H1’2020 Results Season Market Commentary:
Key Themes from an Investor’s Perspective

Being two weeks into the H1’2020 reporting season, we would like to point to some of the major themes of investor interest for those companies preparing to report over the next 3-4 weeks.

While we follow about 40-50 companies across different industries each quarter, which vary greatly by size of free float adjusted market cap and geographic exposure, the Covid-19 outbreak has put every company into crisis management with very different levels of structural and operational adjustment. Whereas professional fund managers might have looked at the „winners and losers“ of the pandemic at an early stage, we now observe conceptually very different enquiries, which go at the very heart of each company’s business model and investment proposition. Many of those who have just reported their H1’2020 results have already announced major investor events later this year in order to address some of investor concerns in greater detail.

The aim of this brief market commentary is to focus on 4-5 major themes of current investor interest, which were frequently discussed in Q&A in recent weeks. At the same time, we scrutinise management’s reaction to those enquiries and propose a balanced and long-term approach to manage market expectations against a backdrop of a potentially long, persistent and severe pandemic over the next few months that may extend well into 2021. The Appendix includes four relevant slides to add some colour on the depth of the current debate and to provide some „best practice“ examples: three from Swiss companies and one from NN Groep at their Capital Markets Day on 24 June 2020, arguably under the pressure of the activist campaign from Elliott.

RESILIENCE VS CHANGE & ADAPTATION
Whereas the major theme of the Q1’2020 results season was to show resilience against the impact of Covid-19, there is now a much greater focus among reporting companies on what has changed, both structurally and operationally, and to what extent corporates have not only adjusted to the new environment, but also essentially accelerated their digital product offering, production automation and/or workforce management. While some might have run ahead of themselves by discussing a „post-Covid world“, we would certainly advise to take a long-term stance in outlining business cycles, capital allocation and investment processes – and this without necessarily following excessive enthusiasm of the V-shaped recovery in the global stock markets, which has so far been largely liquidity-driven and fuelled by economic rescue packages from governments and central banks as well as by some excessive risk-taking by retail investors. The discussion on change and adaptation includes regional sales analyses and global portfolio reviews as shown in the Appendix.

COST SAVINGS AND CUSTOMER BEHAVIOUR
Two other themes go closely hand-in-hand, as professional fund managers are trying to get a feel for incremental cost savings through Covid-19 and to what extent this was demand-driven by changing customer behaviour, i.e. whether this has forced companies to accelerate the existing cost measures and introduce structural step changes going forward. Over the last few days there were repeated questions about „funnels“ in the forward order book, described by one analyst as „orders’ air pocket“, which hugely adds to business uncertainty. At the same time, there is great investor

interest in temporary vs sustainable cost savings through Covid-19 measures, which most companies have so far not been able and/or willing to quantify. Clearly, there is a broad consensus that some of the discretionary spending might become permanent, notably travel but also trade shows, business entertainment and office occupation.

One thought on capex revision as a part of the updated guidance. We have followed a number of companies who had announced in recent days a capex reduction by 20-25% in 2020, without explaining how much of it was „committed“ and „uncommitted“, i.e. what could be easily pushed into 2021. This was a classic pitfall, which left investors guessing a) how management possibly arrived at this new capex number; and b) how serious this cost exercise really was if a large chunk of capex has been „uncommitted“ so far. What is also striking is that hardly any company has shown cost savings from low fuel prices and other raw material inputs given the collapse of the global oil prices earlier this year.

GUIDANCE UNDER FX IMPACT & TAX SITUATION

While most companies opted for suspension of their 2020 guidance after the outbreak of the corona pandemic, we have seen various upgrades in the wake of the economic recovery in June-July 2020, ranging from global logistics to semiconductor businesses, but mostly a cautious reinstatement of previously existing guidance metrics. The latter included, among others, short quarterly updates to the full-year 2020 guidance and beyond, as well as regional and specific segmental guidance. However, we haven't seen much of an adjustment for the significant exchange rate changes in recent weeks, notably with respect to the low US-dollar against an increasingly strong Swiss franc and Japanese yen, but also euro and pound sterling. In our view, any meaningful guidance should include a sensitivity analysis of major currency movements, as we show in the example of Roche in the Appendix. Clearly, most treasury departments have nowadays sophisticated FX models and currency hedging strategies, which should be a part of any fair and balanced outlook policy.

On a separate note, the tax issue has frequently come up as a new evolving theme when updating company guidance, given all the preferential tax treatments in various jurisdictions, short-term work schemes and also simply tax postponements. Although most of the companies we have recently followed provided an outlook on their tax position as a part of the 2020 guidance, we would expect a greater investor interest, both in the wake of the growing ESG investor campaign against offshore tax havens and the recent EU sanctions against large US technology companies.

SECOND WAVE OF THE PANDEMIC

While we had followed close to 50 analyst calls during the Q1'2020 season, only one of them (Deutsche Post DHL) specifically outlined how they get prepared for a second wave of the corona pandemic, possibly in the autumn in conjunction with the next flu season. This was not only fascinating in terms of professional thought leadership, but also got strategically embedded in the company's new guidance published on 7 July 2020, essentially outlining three different scenarios. Again, most of the companies who have reported their H1'2020 results so far tried to avoid a specific answer – pointing to speculation or not having the „crystal ball“ – but we would expect professional fund managers to become more insisting following a dramatic increase in infection rates world-wide in recent days.

With everything we have emphasised so far, the natural conclusion is to opt for a well-balanced and long-term approach, which admits the magnitude of business disruption and seriousness of health threats but, at the same time, outlines change and adaptability of the business model and, most importantly, highlights to what extent management can rely on employees' support, motivation and flexibility.

Peter Kirkow
28 July 2020

APPENDIX

Adapting and accelerating the pace of change

Building on our strengths and momentum in a rapidly evolving environment

Digital client experience and enhanced product offering

- Digital delivery and front-end client solutions
- Client access and interaction
- Enhanced sustainable investing offering

Automation and technology enablement

- Cloud migration
- Remote working collaboration capabilities
- Automation to gain efficiency

Workforce management and real estate footprint

- Flexible working
- Digital journey across employee lifecycle
- Optimization of our real estate footprint

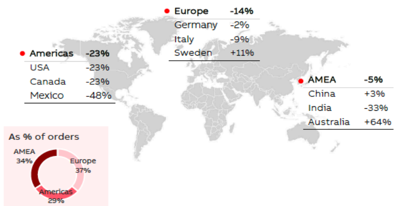
UBS

Q2 2020 orders

Americas strongly impacted by COVID-19

Order development yoy

Growth by region and largest 3 country markets in $ terms



Americas	**-23%**
USA	-23%
Canada	-23%
Mexico	-48%
Europe	**-14%**
Germany	-2%
Italy	-9%
Sweden	+11%
AMEA	**-5%**
China	+3%
India	-33%
Australia	+64%

All data presented on a yoy comparable basis; all growth comments refer to comparable growth trends
AMEA = Asia, Middle East and Africa, EL = Electrification, IA = Industrial Automation, MO = Motion, RA = Robotics & Discrete Automation. BA = Business Area

Americas

Steep drop as pandemic escalated in all BAs

USA: material decline in EL, severe decline in MO, IA, RA

Europe

Material decline

Germany: MO strong, EL subdued, steep drop in RA, IA

AMEA

Strong result in MO outweighed by weak EL, IA and RA

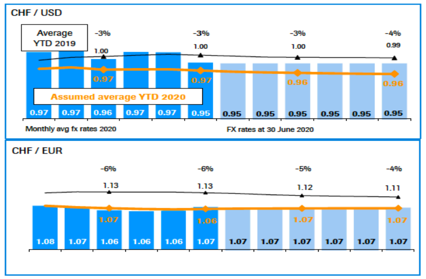
China: moderate growth led by strong MO, EL robust, RA subdued, IA impacted more materially

Slide 7

ABB

High currency impact expected in 2020

Roche



Assuming the 30 June 2020 exchange rates remain stable until end of 2020, 2020 impact [1] is expected to be (%p):

	Q1	HY	Sep YTD	FY
Sales	-5	-5	-5	-5
Core operating profit		-7		-7
Core EPS		-8		-8

[1] On group growth rates

Thorough assessment of individual businesses

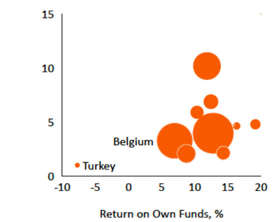
- Regular and thorough assessment of individual businesses at both the business unit and market level, including strategic coherence and right-owner concept

Business unit performance
- Return on Own Funds
- New business profitability
- Net remittances
- Market position

Market attractiveness
- Market growth
- Market size
- Market wealth
- Country risk

Considerations
- Contribution to Group results
- Scale to compete
- Market dynamics
- Distribution strength, bancassurance agreements
- Ability to act
- Conviction to succeed

International business units Return on Own Funds to VNB profit margin[1]



1. Return on Own Funds reflects the 2019 i) Own Funds operating capital generation divided by average Basic Own Funds excluding transitional measures for Solvency II entities, ii) divided by SCR at 150% for Greece, iii) net local GAAP result divided by local GAAP equity for Turkey Life and pension funds; iv) Japan included on an equivalence basis; VNB profit margin defined as 2019 Value of new business as a percentage of the Present value of new business premiums; bubble size reflects the denominator in the return calculations

NN

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