Boubyan Multi Asset Holding Fund

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Boubyan Capital

SUB-MANAGER'S COMMENTARY

Market Overview

Global equities rose in August, recovering from a sharp drawdown in the first few days of the month, triggered by overextended sentiment. Market volatility spiked during the selloff, as investors de-risked portfolios, but solid fundamentals eventually bolstered sentiment, allowing markets to recover losses. Emerging markets (EMs) rose, in US dollar terms, but were outperformed by their developed market counterparts, led by European stocks.

The US Federal Reserve (Fed) did not meet in August, but a speech by Fed Chair Jerome Powell hinted strongly that the Federal Funds Rate would be cut in September. Powell said that the time had come to adjust monetary policy, with the timing and pace of cuts dependent on incoming data. The comments were prompted by deteriorating jobs data and weakness in the US manufacturing sector, which threaten the Fed's stated aim to deliver a soft landing for the US economy. The unemployment rate rose to 4.3% in July, while nonfarm payroll employment edged up by just 114,000. Elsewhere, the Institute of Supply Management said that the US manufacturing sector contracted in August for the fifth consecutive month. Set against this is a relatively robust services sector, which continued to expand in July, according to a purchasing managers' index (PMI) report from S&P Global. Elsewhere, headline consumer price index inflation fell slightly to 2.9% (year-on-year), but core inflation (less food and energy) remained elevated at 3.2%, well above the Fed's target. Against this background, the US Treasury yield curve bull steepened and came close to un-inverting as yields fell sharply at the short end. Corporate bonds rose, alongside US equities, as the S&P 500 index was led by the consumer staples, health care and real estate sectors.

The European Central Bank did not meet in August but remains cautious about balancing further rate cuts against ongoing inflation pressures. Euro area annual inflation is expected to fall to 2.2% in August, down from 2.6% in July, as the disinflationary impact of falling energy prices helps to move inflation back towards target levels. However, core inflation remained elevated at 2.8%, impacted by higher prices for services. PMI data for August, from S&P Global, established that growth in the euro area was fuelled entirely by services activity, which rose at the fastest rate in three months, helped by the Paris Olympics. In contrast, manufacturing production continued to shrink, extending the current sequence of decline in factory output to 17 months. In addition, sentiment among German businesses declined in August, according to the IFO Business Climate Index, adding to scepticism about economic conditions in the eurozone. Against this background, German Bund yields fell at the short end of the curve, which bull steepened.

EM stocks, as measured by the MSCI EM Islamic Index, rose slightly across the period, in US dollar terms. Stocks in China and India were broadly flat, while markets in Indonesia, Malaysia and the Philippines posted strong gains. Operating conditions in China's manufacturing sector improved, as incoming new orders returned to growth, although export orders were subdued amid deteriorating external conditions. Expansion of the service economy was sustained by rising new business inflows in August, bolstered by the tourism sector. Elsewhere, Brazilian equities posted solid gains, driven by a strengthening economy.

The MSCI ACWI Islamic Index returned 0.97% (in US dollar terms) during August, while the Dow Jones Sukuk Index returned 2.00%.

Performance and Positioning

The portfolio posted a net return of 1.23% (in US dollars) during August, underperforming its custom benchmark, which returned 1.65% (also in US dollars).

Equity fund selection detracted, in aggregate, held back by exposure to US and EM equities, which underperformed the broad global equity benchmark. In contrast, our active selection added relative value, notably Comgest Growth Europe Fund, as returns were enhanced by a weak US dollar.

Our defensive holdings detracted slightly from relative performance, in aggregate. An allocation to gold shares had no significant impact on results, as gold prices plateaued in the second half of August. Elsewhere, our Sukuk holdings posted positive absolute returns but trailed the benchmark Dow Jones Sukuk Index, during a period of falling yields.

Outlook

We retain a neutral approach to asset allocation into September, as we balance seasonality and US election uncertainty against relatively supportive economic fundamentals.

We consider August's drawdown as a healthy correction that was quickly erased by most equity markets. The global disinflationary trend remains supportive to risk assets, in our view, allowing major central banks to cut interest rates in support of slowing economic growth. Leading indicators of global growth have ticked up recently, perhaps reflecting an easier policy environment, while US corporate earnings breadth has also improved given the cyclical rotation away from growth stocks. However, risks remain balanced across assets, in our view, particularly given that equity risk premiums remain low in the current uncertain environment. September is traditionally the worst month of the year for equities, while the US election is likely to fuel ongoing market volatility. Given this uncertainty, our preference is to remain neutral and analyse the impact of these factors before adding back to risk.

Within equities, we continue to hold a preference for markets with proven earnings power and corporate resilience. US stocks look healthier, but we hold a slightly diminished conviction toward European markets amid persistent economic weakness. Purchasing managers' index data released by S&P Global in August shows that the eurozone's manufacturing sector started the third quarter of 2024 with a steep reduction in new orders, impacting output and employment. Elsewhere, we are no longer cautious on UK equities amid an improving economic backdrop, although weak macro and corporate fundamentals moderate our enthusiasm for Canada and the Pacific ex-Japan region. We continue to prefer emerging markets (ex China), particularly the Asia region, which should benefit from strengthening semiconductor demand and a buoyant Indian economy. In contrast, headwinds in China seem likely to persist despite recent policy announcements.

Our Sukuk portfolio has increased credit quality recently. Where we do take on higher-risk positions, they are increasingly selective and idiosyncratic and, in our view, compensate us for the elevated risks involved. Credit spreads were volatile during August but remained well anchored, although we expect this to change, with higher-quality issuers potentially starting to perform better, on a relative basis, than they have been over the past year.

Interest-rate volatility is likely to remain elevated as incoming economic data support conflicting growth and inflation narratives, along with a US presidential election cycle exacerbating policy uncertainty.

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