

Emerging Markets Corporate Value Bonds

FIXED INCOME

Still good performance, but...

Tightening conditions in May

Markets In March and April the market did not expect the US central bank to tighten monetary policy in the near future. Together with news from China that the politicians are doing what they can to secure a soft landing and higher commodity prices, Emerging Market assets did very well. The FED has been talking about a hike in rates for several years now, and in May they once again assured the markets that they intend to hike rates two times in 2016. News from the US labour market is still very good, but news from other parts of the economy – e.g. growth and inflation – are still unconvincing, but enough for the US central bank to remind the markets that they should expect a rate hike soon. Let's see if they can deliver on the promises. We have seen before that the FED is warning about what's about to happen and then ... nothing. Hence, in May, the market "played ball" and reconsidered the probability of a rate hike by the US central bank in the near future. Market rates increased and as a result, the dollar also rose.

Renewed concern about the state of the Chinese economy surfaced in May as a couple of bad economic indicators were released. For months, markets have been trying to figure out if the expansionary policies put in place to restore faith in the Chinese economy is working or not. The Chinese policy makers have increased credit growth and as a result debt levels in China have been on the rise – from already high levels. Concerns about the sustainability of the current Chinese policies were raised in May and not only by the market, but also now by insiders in the Chinese government. As a result of China concerns, rising US rates and a stronger dollar, commodities like gold, silver and copper dropped substantially in May. Because of supply concerns, oil had another great month and is now in the high 40s.

Positive performance

Performance The benchmark generated positive total returns in May, despite the headwinds mentioned above. As a result of a fall in the price of base metals, the underperforming sector was mining companies. On a regional basis, the outperforming region was Asia and Eastern Europe and the underperforming region was Latin America.

The fund has a slight overweight to mining related companies, but since that overweight is expressed via primarily Eastern European companies, the fund managed to outperform in May versus the benchmark. Overall, the fund was well positioned in May with an underweight to Latin American credits and at the same time an overweight to Eastern European credits. In particular, the fund is overweight Russian and Ukraine credits, regions that did well in May. Maturity wise, the fund was well positioned with a low duration, since in May it was indeed short maturity credits that outperformed longer maturity credits.

Best performing credit was a company with base in Brazil producing poultry and beef products for the domestic and US market. The company issued a new 7-year bond, but at the same time offered to buy back shorter term paper on favourable prices which resulted in good performance. Worst performing credit was a Brazilian nickel mining company.

Reducing risk

Portfolio Changes We continued to reduce risk in select names and buy financial credits.

Strategy

The strategy focuses on companies with strong or improving underlying credit fundamentals and good growth prospects, across the entire rating universe. It also aims to limit concentration risk by diversifying across countries, industries and issuers. The strategy combines top down macro-economic research with bottom-up fundamental credit and country analysis.