Boubyan Multi Asset Holding Fund

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31 March 2024

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Boubyan Capital

SUB-MANAGER'S COMMENTARY

Market Overview

Global equities continued to rally in March, capping off a strong first quarter, despite signs that a pivot to easier monetary policy will be delayed. Markets responded to a further stabilisation in global growth, leading to a circumspect approach from major central banks as they attempt to contain inflationary pressures. Developed markets marginally outperformed their emerging market (EM) counterparts, led by Europe, although markets in most regions rose.

The US Federal Reserve's (Fed's) monetary policy committee held interest rates at 5.25%–5.5% at its March meeting, influenced by a robust jobs market and still-elevated inflation. Headline Consumer Price Index (CPI) inflation rose slightly to 3.2% (year-on-year) in February, driven by a 0.4% increase across the month, but core inflation fell slightly to 3.8%. Elsewhere, nonfarm payrolls rose by 303,000 in March, while growth for the fourth quarter of 2023 was revised up to 3.4% on an annualised basis. The resilience of the US economy was reflected in Fed board members' latest economic projections, released in March, which upgraded growth and core inflation estimates for 2024. The median projection for the federal funds rate was unchanged, at 4.6% by year-end, but was revised higher for 2025 and 2026. Signs of improving economic conditions and market demand influenced a further expansion of US manufacturing production in March, according to Purchasing Managers' Index (PMI) data from S&P Global, while the services sector also grew, albeit at a more subdued pace. Against this background, US equities rose, while US Treasury yields fell slightly at the longer end of the curve, which remained inverted. Corporate bonds rose slightly as spreads narrowed amid robust investor sentiment.

The European Central Bank's (ECB) Governing Council held its main refinancing rate at 4.5% at its March meeting, despite inflation in the region dropping closer to target levels. Annual inflation in the euro area is expected to fall to 2.4% in March, down from 2.6% in February, but core inflation remains elevated at 2.9%. The ECB cited strong wage growth as a concern, despite tight financial conditions contributing to a downward revision in growth projections to 0.6% for 2024. PMI data for March showed the euro area economy moved back into expansion territory at the end of the first quarter, halting a sequence of contraction stretching back to June last year. Against this backdrop, European equities rose, led by Italy and Spain, while yields fell across the euro government yield curve, which remained inverted.

EM equities gained ground in March, helped by robust gains for EM Asia markets, notably Korea and Taiwan, amid a robust semiconductor industry. Chinese markets posted subdued gains, helped by positive PMI data from Caixin, which noted a fifth successive month of improvement in the manufacturing sector and an acceleration of growth in the services sector. Elsewhere, Latin American markets were mixed, as Mexican stocks benefitted from a strong peso, in US dollar terms, but Brazilian equities lost ground. Oil prices rose during March, influenced by a heightening of Middle East tensions.

The MSCI ACWI Islamic Index returned 2.92% (in US dollar terms) during March, while the Dow Jones Sukuk Index returned 0.70%.

Performance and Positioning

The portfolio posted a net return of 1.92% (in US dollars) during March, outperforming its custom benchmark, which returned 1.43% (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 gold shares, which rose sharply during March amid heightened geopolitical risks. Our Sukuk holdings broadly matched the benchmark Dow Jones Sukuk Index and had no significant effect on relative performance.

Elsewhere, equity fund selection also contributed, in aggregate, helped by exposure to EM equities, via iShares MSCI EM Islamic ETF, and the strong performance of Templeton Shariah Global Equity Fund and Comgest Growth Europe Fund.

Outlook

We have retained our positive view of equities into April as we believe elevated equity valuations are offset by the ongoing stabilisation of growth in major developed market economies. Global leading indicators are also improving, contributing further to our constructive view.

US economic data has recently surprised to the upside, although inflation continues to trend downwards, despite a recent uptick, 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 moderate.

Against this background, the Fed has pushed back against market expectations of interest-rate cuts and may not lower rates until the third 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, influenced by rapidly moderating inflation and a relatively weak economy.

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 negates any possibility of rising interest rates in major developed market economies.

Against this background, we retain an optimistic outlook on US equities amid robust corporate earnings and a low risk of recession. An ongoing enthusiasm for the prospects of artificial intelligence contributes to their relative strength, notably large-cap growth stocks. Our outlook on EMs (ex-China) also remains bullish moving into April, helped by strong long-term growth opportunities, although we have trimmed exposure slightly in favour of Japan. Wage gains in Japan are outpacing inflation, boosting domestic consumption, while valuations remain attractive. Elsewhere, we remain neutral towards China, and we retain our pessimism towards the Pacific ex-Japan region given the importance of China to these economies. Our ongoing caution on European equities stems from concerns about corporate profitability, despite a stabilising eurozone economy, although we have improved our view on the region.

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 and 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. We are maintaining our overweight duration positioning, which we look to increase further, particularly as credit spreads continue to perform and provide fewer opportunities for returns.

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