Monthly Portfolio Update

*Amundi Funds II – Euroland Equity**
31 July 2018

EQUITY COMMENTARY

Market Review

July was a positive month for the European equity market with the MSCI Europe adding over 3%. Looking at sector level, the recovery we saw in July was broad based with all 11 sectors in positive territory. Healthcare, Industrials, and Consumer Staples were among the top performers, while Energy and Real Estate lagged.

Trade continued to dominate the news headlines, with fears that growing tensions between the U.S. and the rest of the world would lead to sluggish investment and slower export growth. Some of the risks have diminished in recent weeks after U.S. President Trump and European Commission President, Jean-Claude Junker agreed a deal to stave off the impending trade dispute with Europe. This, combined with more favourable FX, better inflation and employment numbers helped to boost sentiment towards the asset class in July.

Perhaps worthy of the most attention was of course the Q2 earnings season for European companies which began in July. As we have been flagging in recent communications, for us earnings delivery remains the key to drive further upside from here. The latest results season (which is around 40% complete at the time of writing) has so far delivered mixed results. Looking across sectors, Consumer Staples and Industrials have enjoyed the broadest beats, while Energy and Consumer Discretionary have fallen short of consensus at this point. However, while earnings have been a little lacklustre to date, we are particularly encouraged by the strong revenue growth being delivered, with top line growth tracking above 6% on a weighted basis which should help to support sentiment towards the asset class.

With periods of volatility and market rotations likely to become more prevalent than we have observed in recent years, we continue to seek balance. Our view remains that the best way to navigate these market conditions is by focusing on compelling idiosyncratic investment cases that we believe have the ability to deliver on EPS over the medium-term.

Portfolio Review

The Portfolio underperformed its benchmark, the MSCI EMU, in July. At sector level, Telecommunication Services and Consumer Staples made a positive contribution. In contrast, some of our holdings within Industrials and Energy detracted.

Within Telecommunication Services, our holding of the Dutch telephone and internet services company Koninklijke KPN performed well. The positive performance was on the back of better than expected Q2 results, with adjusted EBITDA climbing 1.3% and improved numbers from its IT services, cloud and workspace segments. In addition, our holding of the integrated telecommunications operator Deutsche Telekom also contributed in July. News that the German Mobile market is performing strongly, combined with news that its U.S. deal with Spirt is not experiencing a high level of resistance, so far, from regulators, created some positive sentiment towards the name this month.

The Portfolio lost ground within Industrials. Of our holdings, the low-fare passenger airline Ryanair was the main detractor. Ryanair numbers Q1 2019 were in-line with consensus. However, the main negative for the earnings was the softer yield guidance for Q2. This has been moved lower to recognise the impact of strikes and disruption on revenue yields. When passengers are affected by disruptions, the airline tends to reallocate more of its late purchase seats to disrupted passengers rather than being able to sell these potentially lucrative seats. This reduces late booking yields, dragging down the overall pricing. This, combined with on-going news of strike action, created negative sentiment towards the name over the month. Our holding in the French based electric company, Schneider Electric, also detracted following a mixed set of results. The negative sentiment was as result of disappointment on the price/cost spread and the 1% below consensus expectations for EBITA. We did take some reassurance from the Q2 growth numbers in addition to the supportive commentary around the demand outlook, we continue to hold the name.

In Consumer Staples, our holding of dairy and waters company Danone performed quite strongly. At the end of the month, the company reported a set of quite solid underlying H1 results. Despite the headwind from the consumer boycott in Morocco and the strikes in Brazil, the company delivered a 7.9% rise in first half profit, helped by strong cost control across the group which was well received by investors.

The Portfolio lost some marginal performance within Energy as the sector paused for breath after a very strong run in recent months. Of our holdings, Royal Dutch Shell underperformed, the company had a mixed set of results. Shell announced the start of its $25bln buyback programme with an initial buyback target of $8bln starting straight away, which is a positive in our view. On the other side, operating expenses were up 5% Y.O.Y., which was disappointing, given the company's focus on taking out costs. The mixed results combined with a competitor releasing more positive news, weighed on sentiment towards Shell in July.

Finally, Consumer Discretionary was a source of positive returns in July. At stock level, our holding of automaker Volkswagen delivered strong performance. During the month, the company reported a strong set of Q2 results, comfortably exceeding expectations, with solid performance across divisions. Management affirmed its full year guidance which was well received, especially given the ongoing regulatory changes within the auto industry.

Sector Allocation	**Portfolio Weight**	**Benchmark Weight**	**Delta**
Energy	7.02%	6.00%	1.02%
Materials	8.68%	8.97%	-0.28%
Industrials	19.49%	14.72%	4.77%
Consumer Discretionary	12.08%	13.73%	-1.65%
Consumer Staples	9.17%	9.90%	-0.73%
Health Care	12.83%	8.26%	4.56%
Financials	15.58%	18.39%	-2.81%
Information Technology	7.14%	9.25%	-2.11%
Telecommunication Services	6.03%	3.60%	2.43%
Utilities	1.97%	5.24%	-3.27%

Source: Amundi Asset Management as at 31 July 2018.

Portfolio Strategy

In our view, bottom-up stock selection is a key driver of Portfolio performance and excess return. We seek to invest in high-quality, undervalued companies with strong fundamentals.

The majority of positions we hold are long-term 'Core' holdings. These companies are characterised by high quality, attractive valuations and strong growth potential, with a medium-term investment horizon.

The remainder of our Portfolio is built using an unconstrained 'Opportunistic' approach, giving us the opportunity to take advantage of different market trends; and enabling us to invest across the market cap spectrum, looking beyond the benchmark for attractive investment opportunities.

Top 10 Overweights	**Portfolio Weight**	**Bench mark Weight**	**Delta**
PRUDENTIAL PLC	2.77%		2.77%
DANONE	3.70%	0.98%	2.72%
DEUTSCHE TELEKOM AG	3.70%	1.14%	2.57%
KERRY GROUP PLC	2.89%	0.35%	2.55%
CRH PLC	3.09%	0.59%	2.50%
AKZO NOBEL NV	2.90%	0.48%	2.42%
CARNIVAL CORP	2.41%		2.41%
BBVA	3.42%	1.01%	2.40%
BAYER AG	4.47%	2.07%	2.40%
VOLKSWAGEN AG	3.20%	0.80%	2.40%

Source: Amundi Asset Management as at 31 July 2018.

Outlook

Looking to the second half of the year, we remain constructive on our outlook for European equities. That said, in our opinion, political uncertainty and more muted economic expansion warrant a less bullish outlook when compared to our view as we entered the year.

We maintain our view that earnings growth should be the key catalyst to drive the market higher. One important positive supporting this view is that the recent FX headwinds for earnings may switch to a tailwind in the second half of the year. Additionally, we view the recent positive developments in the trade discussions between Europe and the US as a support for sentiment, albeit that the market requires to see the details before this risk evaporates. For us, perhaps now more than ever, we believe that a strong focus on those companies with the ability to deliver reliable earnings through the cycle, which will be the key to delivering alpha in this environment. With the prospects of rising volatility and ongoing sectoral rotations, we continue to seek balance within the portfolios with no significant sectoral or regional exposures. As fundamental bottom up stock pickers with a medium-term view, we continue to monitor the current situation, seeking to take advantage of valuation opportunities should they arise.

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