SphereInvest | GROUP

SPHEREINVEST GLOBAL CREDIT STRATEGIES (UCITS) FUND

Weekly Performance Period: 30th May to 26th June 2014

Class F (USD): MTD return: 1.04%   YTD 2014 return: 6.26%   NAV per Share: 120.87

Class D (EUR): MTD return: 1.01%   YTD 2014 return: 6.18%   NAV per Share: 120.09

Portfolio and Market Commentary:

June concluded the first half of 2014 on a solid note for global credit markets, with European, US and EM high yield markets returning 0.84%, 0.95% and 1.77% respectively, while global IG spreads were 4bps tighter (1). Performance, however, was as half-hearted as ever: gains triggered by central banks' announcements were in part offset by profit taking later in the month. Although European markets were buoyed by the ECB finally delivering their much anticipated package of easing measures (including a 10bp rate cut and the provision of cheap loans to Eurozone's banks), June was also the first month since January with significant episodes of weakness, with spreads widening more than 25bps during the last week. Investors in US markets were initially relieved Fed Chair Janet Yellen appeared to dismiss the recent pick-up of inflation as "noise", although this quickly gave way to concern the Fed may risk falling behind the curve and treasuries ended the month broadly weaker. Finally, in EM, signs economic activity in China may have stabilised combined with easing Russia/Ukraine tensions helped allay fears that recent improvements in deficit EM countries, notably the so-called "fragile five", could stall due to higher energy prices triggered by the crisis in Iraq.

While all major credit markets delivered strong total returns during the first half of 2014, return drivers for each varied. In DM, credit returns owed more to Treasuries (or Bunds) and carry than to spread compression. Consensus calling for higher US$ rates in the near term has fuelled investors' perception that a part of this year's gains are therefore "temporary" and bound to be given back. Euro credit investors have been on a more comfortable footing than their US$ peers, with rates expected to remain low for an "extended period of time". However, with credit fundamentals stable but hardly justifying any spread compression and the carry of the market gradually eroded by a significant pipeline of low coupon new issues (while seasoned bonds carrying significantly higher coupons are getting called), European HY markets look bound to deliver positive but mediocre returns in the near term. Finally, the performance of EM credit markets, from being fundamentally driven after February 2014, as major EM countries acted to rebalance their economies, appears to have owed more to yield chasing and relative valuation arguments in recent months as investors shrugged off several geopolitical crises (from Ukraine to Iraq), a possible Sovereign default (Argentina), and signs the outlook in major parts of the EM world remained bleak (notably in Russia and Brazil). The case of China does not fit in that broad timeline: concerns about a "hard landing" peaked in the first quarter, when Chinese credits underperformed the rest of EM as a result, but have largely moved off investors' radar since then, with high beta sectors such as Chinese Real Estate performing best during the second quarter. Confronted with the risk of missing its "7% growth target", the Chinese government blinked as expected - but has left the question of the deleveraging of China's economy largely unanswered.

While a significant correction in credit markets, as experienced in each of the previous 4 years, is by definition impossible to forecast, it appears unlikely to happen in the near term. In our view, the current regime of low volatility is only likely to be disturbed by a dramatic reassessment of a major Central Bank's policy outlook, which could for instance be triggered by more evidence of inflation in the US. While we do not believe positioning for such a reassessment is warranted at this point, neither do we feel there is much emergency to get caught chasing the market at current tight valuations: the recent market malaise, reflecting unappealing valuations and continued strong new issue supply, is likely to continue providing for episodes of similar weakness, which are enough to offset a few months of carry and justify patience in waiting for new entry points.

Most positions in the fund performed well during June, with our investment in Sistema, the Russian holding oil and telecom holding, being the only marginal negative contributor. The strongest contributors included Borets, the Russian electric submersible pump producer, which continued to benefit from the recovery of investor sentiment towards Russian assets, and two Latin American credits, on more credit specific developments: our position in Ajecorp was June's second best performing position, after the bottler and juice producer reported better than expected first quarter earnings; while our investment in Gol, the Brazilian airlines, was June's strongest performer, after the company tendered for some of its US$ Eurobonds, reflecting its better liquidity position and ability to refinance its foreign currency debt with cheaper onshore loans.

(1) Source: Bank of America Merrill Lynch Indices HP00, H0A0 and EMHB

Portfolio Composition:

	Average Rating	Market Value (%)	Price	Mod. Dur.	Yield	Carry	Z-Spread	PnL Contrib.
SphereInvest Global Credit Strategies								
	BB-	100 %	105.1	4.1	5.4 %	6.3 %	405	100 %
Largest 5 Positions								
	B+	19 %	104.4	6.5	7.7 %	8.6 %	591	19 %
Regions								
Latin America	BB-	27 %	103.8	5.6	6.9 %	7.9 %	499	27 %
Developed Europe	B+	24 %	107.7	5.0	6.5 %	7.5 %	495	29 %
Eastern Europe / CIS	BB-	13 %	105.6	3.1	4.9 %	6.9 %	409	15 %
Treasury Bills	AAA	11 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Asia ex-Japan	B+	10 %	105.7	5.2	7.9 %	9.0 %	628	16 %
North America	B+	8 %	107.2	5.5	6.7 %	7.5 %	466	12 %
Cash	AA	7 %						0 %
Middle East / Africa	-	0 %						1 %
Corporates/Financials								
Corps	B+	56 %	105.2	5.6	7.1 %	8.0 %	542	79 %
Financials	BB	26 %	107.1	3.6	5.4 %	7.2 %	400	21 %
Treasury Bills	AAA	11 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Cash	AA	7 %						0 %
Sectors								
Consumer Finance	BB-	14 %	107.4	4.3	6.4 %	7.5 %	470	13 %
Real Estate Management & Development	BB-	12 %	105.3	5.7	7.6 %	8.5 %	618	13 %
Commercial Banks	BB	12 %	106.7	2.8	4.3 %	6.7 %	313	8 %
Treasury Bills	AAA	11 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Media	BB-	11 %	107.9	5.6	5.6 %	6.6 %	412	15 %
Telecommunications	B	10 %	108.2	4.6	6.6 %	7.7 %	463	8 %
Cash	AA	7 %						0 %
Food Products	B	6 %	107.4	3.5	7.2 %	9.1 %	573	7 %
IT Services	CCC+	4 %	111.8	4.2	7.2 %	8.8 %	651	4 %
Airlines	B-	4 %	85.9	9.4	10.2 %	10.2 %	746	8 %
Transportation Infrastructure	B	3 %	107.8	3.7	8.0 %	9.3 %	644	5 %
Beverages	BB+	2 %	92.3	5.9	7.8 %	7.0 %	559	7 %
Gaming	B+	2 %	103.5	5.6	5.4 %	5.8 %	445	3 %
Utilities	-	2 %	104.2	12.6	7.2 %	7.2 %	407	2 %
Machinery	-	0 %						6 %
Oil, Gas & Consumable Fields	-	0 %						1 %
Ratings								
BB-	BB-	18 %	107.7	4.3	6.1 %	7.4 %	457	25 %
BB	BB	15 %	106.2	5.5	6.4 %	7.5 %	481	8 %
B	B	15 %	106.9	3.7	7.5 %	8.9 %	628	24 %
AAA	AAA	11 %	100.0	0.1	0.0 %	0.0 %	0	0 %
B-	B-	9 %	100.5	6.8	7.9 %	8.7 %	552	12 %
BB+	BB+	9 %	103.8	5.8	6.5 %	6.9 %	429	14 %
AA	AA	7 %						0 %
B+	B+	7 %	106.1	4.6	6.2 %	7.1 %	467	11 %
CCC+	CCC+	4 %	111.8	4.2	7.2 %	8.8 %	651	4 %
BBB-	BBB-	3 %	99.6	0.0	0.0 %	4.3 %	0	0 %
NR	-	2 %	104.2	12.6	7.2 %	7.2 %	407	2 %
Currencies								
USD	BB+	73 %	103.5	3.8	5.0 %	5.9 %	373	73 %
EUR	B+	18 %	107.0	5.2	5.9 %	6.7 %	498	25 %
GBP	B+	9 %	112.4	4.1	6.8 %	8.6 %	473	2 %

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%	0.11%	0.54%	1.64%	-0.04%	-2.16%	1.11%	-0.06%	1.70%	1.66%	0.14%	0.67%	**6.40%**
2014	0.84%	1.08%	0.84%	1.10%	1.20%	1.04%							**6.26%**

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%	0.12%	0.54%	1.54%	-0.06%	-2.21%	1.16%	-0.07%	1.67%	1.66%	0.13%	0.65%	**6.11%**
2014	0.85%	1.06%	0.77%	1.09%	1.25%	1.01%							**6.18%**

Past Performance is no guarantee of future results.
Performance figures are net of all fees.

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