

# Stratton Street UCITS - Renminbi Bond Fund UI

May 2015



- Underlying volatility in developed market rates dictated credit spreads
- China easing measures in Q1; signs of supporting growth
- US Q1 growth revised to negative, further disappointing data
- Best performers from positions in quasi-sovereign Russian Issues

## Market Comment

In a month where the Greek tragedy was once again a main feature and US data prints were rather soft, the market witnessed some of the largest swings in developed market sovereign bonds so far this year. As the global bond market sell-off continued into the end of May the yield on the ten-year German bund ended the month twelve basis points higher at 0.49% having spiked to intraday highs of 0.78% mid-month. Meanwhile the US Treasury ten-year yield rose nine basis points in May to 2.12%, settling from year highs of 2.29%; during the month. Away from bonds the S&P Index rose to new heady heights and the US dollar gained 2.44%, measured by the DXY Index (a dollar index).

US data releases for April and May were once again mixed: retail sales failed to meet market expectations in April, the Chicago Purchasing Manager Index reversed April's rise and fell unexpectedly below 50 for the third time this year; suggesting contraction in business activity and, although revised higher, the University of Michigan sentiment remains the weakest reading this year. As we had expected Q1 GDP actually shrank; to -0.7% having been revised down from the initial estimate of +0.2%. The market's inflation expectations were once again tempered as both the headline producer prices and the core reading (ex food and energy) fell; both readings were expected to actually increase marginally.

Meanwhile, data releases out of China suggest policymakers' easing measures and relaxation of fiscal policies provided support for the economy. Industrial profits increased in April, having fallen in March and both manufacturing and non-manufacturing PMI prints were relatively in-line with expectations and pretty unchanged from previous readings.

Over the month both the onshore and offshore renminbi were some of the only currencies to appreciate against the stronger dollar. Despite mounting pressure for currency depreciation over economic growth concerns, the People's Bank of China (PBoC) continued to fix the renminbi stronger during the month in order to maintain currency stability. This is key as the country pushes for the renminbi to be named as a reserve currency in the IMF's Special Drawing Rights (SDR) basket.

## Historical Performance<sup>1</sup>

	2015 %	* Inception %
IDUSD Class	8.12	10.93
IDGBP Class	8.09	12.20
IDEUR Class	8.34	14.22
IDCNH Class	7.85	13.59
ODGBP Class	7.55	9.59

## Performance Summary<sup>1</sup>

Index	Monthly Return %
Renminbi Bond Fund UI (Inst USD Class)	0.56
HSBC China Offshore Renminbi bond index (USD)	1.40
Offshore Chinese Renminbi (CNH)	0.11

## Fund Prices<sup>1</sup>

Institutional Class	Price	Monthly Return %
USD	108.29	0.56
GBP	107.81	0.62
EUR	109.68	0.56
CNH	110.95	0.46
Ordinary Class	Price	Monthly Return %
GBP	109.44	0.49

## Portfolio Statistics

Gross Redemption Yield	4.38%
Gross Running Yield	4.74%
Fund NAV (USD Millions)	36.89
Number of holdings	41
Number of countries	9
Duration	7.86

## Fund Breakdown

Net Foreign Assets		Credit Rating	
Rating	% NAV	Rating	% NAV
7 Star	50.33	Aa	37.49
6 Star	23.96	A	32.38
4 Star	18.45	Baa	24.65
3 Star	3.47	Ba <sup>2</sup>	1.69
Total	96.21	Total	96.21

Entity Type		Region	
Entity	% NAV	Region	% NAV
Sovereign	9.13	Asia Pacific	37.41
Quasi	59.96	C&W Asia	18.45
Corporate	23.65	Middle East	40.35
Supra	3.47		
Total	96.21	Total	96.21

Portfolio Exposure by Country	% NAV
Abu Dhabi	9.65
China	22.30
Hong Kong	12.06
Kazakhstan	3.47
Malaysia	1.66
Qatar	23.47
Russia	18.45
Saudi Arabia	3.76
Singapore	1.39
Total	96.21

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## Portfolio Review

The Fund's USD I Class gained 0.56% taking performance so far this year to +8.12% while the HSBC Offshore Renminbi Bond Index is up only 2.52%.

Once again holdings in Russian quasi-sovereign bonds were resilient despite rates coming off; contributing over 0.7% to performance. These bonds continue to offer attractive risk-adjusted returns; Russian Railways 7.487% 2031 (the best performer) tightened roughly 55 basis points over the month to 525 bps over Gilts or a yield of 7.5% and still offers a 3.5 credit notch cushion. We calculate fair value for this bond at roughly 205 basis points over, if the bond were to move to fair value we would expect a price gain of over 30%. The 5.717% 2021 issue from Sberbank, which accounts for roughly 30% of Russian banking assets, gained roughly 3.5 points over the month; the bond's yield compressed around 80 basis points to 5.9%.

Asian bond spreads were also hardy through this environment and positions in the Middle East, some of the best performers so far this year, saw spreads widen slightly on the back of escalating geopolitical issues; although our quasi-sovereign holdings in Saudi Arabia only lost the portfolio -0.05% in performance.

## Outlook

Having cut their forecast for US growth this year, from 3.1% to 2.5%, the IMF have urged the Fed to delay the first rate hike, stating that although job creation continues to improve, the central bank should wait for "greater signs of wage or price inflations than are currently evident". The IMF suggests a rate hike in 1H2016 would keep the central bank's credibility intact.

With some recent 2Q15 US data prints surprising on the upside, markets will be looking for any further indications of economic improvement in June. Currently a September rate hike is priced in, but some market makers have pushed their expectations out as far as December. The important factor to note is not so much *when* the Fed start normalising rates, as the market has already priced this in, but *how fast* the central bank continues to raise rates. The Fed Vice Chairman, Stanley Fischer recently noted that the Fed Fund trajectory is not "liftoff" i.e. "going straight up with the interest rate" instead he regards it as it's "crawling"; "going up with the interest rate, then along, and then another little jump."

We expect China to continue employing economic policy levers to support sentiment, with inflation looking to rise it is unlikely that the PBoC will look to reducing lending and deposit rates further. We do however believe that further RRR cuts will be deployed along with credit easing and liquidity injections. We believe that the PBoC will keep the renminbi fairly stable in the months ahead of the IMF decision; on whether the currency will be included in the funds Special Drawing Rights (SDR) basket.

## Share class information

Institutional	Current AMC	Minimum Subscription	Subsequent Investment	Front-end load	SEDOL	ISIN	Bloomberg
ID EUR	1%	EUR 250,000	EUR 10,000	None	5078151	LU0850781518	STRBIDE LX
ID USD	1%	USD 250,000	USD 10,000	None	5078175	LU0850781781	STRBIDU LX
ID CNH	1%	USD 250,000	USD 10,000	None	5078186	LU0850781864	STIDCNH LX
ID GBP	1%	GBP 250,000	GBP 10,000	None	5078208	LU0850782086	STRBIDG LX
ID GBP ACC	1%	GBP 250,000	GBP 10,000	None	BVJDP45	LU1163072603	TBC
ID CHF	1%	CHF 250,000	CHF 10,000	None	5078216	LU0850782169	TBC
Ordinary	Current AMC	Minimum Subscription	Subsequent Investment	Front-end load	SEDOL	ISIN	Bloomberg
OD GBP	1.5%	No minimum	No minimum	Up to 3%	5078275	LU0850782755	STRODGB LX
OD EUR *	1.5%	No minimum	No minimum	Up to 3%	5078224	LU0850782243	STRBODE LX
OD USD *	1.5%	No minimum	No minimum	Up to 3%	5078259	LU0850782599	TBC
OD CNH *	1.5%	No minimum	No minimum	Up to 3%	5078267	LU0850782672	TBC
OD CHF *	1.5%	No minimum	No minimum	Up to 3%	5078291	LU0850782912	TBC

\* Classes in red signify currently inactive but available on demand.

# Stratton Street UCITS - Renminbi Bond Fund UI

## Fund Information

<b>Domicile / legal status:</b>	Luxembourg / SICAV (UCITS)
<b>Base currency of the Fund:</b>	USD
<b>Valuation currency:</b>	USD, EUR, GBP, CHF or CNH (depending on share class)
<b>Valuation/dealing:</b>	On every full banking day, which is simultaneously a stock exchange day in Luxembourg, United Kingdom and Frankfurt am Main.
<b>Subscription/withdrawal:</b>	Prior business day by 4pm (Lux time)
<b>Appropriation of earnings:</b>	Distributing (all share classes)
<b>Investment manager fee:</b>	For share classes "I" and "O": up to 1.70% p.a. of the net asset value of the share class. See table above for current annual management charge (AMC).
<b>Management company fee:</b>	For share classes "I" and "O": up to 0.30% p.a. of the net asset value of the Sub-Fund subject to min. EUR 45.000.- p.a. for up to 2 share classes; for additional share classes the Management Company receives additional min. 7.500.- p.a.
<b>Other fees:</b>	Custodian and Paying Agency Fee, Domiciliary and Corporate Agency Services Fee, Registrar and Transfer Agency Fee: up to 0.10% p.a. of the Sub-Fund's net asset value, min. up to € 40.000 p.a. subject to Luxembourgish VAT.
<b>Front-end load:</b>	For share classes "OD USD", "OD CNH", "OD GBP" and "OD CHF" up to 3%. There is no front-end load currently applicable for share classes "ID EUR", "ID USD", "ID CNH", "ID GBP", "ID GBP ACC" and "ID CHF".
<b>Redemption fee:</b>	None
<b>The Company:</b>	Stratton Street UCITS
<b>Name of the Sub-Fund:</b>	Stratton Street UCITS - Renminbi Bond Fund UI
<b>Asset Manager:</b>	Stratton Street Capital LLP
<b>Management Company:</b>	Universal-Investment-Luxembourg S.A.
<b>Auditors:</b>	KPMG Luxembourg
<b>Custodian:</b>	Brown Brothers Harriman S.C.A.
<b>Planned distribution countries:</b>	UK, Austria, Germany, Switzerland, France, Belgium, Netherlands, Sweden and Luxembourg
<b>* Launch Dates:</b>	01 October 2013: IDEUR launched 21 October 2013: IDUSD launched 31 October 2013: IDGBP launched 28 November 2013: IDCNH launched 16 April 2014: ODGBP launched
<b>Footnotes:</b>	1. Bloomberg (as at end of month) 2. The holding in VTB Capital 6.95% 2022 is currently rated as sub-investment grade following on from the downgrade of the Russian sovereign which is now rated Baa2 by Moody's and BBB- by S&P (still investment grade). This VTB issue is subordinated so, although it was investment grade at purchase, it had a lower rating than our other holdings. We continue to have confidence in our Russian holdings and their expected risk adjusted returns, which factor in the current ratings, and we continue to monitor the position closely.

## Platforms and providers

Stratton Street UCITS - Renminbi Bond Fund UI can be accessed via the following platforms and providers:

Aegon	AJ Bell/SIPP Centre
Ascentric	AXA Isle of Man
Canada Life International	Cofunds
Friends Provident Isle of Man	Legal & General
Novia	Royal Skandia
Transact	Seven Investment Management (7IM)
UBS Funds Centre	

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