THE DRIVE YOU DEMAND

INVESTMENT OUTLOOK

UBP Investment Advisors S.A.

September 2019

UBP Investment Advisors S.A.

GLOBAL MACRO OUTLOOK

BY SABINA WEBER SAUSER, SENIOR INVESTMENT MANAGER

After a surprisingly positive first quarter, global economic momentum started to fade during Q2 2019. At the same time, trade tensions between the US and China intensified again in the second half of May increasing the challenges posed by already weaker global demand. In addition to the direct negative impact on global trade, the tensions increase uncertainty and hence weigh on sentiment. A short-term agreement between the two countries seems unlikely, which will have an increasingly negative impact on suppliers in Europe and Asia. Furthermore, it increases fears of a disruption of global supply chains as higher tariffs mean more expensive or even inaccessible components.

For now, the long-term economic consequences are hard to predict. Given this environment, the global economy struggles to stay on its slow growth path, yet remains supported by private consumption and public spending. Structurally slower growth rates would imply less inflationary pressure and hence low interest rates for longer. In the US, these negative economic trends are currently only visible to a minor extent, yet the bond market sends signals of a potentially more severe downturn with a partial yield curve inversion. This could also be due to excessive market liquidity, although market participants should track bond markets and the US yield curve closely in the coming weeks. Yields of 10-year US treasuries fell temporarily below 1.5%, a figure last seen in 2016, while their German equivalent has reached a fresh all-time low with a negative yield of 0.7%.

In this environment, the FED has the difficult task of weighing up the current positive economic situation and the more pessimistic outlook. While investors' sentiment in the first half of 2019 was dominated by hopes of a resolution of the trade issues, focus has clearly shifted to recessionary risks and hence monetary easing. After the 0.25% rate cut in July, market participants have expressed their expectations for more cuts, pricing in between two and four additional rate cuts. Headline inflation is expected to remain subdued throughout the year and into 2020, as investors hope that the raise in tariffs will be partially offset by a weaker Chinese Renminbi and price reductions offered by Chinese exporters. We expect two additional rate cuts by the end of the year.

Meanwhile, the European Central Bank (ECB) has signaled that it is considering various measures to offset the weaker macroeconomic situation. Therefore, market participants are waiting for the ECB to elaborate during its September meeting on the monetary steps it will implement. In addition, the ECB will again grant two-year target long-term refinancing operations between September 2019 and March 2021 to increase overall liquidity and facilitate lending across the eurozone. Moreover, the Swiss National Bank (SNB) is also waiting on the ECB's announcement before it decides on the measures needed in Switzerland. Overall, the more dovish global central banks should provide noticeable support to financial markets.

After an unexpected strong first quarter with 3.1% growth, US GDP expanded at only a 2% annualized rate in Q2/2019 as the first effects of the trade tensions became slowly visible. While there had always been tariffs on imported goods from China of around 3%, they rose to an average of 12.4% in 2018, stand currently at roughly 20% and will further increase to an average of 21.5% in December 2019. For now, these tariff increases are partially offset by the weaker Chinese Renminbi. Meanwhile, looser financial conditions and a robust US labor market are supporting consumer spending, the most important component of the US economy. In addition, government spending remains supportive preventing a potential contraction in 2020.

In the Eurozone the slowdown continued with a feeble quarterly growth rate of 0.2% in Q2/2019 after decent growth of 0.4% in the first quarter. Yet, the labor market across the Eurozone continues to grow with currently over 160 million people employed – the highest level on record. The unemployment rate across the region was down to 7.5% by midyear, almost one percentage point lower than in the previous year and the lowest level since July 2008. In this environment, wages are picking up which should continue to support private consumption in the coming months. In addition, fiscal policy across the region is expected to help stimulate growth. Spain, Portugal and the Netherlands continued to display appealing quarterly growth rates of 0.5% for the second quarter and business and consumer sentiment in Finland, France and the Netherlands surprised positively. In contrast, the Italian economy stagnated as both trade and domestic demand made zero contribution to growth, while the economy in Germany contracted by -0.1%. Moreover, recent estimates hint to a weak start into the third quarter with Germany even facing a technical recession. While uncertainties continue to overshadow the economic outlook, we do not expect a full-blown recession. Headline inflation is currently hovering around 1%, way below the ECB's target of 2%, leaving ample room for the ECB to expand its monetary policy.

Despite trade tensions and weak German industrial production, the Swiss economy displayed resilience, supported by strong contributions from pharmaceutical, food and precision instrument exports as well as healthy private and government consumption. Yet, the outlook for the heavily export dependent Swiss economy is gloomier as it faces additional headwinds from the strong CHF which increased almost 5% year-on-year on a trade weighted basis. Headline inflation is expected to remain around 0.5% this year and throughout 2020. As a result, we continue to expect the SNB's monetary policy to remain ultra-expansionary and negative interest rates to stay in place for longer.

Headlines in the United Kingdom are dominated by domestic politics and Brexit related issues particularly since Boris Johnson became the new Prime Minister in July. Surrounded by pro leave figures in high profile positions, Mr. Johnson asserted that the UK will leave the European Union on October 31, 2019 "do-or-die". As a consequence, the Pound Sterling fell to a two-year low. Latest economic data indicated that growth has slowed while employment remained robust. At the same time, the property market, especially in the Greater London area, came under pressure and prices dropped by 5% over a 12-month period. This is the fastest rate of decline since the financial crisis.

The Japanese economy is currently driven by domestic private demand due to a healthy job market but also by a dynamic construction sector related to the 2020 Olympic Games in Tokyo. In contrast, exports shrunk for the eighth-consecutive month in July. Japan's exports to China fell by 9.3% and to South Korea, due to a bilateral trade conflict, by 6.9% from a year earlier. After the implementation of the sales tax increase in October 2019 from 8% to 10%, consumer spending is expected to weaken and economic growth will mainly depend on public spending. Altogether, we expect the economy to grow by 0.7% in 2019 and 0.5% in 2020.

China's growth rate decelerated to its slowest pace, weakened by the trade conflict with the US and suspended investment decisions. The economy grew by 6.2% in the second quarter, the slowest rate since 1992. The government plans to stabilize the economy by boosting infrastructure investments and tax cuts. Furthermore, the People's Bank of China (PBoC) might turn more dovish by cutting benchmark interest rates and reducing banks' reserve requirements. However, loosening monetary policy could place further pressure on the value of the Chinese Renminbi, an undesirable outcome for Beijing during trade negotiations.

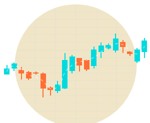
Investors have turned more risk averse as the flare-up in the trade conflict between the US and China took many market participants by surprise. Consequently, safe haven currencies such as the Japanese Yen and the CHF gained further ground, while Emerging Market currencies came under pressure. The SNB tries to limit the strength of the CHF which seems overvalued relative to the EUR, while the JPY still remains undervalued compared to the USD but also to the EUR. At the same time, the trade conflict and political risks remain as the main current driver of the USD exchange rate, probably keeping the USD relatively strong for now. Since Boris Johnson became the UK's Prime Minister, the GBP lost significantly and we expect volatility to stay elevated until the Brexit path becomes clear.

ASSET CLASS OUTLOOK

BY VANGHELI LAKIOTIS, SENIOR INVESTMENT MANAGER

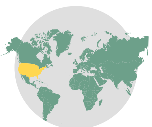
Developed market equities

We maintain a cautious view with respect to developed market equities as sources of volatility are abundant and the business cycle appears to be reaching an advanced stage. In the US, supportive monetary policy may be sufficient to quell recession risks. European markets appear vulnerable and decisive policy measures will be required to keep the economy afloat. Japan may struggle due to decreasing exports and consumption while the undervalued JPY may cap the local stock market by appreciating. Brexit and its potential consequences dominate the UK stock market, even more so since the most recent government change.



Emerging market equities

We apply a similar degree of wariness with respect to the emerging market equities universe. Even if trade frictions and related uncertainty have already taken their toll in these markets, important factors such as declining international trade, commodity prices under pressure and a strong US Dollar hinder a potential recovery. We prefer countries with more diversified economies and deeper domestic markets.

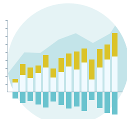


US bonds

Risk aversion, positive returns and excess liquidity have driven US Treasury long-term rates to levels much lower than expected, implying an inversion of the related yield curve. Against this backdrop, we are only willing to take limited duration risk and are ready to react to meaningful corrections. Investment-grade bond spreads are tight and do not justify excessive exposure to that segment, while real rates may still contain value in the medium term as inflation expectations remain low.

International developed market bonds

The strength of the USD and interest rate differentials plead for caution regarding international bond markets. Indeed, EUR, CHF and JPY sovereign bond yields hover at negative or very low levels. Smaller issuers carry their own intrinsic risks and opportunities.



Emerging market local currency bonds

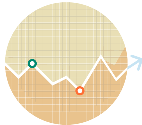
We have a neutral view for this asset class as the attractive average yield-to-maturity of roughly 7.0% and significant policy leeway in these countries to fight a potential downturn come up against expectations of the US Dollar remaining strong and the usual volatility linked to emerging market currencies.

Emerging market hard-currency bonds

Our outlook for this asset class is positive due to its attractive yield-to-maturity of roughly 3% north of US Treasuries and relatively resilient behavior during risky asset market downturns. Due to the inverted pattern of the US yield curve, shorter maturity bonds in particular display an interesting risk-reward trade-off as they combine an average yield-to-maturity of 3.9% with limited interest rate risk.

Global high yield

High yield bond spreads are particularly low, reducing the attractiveness of investor compensation in this asset class. Depressed US Dollar long-term rates and negative rates in other major currencies have pushed investors to hunt for yield in this territory. As the cycle matures, low default rates may increase constituting a risk for valuations. We maintain our negative view.



Alternative investments

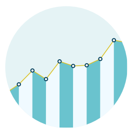
We have a negative view on hedge funds as they struggle to convince against a backdrop of market uncertainty linked to exogenous, often policy-linked factors, reducing the value of alternative managers' research. We currently seek some asymmetry potential in simpler and more liquid alternative pay-offs, such as those provided by convertible bonds.

Commodities

A lower growth path for the global economy and reduced fixed capital investment due to trade-related uncertainty constitute headwinds for this asset class. On the other hand, geopolitical challenges, including but not limited to the Persian Gulf, may create supply deficits implying upside risk. Our view for the asset class is neutral.

Gold

We maintain our positive view on the metal for the time being despite its recent strong performance. Indeed, against a backdrop of geopolitical tensions, volatility in risky asset markets and monetary policy accommodation, we believe appreciation may continue.



Cash and equivalent investments

Despite the recent rate cut by the Federal Reserve, returns remain in decently positive territory. Due to yield curve inversion, such returns closely match longer-maturity fixed income assets, which are more vulnerable to long-term interest rate variations. As such, this asset class remains one of our preferred safe havens.

OUTLOOK FOR SWISS AND GERMAN SMALL-TO-MEDIUM-SIZED ENTERPRISES

BY ANGELIKA STÜCKLER, SENIOR INVESTMENT MANAGER

There was a surprising rise in Swiss GDP in Q2 2019 with 0.3% q/q boosted by strong manufacturing and private consumption. We also noted a deceleration in the Swiss Purchasing Manager Index for SMEs, but it still shows a moderate expansion. Important economic indicators in Germany have declined throughout 2019 and point to a notable deceleration in economic activity. The epicenter of the downswing is the exporting and industrial sector, bringing the German economy to the verge of a recession. An erosion of pan eurozone business confidence, due to the lingering uncertainty around corporate earnings, Brexit and political and economic risks, suggests that the EU's weak pace of growth is unlikely to improve. The widely observed IFO Business Climate Index decelerated strongly in the second quarter with signs emerging that there will be an eventual spillover into the domestic service sector. However, German small-and-mid-sized companies are holding up better than their large-cap peers and expectations for the remainder of the year herald a more moderate deceleration of economic activity. We do not expect a swift rebound, as the demand weakness is becoming synchronized on a global scale and major sources of uncertainty including the US-China trade war are intensifying. We also expect rising CHF exchange rates to be a drag for many Swiss stocks in 2019.

In Switzerland, a study by Deloitte shows M&A transactions in the SME area picked up in 2018-2019 from previous years. The SME sector gained traction not only from domestic and foreign companies, but also from a growing number of private equity funds. Low interest rates in Switzerland and growing funds for risk capital facilitate this trend. For the rest of this year, the study assumes more moderate M&A transaction activity.

Amid the trade disputes, German SME companies have faced scrutiny from investors as many corporations have a strong global footprint. About 44% of German companies export directly or as suppliers to foreign corporations. Even very small-sized companies generate on average more than 20% of sales from their foreign businesses. The share of the industrial sector is higher still in Germany than other developed countries at about 23%. This sector fluctuates inherently more than the service sector.

There is no doubt that challenges for Mittelstand companies are increasing along with cyclical weakness and structural shifts in key industries, such as the automotive sector. The main fact that makes us confident about future growth of SMEs, is that these enterprises are innovation and technology drivers: almost half of the German SMEs have launched a product or process innovation on the market in the last year. Industrial companies are broadly diversified and account for 85% of all private R&D spending, which is among the highest ratios in the world.

Here are two defensive-growth healthcare stocks from our portfolio: Bachem Holding and Nexus AG. Both are well positioned to weather an economic downturn and give stability to our Swiss & German portfolio. A balanced sector and risk factor composition is a key prerequisite for managing equities in volatile times and for protecting wealth in the long term. Swiss and German SME stocks could deliver an impressive double-digit advance this year but most of the advance has been triggered by companies in the service and defensive sectors rather than among industrial or cyclical companies. On a positive note, the Swiss Franc is appreciating as a safe haven asset and many Swiss stocks show lower volatility than their global peers.

Bachem is a Swiss-based pharmaceutical producer, focusing on peptides (amino acids) and complex organic molecules such as active pharmaceutical ingredients (APIs), as well as innovative biochemicals for research purposes. The company has almost 50 years of experience in peptide research and technological processes, and has the potential to achieve a leading global position in peptides. They serve customers from the pharmaceutical and biotech industry. The company has expanded its business solidly in both Europe and the US over recent years and is well positioned in our view to continue growing revenue and earnings.

Nexus AG, based in Germany, produces special computer software, which organises hospital patients' medical records. The company benefits from the megatrends of rising demand for e-health solutions and ongoing consolidation among software providers. They operate in Europe, mainly Germany, Switzerland and the Netherlands and could grow sales and EBIT steadily over consecutive years. After a positive start in H1 in 2019, Nexus reports encouraging orders and sales for new products like ONE / NEXUS, its mobile apps and telemedicine solutions.

Disclaimer

UBP Investment Advisors S.A. | Geneva
Place Camoletti 6, 2nd floor | 1207 Geneva | Switzerland
T +41 22 317 49 60 | F +41 22 317 49 69
info@ubpias.com | www.ubpias.com

UBP Investment Advisors S.A. | Zurich
Bahnhofstrasse 1 | 8001 Zurich | Switzerland
T +41 22 317 49 40 | F +41 22 317 49 69
info@ubpias.com | www.ubpias.com