Monthly Fund Commentary
Muzinich Bondyield ESG Fund
September 2018

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Fund

Muzinich Bondyield ESG 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 on a gross and net basis, outperforming the ICE BofA Merrill Lynch EMU Corporate Index. On a regional basis, the fund’s credit selection in Europe – both Western Europe and the Periphery, contributed strongly to relative returns over the period. From a sector perspective, the overweight positon in banks provided the strongest returns as the sector rallied after concerns around its exposure to Turkey eased. Additional contributors included credit selection in real estate, telecommunications, healthcare and food and beverage. Conversely, the underweight position in energy bonds slightly hampered relative returns over the month, with the sector benefiting from higher oil prices in September. Contribution by rating was positive across the board, with notable returns from the overweight position in BB+, BB and BBB-rated bonds as well as credit selection in the latter. From a duration perspective, credit selection in bonds in the belly of the curve as well as at the very short end (0-1 years) were the largest contributors to relative returns over the period. In terms of positioning, 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.

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.

Important Information

Past performance is not a guide to future performance. The value of investments and the income from them may fall as well as rise and is not guaranteed and investors may not get back the full amount invested. Any research in this document has been obtained and may have been acted on by Muzinich for its own purpose. The results of such research are being made available for information purposes and no assurances are made as to their accuracy. Opinions and statements of financial market trends that are based on market conditions constitute our judgment and this judgment may prove to be wrong. The views and opinions expressed should not be construed as an offer to buy or sell or invitation to engage in any investment activity, they are for information purposes only.

Please note that investment is subject to documentation, including but not limited to the Prospectus and Key Investor Information Document ('KIID') which contain a comprehensive disclosure of applicable risks. Investors in the UK should also access the Muzinich Supplemental Information Document ('SID'). Each of these documents is available in English at www.Muzinich.com, together with the Fund's annual and semi-annual reports. KIIDs are available by share class in each language required in the countries in which the share classes are registered. A complete listing of these KIIDs and the KIIDs themselves are also available at www.Muzinich.com. Investors should confer with their independent financial, legal or tax advisors. Issued in Europe by Muzinich & Co. Ltd, which is authorised and regulated by the Financial Conduct Authority. Registered in England and Wales No. 3852444. Registered address: 8 Hanover Street, London W1S 1YQ.

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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