FOR PROFESSIONAL CLIENTS ONLY

Informed Investor: Alpha/Beta Allocator Q1 2019

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The Alpha/Beta Allocator

6 steps to a better portfolio

1. Look back at how active managers performed in Q1 2019

After a disappointing year in 2018, active managers have bounced back to a degree, notably in fixed income.

Fixed income   Equity   Average

Q1 2019

42%

of *fixed income* managers outperformed. Emerging market debt managers were the main winners, but global bonds (EUR hedged) managers weren't far behind.

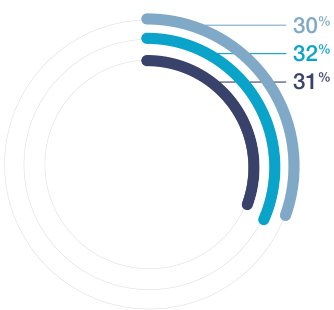
36%

of equity active managers outperformed. As in 2018, US large cap and eurozone large cap managers are still lagging behind.

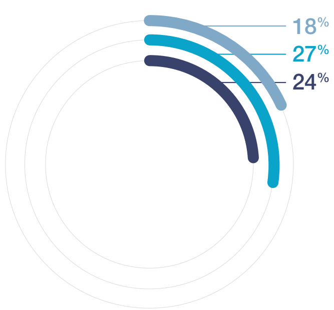
38%

of *all* active managers outperformed (vs. 24% in 2018) as the alpha/beta environment normalised.

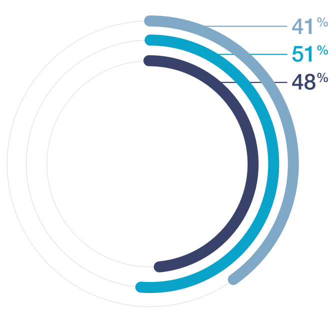
Q4 2018



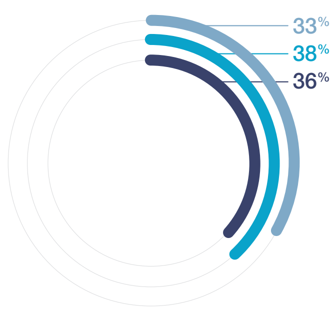
2018



2017



10Y*

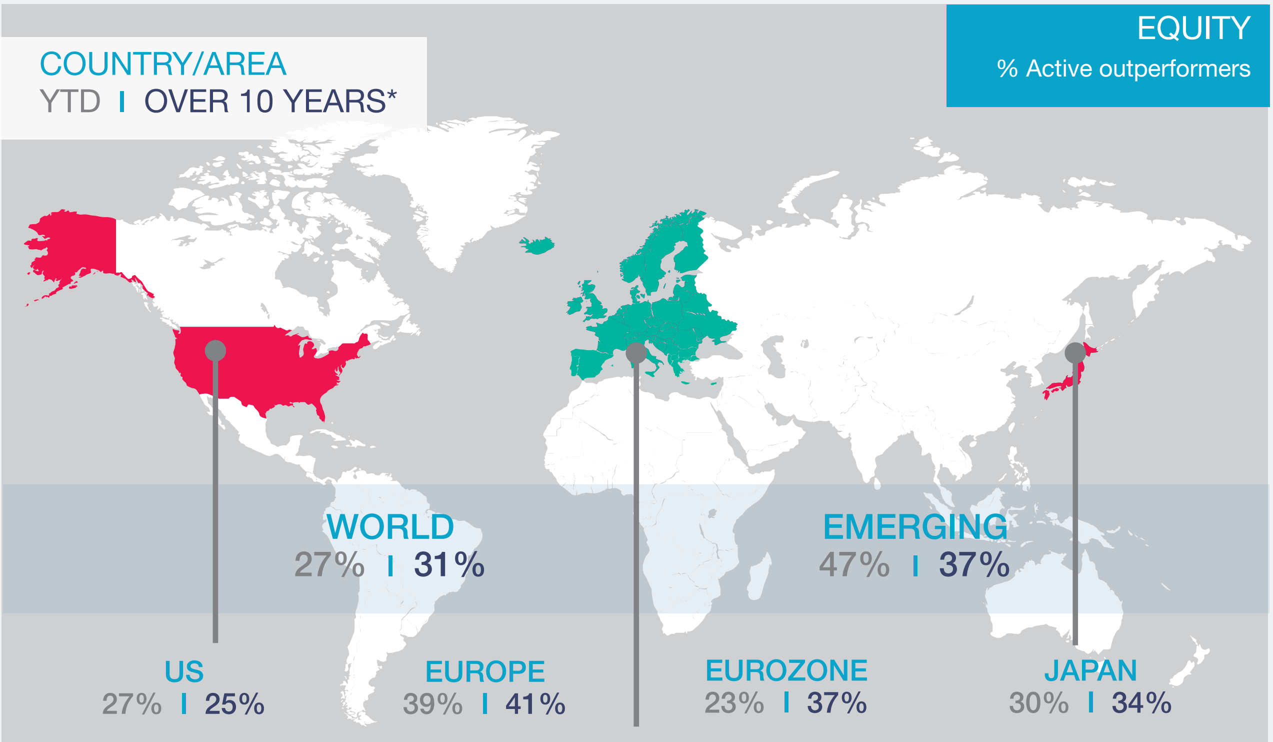


Fixed income   Equity   Average

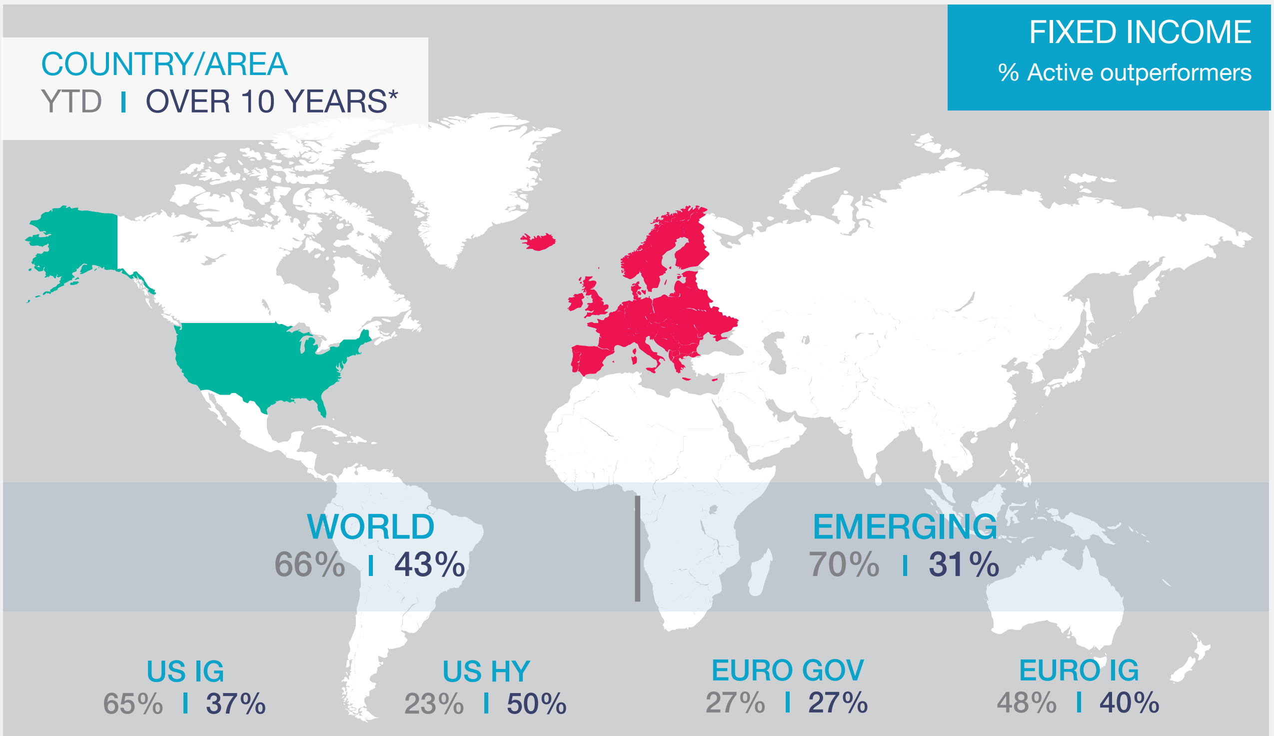
Source: Morningstar & Bloomberg, data from 31/12/2008 to 29/03/2019. Past performance is no guide to future returns. *Yearly average over the last 10Y.

2. Explore the equity and fixed income highlights for Q1

Alpha opportunities were most evident for emerging market equity managers.



After a disappointing 2018, emerging debt managers did well as did US and Europe investment-grade credit managers.



Source: Morningstar & Bloomberg, data from 31/12/2008 to 29/03/2019. *Yearly average over the last 10Y.
Past performance is no guide to future returns.

Hit Miss

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3. Q1 Analyse the full results

EQUITY

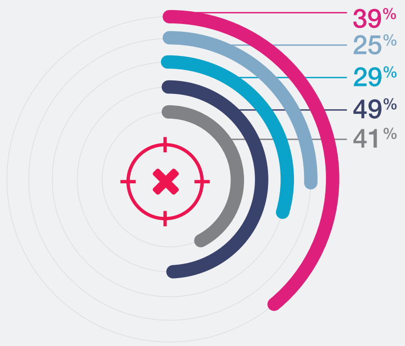
European equities (% of funds outperforming the benchmark)

The best Q1 results for active equity managers were found among emerging market equities. Support from world central banks, stimulus spending in China and receding policy uncertainties lifted sentiment and improved liquidity. Conditions were more difficult in the eurozone, US and world markets.

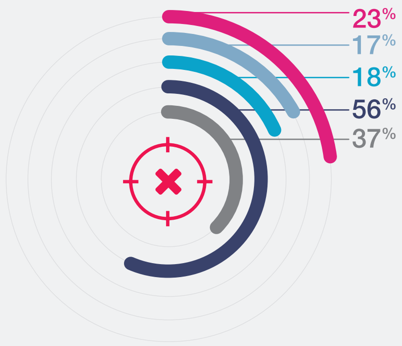
Q1 2019 | Q4 2018 | 2018 | 2017 | 10 year*

✔ Hit: when YTD results are >50% or >10yr figure
✖ Miss: when YTD results are <33% or <10yr figure

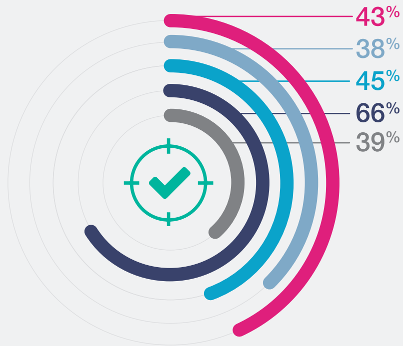
Europe Large Caps



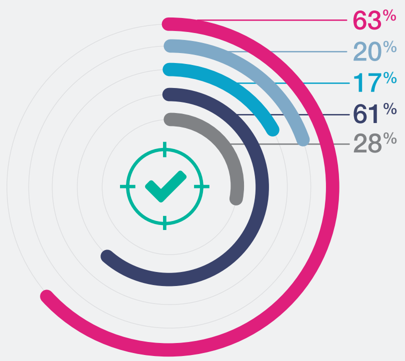
Eurozone Large Caps



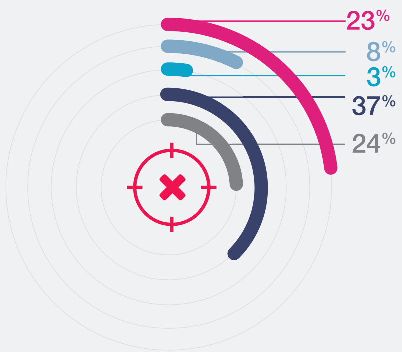
Europe Small Caps



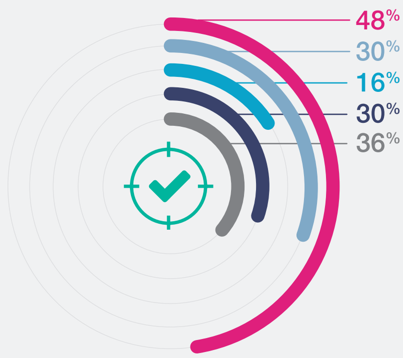
Germany Large Caps



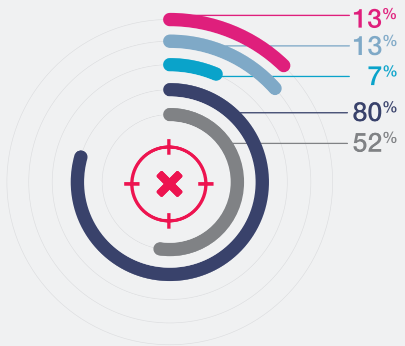
France Large Caps



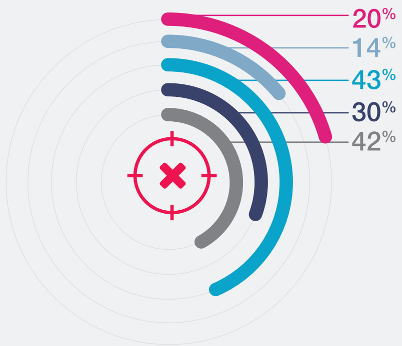
UK All Caps



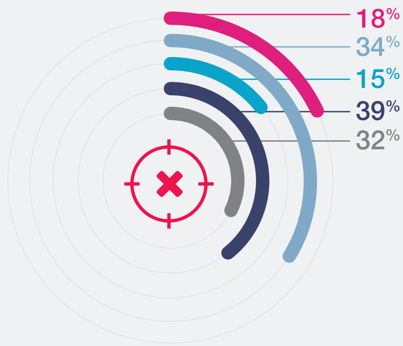
Italy Large Caps



Spain Large Caps



Switzerland Large Caps



Q1 2019 | Q4 2018 | 2018 | 2017 | 10 year*

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3. Q1 Analyse the full results
(continued)

EQUITY
Ex-European equities (% of funds outperforming the benchmark)

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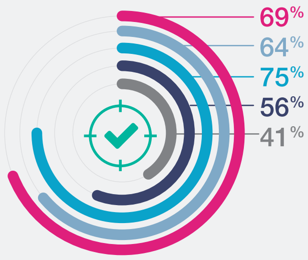
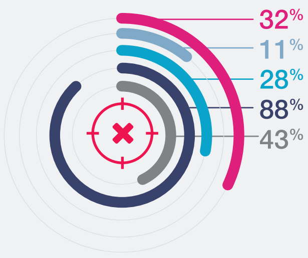
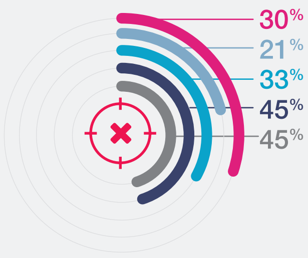
US Equity Growth



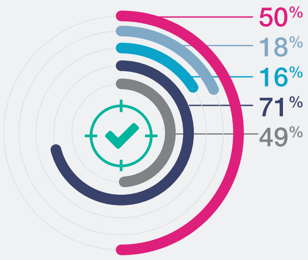
US Equity Value



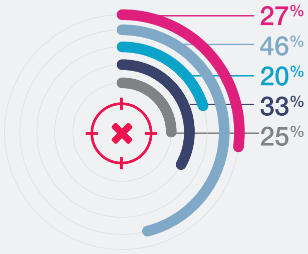
Europe Equity Growth



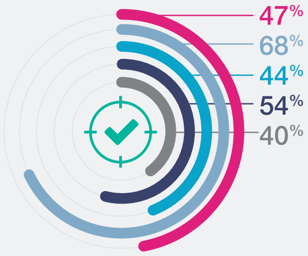
Europe Equity Value



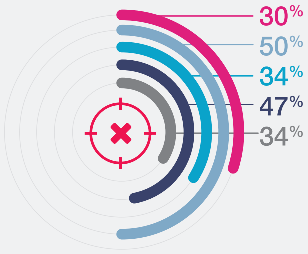
US Large Caps



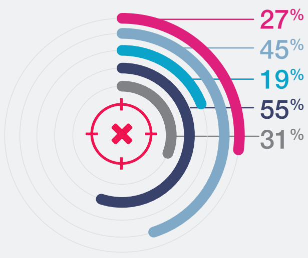
US Small Caps



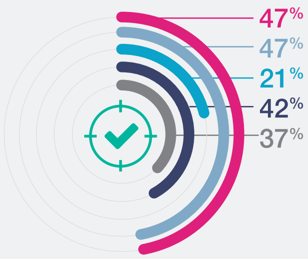
Japan All Caps



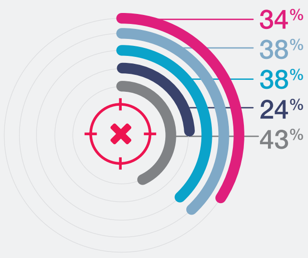
World Large Caps



Emerging Markets Large Caps



China Large Caps



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3. Q1 Analyse the full results
(continued)

FIXED INCOME
(% of funds outperforming the benchmark)

In Q1, global bond and IG managers benefited from an improvement in the credit cycle but government bond managers suffered as interest rates decreased. Emerging debt funds also experienced a very strong rebound, helped by dovish DM and EM central banks and signs of recovery in China.

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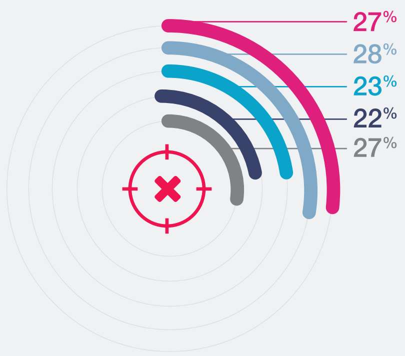
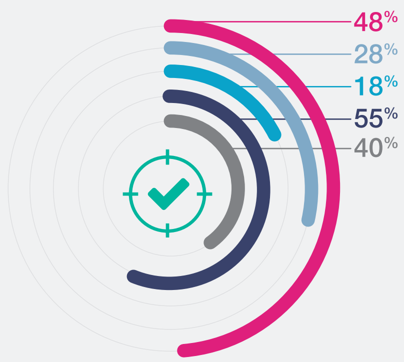
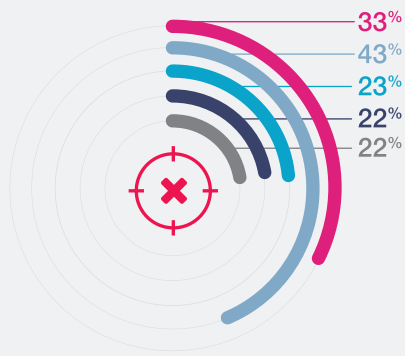
Euro Govies



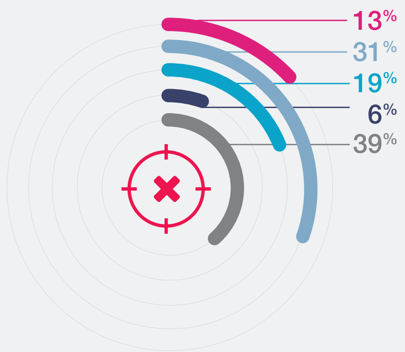
Euro Corporate



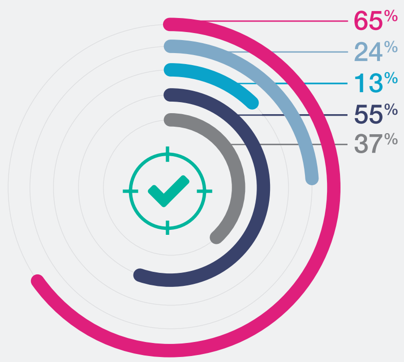
Euro High Yield



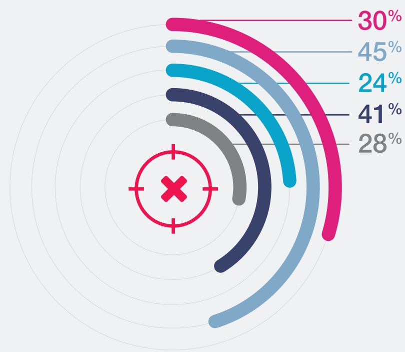
Euro Inflation Linked



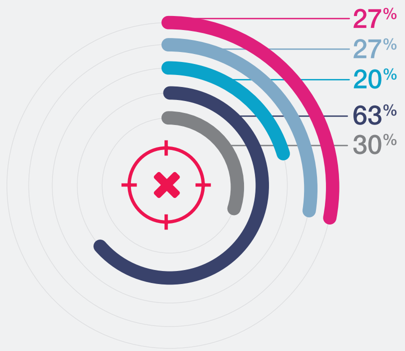
US Corporate



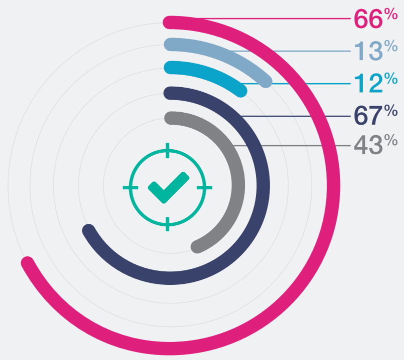
US High Yield



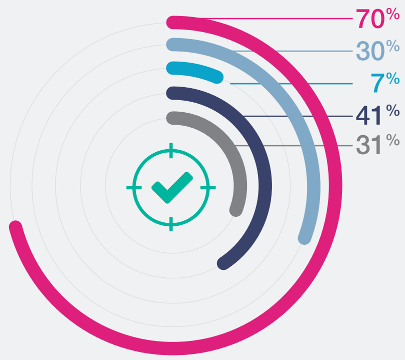
US Govies



Global Bonds - EUR HDG



Emerging Debt



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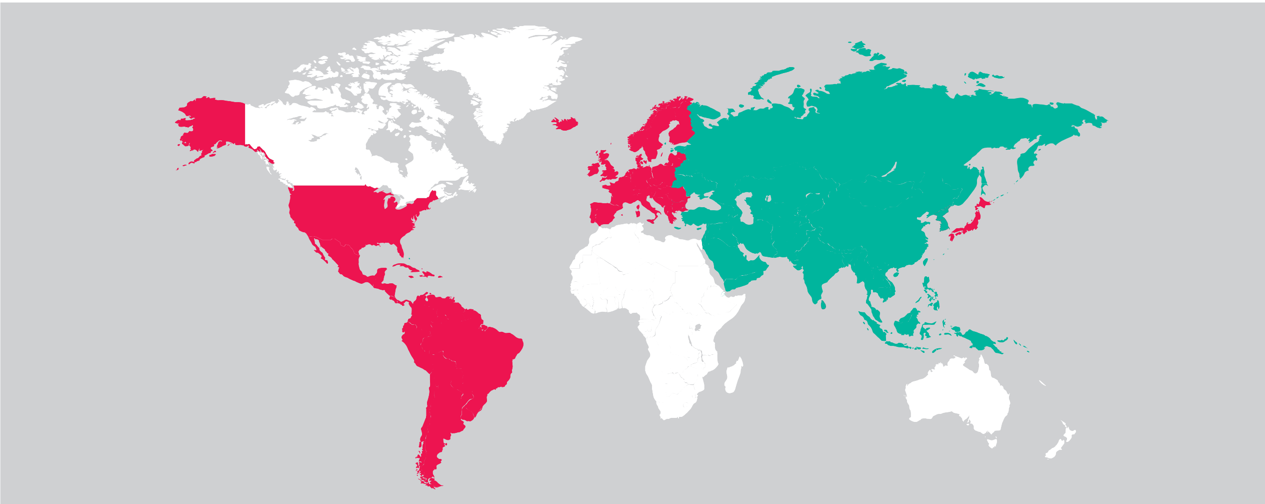
4. Read our views on where to find alpha over the next few months

Investment conditions are normalising after two polarised periods of performance in recent months. For much of Q4 last year, a trade-led slowdown was amplified by a sudden tightening in global liquidity, sending asset prices plunging and hindering both active and passive styles. Since December however, central bank support, stimulus in China and receding policy uncertainties have lifted markets and helped passive and active mutual funds to outperform. We expect less differentiation between passive and active funds this quarter. The economic and market recoveries will be relatively shallow, as each of the main drivers have limitations and are already partly priced in. This modestly positive trend should still favour passive overall. Any move towards more fundamentals-based pricing would improve alpha generation. A tilt towards active might prove opportune later this year. Whether political and policy uncertainties endure, or are resolved, will ultimately prove decisive.

Emerging Markets

While a US-China trade agreement and intensifying Chinese stimulus are broadly priced in already in emerging markets, secondary effects on capex and confidence should contribute positively. Meanwhile, dovish DM and EM central banks, benign inflation and a stabilising dollar should help EM economies and markets recover further. We are positive on the outlook for passive, but also favour those active managers who are capable of generating alpha out of very differentiated country situations. Supply chain changes in Asia, sanctions in Russia and reform implementation in Latin America all offer opportunity.

Verdict: HIT



US

The US economy is gradually converging with the rest of the world, as reflation policies fade and it feels the effects of its trading partners' weaknesses. That said, still resilient domestic data, Fed support and a bottom in earnings revisions could boost passive styles after some short-term consolidation. A move to fundamentals-based pricing, wider sector leadership, less crowded positioning, and a period of less disruptive policymaking ahead of next year's elections would help active funds. Small-cap focused managers should do well, and we also see opportunities at a sector level, where differentiation in pricing and business rationales is appealing (notably in consumer-related areas, healthcare and finance).

Verdict: MISS – except for non-mainstream active.

EU

The European economy is still impeded by its export sensitivity and member weaknesses. Political uncertainties have also had an effect and won't disappear just yet. Brexit may baffle for another six months, depriving companies and active managers of the clarity needed to make good investment decisions. Auto tariffs are a wildcard. However, a soft Brexit looks likelier and a positive surprise in Italy shouldn't be ruled out. We see some catch-up potential for passive, provided data improves more enduringly. Active managers may struggle in the mixed conditions – an absence of clarity and decisive catalysts means bolder stances will require bravery.

Verdict: MISS

Japan

We expect more of the same in Japan. A US-China trade agreement and greater access to Chinese markets would ease pressure on exporting sectors. However, distortions from a dovish Bank of Japan, greater sensitivity to movements in the yen and a lack of catalysts ahead of the VAT tax hike may constrain active managers. Those focusing on specific sectors will find limited differentiation between stocks. We favour passive styles on a relative basis, but they may also lack for compelling catalysts and positive directionality.

Verdict: MISS

Source: Source: Lyxor ETF & Cross Asset Research teams. All views & opinions as at 15 April 2019.

5. Optimise your portfolio for this environment

	US	Europe	Japan	EM Markets
Passive				
Broad	✓	✓	=	=
Countries		✗		=
Sectors	✗	✗	✗	✗
Smart Beta				
Factors	✗	=	=	
Active				
Long/Traditional	=	=	✗	=
Long/Short Hedge Funds	✓	✗	✗	✓
Countries		✗		✓
Sectors	✓	=	✗	✓

✓ Overweight ✗ Underweight = Neutral

The above marks summarize our analysis of Passive and Active environments for the next 3M. They are based on the screening of a wide set of macro-economic and market data, broken down at a regional level.

6. Choose the relevant ETFs

US

Beta at reduced cost	Beta	Sectors/Countries	Style
Core Morningstar (LCUS)	S&P 500 (SP5)	Banks (BNKU)	Russell 2000 (RU2K)

Europe

Beta at reduced cost	Beta	Theme
Core STOXX Europe 600 (MEUD)	MSCI Europe (MEU)	Min Var Europe (MVAE)

Emerging Markets

Beta at reduced cost	Beta	Sectors/Countries
MSCI EM Asia (LCAU)	MSCI Emerging Markets (LEM)	Hwabao WP MSCI China A (CNAA)

Source: Lyxor ETF & Cross Asset Research teams. All views & opinions as at 15 April 2019 unless otherwise stated.

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Conflicts of interest

This research contains the views, opinions and recommendations of Lyxor International Asset Management ("LIAM") Cross Asset and ETF research analysts and/or strategists. To the extent that this research contains trade ideas based on macro views of economic market conditions or relative value, it may differ from the fundamental Cross Asset and ETF Research opinions and recommendations contained in Cross Asset and ETF Research sector or company research reports and from the views and opinions of other departments of LIAM and its affiliates. Lyxor Cross Asset and ETF research analysts and/or strategists routinely consult with LIAM sales and portfolio management personnel regarding market information including, but not limited to, pricing, spread levels and trading activity of ETFs tracking equity, fixed income and commodity indices. Trading desks may trade, or have traded, as principal on the basis of the research analyst(s) views and reports. Lyxor has mandatory research policies and procedures that are reasonably designed to (i) ensure that purported facts in research reports are based on reliable information and (ii) to prevent improper selective or tiered dissemination of research reports. In addition, research analysts receive compensation based, in part, on the quality and accuracy of their analysis, client feedback, competitive factors and LIAM's total revenues including revenues from management fees and investment advisory fees and distribution fees.

Knowing your risk

It is important for potential investors to evaluate the general risks described below and in the fund prospectus on our website www.lyxoretf.com

Capital at risk
ETFs are tracking instruments: Their risk profile is similar to a direct investment in the Underlying index. Investors' capital is fully at risk and investors may not get back the amount originally invested.

Replication risk
The fund objectives might not be reached due to unexpected events on the underlying markets which will impact the index calculation and the efficient fund replication.

Counterparty risk
With synthetic ETFs, investors are exposed to risks resulting from the use of an OTC swap with Société Générale. In-line with UCITS guidelines, the exposure to Société Générale cannot exceed 10% of the total fund assets. Physically replicated ETFs may have counterparty risk if they use a securities lending programme.

Concentration risk
Smart Beta ETFs select stocks or bonds for their portfolio from the original benchmark index. Where selection rules are extensive, it can lead to a more concentrated portfolio where risk is spread over fewer stocks than the original benchmark.

Underlying risk
The Underlying index of a Lyxor ETF may be complex and volatile. For example, when investing in commodities, the Underlying index is calculated with reference to commodity futures contracts exposing the investor to a liquidity risk linked to costs such as cost of carry and transportation. ETFs exposed to Emerging Markets carry a greater risk of potential loss than investment in Developed Markets as they are exposed to a wide range of unpredictable Emerging Market risks.

Currency risk
ETFs may be exposed to currency risk if the ETF is denominated in a currency different to that of the Underlying index they are tracking. This means that exchange rate fluctuations could have a negative or positive effect on returns.

Liquidity risk
Liquidity is provided by registered market-makers on the respective stock exchange where the ETF is listed, including Société Générale. On exchange, liquidity may be limited as a result of a suspension in the underlying market represented by the Underlying index tracked by the ETF; a failure in the systems of one of the relevant stock exchanges, or other market-maker systems; or an abnormal trading situation or event.

Important information

DTP124264