SphereInvest | GROUP

SPHEREINVEST GLOBAL CREDIT STRATEGIES (UCITS) FUND

Weekly Performance Period: 29th August to 2nd October 2014

Class F (USD): MTD return: -0.51% YTD 2014 return: 6.47% NAV per Share: 121.11

Class D (EUR): MTD return: -0.62% YTD 2014 return: 6.27% NAV per Share: 120.19

Annualized Return since inception: 8.73% Annualized Volatility: 2.16% Sharpe Ratio: 3.98

Portfolio and Market Commentary:

September was an eventful month, as geopolitical upheavals in the Middle East, large pro-democracy demonstrations in Hong Kong, the freezing of the conflict in Ukraine, and polarized elections in Brazil, competed for investors' attention with those likely to prove less significant, such as Bill Gross' resignation from Pimco (which raised fears outflows from the firm could affect illiquid bond markets). In high yield markets, familiar macro worries about rising rates in the US, the ECB's policy travails, and the slowdown of China, were for once almost overshadowed by a series of micro shocks, from the collapse of British retailer Phones4U to the house-arrest of Vladimir Evtushenkov (the main shareholder of Sistema, a large Russian holding company), causing investors to pay closer attention to deteriorating fundamentals than they had done in many months. Most credit markets performed poorly during September. Global IG markets returned -0.47% as spreads widened 6 basis points to compound weaker Treasuries. High yield markets had their worst month since June 2013, with spreads pushing 40bps wider than their level at the start of the year, and more than 100bps above their tightest point reached last July. Euro-denominated high yield markets outperformed, returning -1%, while the Sterling HY market suffered from the fallout of the Phone4U bankruptcy and was down -1.85%. US HY returned -1.88%, dragged notably by the underperformance of the energy sector. Finally, EM assets were pressured by the rally in the Dollar and the weakness of the commodity complex. EM HY returned -1.84%, led by Latin American credits (-2.8%), while Asia-ex-Japan credits were more resilient and returned -1.06% (see bottom table for more detail).

Neither the FOMC, which surprised by maintaining its dovish commitment to keeping rates low "for a considerable time after the asset purchase program ends", nor the ECB, which gave further detail on the modalities of its private asset purchases programme, provided much relief as investors focused on signs that global growth may be faltering. In China, Premier Li Keqiang's statement that the government would not be "distracted by short-term fluctuations in individual economic indicators" dashed investors' hopes for a fiscal stimulus, although some targeted easing measures, notably to support the troubled property sector, were announced. September's data confirmed mediocre economic conditions and weak inflationary pressures across much of continental Europe, with Spain a rare source of optimism, while Germany seems increasingly affected by the slowdown in its main export markets. Finally, a strong employment report (published after the Fund's performance period) showing unemployment rate had fallen to 5.9% - a post-recession low - capped a month of mostly solid economic indicators in the US. Confirming that investors are less worried about rates rising per se than by policy mistakes (such as an untimely hike at a time when economic conditions remain too fragile), September's strong employment report was greeted by a rally in risk assets, although it is also making a rate hike as soon as the first half of 2015 marginally more likely.

Sentiment in European HY markets deteriorated after the unexpected bankruptcy of Phones4U. Surprisingly, although the reasons behind the collapse of Phones4U were largely issuer-specific and had limited read-across to other credits, investors chose to make it a watershed event. We believe several factors explained the apparent disproportionate market reaction. Phones4U's secured bonds were priced "to first call", a widespread market convention which means investors assume a refinancing on the first call date is very probable, making them willing to accept lower yields to hold the bonds. Once it proved so spectacularly wrong in the case of Phones4U, investors started revisiting their assumptions for their "priced to call" holdings, causing significant maturity extensions in some cases. The failure of

Phones4U also triggered a widespread revision of credit risk in the retail sector, which was amplified as many retailers in continental Europe continue reporting poor results affected by near deflationary conditions or, in the case of UK retailers, an increasingly difficult competitive environment (also illustrated by the rapid succession of profit warnings by Tesco). At its core, we believe that Phones4U exposed the increasing gap between valuations based on the notion that “default rates are low because rates are low” and the creditworthiness of companies coping with difficult business conditions, overleveraged balance sheets, and, in some cases as in Phones4U's, vulnerable business models.

Reflecting a difficult market backdrop, most positions in the fund struggled during September. Generically, our “priced-to-call”, lower-rated, or Sterling positions were most affected by the bankruptcy of Phones4U. We remain comfortable with the underlying fundamentals of those positions and made only limited adjustments during the month since we believe their repricing may have largely run its course. Arrow Global, the British debt collection agency, was the only position to be impacted by credit specific developments, after the company announced the debt-funded acquisition of a smaller rival. While we were disappointed by Arrow's departure from the financial guidelines it had laid out at the time of its recent IPO, we believe the bonds are fundamentally cheap, although the expectation of a new issue and the pending opinion of rating agencies on the acquisition, may limit near-term upside. Elsewhere in the portfolio, we pared down our exposure to Brazil, given the increasing volatility of Brazilian assets during the election period and the likelihood that the incumbent, who ran on an increasingly populist and market unfriendly platform, will be re-elected.

Our near-term market outlook is cautious. The failure of high yield to hold onto its August gains, increased market volatility and macro challenges in EM and Continental Europe do not justify a rapid decline of risk premiums, in our view. Although the recent underperformance of US HY was intriguing given its broadly more supportive economic backdrop, a more granular analysis shows a trend of "decompression" similar to European HY: lower-quality credits led the sell-off, while the valuation of higher-quality credits typically targeted by the Fund remains less attractive. While a near-term market rebound is possible, the Fund is currently positioned to limit market beta and focus on taking advantage of bottom-up opportunities as they arise.

Market Overview

				Month-to-date (1)		Quarter-to-date (3)		Year-to-date	
Ticker	Index	Yield	OAS	Total Return	Chg in OAS (2)	Total Return	Chg in OAS (2)	Total Return	Chg in OAS (2)
G0Q0	US Treasury Index	1.6	-2	-0.25%	-1	0.40%	0	4.07%	-1
G0BC	Global Corporate Index	2.6	115	-0.47%	6	0.27%	1	6.39%	-9
GI00	Global Corporate & High Yield Index	3.3	184	-0.71%	15	0.24%	2	5.96%	1
HW00	Global High Yield Index	6.0	467	-1.68%	58	0.13%	3	4.19%	44
H0A0	US High Yield Index	6.1	442	-1.88%	60	0.19%	2	3.80%	42
HP00	European Currency High Yield Index	4.5	402	-1.00%	47	0.05%	2	4.72%	41
HL00	Sterling High Yield Index	5.9	425	-1.85%	48	0.12%	1	4.54%	56
EMIB	High Grade Emerging Markets Corporate Plus Index	3.7	210	-0.82%	14	0.09%	5	6.16%	-8
EMHB	High Yield Emerging Markets Corporate Plus Index	8.1	680	-1.84%	62	-0.05%	8	5.03%	46

(1) From 29/08/14 to 02/10/14
(2) Option Adjusted Spread
(3) From 30/09/14 to 02/10/14

Source: Bank of America

Portfolio Composition:

SphereInvest Global Credit Strategies	Average Rating	Market Value (%)	Price	Mod. Dur.	Yield	Carry	Z-Spread	PnL Contrib.
	BB+ (*)	100 %	103.6	3.2	5.2 %	5.8 %	420	-100 %
Largest 5 Positions								
	BB-	19 %	106.6	4.2	6.7 %	7.7 %	567	-31 %
Regions								
Latin America	BB-	22 %	103.2	4.9	6.7 %	7.5 %	485	47 %
Developed Europe	B	18 %	104.5	3.5	8.0 %	8.8 %	675	-83 %
Cash	AA	17 %						0 %
Eastern Europe / CIS	B+	14 %	106.0	4.6	6.4 %	7.2 %	558	-21 %
Treasury Bills	AAA	12 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Asia ex-Japan	B+	11 %	105.8	5.6	7.7 %	8.6 %	578	-10 %
North America	B	3 %	103.6	3.6	9.0 %	9.7 %	736	-15 %
Middle East / Africa	B	3 %	96.5	3.8	9.3 %	8.7 %	757	-18 %
Corporates/Financials								
Corps	B+	56 %	103.6	4.8	7.5 %	8.1 %	604	-66 %
Cash	AA	17 %						0 %
Financials	BB-	15 %	106.5	3.4	6.7 %	8.2 %	508	-34 %
Treasury Bills	AAA	12 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Sectors								
Cash	AA	17 %						0 %
Treasury Bills	AAA	12 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Real Estate Management & Development	BB-	11 %	105.4	5.1	7.4 %	8.2 %	598	21 %
Media	B+	11 %	105.3	4.2	6.4 %	7.3 %	559	-45 %
Telecommunications	B+	10 %	105.8	4.4	7.1 %	7.8 %	521	4 %
Consumer Finance	BB-	8 %	105.3	3.8	7.9 %	8.8 %	609	-35 %
Commercial Banks	BB-	7 %	108.0	3.0	5.3 %	7.6 %	390	1 %
Transportation Infrastructure	B	3 %	103.6	3.6	9.0 %	9.7 %	736	-12 %
Machinery	B	3 %	102.0	1.4	7.1 %	8.5 %	646	-1 %
Building Products	CCC+	3 %	96.3	3.8	8.8 %	8.2 %	840	-21 %
Communications Equipment	B	3 %	96.5	3.8	9.3 %	8.7 %	757	-21 %
Food Products	B	3 %	110.2	4.2	6.6 %	8.1 %	472	0 %
Utilities	-	3 %	104.5	12.3	7.2 %	7.2 %	422	3 %
IT Services	CCC+	2 %	104.8	3.9	8.7 %	9.4 %	824	-34 %
Airlines	B-	2 %	90.0	10.0	9.8 %	9.7 %	708	48 %
Diversified Financial Services	BB-	2 %	98.1	4.0	6.7 %	6.4 %	496	-7 %
Automobiles	-	0 %						-11 %
Auto Components	-	0 %						1 %
Beverages	-	0 %						9 %
Ratings								
B	B	22 %	103.7	3.6	7.9 %	8.5 %	653	-38 %
AA	AA	17 %						0 %
BB-	BB-	15 %	105.9	3.5	6.8 %	8.0 %	515	-33 %
BB	BB	14 %	105.0	5.0	6.4 %	7.5 %	496	30 %
AAA	AAA	12 %	100.0	0.1	0.0 %	0.0 %	0	0 %
B+	B+	7 %	104.5	4.2	7.0 %	7.7 %	567	-41 %
CCC+	CCC+	5 %	100.2	3.9	8.8 %	8.7 %	833	-51 %
B-	B-	5 %	102.3	6.6	8.2 %	9.0 %	597	39 %
NR	-	3 %	104.5	12.3	7.2 %	7.2 %	422	3 %
BBB-	-	0 %						-4 %
A+	-	0 %						-2 %
BB+	-	0 %						-3 %
Ratings								
USD	BB+	71 %	102.9	3.0	4.6 %	5.2 %	351	24 %
EUR	B	19 %	103.5	3.8	6.1 %	6.5 %	570	-87 %
GBP	B+	10 %	107.9	3.8	7.4 %	8.6 %	567	-37 %

(*) Weighted Average

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%	-0.20%	0.91%	-0.51%				**6.47%**

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%	-0.21%	0.92%	-0.62%				**6.27%**

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