HAU Quarterly Commentary

Q2, 2020

Market Overview

In Q1 2020, the market experienced a sharp downturn from the COVID-19 pandemic; however, the portfolio had strong positive alpha and provided downside protection. The markets have had a V-shaped recovery in Q2 2020 as global central banks added unprecedented liquidity to stabilize the markets. With this significant bounce in the market, the mandate lagged the market, but beat its style index.

The largest underperformance came from the consumer discretionary sector, where McDonald's, Ross Stores and TJX had negative stock selection effects, and an underweight of this sector led to a negative allocation effect. However, Home Depot had a positive stock selection effect. The positions in TJX and Ross Stores were sold in this quarter. The communication services sector underperformed due to negative stock selection, though the portfolio's underweight in this sector provided a positive allocation effect. Verizon and AT&T were relative performance laggards within the sector; AT&T was sold. In the industrials sector, Northrop Grumman, Waste Management, Raytheon Technologies and Republic Services were detractors to relative performance. Positions in real estate investment trusts, energy, utilities and consumer staples also lagged the benchmark for those sectors.

The outperforming sectors were financials, information technology, healthcare and materials. The underweight of the financials sector contributed a positive allocation effect; within this sector, MarketAxess Holdings had a positive stock selection effect. The overweight of information technology had a positive allocation effect, and positive stock selection effects came from the positions in Lam Research, Accenture and Broadcom. Broadcom was added to the portfolio this quarter. In the healthcare sector, Resmed and Zoetis had positive contributions to stock selection effect.

Quarter in Review

The U.S. stock market had a V-shaped strong rebound in the second quarter of 2020, leading the worldwide rally of equities. This is in part due to the optimistic expectations for a speedy recovery of the global economy and the strong commitment of support from the central banks and other policymakers for confidence and liquidity of financial markets. The U.S. Federal Reserve's Federal Open Market Committee ("FOMC") left its monetary policy stance unchanged in the latest decision from April's iteration, holding policy rate targets in the 0.00% to 0.25% range. The Fed is going to continue to do what it can to keep monetary conditions ultra-loose to help the broader economy overcome the significant shock from COVID-19 pandemic. However, global economic activity is still significantly lower than it was a few months ago. There are growing indications that conditions are improving; however, with governments around the world still working on proper ways and phases to reopen business and social activities, the answer to the question of how long it will take economic output to fully recover remains unsolved. The risk of a second wave of COVID-19, the U.S. presidential election and increasing U.S.-China political tensions would add fuel to market uncertainties. As a result, there is high probability that higher than normal market volatility may continue throughout the rest of the year.

At the beginning of 2020, we called for increased volatility and, based on our models, we had reduced risk and exited holdings that have higher cash flow variability and cyclical sensitivity. The machine learning Dividend Cut Probability aggregated at the sector level created further separation between the cyclical and defensive sectors. With the outbreak of the COVID-19 crisis, the markets plummeted in Q1 2020 and the CBOE Volatility Index ("the VIX") traded near its all-time highs. HAU owns high-quality global companies with strong fundamentals, visible cash flows and sustainable growing dividends, and historically tends to outperform when market volatility rises. In the past, HAU's alpha is positively correlated to the VIX.

HAU Quarterly Commentary

Q2, 2020

Yield for yield's sake can be dangerous in the market as many companies will not have the cash flow to pay dividends and will be forced to cut. We focus on high-quality companies with strong fundamentals, visible cash flows and sustainable growing dividends. We continue to stay disciplined and believe exposing our portfolios to those holdings with greater earnings and cash flow visibility — plus a sustained growth in dividends and a low probability of dividend cuts — is critical for income-oriented mandates.

In Q2 2020, we reduced our weights in some of the defensive sectors and increased our weight in the information technology and healthcare sectors, purchasing stocks with strong long-term dividend and earnings growth profiles.

We reduced some of our overweights in the more defensive sectors, selling AT&T, Colgate-Palmolive, Dominion Energy, Public Service,and Excelon Corporation. With low forecasted interest rates for the future, we do not see a strong growth trajectory for these stocks, and therefore, we have sold them to enter stocks with stronger longer-term dividend and earnings growth trajectories. Walmart and Ross Stores were also sold. TJX was sold as the worry of a dividend cut or suspension increased. After it was sold, TJX did suspend its dividend.

We increased our weight in the information technology sector, purchasing Broadcom and Skyworks Solutions. In the healthcare sector, Resmed and UnitedHealth Group were also purchased. These stocks generate strong, secular runways of cash flow that maintain visibility, which support the future dividend growth aspects of these companies. Crown Castle and Oneok were also purchased.

As of April 23, 2020, 111 U.S. companies have cut their dividends and the Global Dividend mandate has avoided owning stocks that cut their dividends.

Market Overview:

In the second quarter of 2020, equities outperformed other asset classes. The S&P 500 had an unprecedented V-shaped rebound throughout the quarter with a 20.5% return, significantly outpacing Bloomberg Barclay's U.S. Aggregate Total Return Index, which was up 2.9%. However, YTD, stocks still underperformed bonds due to the market shock in Q1 2020; the S&P 500 was down -3.1%, while Bloomberg Barclay's U.S. Aggregate Total Return Index had a 6.1% return. In Q2 2020, the NASDAQ Composite was the leading index in major U.S. equity indices during the market-wide rebound, jumping 30.6% in the quarter and experiencing a 12.1% return YTD. For the S&P 500 index, consumer discretionary, information technology and energy were the best performing sectors for this quarter, while information technology, consumer discretionary and communication services were the top three sectors YTD. Overall, the US stock markets outperformed international equities as, in USD terms, the MSCI World Index, MSCI EAFE Index and the MSCI Emerging Markets index all trailed the S&P 500 and the NASDAQ Composite in Q2 2020 and YTD.

Geographically, for the MSCI All Country World Index (USD), all regions across the globe had double-digit returns in Q2 2020 as markets bounced back. Latin America, Africa and the Middle East and North America were the best-performing regions. As for YTD performance, North America outperformed all other regions; however, no region posted positive returns due to the worldwide market shock in Q1 triggered by the outbreak of the COVID-19 pandemic.

HORIZONS ETFs by Mirae Asset