Boubyan Multi Asset Holding Fund

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Boubyan Capital

SUB-MANAGER'S COMMENTARY

Market Overview

Global equities continued to rally in February, despite signs that a pivot to easier monetary policy will be delayed. Markets responded to robust economic data and a stabilisation in global growth, leading to a more circumspect approach from major central banks as they attempt to contain inflationary pressures. Emerging markets (EMs) outperformed the rest of the world, led by China, while US equities led gains among developed markets.

The US Federal Reserve's (Fed's) monetary policy committee did not meet in February but has kept interest rates at a restrictive level since its last increase in July 2023. Policy easing has been delayed by surprisingly strong economic data, as non-farm payrolls rose by 353,000 in January, while fourth-quarter growth slowed less than expected, to 3.2% on an annualized basis. Headline consumer price index (CPI) inflation fell slightly to 3.1% (year-on-year), although core inflation (less energy and food) remained elevated at 3.9%. The case for a broad strengthening of the US economy was supported by purchasing managers' index (PMI) data from S&P Global, which highlighted an improvement in manufacturing activity during January, despite a slight softening in service sector growth. US factory output increased at the fastest pace since April 2023, as goods producers experienced stronger client demand and a sharper uptick in new orders. Against this background, US Treasury yields rose as the curve flattened slightly and remained inverted, while US investment-grade corporate bonds fell.

The European Central Bank's (ECB) Governing Council did not meet in February but held its main refinancing rate at 4.5% in January as it assessed tight financial conditions. Early estimates of euro area inflation predicted an annual rate of 2.6% in February, down from 2.8% in January, with core inflation expected to fall to 3.1%. Despite evidence of good progress towards the 2% inflation target, signs of recovery in the eurozone economy have promoted a cautious policy approach from the ECB. PMI data from S&P Global showed that forwardlooking indicators such as new orders and purchasing activity signalling their softest falls in close to a year in February, with the strongest performances seen in the periphery of the eurozone. Against this backdrop, German Bund yields rose, as the curve flattened and remained inverted.

EM equities gained ground in February, helped by robust gains for Chinese stocks following recent weakness. Chinese manufacturers signalled a sustained improvement in operating conditions, according to PMI data from Caixin, noting upturns in production and new work and a rise in new export orders. Investors also responded to state-backed equity purchases and stimulative measures from the central bank aimed at supporting the Chinese economy. Elsewhere South Korean markets rose, helped by a recovery in semiconductor exports, while European EM markets also gained, notably Poland. In contrast, Latin American markets were relatively weak. The MSCI ACWI Islamic Index returned 3.31% (in US-dollar terms) during February, while the Dow Jones Sukuk Index, returned -0.29%.

Performance and Positioning

The portfolio posted a net return of 1.01% (in US dollars) during February, outperforming its custom benchmark, which returned 0.90% (also in US dollars). An underweight to Sukuk proved positive for relative results during the month, as the asset class underperformed equities.

Our defensive holdings contributed to relative results, in aggregate, primarily Emirates Global Sukuk Fund, which outperformed the benchmark Dow Jones Sukuk Index, amid positive security selection. In contrast Franklin Global Sukuk Fund detracted, held back by a duration overweight during a period of rising rates. Our exposure to gold shares generated a positive absolute return, bolstering defensive positioning.

Equity fund selection also proved to be a slight contributor, in aggregate, helped by the strong performance of Comgest Growth Europe Fund and Templeton Shariah Global Equity Fund.

Outlook

We have retained our positive view of equities into March as we believe elevated equity valuations are offset by lower inflation and a stabilisation of growth in major developed market economies. Leading indicators are also turning upwards, contributing further to our constructive view of growth.US economic data have recently surprised to the upside, notably strong job numbers, although inflation continues to trend downwards, suggesting a low risk of growth stability leading to reflation. Core inflation may remain persistent for some time but should also ease as wage pressures continue to moderate.

Against this background, the Fed has pushed back against market expectations of interestrate cuts, and may not lower rates until the second quarter of 2024, in our view. A slight extension of the 'higher-for-longer' rhetoric we saw in 2023 should not be overly detrimental to risk assets, although we remain nimble in our cross-asset positioning, given expensive equity valuations and rich credit spreads. We expect the ECB to begin its easing cycle earlier than the Fed, given a relatively weaker economy.

Increased supply-side pressures linked to the Middle East crisis could be perceived as inflationary, particularly given a strengthening US economy, but we believe that an easing of supply bottlenecks elsewhere, alongside subdued oil prices, negates any possibility of rising interest rates in major developed market economies.

Against this background, we retain an optimistic outlook on US equities amid strong economic activity and robust corporate earnings. An ongoing enthusiasm for the prospects of artificial intelligence (AI) contributes to their relative strength, notably large-cap growth stocks. Our outlook on EMs (ex-China) also remains bullish moving into February, helped by attractive valuations, as strong long-term growth opportunities and latent developed-market demand should boost earnings further. Elsewhere, we remain neutral towards China, while retaining pessimism towards the Pacific ex-Japan region given the importance of China to these economies. Elsewhere, our caution on European equities stems from the impact of wage increases on profit margins, despite a stabilising eurozone economy.

Our Sukuk positioning continues to show a preference for higher-quality credits that have financial buffers to manage slowing economic activity. Where we do take on higher-risk positions, they are increasingly selective, idiosyncratic and, in our view, compensate us for the elevated risks involved. On average, however, our portfolios do have higher credit quality than their historical average.

Rates volatility is likely to be elevated as economic data releases project different growth paths and as the US presidential election cycle highlights long-term challenges, affecting market sentiment. As a result, we maintain overweight duration exposure, particularly as credit spreads remain tight and provide less opportunity for returns.

Past performance is not an indicator or a guarantee of future performance.