Monthly Fund Commentary
Muzinich Enhancedyield Short-Term Fund
September 2018

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Fund

Muzinich Enhancedyield Short-Term Fund

Market Review

There was a strong bifurcation in global credit market performance with high yield bonds producing strong returns, boosted by increased activity in the primary market, while investment grade credit felt the impact of rates pressures. Following a quiet summer, issuance picked up steam in September with notable high yield deals from Akzo Nobel and Thomson Reuters, totalling more than US$20bn, which saw strong demand. Other, smaller deals came to the market priced at relatively tight levels, supported by investors who were keen to participate after several months of much lighter supply. In the US, the Federal Reserve (Fed) implemented another 25bps rate hike and hinted at a further rise in December on the back of strong economic performance. In Europe, the European Central Bank reaffirmed its commitment to end its bond-buying programme, reducing its monthly purchases to €15bn from €30bn until the end of the year, although emphasised the continuation of loose monetary policy. Eurozone economic data prints continued to show a weakening of the economy, as the impact of the US/China trade war began to bite. The Italian budget dominated news flow towards the end of the month. While the final budget is not expected until later in October, the preliminary numbers emphasised a higher than expected deficit. Within emerging markets (EM), September was a month of recovery following an eventful summer dominated by idiosyncratic political and geopolitical events. The countries that had made headlines earlier in the summer – Argentina and Turkey - were among the strongest performers in September as both countries made steps towards economic reform. In Brazil, the presidential election campaign continued to gain momentum with the polarisation of voters made evident in the increasing popularity of far right and far left candidates in early polls. However, with the results not due until the end of October, we are likely to continue to see some uncertainty within EM.

Fund Review

The Fund produced a positive return and outperformed the ICE BofA ML German Federal Government (1 to 3 years) Index on a gross and net basis. From a regional perspective, bonds in Peripheral Europe, and the small position in Latin America, were the most notable contributors to returns over the month, while positive returns also came from the US and Western Europe. By sector, contributions came from telecommunications, healthcare, technology, energy, cable & satellite and banking, while positions in utilities and chemicals detracted. From a ratings perspective, positive returns were generated by bonds in most of the ratings spectrum and the same applied to duration. In terms of positioning, over the month the fund reduced its exposure to banks in countries where we see elevated idiosyncratic risk including Italy, due to the uncertainty around the country's economic and fiscal position, as well as the UK on concerns around Brexit. While the fund continues to hold some Italian banking paper (around a 2%), it has zero exposure to lower-rated AT1 bonds.

Outlook

In our view, the combination of macro and credit events that have occurred so far this year have increased the odds of the global credit cycle nearing its final phase. Divergence in fiscal and monetary policies and the changing international trade landscape are increasing downside risk. While US tax cuts have benefited corporates and boosted domestic demand, we believe a lack of long-term productivity is preventing a prolonged extension of the US cycle. As a consequence, we could see a major US economic slowdown in 2020/2021. Moreover, aggressive US trade tariffs could begin to weigh on the global economy in 2019, therefore bringing forward the chances of a slowdown. However, we believe current momentum in US domestic demand offers protection against what could become a sudden slowdown in the global trade cycle. Market participants are questioning how far the Fed will tighten monetary policy. Recent data points indicate the rate cycle could still be some way from maturing and therefore we could see another rate hike in December, bar any dramatic developments in financial markets. In Europe, the macro picture looks to be weaker than the US and economic growth appears to be decelerating. Uncertainty around Italy's budget and debt path is a concern and EU/US trade relations also remain a risk. European yields are low and, in our view, the spread widening witnessed during the first half of 2018 does not fully compensate investors for the risks we see developing in the Euro area. The unknown impact of the end of quantitative easing is also adding to the general uncertainty. Within emerging markets, lower US dollar liquidity and rising US short rates have challenged the most vulnerable countries, which cumulated in high foreign currency debt and too loose fiscal policies (e.g. Argentina, Turkey). Other countries, like Brazil, which are not suffering from high external imbalances, are going through their election calendar and therefore have limited policy responses to international pressure. Although the succession of idiosyncratic stories has resulted in a reassessment of the fundamentals of emerging market economies by some investors, we believe recent events have created more attractive valuations which should see more recognition from global portfolios, after the political uncertainties have passed. Overall, from a credit perspective, we do not anticipate negative credit-specific event risk. Defaults remain historically very low and leverage ratios are also at or below cycle levels. However, we believe end-of-cycle psychology is likely to create increasing bouts of volatility as well as liquidity concerns. From an investor's perspective, the increased dispersion we have seen on the back of headlines and localised weak sentiment has created what we believe to be opportunities for those willing and able to capture these dislocations.

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For Switzerland –

The prospectus (edition for Switzerland), the Key Investor Information Documents, the Trust Deed, the annual and semi-annual report, in French and further information can be obtained free of charge from the representative in Switzerland: Carnegie Fund Services S.A., 11, rue du Général-Dufour, CH-1204 Geneva, Switzerland, tel.: + 41 22 7051177, fax: + 41 22 7051179, web: www.carnegie-fund-services.ch. The Swiss paying agent is: Banque Cantonale de Genève, 17, quai de l'Ile, CH-1204 Geneva, Switzerland. The last unit prices can be found on www.fundinfo.com.

For Singapore –

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