-zero interest rates increase the focus on higher-yielding assets such as equities. Ideas revolving around the possibility of direct purchases of stocks by the US Federal Reserve, for example, also support equity markets.

Risk – Capital market signals suggest “peak risk” may be behind us. The gradual decline of the “fear” index VIX since its March 16 peak suggests that the worst risk aversion may have passed (always subject to news about new infections). The leading companies that we own in the fund have superior risk profiles on average, leading to a beta below 1 (currently at 0.98). We believe this crisis is perceived as event-driven. This means the market looks set to face less pressure than in the case of a cyclical or structural crisis, hence could recover at a faster pace.

Flows – The worst seems over unless virus and recession fears re-emerge. The indiscriminate selling of equities that started mid-February was accompanied by market outflows of 84 billion US dollars (0.5% of total assets under management). Emerging market funds were hit particularly hard with outflows reaching 30 billion US dollars (2.5% of emerging market assets under management). This stopped towards the end of March, and we are optimistic that the worst is over. Outflows may resume should the health crisis see lockdowns extended well into the third and fourth quarter of 2020, which, however, is not our base case assumption.

Performance (in %)

Net returns			Rolling 12-month net returns			
USD	Fund	Index	Start date	End date	Fund	Index
MTD	7.7	8.4	01.07.2019	30.06.2020	4.1	1.7
YTD	-2.5	-4.7	01.07.2018	28.06.2019	-1.5	-0.5
2019	18.8	18.7	01.07.2017	29.06.2018	15.0	9.9
3 years p.a.	5.7	3.6	01.07.2016	30.06.2017	36.8	26.7
5 years p.a.	7.0	4.4	01.07.2015	30.06.2016	-12.9	-12.0
10 years p.a.	9.0	5.9	Index: MSCI AC Asia (ex Japan) net TR USD			
Since launch p.a.	12.9	10.6				
Launch Date		17.11.2008	Share class: I			
			ISIN: LU0384410279			

Past performance is not a reliable indicator of current or future performance. Performance data does not take into account any commissions and costs charged when shares of the fund are issued and redeemed, if applicable. The return of the fund may go down as well as up due to changes in the rates of exchange between currencies.

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Vontobel Asset Management AG
Gotthardstrasse 43, 8022 Zürich
Switzerland
T +41 58 283 71 11, info@vontobel.com

vontobel.com/am