Rates are on the up

The first quarter of 2017 was a very strong quarter for credit investors. As seen in the table below, all our credit products performed well and so did Emerging Market Debt. With the exception of market weakness in March, which again turned out to be a dip to buy, markets were strong. Our global strategies were flat to slightly ahead of their benchmarks and our emerging market strategies lagged their benchmarks. For more details, please see our monthly commentary on the specific funds.

Q1 2017 Performance

- gross, quarterly, main funds only

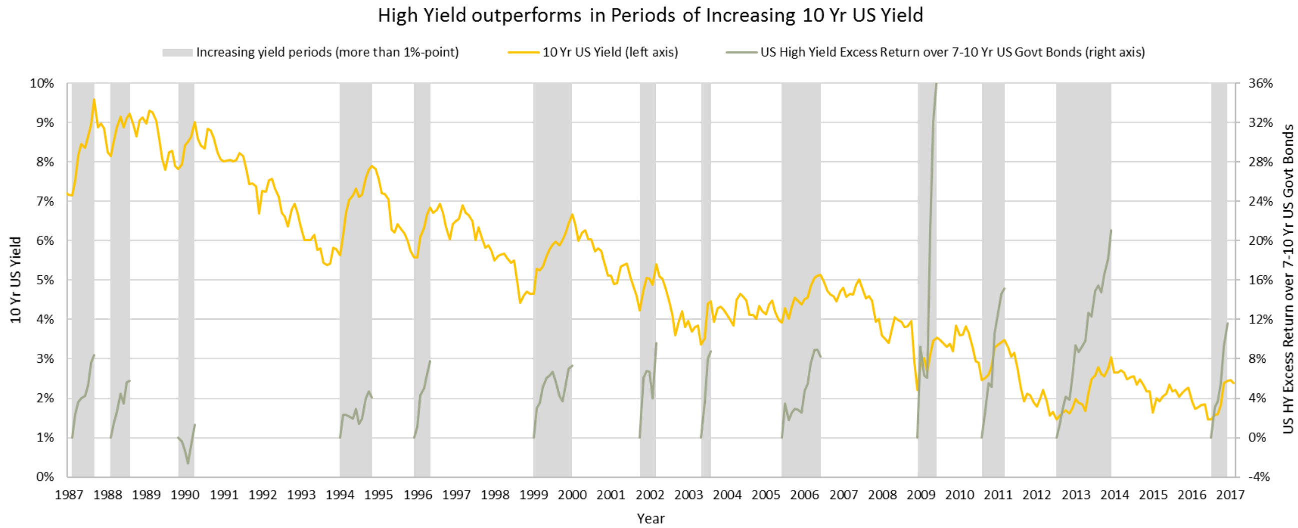
Strategy	Danish Fund	UCITS Fund	Benchmark	Comments
Global High Yield	2.5%	2.7%	2.5%	UCITS is ethical
Global Investment Grade	1.1%	0.9%	0.9%	Danish fund has a target duration of 3.0
Emerging Market Corporates	2.3%	2.2%	2.6%	
Emerging Market Debt Hard Currency	2.9%		3.4%	

Rising rates on the menu

Global trade, Trump's policies and interest rates have been the main macro headlines driving our markets in Q1 2017. The Dutch election and French election expectations have eased markets fear of a collapse of the European Union. After years of falling rates and negative rates, we are now in an environment where the talk is of the timing and steepness of rising rates. Even in Europe, we have had hints of a potential rate increase before ECB quantitative easing (QE) rolls off.

> *Global trade, Trump's policies and interest rates have been the main macro headlines driving our markets*

On that note, we have looked at the performance of High Yield in periods where interest rates rose over the last 30 years. In order to capture more data points we have focused on US High Yield and periods where 10-year treasuries have increased by more than 1%. On top of that we have plotted the excess performance of High Yield over treasuries. High Yield gave investors positive returns in all but two of these 13 periods and it suggests that High Yield is not the worst place to be if you are concerned over rate increases.

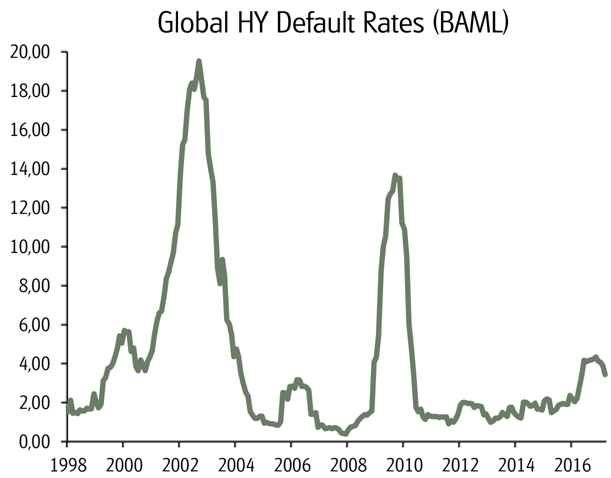


Source: Bloomberg, Merrill Lynch, Sparinvest, March 2017

The outperformance to treasuries can be explained by lower duration and spreads compressing as they benefit from positive economic environment that is associated with rising rates. Despite spreads being at historically tight levels, we have already seen such behavior with each "taper tantrum" correction in rates, where we saw long dated corporate bonds outperform government bonds.

Defaults remain benign further supporting the case for staying with High Yield. The recent spike in 2016 defaults seen is due defaults across Energy issuers.

Defaults remain benign further supporting the case for staying with High Yield



Source: Merrill Lynch, March 2017

So the question is what are the risks for High Yield investors in this environment? As with all risk asset classes, QE and resulting grab for yield has compressed spreads so performance will be coming primarily from coupons as opposed to further spread compression. Further, High Yield is a relatively illiquid asset class with high trading costs. With the rise of ETFs in the High Yield space their flows have increasing impact on market liquidity. Simply put, trading on the opposite side of such flows allows us to reduce trading costs. This is not always possible but we now have our own tools following these closely.

High Yield is a relatively illiquid asset class with high trading costs

In response to the continued discussions surrounding rate increases, in June we are launching our Short Dated High Yield fund in Luxembourg, which will focus on bonds shorter than 5 years to maturity and with limited exposure to perpetuals and lower rated bonds. A similar fund for Danish investors will follow. These new vehicles will be an attractive proposition also for our existing maturity fund investors which have been performing extremely well over the first quarter of 2017.

In June, we are launching our Short Dated High Yield fund in Luxembourg

In this quarterly report we have focused on High Yield, but for those interested, please reach out to your sales representative to receive a copy of presentation which includes performance of investment grade and emerging market product at times of rising rates.

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