

UBS Tactical Beta Fund – Balanced

February 2023

Fund description

The Fund is a diversified Australian and global portfolio with the long term neutral (or average) exposure to income and growth assets expected to be 50% / 50% respectively of the total portfolio.

Target market

The Target Market Determination (TMD) for the Fund sets out the class of consumers for whom the product, including its key attributes, would likely be consistent with their likely objectives, financial situation and needs. To access to the TMD and other Fund documentation visit our website.

Investment strategy

The Fund comprises a diversified portfolio of income and growth assets predominantly using index funds, exchange traded funds (ETFs), direct securities, cash, cash equivalents and derivatives. The Fund tactically allocates between asset classes and currencies based on their relative value, whilst managing the overall risk and return of the portfolio. The Fund is not permitted to use leverage to amplify the exposure of the Fund to an investment.

Investment objective

The Fund aims to outperform (after management costs) the Benchmark (see Investment guidelines) over rolling five year periods.

Key statistics

Tactical asset allocations



Income Assets [^]	48.8%
Growth Assets	49.2%
Alternative Strategies	2.0%

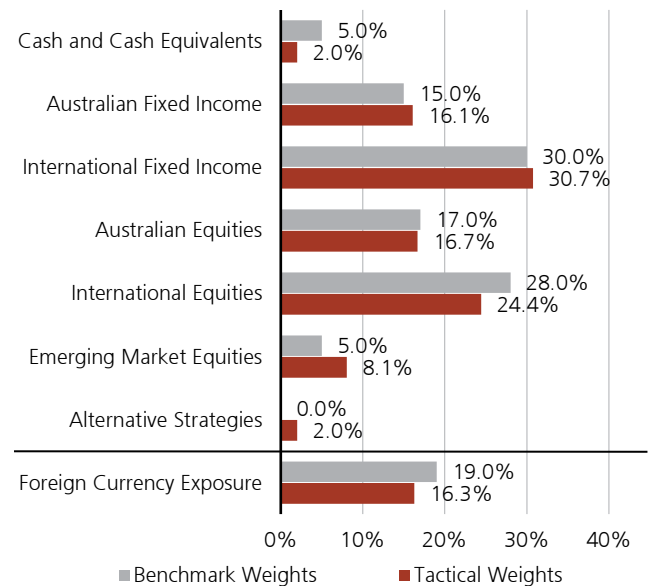
[^] includes cash

Fund information

Inception date	12 October 2012
Fund size	\$ 39.0m
Management fee	0.29% pa
Indirect costs	0.07% pa ¹
Minimum initial investment	\$ 50,000
Distributions	Quarterly
Buy/sell spread	+ 0.10% / - 0.10%

¹ Estimate of the fees the Fund will incur through the Fund's investment in underlying funds. These fees and expenses will vary from time to time.

Fund tactical and strategic allocations²



² Asset allocation includes derivatives used to hedge market exposures

Investment performance

Fund	1 month %	3 months %	1 year %	3 years % pa	5 years % pa	Since inception* % pa
Total return	(1.48)	(0.82)	(5.35)	1.31	2.83	5.37
Benchmark**	(1.22)	(0.58)	(3.87)	2.53	4.02	6.25
Added Value	(0.26)	(0.24)	(1.48)	(1.22)	(1.19)	(0.88)

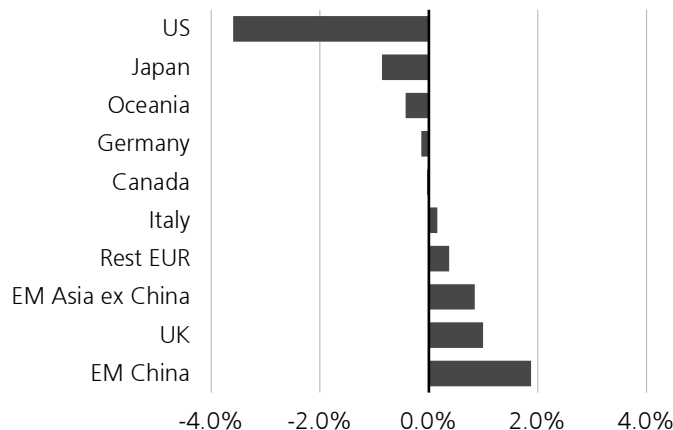
* Inception date: 12 October 2012.

** Neutral Allocation (refer to PDS).

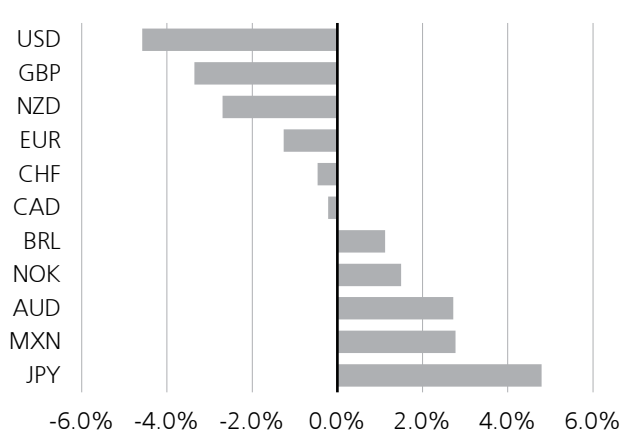
Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile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

Active portfolio positioning

Equities



Foreign currency



Market review

After an upbeat start to the year, markets turned pessimistic again in February, with major equity markets delivering negative returns over the month, except for Japan, UK and the Eurozone. The main concern was that stubbornly high US inflation and robust jobs data would force the US Federal Reserve to raise rates higher than expected and keep monetary policy restrictive for longer. The potential for a steeper and longer rate cycle contributed to a decline in the S&P 500 in February. At the same time, it boosted the US dollar which added to the headwinds for emerging markets, reducing liquidity and adding to the burden of dollar-denominated debt. Emerging market and China equities suffered the most among the major markets despite further evidence that consumption in China is recovering faster than expected following the dismantling of pandemic restrictions. On the other hand, Eurozone and UK equities delivered positive returns in February, benefiting from signs that the region's economy is weathering the winter better than previously feared. Japan equities also delivered positive returns over the month. Fixed income assets mostly fell in value over the month, amid renewed concerns over elevated inflation and central bank tightening. The yield on 10-year and 2-year US Treasury bonds both climbed over the month, and yield curves remain inverted.

Locally, Australian equities dropped in February which was in line with the downward trend of global equities. Australian 10-year bond yield reversed its January decline and climbed a bit over the month, creating a headwind for fixed income markets broadly. The Australian dollar depreciated against US dollar over the month.

Commodities faced a challenging month and delivered negative return in February. The oil price was volatile during the month and eventually delivered a negative return amid pull and push among the geopolitical escalation in Ukraine and the recovery of Chinese demand.

Performance review

After fees and expenses, the portfolio returned -1.48% (gross of fees return of -1.45%) in February which underperformed the benchmark return of -1.22% by 26bps. At the end of February, the Fund's equity weight was -0.8% underweight relative to the benchmark as we retained a small underweight to equities in aggregate throughout the month.

Foreign currency exposure was at 16.3% with key underweights in USD, GBP, NZD, EUR and KRW and overweight in JPY, MXN, AUD, NOK and BRL.

Positioning review

Within equities, we continued to focus on sector diversification between defensiveness and cyclical over the month. We retained our regional preference for the UK given its defensive characteristics and kept a neutral stance in Europe ex-UK equities, on the back of better-than-expected macro data pointing to a more resilient economy in the Eurozone. We also retained our overweight position in China and emerging market equities as China's COVID reopening remains a source of strength. US equities remained the largest underweight position followed by Japan equities. From an equity sector perspective, we further rotated to cyclicals by closing our overweight position to healthcare on expectation of earnings headwinds. We also opened an overweight to European banks, which is pro-cyclical, amid strengthening growth expectations and recent positive momentum. We retained our preference to US small cap over US large cap. We also maintained our position in energy equities and added more exposure to broad commodities positions amid recent weakness.

At the end of February, we were approximately neutral in aggregate duration in aggregate which remained intact throughout the month. We retained our preference for Canadian and Australian duration relative to the US on potential for diverging pace of interest rate hikes. We retained our overweight position to short-term US IG credit on the back of attractive yield pickup and underweight to the 5-year US treasury bonds which reflected our view on steepening of this part of the curve. We also prefer Italy over German duration as we see an opportunity at current relative spread levels. We kept our positions in emerging market bonds as we are expecting a favorable environment for this asset class amid a slowdown in rate hikes and a potential weakening of US dollar.

To balance the equity cyclical sector exposures we have added throughout the month, we have made various adjustments to our active currency trades. We reduced our cyclical currency exposures by adding to our underweight position in NZD. We also further trimmed our underweight position in USD amid the potential for USD strength should US rate hikes persist, which was funded out of cyclical Asian currency.

Asset Allocation

Asset allocation detracted from performance in February; while our defensive positions in the portfolio added value amid the correction seen over the month, exposures to commodity-linked and EM assets, and underweight to USD more than counterbalanced. In aggregate, our equity allocations, active currency trades as well as our allocation to alternatives detracted from the relative performance, while our positions in fixed income did not contribute meaningfully this month.

As global risk assets lost ground in February, our underweight position to equity contributed positively to performance. Our defensive equity relative value trade such as UK equities, as well as overweight to healthcare sector which we closed over the month were additive to performance. Our newly opened overweight to European banks was also one of the key contributors in February. Our overweight to US small cap against US large cap position marginally added value to performance. This was mostly offset by our overweight position to China and Emerging market equities as well our underweight to Japan equities. Overweight to energy equity sector was mostly flat in February.

Our overweight in commodities detracted from the relative performance amid a challenging month for most commodity markets this month.

Fixed income positioning did not contribute meaningfully in February. Our overweight position in Australian and Canadian durations against US duration as well as our overweight position in Italian duration against German duration also added value. This was partly offset by our holdings in emerging market bonds amid the continuous rate hikes over the month. Our overweight position in short-dated US IG credit was flat over the month.

Active currency trades in aggregate detracted this month. Our underweight position in NZD and GBP, and overweight position in MXN contributed positively over the month, which was mostly offset by our overweight position in JPY amid a continuous strengthening of USD in February. Our overweight in BRL, NOK and AUD also detracted from the relative performance in February.

Asset Allocation and Currency Strategy

After rallying in January, global equities lost ground in February as signs of stubbornly high US inflation and a still-tight jobs market prompted concerns about higher-for-longer Fed policy rates. In the US, the Q4 earnings season revealed a contraction in profits year over year, with much of the effect of last year's monetary tightening still to be felt. The sticky inflation and concerns of longer than expected rate cycled dragged the performance of US equity over the month. Chinese equities consolidated in February, delivering a negative total return over the month after rallying more than 40% from their November lows. China's performance weighed on emerging market equities more broadly, with emerging market also delivering negative return over the month. In Europe, the economy and market have turned out to be more resilient than expected, as the hit from energy shock seems to be much less severe than feared.

Market outlook

In our view, the risk-reward proposition for global equities at an index level is not particularly attractive. Stocks remain expensive vs. bonds based on the equity risk premium, and we believe earnings estimates are biased lower from here. We are more optimistic on global economic activity than consensus for 2023, but there are better ways to express this view than through equities at the index level. Long-term bond yields should be rangebound as robust labor market data and resilient economies square up against the fact that central bank tightening cycles are well advanced and that the risk of an eventual recession has not gone away.

Global markets retreated in February after an “everything rally” January in 2023. Indeed, US activity and inflation data have started off the year surprisingly strong relative to consensus, causing the market’s expectation for the Federal Reserve’s terminal policy to break to the upside, as well as a sharp surge in the US dollar in recent weeks. In our view, we believe that the US economy is neither as sluggish as December’s data made it out to be, nor in full-blown boom mode as some of the January figures would imply. The truth is probably somewhere in between. It is likely that US economic data still points to a solid expansion in February, but with a step-down in momentum. We do not expect US activity and inflation data to be so strong as to provoke a return to 2022 in rates and foreign exchange markets, where expectations for the Fed’s policy rate, and the US dollar versus other currencies, trended persistently higher.

At the same time, our positive conviction towards China remains intact, despite recent pull back due to reemergence of geopolitical tensions and a counter-trend rally in the US dollar. In our view, we believe the next leg of the mini reacceleration in global activity will be driven by China, which will also benefit the assets most sensitive to its economic rebound. In our view, our belief is that President Xi Jinping will largely be able to achieve the policy goals he sets, namely maintaining zero-Covid policy and addressing perceived excesses in the real estate and technology platform sectors in the past, as well as reestablishing a solid foundation for Chinese growth now and in the foreseen future. What is more, China’s pro-growth policy changes are bearing fruits. High-frequency data already suggested that a durable economic reopening is well underway, for example, road traffic and travel intensity data is telling a similar story of enhanced domestic mobility. In addition, the factors that interrupted the outperformance of Chinese equities, such as a resurgent US dollar and geopolitical concerns, will not have much more staying power as we already illustrated in the last paragraph. In summary, we believe China is set to become a leader rather than laggard in economic growth, and this dynamic will prove a more potent catalyst for markets than recent geopolitical disputes or the ultimate peak for the Federal Reserve’s policy rate.

Client Services

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