Strategic Bond Opportunities Fund

December 2019 Fund Commentary

MARKET DEVELOPMENT

During December, the US fixed income market remained broadly stable and the 10y yield climbed slightly during the last week of the year. This month could have been more difficult for the bond market as global risk receded, pushing equity markets to record highs. Despite some good news leading to a significant decrease of uncertainties, the 10y Treasury yield did not climb above 2%. The month began with a nice surprise, a higher PMI in China (both manufacturing and services) which could prompt the markets to forecast a rebound of the activity in the country. The unemployment figures in the US were strong with 266,000 job creations, the unemployment rate dropping to 3.5% and wage growth at +3.1% YoY. The final FOMC of the year occurred, unsurprisingly, with no rate hike and a probable status quo for the whole of 2020. In the UK, Boris Johnson's triumph was perceived as a relief: his "get Brexit done" policy will eventually be implemented. At the same time, the US administration revealed that phase one of the trade deal with China would be signed in January. In Europe, Christine Lagarde chaired her first ECB meeting and mentioned two important things: the ECB is aware of the collateral damage of the negative rate policy and, in the course of 2020, they will review their strategy in depth (mission, objectives, toolbox, communication…).

PORTFOLIO STRATEGY

In December, the Investment Adviser actively managed the duration of the portfolio, trading exclusively US Treasuries. The main strategic decision of the month was to decrease the duration of the portfolio sharply on the 19th December, before the Christmas and New Year holidays, as the risk of a correction of long bonds (with 10y climbing above 2% and 30y reaching 2.5%) was increasing dramatically. The Investment Adviser sold all the US Treasuries maturing in 2026, 2029 and 2049 and as a result, the longest maturity was a bond maturing in November 2024. Four Treasury notes maturing in 2021 (in March, May, July and September) were purchased at the same time. These important transactions led to a sharp decrease of the modified duration from 5 to 3.7. However, regarding the real yield strategy, the 30y TIPS position has been maintained and unchanged.

MARKET OUTLOOK

The Investment Adviser's outlook remains tied to two major themes, the macroeconomic situation (including growth and inflation) and Central Banks' behavior. Inflation risk remains subdued in the US and substantially below the ECB's target in the Eurozone. Growth is lower (mainly in China and Germany, possibly in the UK depending on Brexit consequences) except in the US for the time being, where the domestic economy remains robust, however markets and central banks are aware that this safe haven position is temporary. The Team believe that yield curves may flatten, increasing fears of a significant global growth slowdown spreading into the domestic economy. In the short term, the US yield curve could steepen due to the Fed's purchases in the short term US bills and notes markets in order to increase the size of its balance sheet and fix the turmoil in the repo market.

In the US market, the Investment Adviser believes that long term US Treasuries are still attractive and may increase duration against escalating global trade tensions, recession fears and the implementation of the QE4. Considering inflation expectations, the Team will maintain a significant exposure to US inflation protection securities. According to the

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PORTFOLIO MANAGER

INVESTMENT APPROACH

The Fund is a diversified bond fund, investing in bonds predominantly denominated in USD, including Sovereigns, Supranationals and Agencies (together SSAs), corporate bonds across all sectors and financials. A strong conviction portfolio of 30-60 issuers, seeking exposure to all continents (including developed as well as emerging markets), all types of ratings from AAA/Aaa to BB/Ba2 (Standard & Poor's/Moody's) and non-rated bonds (10% maximum), senior or subordinated debt (hybrid corporates and Tier II bank debt) with either fixed or floating coupon rates.

INVESTMENT OBJECTIVE

To achieve a total return through a combination of capital growth and income by investing in a globally diversified portfolio of fixed income securities.

A sub-fund of E.I. Sturdza plc. Registered in Ireland**.**

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Investment Adviser, a flatter US curve slope can still not be excluded in the middle term, with markets concerned that the Fed may stay behind the curve. The Team believe that the best strategy today is to invest in a timely manner, maintaining a selection of short term high quality corporate bonds and investment grade emerging markets bonds, combined with a barbell strategy on the US Treasury yield curve, with an overweight of 1-2y combined with long dated US Treasuries (both nominal and real yields). The Fed has delivered its first three rate cuts since the financial crisis and the FOMC may be forced to implement more rate cuts should global growth continue to weaken, trade tensions remain and the dollar strength persist. In this context, the Investment Adviser believes that the Fed, after a probable pause during the first quarter of 2020, will continue to ease monetary policy in the coming months and increase its QE4 at some point if needed.

In Europe, the Investment Adviser believes that current macro conditions and Brexit uncertainties support the recent accommodation measures from the ECB. Following the decisions made in September, the Team believe that monetary policy should be less aggressive, with central bankers asking some major governments to implement a common fiscal stimulus policy. The first mission of Christine Lagarde will be to provide the German Government with enough convincing evidence. In the Investment Adviser's view, the ultra-accommodative monetary policy (negative rates in particular) has probably reached its limits.

As for Emerging Markets, the Investment Adviser will continue to monitor the spreads' patterns closely (for both governments and corporates) and Emerging Markets countries ability to absorb trade shocks in the context of weak FX and a broad commodity market which is under pressure.

In conclusion, the Team still believe that the best performing asset class is a mix of high quality short term Investment Grade bonds (USD denominated corporates and emerging markets) combined with long term US Treasuries. This said, and given the current environment of a global spread widening risk, the Investment Adviser may continue to increase the weight of US Treasuries, whilst reducing exposure to the three other pillars (corporate spreads in dollars, emerging markets in dollars and corporate spreads in euro). The Team believe that a mix of High Grade corporate carry and US Treasuries will present an opportunity to deliver a robust performance in the coming months; despite a very low yield environment and an already strong performance delivered by the Fund since inception.

PERFORMANCE DATA As at end of December 2019

CUMULATIVE PERFORMANCE %

	1M	3M	1Y	Fund Inception
USD I	-0.17	-0.30	7.47	7.97
Composite Benchmark	0.05	0.24	5.67	6.24

CALENDAR YEAR PERFORMANCE %

	YTD 2019	Annualised Inception
USD I	7.47	7.59
Composite Benchmark	5.67	5.94

Past performance is not an indicator of future performance.

IMPORTANT INFORMATION

The views and statements contained herein are those of the Eric Sturdza Group in their capacity as Investment Advisers to the Funds as of 16/01/2020 and are based on internal research and modelling.

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