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Global Convertibles Strategy

In times of uncertainty, we have increased the convexity of the strategy

- Equity and bond markets experienced a difficult month in February
- Our strategy outperformed the Global Convertible market
- We have more moderately sized relative risk positions in our strategy

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What's happening?

Equity and bond markets experienced a difficult month in February as concerns surrounding the Russian invasion of Ukraine took hold. In the first half of the month, expectations for the number of interest rate hikes that would be delivered by the US Federal Reserve (Fed), the Bank of England (BoE) and the European Central Bank (ECB) ramped up quickly. Investors were concerned that the central banks may dampen growth in their efforts to get inflation under control. In the second half of the month, investors' attention was absorbed by the conflict in Ukraine. This dampened expectations for rate hikes compared with the intra-month peak and delivered also a further hit to growth expectations.

The MSCI All Country World declined by 2.6%¹ (USD) in February. The S&P 500, the Nasdaq 100 and the Euro Stoxx 50 were also down 3%¹ (USD), 4.5%¹ (USD) and 5.9%¹ (EUR) respectively. Convertible bonds lost grounds with the TR Global Focus Hedged (EUR) index being down -2.0%¹.

Portfolio positioning and performance

Over the month, our Global Convertibles strategy outperformed the Global Convertible market (TR Convertible Global Focus Hedged).

Pioneer Natural Resources, the US oil producer, soared during the month as oil prices rose powerfully (WTI up 10%¹) with demand above supply and Russia-Ukraine conflict. A threat of further sanctions to ban imports from Russian oil and gas can continue to impact the energy market.

¹ Source: Local Currencies, Bloomberg as at 28/02/2021.

Palo Alto Networks, a cybersecurity software company, soared following the announcement of strong results: product revenue grew 21%² year-over-year last quarter, well above consensus estimates of 15%, as strong demand continues to outstrip supply chain constraints. We see this print validating our thesis that Palo Alto Networks' product sales are defensible, and the company has built growth engines outside of firewall, in cloud security.

Our exposure to **SolarEdge Technologies** and **Neoen** contributed positively on a relative basis as the stocks benefited from the overperformance of sustainable energy market linked to the oil price surge.

On a relative basis, we benefited from the fall of **Delivery Hero** as the company reported a Q4 missed and FY2022 guidance below expectations. More importantly the overinvestments and losses are pushing group profitability & positive free cash flow out by a couple of years putting at risk the company's solvency.

Zalando, a leading online fashion retailer in Europe, dropped during the month as the revenue momentum is slowing, led by the returning competition from physical stores, supply-chain disruptions, surging inflation and weakening consumer sentiment.

Puma dropped during the month like many discretionary companies as the Russia - Ukraine conflict can impact the already deteriorating consumer confidence in Europe.

Finally, our underweight in **Yandex**, the Russian internet company providing online search, e-commerce, and ride hailing, helped us to outperform during the month. We owned a marginal and underweighted position compared to the Global Convertible market. We have since then closed it and do not hold any other Russian exposures in the strategy.

Global convertibles issuance continued its sluggish pace in February as just \$3.3bn³ of new paper was offered last month, all from US borrowers-the first time that's occurred since August 2015. Indeed, the monthly total was well-below the historical February average of \$8.0bn³. We participated in the **Snap** and **Wolfspeed** convertible bond. We continued to take some profit in high-delta positions like **Silicon Labs**, **Datadog** and **Sony** and reinvested into **Splunk** and **Akamai** with more balanced profiles.

Outlook

The evolution of the Russia – Ukraine conflict remains uncertain. At this stage the clearest economic impact on developed markets is via food and energy prices. Russia is a significant exporter of commodities, accounting for 13%³ of global crude oil production, 17%³ of natural gas production and nearly a tenth³ of global wheat supplies. Brent oil ended the month at \$100³ per barrel and European natural gas prices rose 15%³ in February. Higher energy prices could fuel higher or at least more persistent inflation, eating into household incomes.

It is not yet entirely clear whether central banks will react to higher energy prices by increasing the magnitude/speed of interest rate rises in order to combat inflation ; or will reduce their pace of tightening in order to support the economy. The answer will depend on the extent to which higher energy prices dampen growth or alternatively fuel strong wage rises as workers try to protect their purchasing power amid a tight labour market. However, towards the end of the month, bond markets scaled back rate hike expectations for 2022, causing these expectations to end the month only marginally higher than they were at the start of the month.

In times of current uncertainty, it makes sense to have more moderately sized relative risk positions in our strategy. As such, we have increased the convexity of the strategy towards more convex convertible bonds that would enable to

² Source: Palo Alto Networks Fiscal Second Quarter 2022 Financial Results, 22/02/22

³ Source: Bloomberg as of 28/02/22

capture any upside move while protecting against **any deterioration of the conflict**. We retain the view that high quality management teams, operating businesses with a sustainable competitive advantage in their markets and with the benefit of secular tailwinds are best placed to weather the current storm and to seize opportunities for growth.

No assurance can be given that the Global Convertibles strategy will be successful. Investors can lose some or all of their capital invested. The Global Convertibles strategy is subject to risks including equity; Emerging markets; credit risks; counterparty risks; Investments in specific sectors or asset classes; Global investments.

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