

April 2022 | Rothschild & Co Asset Management Europe



Fund update

R-co Conviction Equity Value Euro



Anthony Bailly
European Equities
Fund Manager

Fund positioning & outlook

Financial markets were still driven by many different concerns in March. Firstly, the Russian-Ukrainian crisis which, despite a diplomatic channel that remained open and facilitated by the international community, was instead part of an escalation scenario with several waves of economic sanctions imposed on Russia. Another concern was the worsening of the Covid-19 situation in China, with the resurgence of lockdowns that are once again threatening global production chains and exacerbating inflation expectations. And, lastly, surges in inflation were confirmed in the latest CPI figures, which were higher than expected on both sides of the Atlantic (+7.9% in the US and +7.5% in Europe)⁽¹⁾, prompting central banks to speed up the tightening of their monetary policies.

As a result, the Fed made an initial increase of 25 basis points (bps) at its meeting on March 16th and has since then reiterated its resolutely “hawkish”⁽²⁾ stance, while the ECB has announced that its asset purchase programme is expected to end this summer. In that context, the US 10-year rate increased by 51 bps over the month, while the Bund⁽³⁾ gained 41 bps.



Vincent Iméneuraët
European Equities
Fund Manager

While this surge was common to nominal rates, it conceals discrepancies in real rates. As inflation expectations intensified, particularly in Europe, the German real rate fell by -9 bps while its American counterpart rose by 30 bps. Over the month, we also witnessed a flattening US yield curve, with the 2-10-year curve ultimately reversing at the end of March, in reaction to increased concerns about growth and pointing to a forthcoming recession.

This anxiety-inducing environment naturally hit consumer sentiment. The European confidence index experienced its biggest drop (to -18.7)⁽⁴⁾ since the first Covid-19 wave, but only made a slight dent in business optimism, as the European composite PMI fell by 1 point over the month and stayed at a high level (54.9)⁽⁵⁾. This optimism was confirmed in earnings per share (EPS) forecasts, which continued to be revised upward (+2.2% on the STOXX Europe 600 in March, thus raising year to date EPS forecasts to 11.2%)⁽¹⁾.

After dropping by 11% between February 28th and March 8th and bottoming out on that date, which was also when Brent peaked at \$128, the EuroStoxx with dividends reinvested appeared to have gradually absorbed these risks, rallying by 12% and enabling it to close the month of March at an almost stable level. However, if financials market quickly returned to early March levels, they did so via a sectoral rotation favouring defensive sectors (insurance, media, healthcare and telecoms), and at the expense of cyclical sectors (especially cars and leisure & travel). This rotation resulted in an underperformance of the Euro Stoxx Total Market Value by 3.5 points vs. its growth counterpart, the Euro Stoxx Total Market Growth, lowering Value year-to-date outperformance to +6.9 points as of the end of March⁽¹⁾. In addition, and according to a Goldman Sachs report, the recent underperformance of cyclical vs. financials is in line with the expectation of a level of contraction in the economy, with the Eurozone PMI level falling below 50.

(1) Source: Bloomberg, 31/03/2022.

(2) A stance that is more in favour of a less accommodative monetary policy to combat inflation.

(3) A German government bond maturing in 10 years, regarded as the benchmark rate for European markets.

(4) Source: Bloomberg, 23/03/2022.

(5) Source: Bloomberg, 05/04/2022.

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More than a month after Ukraine's invasion, it seems appropriate to underline the fact that the economy is nonetheless showing resilience. Most major institutions have incorporated geopolitical risk and uncertainty into their forecasts and Eurozone growth prospects have been downgraded by about 1.5 percentage points to a level of 2.5-3%, significantly higher than the area's long-term potential (1-1.5%)⁽⁶⁾.

Based on this scenario, we believe that the current crisis is an interruption to the economic cycle, but not the end of it. With this in mind, we have maintained the fund's cyclical and financial bias, believing that these sectors, which have been overly penalised since the Russian invasion, now offer substantial potential for revaluation.

Main transactions & contributions

In March, the fund posted a performance of -2.3%, underperforming its benchmark⁽⁷⁾ by -2.1%, and dragging its year-to-date outperformance to +0.8%⁽⁸⁾. The fund suffered from its cyclical and financial bias, but we decided to maintain this positioning.

About 40% of March's underperformance was due to the allocation effect and 60% to the selection effect. As regards the allocation effect, exposure to the automotive and leisure & travel sectors was the most detrimental, markets anticipating fears of a fall in real household incomes. The decrease in real rates, which is specific to Europe, and the flattening curve, also pushed the banking sector into negative territory, contributing to the negative allocation effect.

Regarding stock selection, Faurecia, caught between inflation on the one hand and its need for refinancing (following the acquisition of Hella) on the other, came under pressure from the market (and probably hedge funds), with a decline of 30% over the month, although this did not call into question its medium and long-term prospects. Italian banking stocks, such as Unicredit (-13%) and Intesa (-9%), were also under pressure, with the market questioning their commitment to return cash to shareholders, which will ultimately be related to how well economic growth holds up.

Despite heightened uncertainty and in accordance with our reading of the economic cycle and its current features, we did make some adjustments to the portfolio.

First, we raised our exposure to banking stocks that were hit the hardest despite their limited exposure to Russia and Ukraine, especially BNP and Intesa. Adjustments were also made to some cyclical stocks that we felt had been punished too hard by the market, with the best examples being Stellantis and Alstom.

In addition, we took advantage of the fall in prices to carry out an arbitrage within the leisure and travel sector by taking a position in Ryanair, financed by the sale of Sodexo shares. Market conditions offered us the opportunity to gain exposure to this quality player in the airline sector, with a strong balance sheet and an attractive competitive advantage in oil hedging. On the other hand, Sodexo, whose multi-local and defensive nature had offered a certain resilience, seemed to us to have mortgaged its strategic options (sale of the Benefits & Rewards business) with the appointment of Sophie Bellon as CEO, daughter of the Group's founder, when an outside personality was expected.

In the energy sector, we sought to maintain our overweighting by expanding our position in Technip Energies, which had taken a hit early in the crisis from its Russian exposure, but which we believe is particularly well positioned to benefit from the energy independence plan announced in Europe. We financed this expanded position by lowering our exposure to Total Energies and ENI, which held up during the month.

Lastly, within the more defensive pillar of the fund, we arbitrated part of AB Inbev (sensitive to the rise in the price of wheat and hops) to Danone, a more defensive position that took advantage of its strategic review at the beginning of March to assert the much more pragmatic nature of its new governance.

Completed on 7 April 2022

(6) Source: Bloomberg, 31/03/2022.

(7) Benchmark index: Euro Stoxx[®] NR.

(8) Source: Rothschild & Co Asset Management Europe, 31/03/2022.

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Performance	Since the beginning of 2022	2021	2020	2019	2018	2017	Since inception	1 year volatility
R-co Conviction Equity Value Euro C EUR	-8,16%	26,30%	-9,85%	17,64%	-18,01%	14,74%	96,41%	19,88%
Euro Stoxx® NR ⁽¹⁾	-8,94%	22,67%	0,25%	26,11%	-12,72%	12,55%	92,19%	16,07%

(1) Benchmark.

Sources: Rothschild & Co Asset Management Europe, 31/03/2022.



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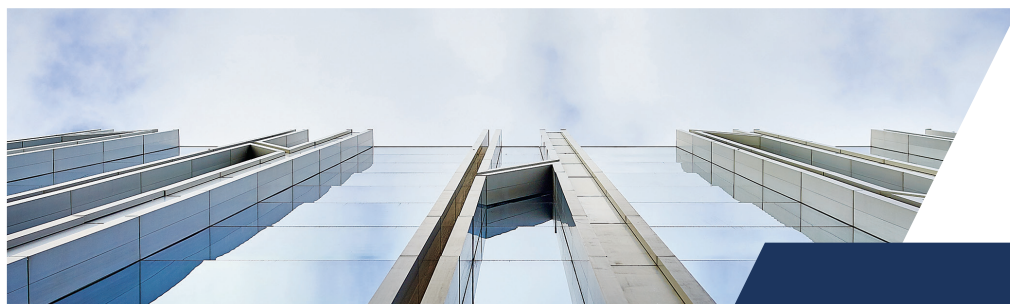
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