

Value Bonds 2018 - 50/50

FIXED INCOME

Positive credit markets despite negative headlines in Europe

July was tough on Europe

Markets Just over a month has passed since Brexit and besides some short-term volatility, markets adapted quickly to the new situation and many UK assets have resumed same price levels as before the referendum.

Unfortunately, negative headlines continued to come out in Europe throughout July, first with the attempted coup in Turkey, then numerous terrorist attacks in France and Germany while the lack of large negative surprises in the European Bank stress test provided some short term support for subordinated bank paper.

Although the coup in Turkey was suppressed the subsequent events, among others Prime Minister Erdogan's declaration of state of emergency resulted in declining Turkish assets prices and eventually a downgrade of the country by the rating agencies. There is no doubt that the EU accession process for Turkey - and others in the region - is left very challenged.

Oil prices was also affected by the events as majority of Middle Eastern production is transported via pipelines and shipped from Turkish ports. Along with an unexpected rise in US inventory oil dropped to the lowest level in 3 months.

Despite the many attempts to disturb world-order, spreads in general continued to tighten in July. A strong US economy, chatter about "helicopter" money in Japan and the ECBs aggressive buy-back program were the main drivers of performance.

Positive performance across sectors

Performance The fund delivered a satisfactory positive return in July. Consumer discretionary was the best performing sector in the portfolio followed by financials. Utilities and information technology were the two worst performing sectors. All sectors contributed positively to the return of the fund in July.

The best performing position in the portfolio in July was a US consumer company that provides automated retail solutions. The shareholders of the company received a buyout offer from a capital fund. The shareholders are offered a 11% premium to the share price before the announcement. If the deal goes through (we expect that) the bondholders have a change-of-control option to redeem the bonds at an attractive price compared to the price before the buyout offer was announced. Furthermore, the company posted far better than expected Q2 results which will support the bond if the deal does not go through. Another strong performing position was a UK education company that rebounded after the negative performance from "Brexit" last month.

The worst performing position in July was an oil service company. The oil price fell from 50\$ to 43\$ during July which is the main reason why this position performed slightly negative. Another weak performing position was a Kurdish oil producer.

No major changes

Portfolio Changes During July the team reduced one position slightly. No new positions were added to the portfolio and no positions were called or sold completely during July.

Strategy

The strategy aims to provide a positive absolute return on a mid-term horizon by investing in short-dated corporate bonds. The selection process is based on in-house bottom-up research with focus on companies with strong cash flow. Our approach also makes it possible to exploit market premiums from less liquid issues and out of favour situations.

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