STRATEGY UPDATE

22/02/18

MIRABAUD – CONVERTIBLE BONDS GLOBAL

FACTS

Since the end of January, equity market volatility has picked up sharply, with big declines followed by marked rebounds. All in, between their peak in late January and February 21st, equity benchmark indices remained in negative territory: -5.97% for the S&P 500, -5.39% for the DJ Stoxx 600 and -8.93% for the Nikkei 225.

As of February 21th, the Mirabaud – Convertible Bonds Global Fund is up +0.42% YTD and down -0.34% MTD.

SHORT TERM VIEW

Just because the economic expansion is maturing doesn’t mean that convertible bonds should falter. Our expectation for 2018 is that global equities will encounter rising volatility and several corrections in the range of 5% to 10%. We believe that the market has begun a broad congestion phase, but could end the year with a single digit gain.

The reason behind this cautious near term view is inflation, which could start to rise more quickly than currently expected by the markets and would increase the odds that the FOMC's dots for the year rise from three to four hikes.

In that context, we could see the return of a positive correlation between stocks and bonds while credit spreads would widen in tandem with rising volatility.

RECENT ACTIVITY

With this scenario in mind, as active manager, we have bought several convertible bonds in the selloff that have been hit hard in the wake of a strong correction of their underlying shares. We swiftly were proved right as some profiles have bounced back sharply since.

As we expect the rebound not to last and a second down leg to follow that could make the same percentage drop as the initial weakness, we have already sold the names that made up much of their earlier loss, mostly among technology (Advantest, Citrix, STMicroelectronics, Microchip, On Semiconductor), industrials (MTU, Toray, Vinci), healthcare (Qiagen) and financials (SBI Holdings) sectors.

We have reinvested the proceeds into balanced profiles (Arconic, All Nippon Airways, ICA Gruppen, Kansai Paint, Sampo, Sumitomo Forestry, Suntec) as well as into also bond profiles which provide attractive short term yields (Suntec, Teva, Twitter, Vodafone).

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POSITIONING

Overall, the Mirabaud — Convertible Bonds Global fund has reduced its duration, its credit risk and its equity sensitivity, all contributing to increase the natural convexity of the asset class.

Sector wise, the fund is now underweighted cyclicals in favor of defensives while the biggest industry exposure is materials, through gold mining companies, as the precious metal is usually a strong performer when inflation rises and real interest rates become negative.

Regionally, we remain strongly overweighted in Japan as we see the reappointment of BoJ Governor Kuroda for a second term very supportive for the broad economy. We also overweight the Eurozone, which is seeing some of its best growth trends in a decade while we are underweighted In the US as we expect a derating of valuations despite the earnings boost linked to fiscal reform and the weakening of the dollar.

CONCLUSION

The overall downswing could last a couple of months, but then equities should recover as they are much later-stage casualties of inflation's revival. In that context, we will continue to be active and positioned on the most convex segment of the valuation curve in order to offer our investors the benefits offered by the asset class.

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