UBS Global High Conviction Fund

July 2020

Fund description
The Fund is an actively managed fund investing in a concentrated portfolio of 30–45 global equities across a range of geographic regions and economic sectors. It seeks to be fully hedged to the Australian dollar.

Investment strategy
The Fund is a high conviction concentrated strategy, taking meaningful positions at the company level seeking to identify the best opportunities to add value. There are no limits on sector, country or industry weights. The Fund’s largest active positions are in companies where we see the greatest mispricing and in which we have the most conviction.

Investment return objective
The Fund aims to provide a total return consisting of capital growth and income that outperforms (after management costs) the MSCI World ex Australia (net dividends reinvested) (AUD Hedged) Index over rolling three year periods.

Country/regional allocation (%)

Active security positions

Active industry positions

Investment performance

<table>
<thead>
<tr>
<th>Fund</th>
<th>1 month %</th>
<th>3 months %</th>
<th>1 year %</th>
<th>2 years % pa</th>
<th>3 years % pa</th>
<th>Since inception % pa</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total return</td>
<td>2.61</td>
<td>7.43</td>
<td>(4.47)</td>
<td>(2.35)</td>
<td>1.80</td>
<td>3.56</td>
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<tr>
<td>Benchmark**</td>
<td>3.29</td>
<td>10.63</td>
<td>3.46</td>
<td>3.76</td>
<td>6.86</td>
<td>7.33</td>
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<tr>
<td>Added Value</td>
<td>(0.68)</td>
<td>(3.20)</td>
<td>(7.93)</td>
<td>(6.11)</td>
<td>(5.06)</td>
<td>(3.77)</td>
</tr>
</tbody>
</table>

*1 March 2017. **MSCI World ex Australia (net dividends reinvested) (AUD Hedged) Index.

Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.
**Portfolio review**

After fees and expenses, the portfolio increased by 2.61% over the month, underperforming its benchmark by 68bps. In line with the investment process and thus as expected, sector and country allocation were close to neutral. The majority of the underperformance stemmed from stock selection. During the reporting period, security selection detracted particularly in IT, followed by health care and industrials, while it added value in communication services and real estate.

Key contributors/detractors on a stock level:

- **Apple**, not held by the Global High Conviction, soared towards the end of the month and thus was a notable negative contributor. Apple, along other large US technology companies, is thriving in a pandemic that has increased dependence on their products and services while the traditional economy suffered. Quarterly results from Apple and Amazon.com came in strong end of July and the respective stocks went up. Amazon.com was an overweight and contributed positively to relative returns.

- **Mohawk Industries**, a manufacturer and distributor of flooring for residential and commercial applications, underperformed in July. The stock fell sharply early July amid concerns over a lawsuit against the firm regarding alleged financial misconduct.

- **VMware** provides virtualisation solutions from the desktop to the data centre. The stock dropped when news came out that Dell was exploring a potential spin-off of 81% ownership of VMware. The transaction is not expected to happen before the second half of 2021. VMware’s valuation is undemanding and incremental buybacks could be supportive for its stock price.

- **Japanese conglomerate SoftBank** was the top positive contributor in July. Nvidia was said to be in advanced talks to buy Softbank’s chip company Arm. Also, SoftBank-backed oncology drug developer Relay Therapeutics raised USD 400 million in an IPO.

- **Osisko Gold Royalties** outperformed in July backed by a soaring gold price.

**Top overweights**

- **Amazon** is the leading internet retailer. We believe that Amazon’s revenue will continue to grow at high double digit rates as it expands Amazon Prime; expands its fulfillment centre network; expands the number of its merchandise segments; expands its hardware offerings to facilitate delivery of its content; exploits its sales tax advantage relative to traditional retailers; and as AWS continues to lead the public Cloud IT infrastructure market. Amazon’s operating margin improves modestly as it gains scale in an increasing number of its businesses; its growth moderates somewhat; it improves efficiency in new fulfillment centres; its investment in Kindle marketing gains leverage; its mix of third party sales expands relative to internal Amazon sales; and it gains scale in public cloud services and early, less efficient competitors exit the market.

- **Visa** is familiar to many as a brand of credit card. It is a payments technology company that connects consumers, merchants, financial institutions, businesses, strategic partners and government entities to electronic payments. The company is a high quality compounding, with good growth opportunities, very high barriers to entry, strong margins and strong cash generation. The group benefits from huge economies of scale due to its global leading position and also faces a rational competitive environment. As the shift away from cash payments towards cards and electronic payments continues we should see sales growth averaging around 10% for the next five years. Operating leverage and use of cash for buybacks should mean the company is able to post mid-teens EPS growth. Competitive risks appear fairly low — even supposed competitors such as ApplePay and PayPal actually use the card networks to facilitate their payments. There are some risks from litigation and regulation, but these should be manageable. We believe that despite Visa being a consensus long among investors, the current rating does not fully reflect the long track record of growth, high returns, margin expansion and cash generation.

- **Itochu** is an oversold commodity related company with a good valuation. The stabilization of China and the subsequent recovery in the iron ore price is a positive for the stock. Current management still focused on growth but also keeps a progressive dividend policy. This means that the yield for this year and next will be “real”. In the longer term there will be uncertainty after the current president steps down, since he was a major driving force behind Itochu’s current success.

- **Digital Realty Trust (DLR)** is a US based real estate investment trust focusing on data centre, colocation and interconnection solutions. We believe that DLR will continue to benefit from modestly improved occupancy at rents that generate attractive margins. The acquisitions and new developments that DLR is making are aggressively improving its global data centre portfolio and contributing to higher adjusted funds from operations. We believe they are well placed in providing the infrastructure to house the infrastructure of the internet. They are the leading operator in a sub-sector that has consistently generated higher levels of net operating income growth and industry-leading stabilized development yields. Finally, we believe they should be insulated somewhat from the effects of a slowing economy now that we may be in the late stages of the business cycle.

- **Marsh & McLennan Companies (MMC)** is a professional services firm offering clients advice and solutions in risk, strategy and people. One of the companies in the group — Marsh — is an insurance broker. Another — Guy Carpenter — specialises in risk and reinsurance. Mercer provides human resource and investment related financial advice and services and Oliver Wyman Group is a management and economic consultancy. Marsh remains well positioned to continue generating margin improvement, increasing its industry-leading profitability levels and we do not believe the stock reflects the strength and consistency of these superior returns. As well, at MMC’s current valuation, we believe investors are effectively being given a ‘free look’ at possible earnings accretion related to: 1) the widespread adoption of new — but rapidly growing — lines of insurance coverage in areas like cybersecurity protection and flood coverages (which continues to gain public attention as more incidents of mass cybertheft worries consumers and businesses alike); and 2) modest improvements in overall operating margins, which we estimate can be achieved even if global GDP growth underwhelms relative to current expectations.
Market review and outlook

In July, the interplay between economics and epidemiology continued to drive markets. Despite daily news headlines on resurgent infections in the US and other countries, as well as an escalation in US-China tensions, risky assets continued to rise. Global equities are now 40% up from their low point in March 2020. As the Federal Reserve maintained its dovish stance, treasury yields fell, the USD continued to depreciate and gold rallied. The volatility index VIX confirmed the lower volatility environment decreasing from 30 to 24 during the month.

In the US the most recent data surprised to the upside but the outlook remains highly uncertain. The Fed has eased monetary policy aggressively and fiscal policy has additionally provided strong support. The negotiations on a new package continues in congress with elections in November adding uncertainty to the outlook.

Europe is on the path to normalization as the COVID-19 restrictions are eased. Fiscal support has been plentiful thus far, and an EU recovery fund was agreed in July. The commitment to protect the European Union should remove any lingering doubts around the single currency, enabling investment in the Eurozone to rise.

In China, the economy has recovered from the trough in the first quarter and the Manufacturing PMI stayed above 50 in June for the fourth consecutive month. Announced fiscal stimulus is worth around about 7%–8% of GDP and monetary support remains strong. US-China relations remain tense providing some headwinds to the outlook. Outside of Asia, the fundamental picture for emerging markets remains challenged, with India, Latin America, and South Africa now among the most coronavirus-affected regions globally.

Global equities returned approximately 5% in USD terms in July and are now trading above its peak in February 2020. The best performing markets in local currency terms were US equities and emerging market equities, while European markets were flat-to-down. The corporate earnings season demonstrated broad-based earnings beats by US companies in particular, with consensus also revising up earnings expectations for the third quarter amid positive guidance.

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