SphereInvest | GROUP

SPHEREINVEST GLOBAL CREDIT STRATEGIES (UCITS) FUND

Weekly Performance Period: 1st January to 31st January 2013

Class F (USD) MTD return +0.97% YTD 2013 return +0.97% NAV per Share $107.94 Since Inception [(1)] 7.94%

Class D (EUR) MTD return +0.87% YTD 2013 return +0.87% NAV per Share $107.52 Since Inception[(1)] 7.52%

[(1)] on 2nd July 2012

Portfolio and Market Commentary:

January was the first month since the summer of 2012 when meeting market expectations was no longer enough justification to drive corporate bond valuations tighter. The month did start in a frenzy of buying: within days of the US Congress having reached an agreement on the fiscal cliff negotiations, yields had collapsed by around 30 basis points (1). From the middle of the first full trading week, however, credit markets were already treading water and the month ended on a particularly weak note, with yields in High Yield and Emerging Markets rising on average by 25 basis points during the last week alone. For the whole of January, global investment grade returned -0.76%, marginally outperforming core rates. US, European and EM high yield markets returned 1.4%, 0.4% and 1.2%, respectively (2).

We have been cautious about valuations in high yield markets for several months already, although we recognized the strong technicals underpinning the market, as well as the discipline shown so far by credit investors, notably in the all important primary market. In both respects, January brought interesting developments. Demand for fixed income remains strong, as shown by inflows into EM hard currency bond funds reaching $1.8 billion during January (3). However, the strength of the primary market seems to have caught many investors wrong-footed and partly explained the change in market tone after the second week of the month. During the second half of 2012, the primary market often validated yields reached in the secondary market, with supply in the former leading to more demand in the latter. We saw little of that virtuous feedback during January. By contrast new issues exposed secondary levels as expensive rather than reflective of a broad consensus. Those investors who had been positioning for a strong supply-demand imbalance were left scrambling to sell recent issues, dragging down the performance of more seasoned bonds as they did so. Many EM corporate investors were also probably unpleasantly surprised by the rapid deterioration of lending standards. Indeed, primary markets registered a number of “first times” during the month. In a matter of days, Hopson Development, a Chinese developer, was able to issue the first ever CCC-rated new issue for an Emerging Markets corporate, and Agile Property, also a developer in China, managed to convince investors to bid for US$700 million of junior subordinated perpetual bonds bearing an 8.25% coupon. For investors wary that, even when contractually senior, Chinese corporate Eurobonds are still structurally subordinated, the issue of a contractually subordinated offshore bond without a maturity date by a Chinese junk-rated issuer was an absurd proposition. The subsequent very poor performance of the Agile perpetuals should have provided a healthy reality check for corporate treasurers and their banking syndicates. We believe the Agile perpetuals are likely to remain one-offs, rather than signs of unchecked exuberance in credit markets.

With the fiscal cliff temporarily avoided, the prospect of another standoff about the Debt Ceiling in the US postponed, and fears about a breakdown of the Eurozone now almost a distant memory, the importance of some of the primary common drivers of global financial markets over the last three years has clearly declined. Perversely, this also suggests that any renewed deterioration of investor perception about the fiscal debate in the US or the debt crisis in the Eurozone may have a disproportionate impact, given how much risk premiums have narrowed in recent months. From that perspective, the recent rise in core rates may be a worrying development for highly indebted Eurozone Sovereigns and we will continue to watch closely for any deterioration of financial conditions in the Eurozone and Emerging Markets.

Our investment activity during January was mostly focused on de-risking the portfolio after we felt the strong performance experienced during the first week had been overdone. We took profit in some the higher cash price bonds bought during the last quarter of 2012, such as our investments in Agrokor, a Croatian retailer, Cemex, a Mexican cement producer, and Ciech, a Polish soda-ash producer. Given the dynamic of the primary markets described above, a few of our participations proved unprofitable and were closed. Those included investments in MIE Holdings, a Chinese oil & gas producer, and Atalia, a French services company. While we do not believe our portfolio is meaningfully exposed to the risk of a further rise in core rates, we nonetheless reduced duration by selling positions in lower spread and longer dated financials positions. With the exception of the profit taking activity described above, our core portfolio remained largely unchanged during the month.

We regard the recent correction in high yield markets as healthy, although still insufficient to make us change our stance on markets meaningfully. We continue to believe valuations are stretched and that the recent regime of low volatility, however credit friendly, is unsustainable. We will therefore look for a more pronounced correction before reducing significantly our cash balances in the portfolio. Meanwhile, we are likely to increase idiosyncratic risk in the invested part of the portfolio. We believe generic “BB to BBB” credit risk was particularly overbought during the recent months of strong inflows into large bond funds, leaving valuations somewhat distorted and favourable to smaller and off-the-run issues.

Sources: (1) Bank of America Merrill Lynch Global High Yield & Emerging Markets Plus Index; (2) Bank of America Merrill Lynch Indexes; (3) EPFR

Portfolio Composition:

	Average Rating	Market Value (%)	Price	Mod. Dur.	Yield	Carry	Z-Spread	PnL Contrib.
SphereInvest Global Credit Strategies								
	BB	100 %	105.3	3.9	5.0 %	5.6 %	398	100 %
Largest 5 Positions								
	BB	20 %	108.0	6.2	6.8 %	7.7 %	524	10 %
Strategies								
Low Vol Portfolio	BB-	41 %	106.5	5.8	6.8 %	7.6 %	538	58 %
Cash and Equivalents	AA+	31 %						0 %
High Vol Portfolio	BB-	28 %	106.0	5.6	7.9 %	8.8 %	643	42 %
Regions								
LATAM	BB	39 %	106.2	6.6	6.5 %	7.2 %	494	43 %
Cash and Equivalents	AA+	31 %						0 %
Developed Europe	BB	13 %	110.3	4.2	7.2 %	9.1 %	591	1 %
NJA	B	8 %	99.6	5.5	10.1 %	9.7 %	858	17 %
MIDDLE EAST	BB	3 %	107.7	5.3	6.5 %	7.3 %	509	5 %
North America	B	3 %	105.1	4.0	6.0 %	6.9 %	507	6 %
Eastern Europe / CIS	B-	3 %	108.3	3.7	11.8 %	12.9 %	1085	28 %
Corporates/Financials								
Corps	BB-	52 %	105.8	6.2	7.2 %	7.7 %	564	63 %
Cash and Equivalents	AA+	31 %						0 %
Financials	BB-	17 %	107.7	4.2	7.5 %	9.2 %	632	37 %
Sectors								
Cash and Equivalents	AA+	31 %						0 %
Consumer Finance	BB-	13 %	111.2	3.8	8.3 %	10.4 %	713	12 %
Commercial Banks	BB-	9 %	104.3	5.1	6.7 %	7.5 %	541	21 %
Real Estate Management & Development	BB-	9 %	102.9	8.9	9.6 %	9.6 %	739	10 %
Media	BB	6 %	107.9	4.8	6.1 %	7.1 %	489	6 %
Oil, Gas & Consumable Fuels	B	5 %	104.7	3.2	6.5 %	7.6 %	573	6 %
Utilities	BBB	4 %	107.0	12.2	4.9 %	5.1 %	228	-2 %
Road & Rail	B	4 %	103.8	2.2	8.9 %	10.1 %	834	4 %
Beverages	BB+	4 %	110.8	7.0	5.0 %	5.9 %	320	6 %
Hotels, Restaurants & Leisure	B	3 %	106.2	4.0	6.3 %	7.4 %	541	4 %
Pharmaceuticals	BBB-	3 %	103.5	7.6	4.7 %	4.9 %	273	-1 %
Metals & Mining	BB	3 %	107.4	11.6	8.0 %	8.0 %	545	4 %
Telecommunications	BB	3 %	104.0	5.4	6.6 %	7.1 %	524	4 %
Auto Components	B-	3 %	100.5	1.4	9.2 %	8.0 %	869	1 %
Environmental Services	-	0 %						-3 %

	Average Rating	Market Value (%)	Price	Mod.Dur.	Yield	Carry	Z-spread	PnL Contrib
Sectors								
Food Products	-	0 %						19 %
Building Products	-	0 %						8 %
Chemicals	-	0 %						1 %
Ratings								
AA	AA	19 %						0 %
BB-	BB-	15 %	108.9	4.1	7.3 %	8.6 %	622	10 %
BB	BB	15 %	105.7	8.3	7.0 %	7.3 %	499	13 %
AAA	AAA	13 %	100.0	0.0	0.0 %	0.0 %	0	0 %
B	B	11 %	105.0	3.3	7.2 %	8.3 %	640	35 %
BB+	BB+	7 %	112.7	4.7	5.0 %	7.8 %	366	10 %
B-	B-	5 %	104.6	2.6	10.6 %	10.6 %	982	12 %
NR	-	5 %	101.0	6.5	9.1 %	9.7 %	740	-7 %
BBB	BBB	4 %	107.0	12.2	4.9 %	5.1 %	228	0 %
BBB-	BBB-	3 %	103.5	7.6	4.7 %	4.9 %	273	12 %
B+	B+	3 %	99.5	4.8	10.8 %	10.8 %	950	15 %
Currencies								
USD	BB+	90 %	104.6	3.9	4.7 %	5.1 %	377	88 %
GBP	BB-	7 %	110.7	4.6	8.3 %	9.5 %	695	-3 %
EUR	BB+	3 %	114.9	2.0	4.6 %	9.2 %	385	15 %

Performance Table since Inception:

Class F (USD)

	Jan	Feb	Mar	April	May	Jun	July	Aug	Sep	Oct	Nov	Dec	YTD
2012							0.15%	0.72%	0.78%	2.11%	1.24%	1.72%	**6.90%**
2013	0.97%												**0.97%**

Since Inception: 7.94%

Class D (Euro)

	Jan	Feb	Mar	April	May	Jun	July	Aug	Sep	Oct	Nov	Dec	YTD
2012							0.20%	0.66%	0.70%	2.04%	1.20%	1.62%	**6.59%**
2013	0.87%												**0.87%**

Since inception: 7.52%

Past Performance is no guarantee of future results.

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