SphereInvest | GROUP

SPHEREINVEST GLOBAL CREDIT STRATEGIES (UCITS) FUND

Weekly Performance Period: 4th October to 31st October 2013

Class F (USD): MTD return: 1.66% YTD 2013 return: 5.55% NAV per Share: 112.84

Class D (EUR): MTD return: 1.66% YTD 2013 return: 5.28% NAV per Share: 112.22

Portfolio and Market Commentary:

- *Credit markets performed strongly during October, led by the strength of treasuries*
- *Performance was in our view mostly technically driven. We remain concerned the recent duration rally was not sustainable and could set the stage for a bigger correction if data in the US surprises on the upside*
- *Fundamentals in EM remain challenging, but we believe investors will continue focussing on signs that EM policymakers are ready to implement structural reforms*
- *Given current tight market spreads, we continue to see better risk/reward in credit risk over duration risk.*

Credit markets performed strongly during October, as anxiety over the debt ceiling dispute in the US gave way to a perception that all "known risks" have been dealt with or postponed to 2014. Although the end of the month saw some renewed tension in US$ rates, a consensus appears to have now formed that the last two months of 2013 will be a period of low volatility favourable to carry strategies. Surveys suggest that investors carried a large duration underweight going into September's FOMC meeting and have since been correcting their positioning, fuelling further the rally started in September. For the month, global investment grade markets returned 1.2%, with spreads tightening 9bps. In high yield markets, US and Euro markets returned 2.1% and 1.9%, respectively, while EM high yield returned 2.7% and is now back in the black for the year, having been down as much as 4.2% during June (1).

The Fed policy statement on October 30th was, in our view, largely a non-event. It did bring some volatility in rates, as investors appeared to believe that the government shut down could spur the Fed to pre-commit to a tapering calendar. In the event, this proved to be another triumph of hope over experience, and the Fed only reiterated that its policy path remained data-dependent and left all options open, including that of tapering before the end of the year. Data during October has remained consistent with slow but steady growth in the US, with manufacturing a key area of strength while the recovery in housing appears to have slowed down. On balance, given the limited data available for the Fed to change its view about the US economy before year-end, we still believe that tapering is more likely to be an early 2014 event. In Europe, Sovereign bond markets in Southern Europe provided further evidence of mending, with, for instance, 10-year Greek government bonds falling below 8% and Spain's 5-year CDS spread falling below that of Brazil for the first time since mid-2010. Less positively, the risk of deflation in the Eurozone appears to be rising, as high and rising unemployment, weak credit growth, and the strong Euro currency combine to put pressure on prices. October saw the lowest annual inflation print in four years, which could force the ECB into more accommodation – possibly with a rate cut as early as the next meeting on November 7th. Finally, in Emerging Markets, the end of the month brought a raft of worse than expected data, underscoring the challenges still faced by large countries such as Turkey, Indonesia, or Brazil. While concerning, we believe data may be lagging, and investors are more likely to focus on signals that EM policymakers are willing and able to tackle those challenges. Brazil illustrates that dynamic, with investors currently balancing the further deterioration of its fiscal position with signs that the administration may finally be getting serious about reining in its public banks' out-of-control lending growth. Belying the recent conventional wisdom that BRIC countries (with the exception of China) have been unable to implement structural reforms over the past five years, we would conclude here with the surprisingly strong showing by Russia in the World Bank's widely followed "Doing Business" annual ranking, published during October, suggesting that Russia may be tackling its poor investment climate and ongoing capital flight issue.

For the fund, October was a relatively frustrating month, as the primary market and event risk provided only few interesting opportunities, while our strategy of favouring credit risk over duration risk did not allow the fund to benefit fully from October's treasury-led rally. With high yield credit spreads now back to the tight end of their 4-year range (as in the US or Europe) or having largely recovered from their widening since May (as in Emerging Markets, where spreads have now retraced some 60%), credit's cushion to absorb rates volatility has inevitably diminished again. Starting from today's tight levels, we are concerned that the correlation between spreads and rates could turn positive again, similarly to the "double whammy" effect experienced during last summer, if incoming data in the US surprises on the upside and allows the Fed to taper sooner than currently priced in. All in all, we believe it is too late to jump on the duration bandwagon, and continue to find better risk/reward in credit risk.

All of the fund's positions performed satisfactorily during October, with three positions recording marginally negative returns and together accounting for 1 basis point of negative performance. Our holding in the subordinated notes of Banco ABC, the Brazilian mid-sized lender, recovered from their summer weakness, and was the single largest positive contributor. We continue to like the bank's cautious lending approach, which has historically resulted in steady if unspectacular quarterly earnings, as shown again in their third quarter of 2013 earnings reported in early November. Group Virgolino de Oliveira (GVO), a Brazilian sugar and ethanol mill, was the second best performer last month, as stronger sugar prices during October attracted new investors to the credit. Our rationale for buying GVO's bonds was not predicated on a view on sugar prices, but on the announcement late in September that it had refinanced most of its short-term debt maturities and had hedged its two next coupons on its US$ debt, two positive developments which we believed were not adequately reflected in the market level of its US$ notes. We exited our position during October after it exceeded our fair value target. Parker Drilling, the US contract drilling operator, was the third strongest contributor during October, as the company continued reporting improved monthly operating updates, which should confirm that the company's recovery is taking hold when it reports its next earnings later in November.

(1) Source: Bank of America Merrill Lynch indexes G0BC, HP00, H0A0, and EMHB.

Portfolio Composition:

	Average Rating	Market Value (%)	Price	Mod. Dur.	Yield	Carry	Z-Spread	PnL Contrib.
SphereInvest Global Credit Strategies								
	BB-	100 %	104.8	3.7	6.3 %	7.0 %	510	100 %
Largest 5 Positions								
	BB-	20 %	105.6	3.9	7.4 %	8.1 %	608	19 %
Regions								
LATAM	BB	29 %	102.8	5.0	6.5 %	7.0 %	486	41 %
Eastern Europe / CIS	B+	20 %	105.5	4.6	8.6 %	9.3 %	723	18 %
Developed Europe	B+	19 %	108.7	4.1	7.3 %	8.9 %	591	24 %
Cash	AA	13 %						0 %
NJA	B+	13 %	104.1	2.5	8.3 %	9.9 %	753	10 %
North America	B+	3 %	104.4	5.2	6.7 %	7.2 %	479	7 %
Treasury Bills	AAA	3 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Corporates/Financials								
Corps	B+	53 %	104.7	4.4	7.3 %	8.2 %	589	77 %
Financials	BB-	31 %	105.6	4.2	7.8 %	8.9 %	642	23 %
Cash	AA	13 %						0 %
Treasury Bills	AAA	3 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Sectors								
Commercial Banks	BB+	17 %	102.5	4.6	7.1 %	7.6 %	572	17 %
Oil, Gas & Consumable Fuels	BB-	15 %	102.7	4.4	7.2 %	7.7 %	561	22 %
Consumer Finance	B+	14 %	109.1	3.8	8.6 %	10.3 %	720	7 %
Cash	AA	13 %						0 %
Media	B+	6 %	104.6	2.6	8.2 %	9.9 %	737	3 %
Food Products	BB-	5 %	108.4	4.1	6.7 %	8.0 %	556	13 %
Utilities	BBB-	5 %	103.1	5.4	4.8 %	5.1 %	308	2 %
Telecommunications	B+	5 %	104.8	4.8	7.7 %	8.2 %	589	6 %
IT Services	CCC+	4 %	109.1	4.4	7.9 %	9.0 %	670	7 %
Treasury Bills	AAA	3 %	100.0	0.1	0.0 %	0.0 %	0	0 %
Gaming	B+	3 %	108.4	3.4	7.4 %	9.0 %	650	5 %
Machinery	B+	3 %	104.2	2.2	6.7 %	8.2 %	612	5 %
Metals & Mining	BB	3 %	98.1	10.8	8.8 %	8.8 %	572	3 %
Chemicals	B	2 %	113.0	4.5	6.8 %	8.4 %	559	4 %
Real Estate Management & Development	B+	1 %	99.1	3.4	11.9 %	11.7 %	1069	0 %
Building Products	BB+	1 %	100.9	7.1	7.0 %	7.1 %	449	2 %
Hotels, Restaurants & Leisure	-	0 %						2 %
Auto Components	-	0 %						2 %

Ratings								
B+	B+	19 %	104.4	3.4	8.4 %	9.5 %	727	21 %
BB	BB	15 %	101.4	5.5	7.4 %	7.8 %	558	16 %
BB-	BB-	14 %	105.6	3.2	8.0 %	9.1 %	697	8 %
AA	AA	13 %						0 %
B-	B-	9 %	108.9	3.9	8.9 %	10.1 %	741	8 %
BB+	BB+	8 %	104.1	4.6	5.8 %	7.0 %	424	9 %
BBB-	BBB-	7 %	103.2	4.6	4.7 %	5.1 %	319	5 %
B	B	6 %	110.5	4.7	6.8 %	8.1 %	546	21 %
CCC+	CCC+	4 %	109.1	4.4	7.9 %	9.0 %	670	7 %
AAA	AAA	3 %	100.0	0.1	0.0 %	0.0 %	0	0 %
NR	-	2 %	102.5	12.1	7.7 %	7.7 %	439	5 %
Currencies								
USD	BB	72 %	103.1	3.7	6.5 %	7.1 %	526	71 %
EUR	B+	20 %	109.0	3.1	5.0 %	6.3 %	419	22 %
GBP	B+	8 %	110.6	4.5	7.4 %	8.8 %	563	7 %

Performance Table since Inception:

Class F (USD)

	Jan	Feb	Mar	April	May	Jun	July	Aug	Sep	Oct	Nov	Dec	YTD
2012							0.15%	0.72%	0.78%	2.11%	1.24%	1.72%	**6.90%**
2013	0.97%	0.11%	0.54%	1.64%	-0.04%	-2.16%	1.11%	-0.06%	1.70%	1.66%			**5.55%**

Class D (Euro)

	Jan	Feb	Mar	April	May	Jun	July	Aug	Sep	Oct	Nov	Dec	YTD
2012							0.20%	0.66%	0.70%	2.04%	1.20%	1.62%	**6.59%**
2013	0.87%	0.12%	0.54%	1.54%	-0.06%	-2.21%	1.16%	-0.07%	1.67%	1.66%			**5.28%**

Past Performance is no guarantee of future results.

Performance figures are net of all fees.