Global Dynamic Bond US Election Update

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Performance of the Global Dynamic Bond Fund (GDBF) has been exceptional in recent days and weeks, adding to a longer-term picture of exceptional returns achieved for modest levels of risk. This note aims to explain what has been driving recent returns.

Net returns as at 10th Nov 2020	Sep	Oct	Nov	3 Mths	YTD	12 Mths	2 Yrs	3 Yrs	4 Yrs	S.I.*
I EUR Hedged Returns (%)	**-0.75**	**0.45**	**2.42**	**2.11**	**7.27**	**8.64**	**10.56**	**5.97**	**6.16**	**5.39**
Volatility (%)	-	-	-	4.38	8.26	7.93	5.94	4.99	4.42	4.17
Reward to Risk	-	-	-	0.48	0.88	1.09	1.78	1.20	1.40	1.29

*Since inception for the I EUR Hedged Share class was 5th November 2015

Source: Nomura Asset Management U.K. Ltd. Data as at 10th November 2020 and shown for the Nomura Funds Ireland Plc Global Dynamic Bond Fund I EUR Hedged share class, net of fees in EUR. Performance greater than 1 year has been annualised. Peer universe for comparison is the Morningstar Open Ended Funds Global Flexible Bond universe. Morningstar Overall Ratings relate to the Nomura Funds Ireland plc Global Dynamic Bond Fund I USD share class. Past performance is no guarantee of future results.

For months now, Richard Hodges and his team have been warning of short-term risks to a longer-term positive picture for financial markets. A direct quote from their reporting at the end of September reads:

- Our medium- to long-term view of markets remains positive – we believe that current and future waves of both fiscal and monetary policy will drive risk markets higher, even though economic recovery will take longer.

- Over the next few months, a number of key uncertainties will be removed from markets. Each is likely to cause some volatility and then, should the results be viewed favourably, each should then lead to another leg higher for risk.

- The US election is one such uncertainty. Although the Democratic candidate appears to have a healthy lead in the polls, we know that the end result does not always reflect the polls. The markets tend to like a Republican winner, but even if Joe Biden wins, the market will probably expect further stimulus regardless and, if he appoints a more centrist team, this will also likely be taken as a positive.

- However, surely the greatest risk surrounds Covid… …We suspect that a vaccine that Western medical authorities are comfortable with will be released and distributed, but a delay to that would weigh on markets. Progress on a vaccine is likely to see capital markets move higher.

Writing this piece on the 11th November, I am conscious that there is still potential for the US election to be disputed, but the markets more broadly have now moved on from election risk. The race was closer than the polls suggested, and there was volatility on the run-in, but that was quickly replaced by a rally as the result became more clear.

In the last couple of days, markets have also priced-in much less Covid vaccine-related risk, after Pfizer's very welcome statement regarding the progress of their clinical trials. I should stress that there remain great challenges ahead in distributing and administering this and/or other vaccines as they are approved, but nonetheless the progress seen so far is entirely in line with the GDBF team's expectations.

More importantly, the reaction of capital markets has also been entirely in line with the team's expectations. As a result, the major risk positions within the Fund have performed exceptionally well through this period, with the Fund gaining well over 2% in November alone, and more than 7% over calendar 2020 to date.

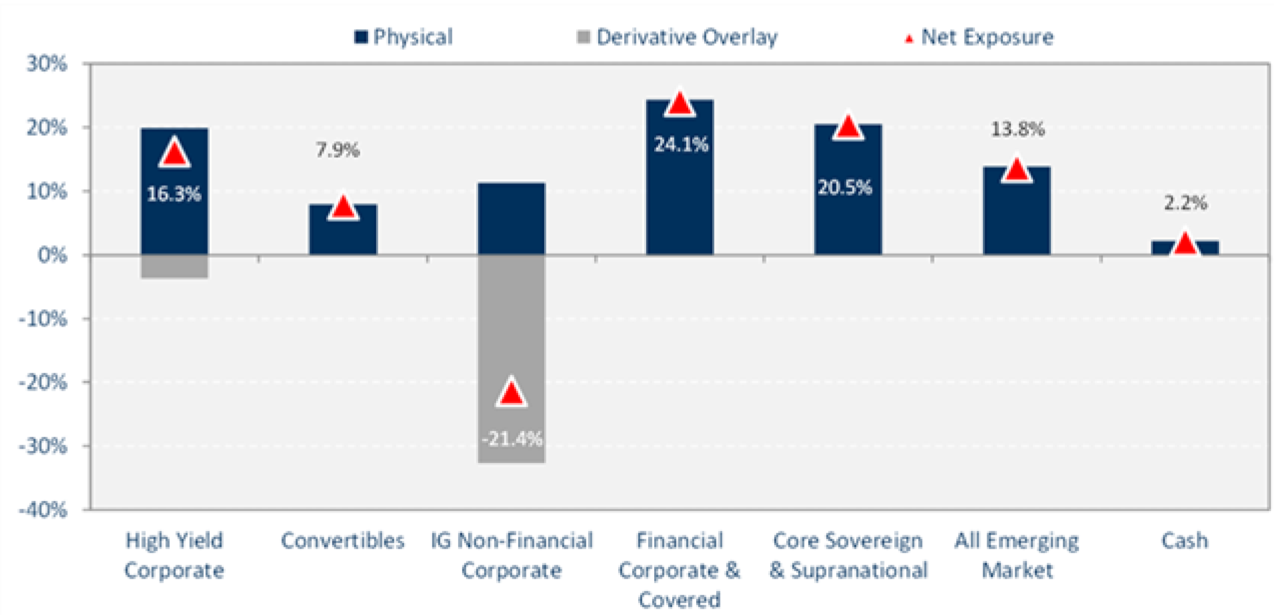
Those major risk positions include:

Emerging Markets	Where exposure to Russia Local Currency Sovereign debt has contributed strongly through both spread compression and currency movements after exposure to the Ruble was left unhedged.
Subordinated financials	The Fund has a significant position in the subordinated debt of European banks, and this exposure, diversified across Spanish, Italian and German institutions (amongst others) has proved positive as demand for these risky securities has soared
High Yield Bonds	Recently the Fund's exposure to High Yield debt has increased, as the team recycled capital from falling allocations to Investment Grade securities in Europe in particular. Why? Investors are desperate for yield, and more so now, particularly in Europe where sovereign yields are negative and investment grade spreads are increasingly squeezed.

Each of these allocations on their own represents risk. Together they represent substantial risk. The GDBF team is paid to take such risks and they will do so when and if market conditions justify them. Moreover, they have access to a wide range of hedging tools, and recently, these tools have been in great evidence.

In early September, Richard Hodges led the team to install additional hedges to the portfolio to combat the short-term risks of the US election, and to reflect the recent run-up in the prices of Investment Grade bonds in particular. Option-based hedging (previously used to such great effect during the Covid crisis of February and March) was eschewed – protective options were expensive, with implied volatility high. Instead, an outright index CDS hedge with a notional size one third of the value of the $2.3bn Fund was deployed to guard against a sell-off in spreads.

Asset Allocation – as at October 2020



Source: Nomura Asset Management as at 31.10.2020

The hedge took the Fund's exposure to both investment grade securities and the US negative, and was a key driver of Fund performance in October and the first few days of November, before being cut in scale as the rally took hold. Although this was not the only hedge employed, it was of the greatest scale and perhaps gives an indication of how a truly flexible fixed income Fund can serve to protect its investors' capital.

Now these events are behind us. As mentioned above, the hedging of the Fund has been reduced, leaving the risky exposures of the Fund more open to deliver attractive returns in what should prove a relatively benign environment for risk, with central banks remaining accommodative, and major governments providing fiscal stimulus.

With global yields at ultra-low levels and investors still clamouring for yield from their fixed income allocations, yet unwilling to take the risk associated with market segments that still offer those yields, Nomura's Global Dynamic Bond Fund offers a compelling opportunity.

If you would like to know more, please contact MarketingSupport@nomura-asset.eu or your usual Nomura Asset Management representative.

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