Insight INVESTMENT

SEPTEMBER 2021

ABSOLUTE RETURN GLOBAL CONVERTIBLE STRATEGY
MONTHLY DESK REPORT

MARKET BACKDROP

Global equity markets experienced profit-taking in September. Even though the delta variant risk subsided, other headline risks came to bear. The solvency of China's Evergrande, the US debt ceiling, growing supply-chain worries, the inflation/growth argument and generally rising global rates all weighed on equities. Technology and momentum stocks were significant underperformers and, to a lesser degree, cyclicals and the reopening trade came under pressure. The risk-off sentiment elevated yield curve volatility which inevitably spilled over into the volatility of equities, leaving both near multi-month highs.

Core interest rates rose as curves steepened globally and fears of early tapering by the Federal Reserve exacerbated nervous sentiment. Inflationary fears resurfaced, causing credit markets to underperform and spreads to widen slightly. US fiscal policy remained mired in a split Congress. Threats of breaching the US debt limit and setbacks for President Biden's infrastructure package continued to weigh on risk assets. This added to suspicion over Powell's reappointment, which added to market uncertainty. The resultant spike in volatility provided us with the opportunity to capitalise through a number of positions.

Global convertible issuance was dynamic in September totalling $14.4bn across 24 issues. This was skewed towards Asia which accounted for almost 50%, the US about 40% and Europe only 10%, as the region continued to be quiet on the new issue front. Global issuance year-to-date now exceeds $124bn, which remains on par with last year's record pace.

PERFORMANCE REVIEW

The strategy return was positive in September as we benefited from the volatility and an improving new-issue calendar which led to market participants who had been quiet for the last few months re-engaging – a positive for potential returns. Information technology/communications weighed on returns while industrial and consumer discretionary performed well as valuations improved. A few energy positions we feel comfortable investing in added to our positive results.

We continue to closely monitor developments in new COVID-19 variants as we see this as the single biggest risk to reopening and supply-chain normalisation. Our positioning remains mostly neutral and risk-averse given the headline risk. However, this is a name-specific market, and we have selectively added names which we deem are oversold in tech, artificial intelligence (AI) lending, enterprise software and industrial materials. We believe the portfolio is well positioned to take advantage of growing reopening opportunities, a shift away from tech and expected volatility resulting from the approaching earnings season. The portfolio remains well anchored with solid credits, tight interest rate and equity hedging and improving diversification.

The geographical allocation remained unchanged, but we continue to look for new volatility-capture opportunities with robust underlying credits in Europe and Asia. We are carefully monitoring portfolio duration as we protect against rising rates. Net equity exposure remained negligible but targeted in a few select stocks where we feel the opportunity is strong enough to warrant additional risk. Single-name exposure continues to be tightly hedged with all exposure at +/-0.5%. As always, our largest positional credit exposure is concentrated in the best credit quality names with implied spreads near or below 50bp. Overall portfolio composition remains well diversified with no single sector dominating, but we are focused more on sectors we think offer the best risk/reward trade-off: specifically, oversold information tech/communications, consumer discretionary, industrial, energy and financials. We continue to maintain a smaller number of overall positions to focus more on individual companies we like. As a result, gross leverage was mostly unchanged; however, we expect this to eventually increase as we re-shape the portfolio.

Volatility increased in many individual names as stocks were re-rated amid analysts' changing forward guidance. With indices at or just off their all-time highs, but underlying stock action much weaker, we anticipate that indices will again pull back and offer a better entry point for some investments in the portfolio.

Attribution was spread across several positions with only a new position in AI-based lending provider, Upstart Holdings, generating any material positive contribution.

We maintain balanced convertible positioning with name-specific exposures for the same reasons we've highlighted recently: violent equity rotation, historically tight credit spreads, continued supply-chain issues and US tapering. Our largest exposures continue to be skewed toward strong credit and shorter-maturity gamma. We maintain a healthy interest rate hedge since we believe rates are at risk of moving higher. We expect our well-balanced portfolio, robust credit profile, interest rate hedges and minimal/targeted equity exposure, combined with increased volatility, to materialise into strong and steady returns. Issuance is buoyant, investor demand is still healthy and volatility is on the rise, which in our view are all positives for the long-term health and performance of the strategy.

Q3 in focus

Q3 performance rebounded after a difficult Q2, and year-to-date returns are positive and trending in the right direction. The quarter's financial market activity was bifurcated. Stocks were mixed, but cyclicals and reopening trades were lower, while large tech continued to grind higher. Rates did not rise materially but were extremely volatile. Energy (natural gas and oil) spiked, which caused major disruptions in Europe. Extraordinary supply-chain issues, combined with the energy price concerns, sparked inflation fears. Unforeseen Chinese government intervention, the Evergrande saga, uncertainty over COVID-related closures (Vietnam) and concerns over margin compression in future earnings caused volatility to realign higher.

There was approximately $30bn of new convertible issuance. While not a record, issuance is still on track to meet or exceed last year's record totals. The issuance was well distributed among various global regions which is very encouraging and bodes well for the health of the convertible marketplace.

Returns were spread across names and sectors with no one standout. As we look forward to Q4 and 2022 we are encouraged. Returns have come from old-fashioned volatility, strategic equity exposure and inherent cheapness in the market.

We believe this is a sign of a healthy market which is working on rational supply-demand metrics. As such, in our view, the marketplace shows that convertibles offer a way to participate in equity upside while mitigating potential downside risks. We expect there will be continued pockets of market disruption, but we plan to manage those risks and expect to deliver positive performance. We believe that the cheapening in convertible valuations during Q2 has helped to create opportunities in Q3 and should continue into Q4.

REPRESENTATIVE PORTFOLIO PERFORMANCE AND EXPOSURES (AS AT 30 SEPTEMBER 2021)

Table 1: Performance

EUR (%)	1 month	YTD	1 year	S.I. (pa)
Strategy	0.39	0.58	4.34	6.43
1-Month EURIBOR	-0.10	-0.42	-0.56	-0.49

Figure 1: Cumulative returns (since launch)

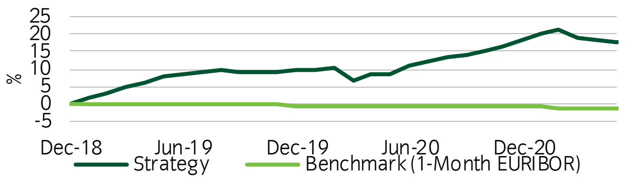


Figure 2: Risk statistics (since launch)[1]

Volatility (pa)	3.61%
Maximum drawdown	-4.91%
Realised beta to global equities[2]	0.08
Correlation to global equities[2]	0.41
Realised beta to global bonds[3]	0.03
Correlation to bonds[3]	0.03
Positive months	78.79%

Figure 3: Discrete periods

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2021	1.74	1.00	-2.00	-0.48	-0.43	-0.06	0.27	0.20	0.39				0.58
2020	0.24	0.49	-3.48	1.59	0.12	2.19	1.29	1.19	0.25	1.05	1.04	1.60	7.72
2019	1.46	1.45	1.65	1.55	1.67	0.47	0.47	0.70	-0.77	-0.08	0.14	0.52	9.57

Figure 4: Attributes

No. of strategies[4]	51
VaR (1day, 99% confidence)	0.14%
Net equity exposure[5]	0.90%
Gross leverage (long MV)	141%
Net leverage (long MV – short MV)	66%
Weighted average equity delta of bonds[6]	59%
Value Weighted Spread	176.4
Weighted average bond conversion premium[6]	28%
Portfolio duration	2.1

Figure 5: Long bond exposure by region

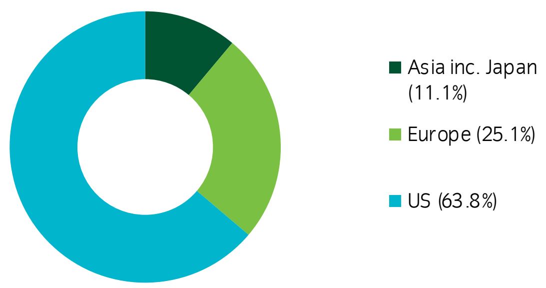


Figure 6: Long bond exposure by sector

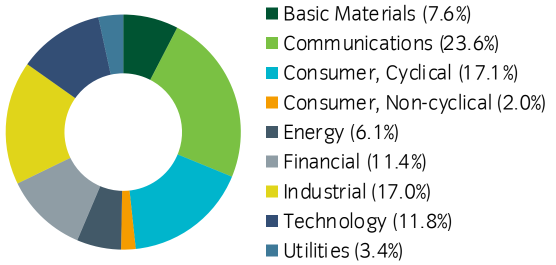
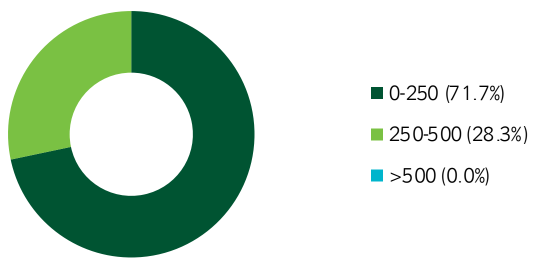


Figure 7: Long bond exposure by credit spread (bp)[7]



From strategy inception on 1 January 2019 to 3 June 2019, performance relates to a model portfolio. From 3 June 2019 to date performance relates to a UCITS pooled vehicle that employs the absolute return global convertible strategy. [1] All risk statistics are calculated using daily data points. For beta and correlation calculations we have used the rolling 5-day average of the daily returns of both the portfolio and the indices in order to smooth out the volatility related to securities being priced at different times in the portfolio and the indices. [2] Relative to MSCI World Total Return Hedged EUR. [3] Relative to JP Morgan Govt. Bond Hedged EUR. [4] Strategy refers to number of individual long bond positions, inclusive of specific dynamic hedge where appropriate. [5] Equity exposure of the convertible bonds less equity hedges (net delta adjusted exposure). [6] Relates to long bond positions, exclusive of individual hedges or portfolio overlays. [7] Exposure by the credit spread associated with the valuation of each convertible. Returns are shown in EUR on a net basis (with a 0.75% annual management charge and performance related fee applied). Performance is shown for representative portfolios. The representative portfolio is an account we believe most closely reflects current portfolio management style for the Insight's Absolute Return Global Convertible strategy. The characteristics of the representative portfolio shown may differ from those of other accounts in the strategy. Information regarding the representative portfolio and the other accounts in the strategy is available upon request.

IMPORTANT INFORMATION

FIVE-YEAR PERFORMANCE RECORD TO 30 SEPTEMBER 2021

	Calendar year returns					12-month rolling returns				
	2020	2019	2018	2017	2016	2020-2021	2019-2020	2018-2019	2017-2018	2016-2017
Representative portfolio	7.72	9.57	--	--	--	4.34	4.43	--	--	--
1-Month EURIBOR	-0.50	-0.44	--	--	--	-0.56	-0.49	--	--	--

Please refer to the following risk disclosures. Returns are shown in EUR on a net basis (with a 0.75% annual management charge and performance related fee applied). Performance is shown for representative portfolios. The representative portfolio is an account we believe most closely reflects current portfolio management style for the Insight's Absolute Return Global Convertible strategy. The characteristics of the representative portfolio shown may differ from those of other accounts in the strategy. Information regarding the representative portfolio and the other accounts in the strategy is available upon request. From strategy inception on 1 January 2019 to 3 June 2019, performance relates to a model portfolio. From 3 June 2019 to date performance relates to a UCITS pooled vehicle that employs the absolute return global convertible strategy.

RISK DISCLOSURES

Past performance is not indicative of future results. Investment in any strategy involves a risk of loss which may partly be due to exchange rate fluctuations.

Portfolio holdings are subject to change, for information only and are not investment recommendations.

The specific securities identified and described are subject to change, for information only. No assumptions should be made that the securities identified and discussed were or will be profitable. A complete list of contributors/detractors for the period covered is available upon request.

ASSOCIATED INVESTMENT RISKS

Absolute Return Global Convertible Strategy

• Currency hedging techniques aim to eliminate the effects of changes in the exchange rate between the currency of the underlying investments and the base currency (i.e. the reporting currency) of the portfolio. These techniques may not eliminate all the currency risk. Derivatives may be used to generate returns as well as to reduce costs and/or the overall risk of the portfolio. Using derivatives can involve a higher level of risk. A small movement in the price of an underlying investment may result in a disproportionately large movement in the price of the derivative investment.

• Investments in bonds are affected by interest rates and inflation trends which may affect the value of the portfolio.

• Where high yield instruments are held, their low credit rating indicates a greater risk of default, which would affect the value of the portfolio.

• Where leverage is used through the use of swaps and other derivative instruments, this can increase the overall volatility. Any event that adversely affects the value of an investment would be magnified if leverage is employed by the portfolio and losses would be greater than if leverage were not employed.

• Where the portfolio holds over 35% of its net asset value in securities of one governmental issuer, the value of the portfolio may be profoundly affected if one or more of these issuers fails to meet its obligations or suffers a ratings downgrade.

• The issuer of a debt security may not pay income or repay capital to the bondholder when due.

• Derivatives may be used to generate returns as well as to reduce costs and/or the overall risk of the portfolio. Using derivatives can involve a higher level of risk. A small movement in the price of an underlying investment may result in a disproportionately large movement in the price of the derivative investment.

• Investments in emerging markets can be less liquid and riskier than more developed markets and difficulties in accounting, dealing, settlement and custody may arise.

• Where high yield instruments are held, their low credit rating indicates a greater risk of default, which would affect the value of the portfolio.

• The investment manager may invest in instruments which can be difficult to sell when markets are stressed.

FIND OUT MORE

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