

OUTCOMES
BEYOND
PERFORMANCE

STRUCTURAL CHANGE IN THE GLOBAL CREDIT WORLD

Rankia Funds Experience, Andorra

Fraser Lundie, CFA, Head of Credit
12-13 December 2019

For professional investors only


HERMES
INVESTMENT MANAGEMENT

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Hermes Fixed Income Team



Andrew Jackson¹
Head of Fixed Income
Industry experience: 25 years

Helen Redman
Team Support

Credit		Fraser Lundie, CFA¹ Head of Credit Industry experience: 15 years		Sustainable Fixed Income		Mitch Reznick, CFA¹ Head of Credit Research and Sustainable Fixed Income Industry experience: 22 years	
Andrey Kuznetsov, CFA Senior Portfolio Manager	Nachu Chockalingam, CFA Senior Portfolio Manager	Vincent Benguigui Portfolio Manager	Aaron Hay Lead Engager	Audra Stundziaite, CFA Deputy Head of Credit Research	Ilana Elbim Senior Credit Analyst		
Filippo Maria Alloatti Senior Credit Analyst	Anna Chong Senior Credit Analyst	Joe Howes Credit Analyst	Robin Usson, CFA Credit Analyst				

Mark Bruen, CFA¹ Multi Asset Credit Solutions Strategist	Kimberley Howlett Product Specialist
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Offshore Research Team²

Shubhajit Dhar Team Leader/ Research Analyst	Sonali Patil Research Analyst	Pooja Palsekar Research Analyst
Rushikesh Prabhudesai Research Analyst		

Asset Based Debt		Vincent Nobel¹ Head of Asset Based Debt Industry experience: 14 years	
Ben Patton Head of Real Estate Debt	Khalid Khan Structurer	Stephan Michel, CFA¹ Senior Portfolio Manager	
Andrew Lennox¹ Portfolio Manager	Rahul Malde, CFA Investment Analyst	Angela Sheahan Strategy & Investment Analyst	

Private Debt		Patrick Marshall¹ Head of Private Debt Industry experience: 23 years	
Laura Vaughan Head of Direct Lending	Maria van der Veer Director	Alexandra Trapes Director	
Carina Spitzkopf Director	Kevin Roche Director	Emeric Chenebaux Portfolio Manager	

Trading/ Execution

Jonathan Lee Head of Credit Trading	Michael Vaughan Multi Asset Trader	Rob Elston ABSTrader
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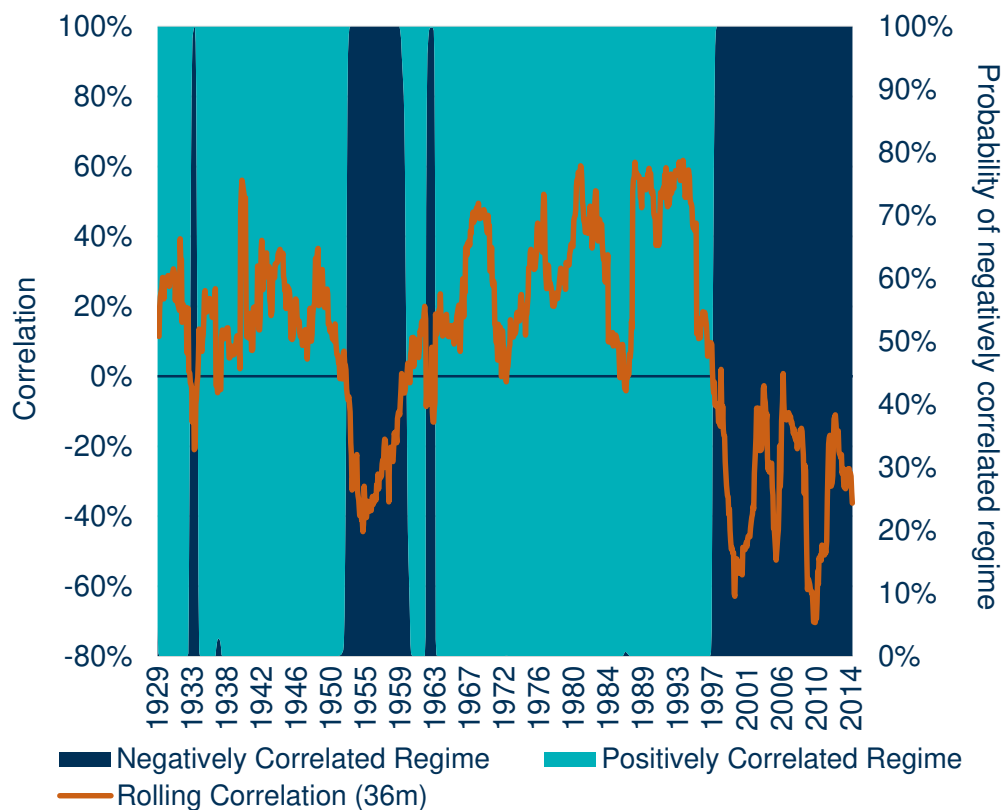
Investment Office 5 employees	Economists 2 employees	Hermes EOS 21 employees	Hermes Responsibility 7 employees	Multi-Asset 6 employees
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¹ Member of MAC Investment Committee. ² Employed by Sutherland, an outsourced third party researcher. CFA® is a trademark owned by the CFA Institute.

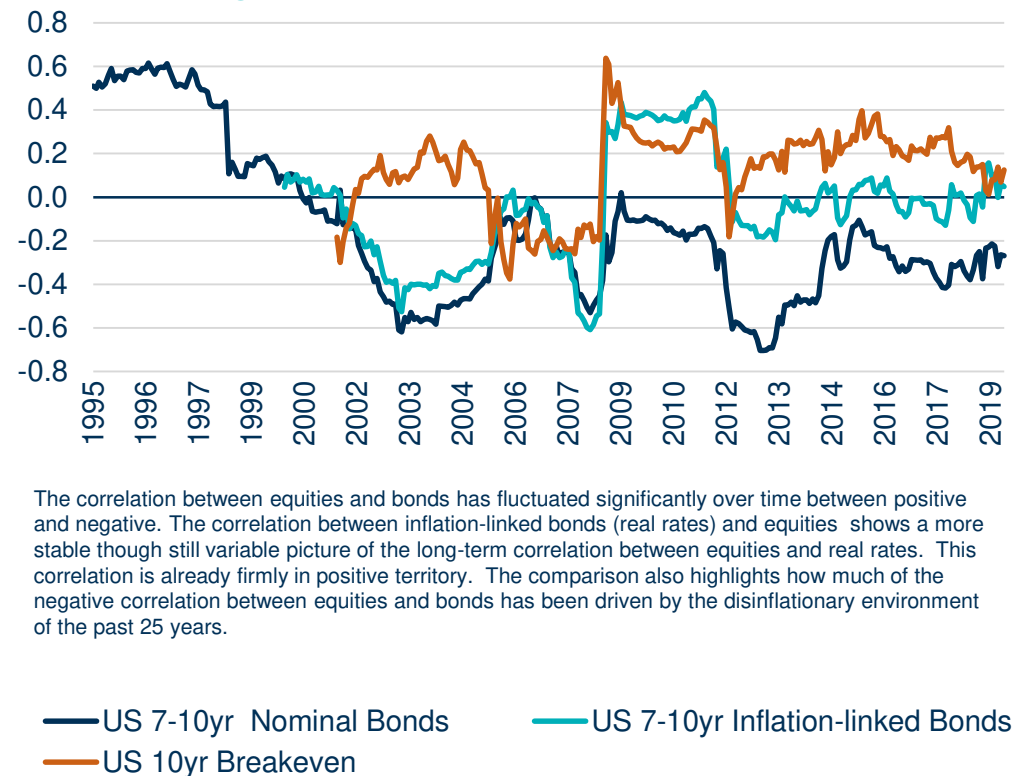
Risk: Duration

The importance of dynamic duration management

Stock-bond correlation regimes¹



US bond and equity correlation (36m rolling v S&P 500 Index)²



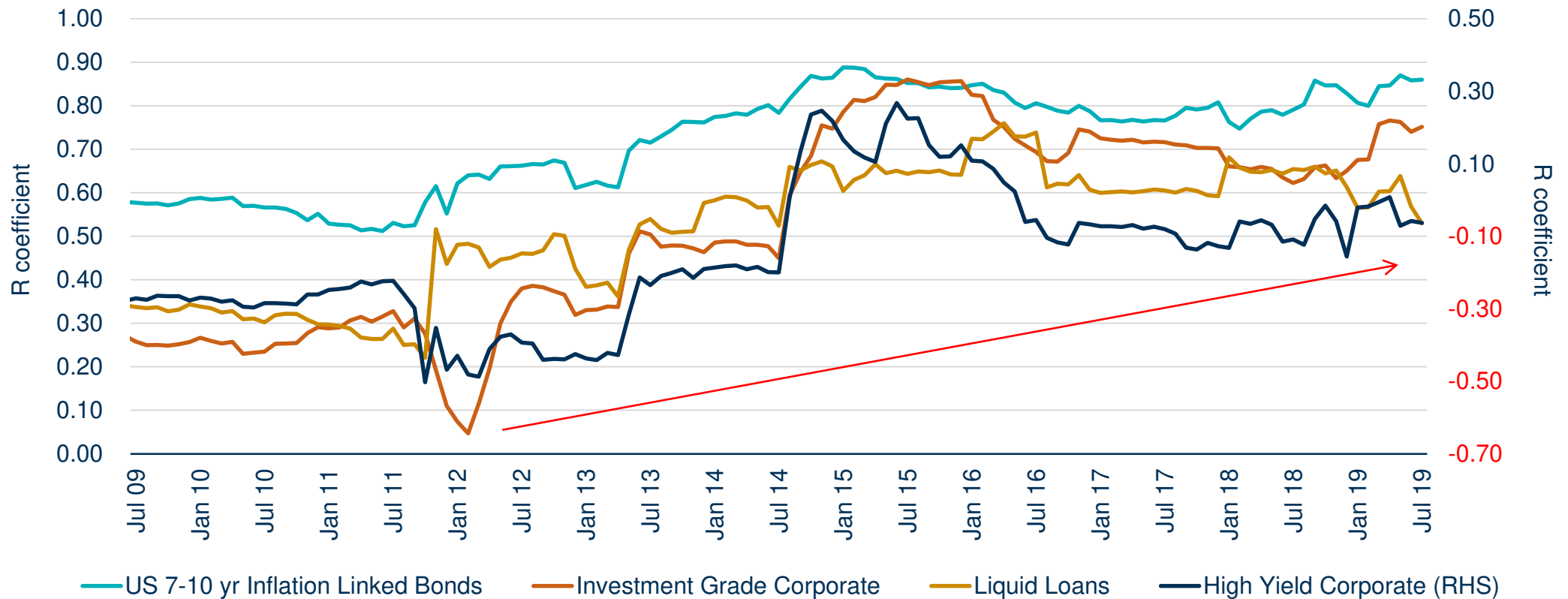
The correlation between equities and bonds has fluctuated significantly over time between positive and negative. The correlation between inflation-linked bonds (real rates) and equities shows a more stable though still variable picture of the long-term correlation between equities and real rates. This correlation is already firmly in positive territory. The comparison also highlights how much of the negative correlation between equities and bonds has been driven by the disinflationary environment of the past 25 years.

¹ Source: Bloomberg as at 31 October 2014. ² Source: Bloomberg as at 31 July 2019.

Diversification is not a complete defence

Rising correlations have eroded the impact of diversification

Fixed income asset class correlation (36m rolling v US Government Bond)

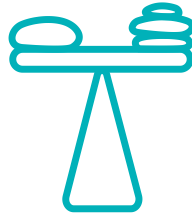


Source : Hermes Credit Team, Bloomberg and Bank of America Merrill Lynch as at 31 July 2019.

Tools to manage downside risk in global credit



1 Dynamic duration management



2 Structural downside protection via defensive credit



3 Diversification across different classes



4 Dynamic allocation across types of credit



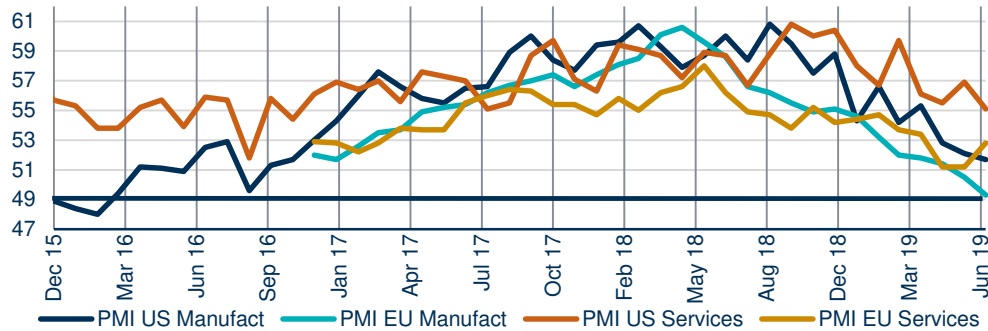
5 Fundamental credit analysis



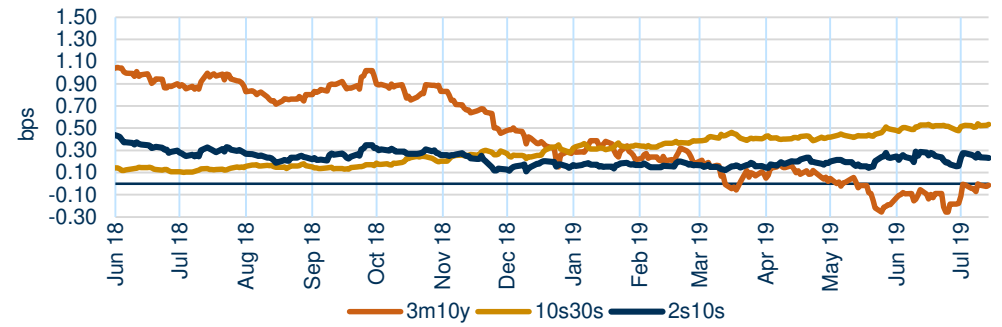
6 Holistic risk management

Market review

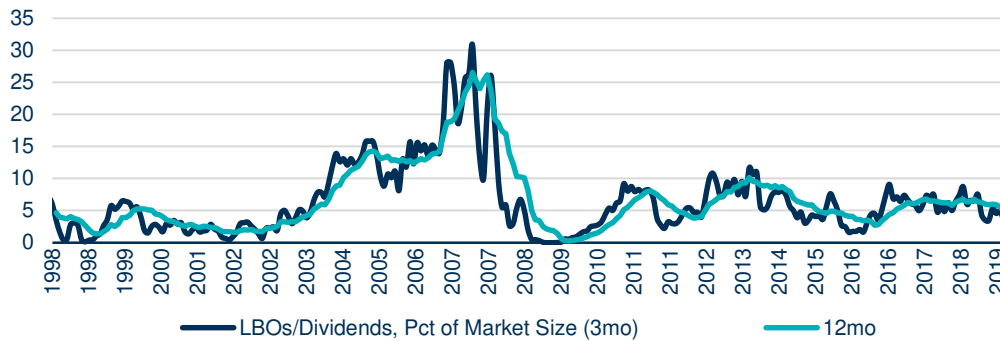
Global PMI surveys¹



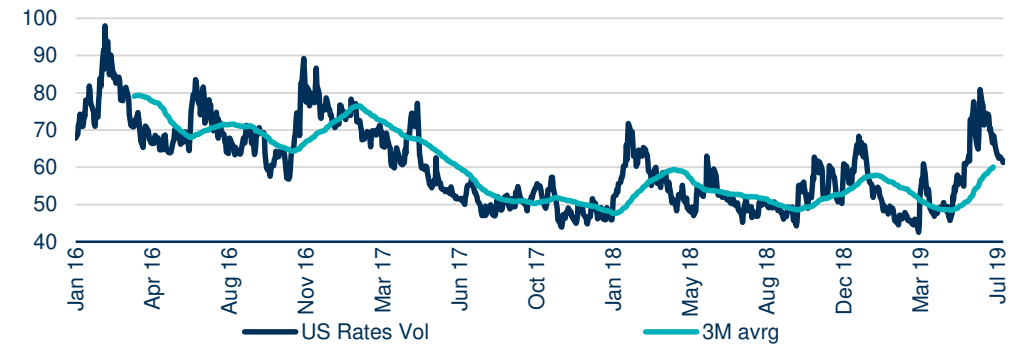
2s10s, 3ms10s, 10s30s²



Issuance for LBO/dividends³



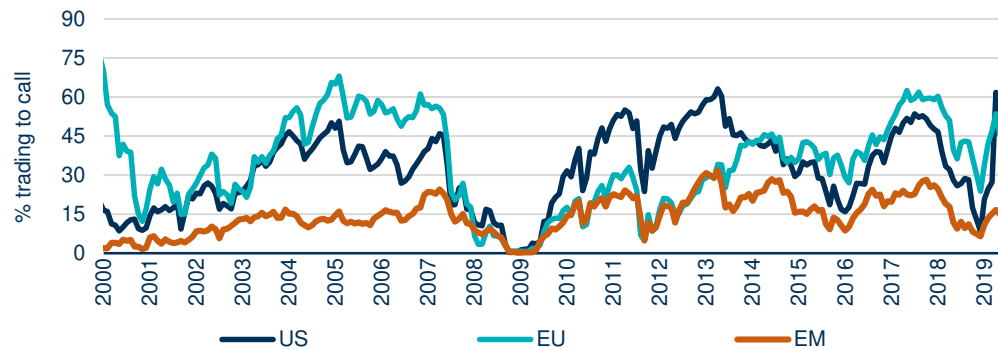
US rates volatility⁴



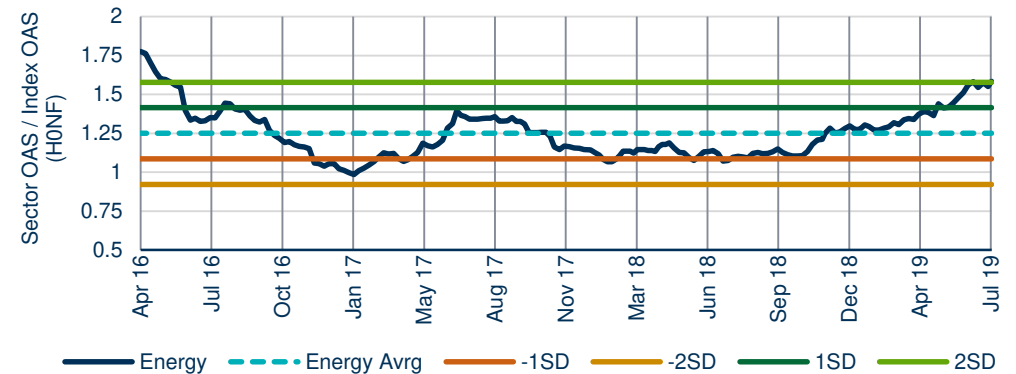
Source: ¹ Hermes and Bloomberg as at 22 March 2019. ² Hermes and Bloomberg as at 23 July 2019. ³ BAML as at 30 June 2019. ⁴ Hermes and Bloomberg as at 16 July 2019.

Convexity: a key challenge for 2020 in global credit

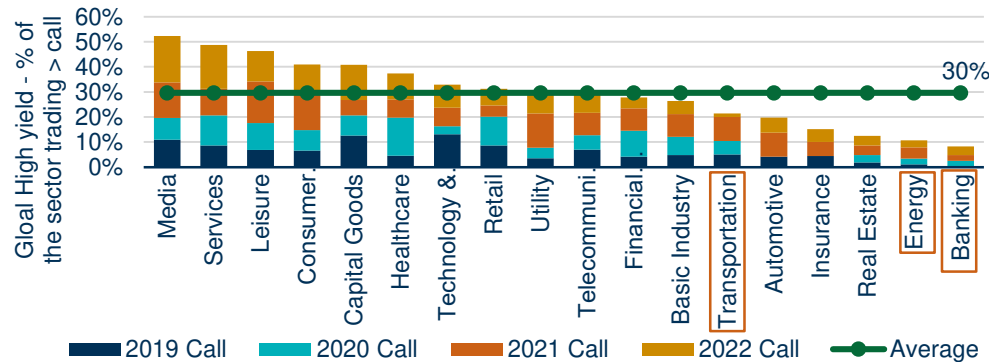
Convexity by region (% above call)¹



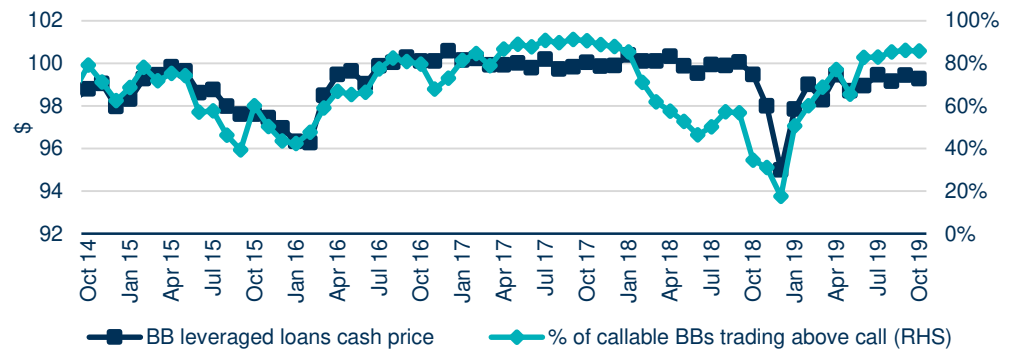
Energy³



Convexity by sector³



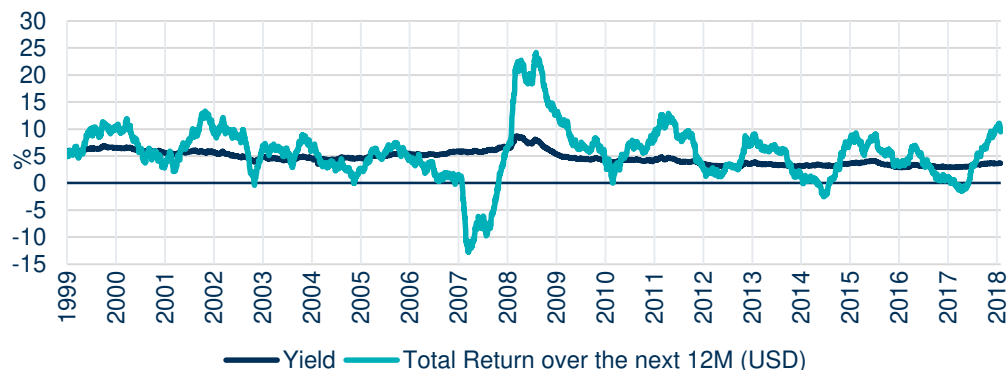
Leveraged loans v high yield for press⁴



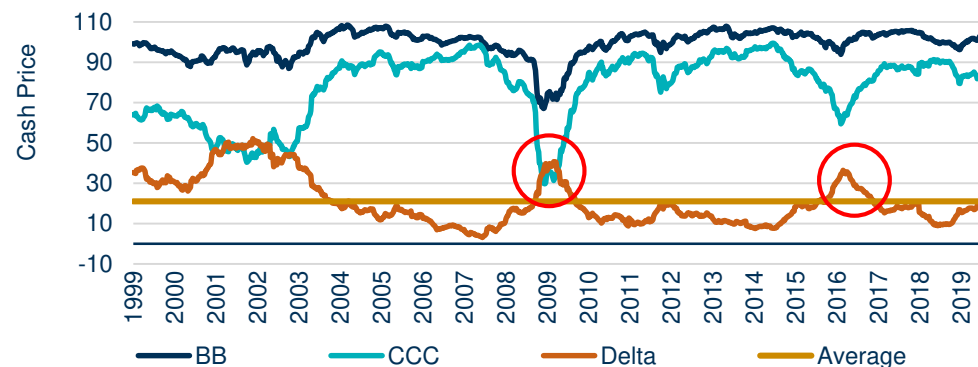
Source: ¹ BAML as at 30 June 2019. ² Hermes Credit and ICE Bond Indices as at 16 July 2019. ³ Hermes Credit as at September 2019. ⁴ Hermes Credit, CS Indices, BAML data as at 31 October 2019.

Dispersion creating opportunities

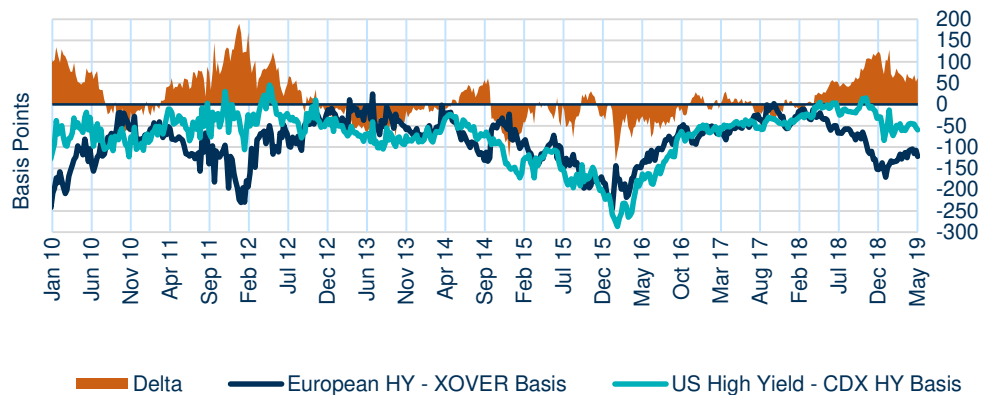
Global corporate Credit (IG & HY)¹



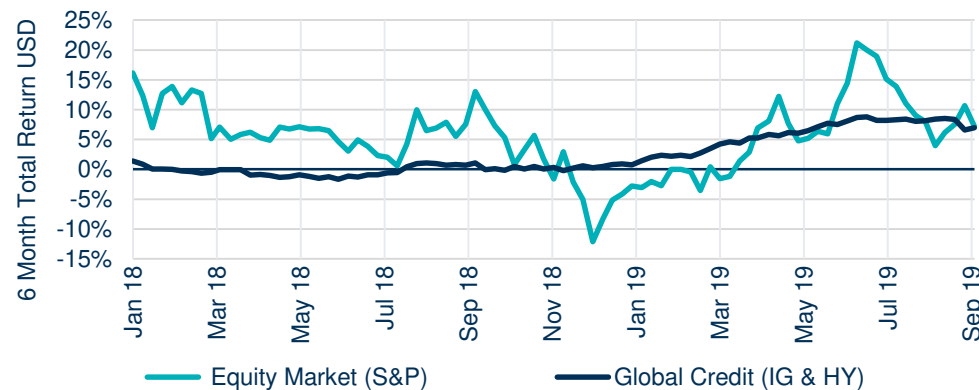
Cash price differential BB-CCC²



CDS cash basis²

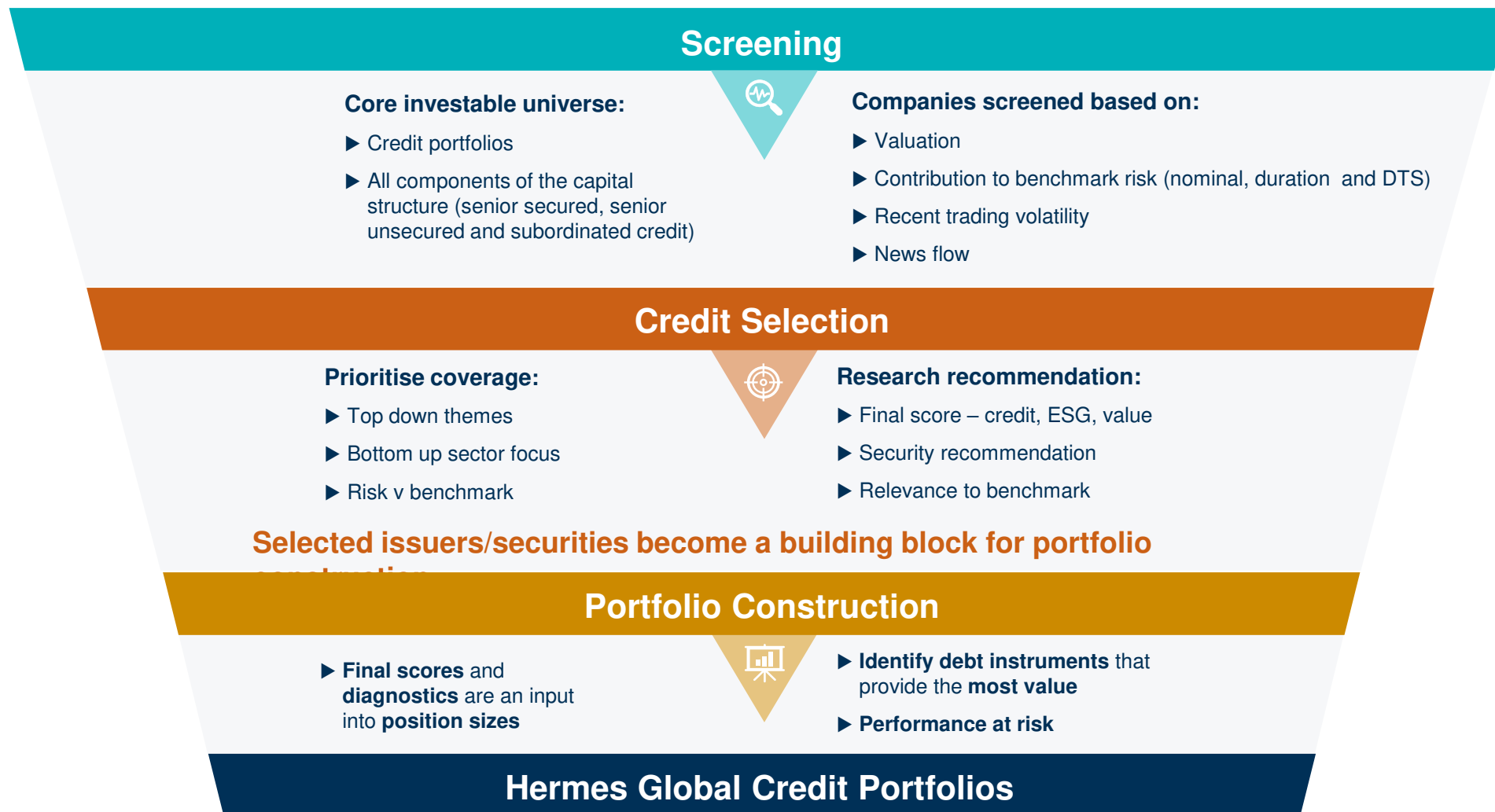


Equity v credit⁴



Source: ¹ Hermes Credit as at 14 September 2018. ² Hermes Credit, ICE Bond Indices as at 27 September 2019. ³ Hermes and Bloomberg as at 13 May 2019. ⁴ Hermes Credit as at 20 September 2019.

Investment process

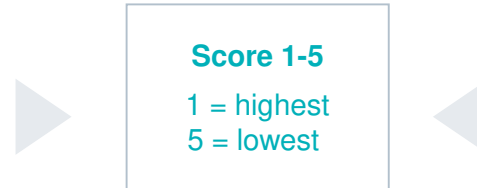


Scoring ESG risk at the company level

The Tear Sheet combines credit, ESG and valuation analysis

Research outcomes

- ▶ Financial risks
- ▶ Operating risks
- ▶ ESG risks
- ▶ Investment and ESG scores



Relative-value

- ▶ Degree of expected performance v investment universe
- ▶ Bond v loan v CDS
- ▶ EUR v USD v GBP

HERMES INVESTMENT MANAGEMENT												
Hermes Investment Management Credit Research Tear Sheet												
L BRANDS INC Retail March 2, 2017												
Analyst: Ilana Elbim			Tel: 02076802116			Email: ilana.elbim@hermes-investment.com			Coverage Level: 3			
Equity Ticker:	LB US Equity	Corporate Ticker:	LB CORP	CDS Ticker:	CLTD1U5 CORP							
Capital Structure	Commit.	Amt o/s	Gross Lev	Net Lev	Credit Ratings	Moody's	S&P	Fitch	Credit Indicators (12-18 mos)			
Cash & Equivalents		(654)			Corporate Rating	Ba1	BB+	BB+	Probability of Rating Downgrade:	Low		
1st Lien Debt	5,724	2.2x	2.0x		Date	10-Oct-13	13-Jan-11	01-Jul-08	Probability of DG to HY:	NA		
Senior Debt	-	2.2x	2.0x		Outlook	STABLE	STABLE	STABLE	Probability of Default:	Low		
Sub Debt	-	2.2x	2.0x		Date	07-Mar-11	24-Oct-11	22-Jul-10	Event Risk:	Low		
Net Debt	5,070	2.2x	2.0x		Sr Unsecured Rating	Ba1		BB+	Liquidity Risk:	Low		
Market Cap	14,581		5.6x		Date	10-Oct-13			Credit Direction	Declining		
Enterprise Value	19,653		7.6x		Short Term Rating	NP	NR	WD	Final Score:	3		
Last Fiscal Year End:	31-Jan-17	Country:	US	Stock Price:	50.99	MTD	-8.04%	Internal Credit Score:	3	3YR CDS	67	
Next Reporting Date:	17-May-17	Reporting Currency:	USDm	52 Wk High	88.77	YTD	-33.78%	Internal Value Score:	2	5YR CDS	205	
Company Contact:				52 Wk Low	47.93	LTM	-38.80%	ESG Score	3	7YR CDS	260	
BUSINESS DESCRIPTION												
L Brands, Inc. sells women's apparel and beauty products. The Company offers various products including women's apparel, women's lingerie, beauty and personal care products, home fragrances, and other related products and accessories. L Brands serves customers in the United States, Canada, and the United Kingdom through specialty retail stores, websites, and catalogues.												
STRENGTHS / OPPORTUNITIES						WEAKNESSES / RISKS						
1) Strong market share and robust brand awareness 2) high profit margin vs peers 3) No upcoming maturity, good liquidity 4) 5)						1) Challenging US retail trends putting pressure on footwear 2) New promotion strategy and exit of some segments to add pressure in the short term 3) Guidance for 2017 is weak (weaker FCF, low comp sales,...) 4) Use of excess cash skewed towards shareholder distribution 5) No intention to target IG						
TERM LOANS												
LB REV 1L USD	USD	1,000		May-22	L+150							
na	na	na	na	NC	Invalid Sec	na	na	NR/NR	BBB-/S	na	na	na
CASH BONDS												
LB 8 1/2 06/15/19	USD	500	Ba1/s	BB+/s	NC	NC	2.08	-	112.63	2.76	2.76	155
LB 7 05/01/20	USD	400	Ba1/s	BB+/s	NC	NC	2.81	-	110.25	3.54	3.54	212
LB 6 5/8 04/01/21	USD	1,000	Ba1/s	BB+/s	NC	NC	3.53	-	110.40	3.85	3.85	224
LB 5 5/8 02/15/22	USD	1,000	Ba1/s	BB+/s	NC	NC	4.34	-	104.90	4.51	4.51	272

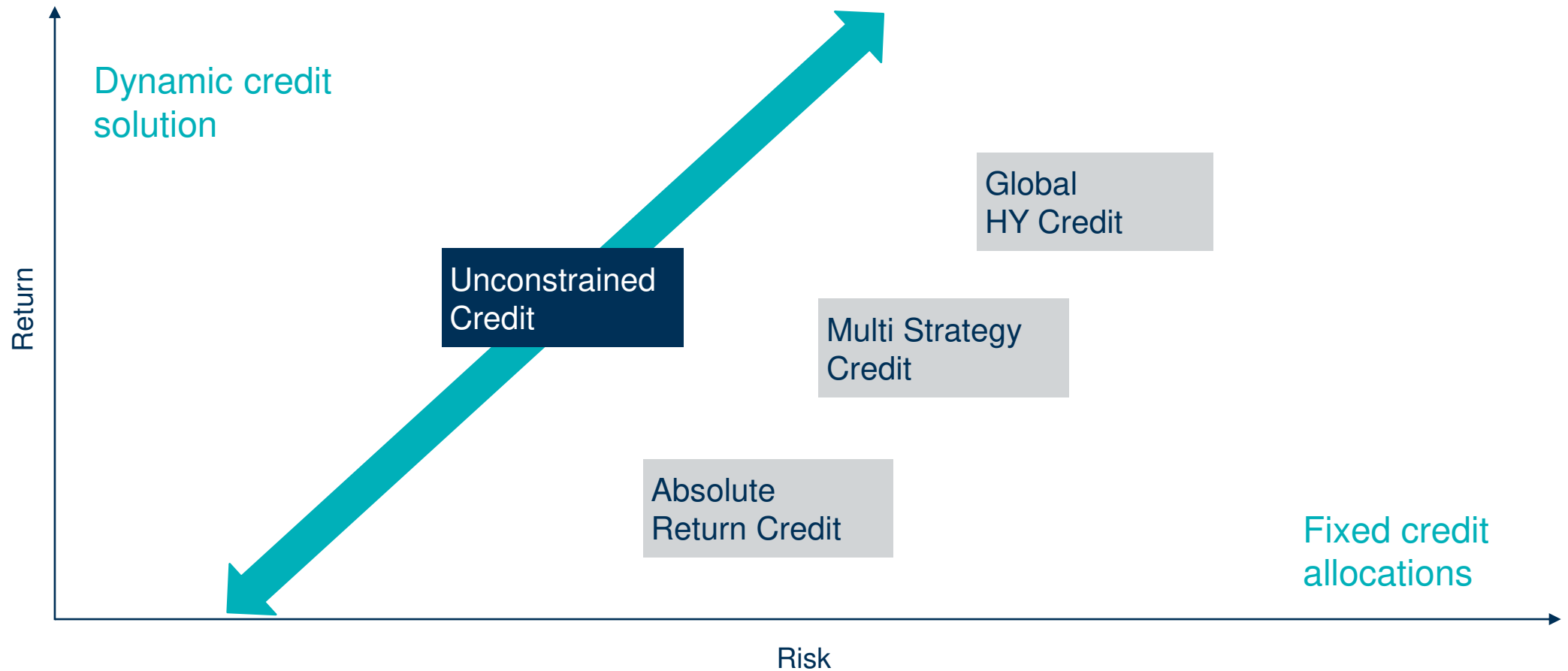
ESG Score
1-5 credit score

Cash, loan and
CDS valuations

Source: Hermes. Model data for illustrative purposes only.

Hermes credit strategies

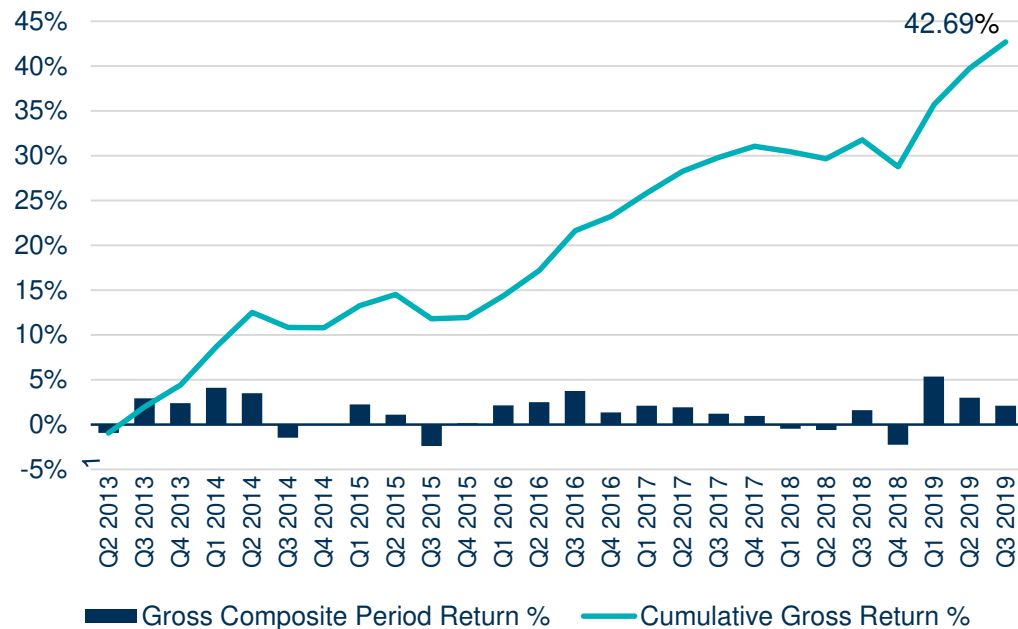
Diversification to concentration – US\$3.3 billion invested across the range



Source: Hermes as at 30 September 2019.

Multi Strategy Credit

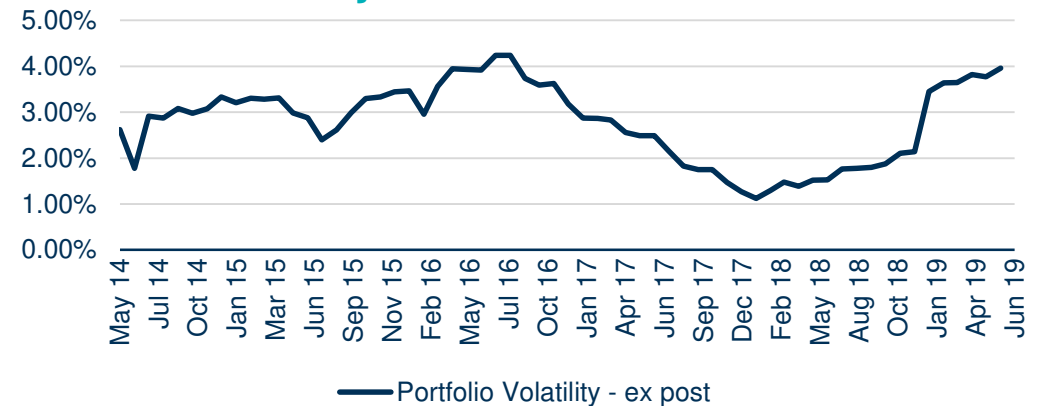
Strategy performance



Rolling year performance (%)

	30/09/2018 to 30/09/2019	30/09/2017 to 30/09/2018	30/09/2016 to 30/09/2017	30/09/2015 to 30/09/2016	30/09/2014 to 30/09/2015
Strategy ²	8.30	1.51	6.73	8.79	0.86

Portfolio volatility³

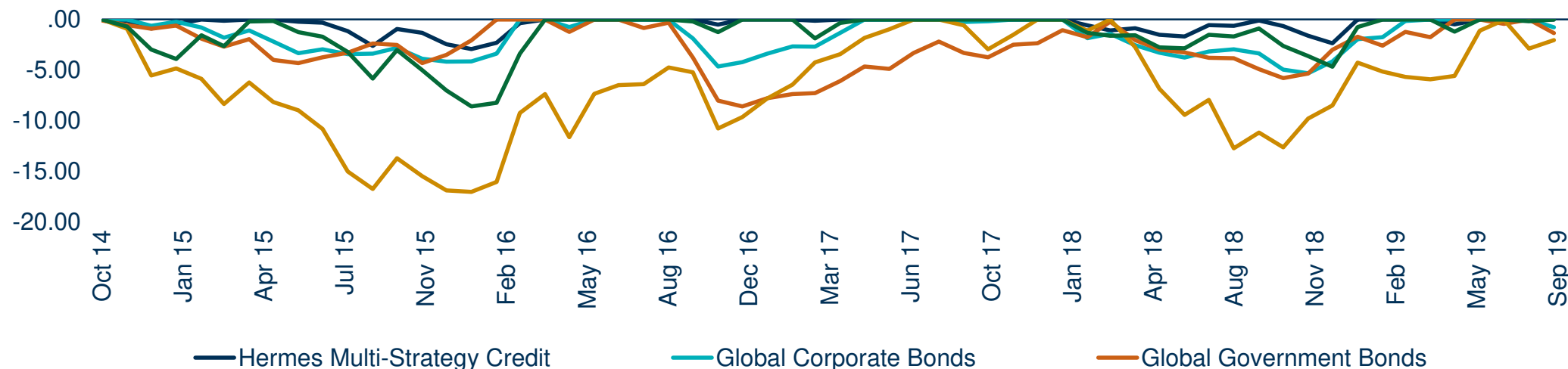


The value of investments and income from them may go down as well as up, and you may not get back the original amount invested. Any investments overseas may be affected by currency exchange rates. Past performance is not a reliable indicator of future results and targets are not guaranteed.

¹ Inception date: 01 June 2013. Performance as at 30 September 2019 in USD, gross of fees. ² Performance shown is of the strategy upon which the Hermes Multi Strategy Credit portfolio is based, in USD gross of fees. Source: Hermes Credit Team. ³ Ex post volatility shown of the representative account within the composite. Source as at 30 June 2019. The information on this slide is the composite and is supplemental to the GIPS® compliant presentation that follows. This strategy does not have a benchmark.

Hermes Multi Strategy Credit Strategy

Max drawdown over past 5 years



	1Y Max drawdown	5Y Max drawdown	1Y Standard deviation	3Y Standard deviation	5Y Standard deviation
Hermes Multi-Strategy Credit	-2.34	-2.92	4.05	2.83	3.15
Bloomberg Barclays Global Aggregate – Corporate	-5.30	-5.30	4.55	4.18	4.02
JPM GBI	-8.30	-8.59	5.19	5.39	5.13
JPM GBI-EM Broad Diversified	-12.71	-17.02	8.21	8.73	9.46
ICE BofAML Global High Yield	-4.67	-8.57	6.05	4.73	5.84

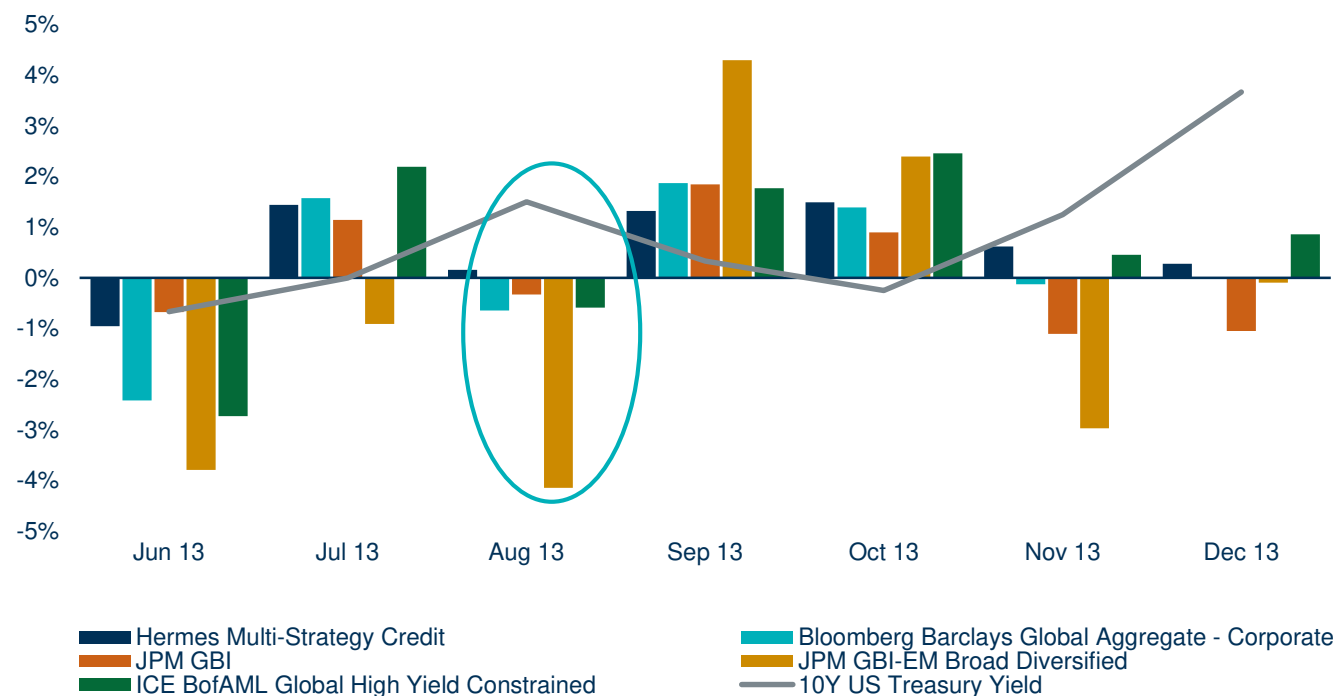
Past performance is not a reliable indicator of future returns. The value of investments and income from them may go down as well as up, and you may not get back the original amount invested.

Source: Evestment. Hermes Multi Strategy Credit Strategy, USD, gross of fees. Performance from 30 September 2014 to 30 September 2019. Indices used (from left to right): Bloomberg Barclays Global Aggregate – Corporate, JPM GBI, JPM GBI-EM Broad Diversified, ICE BofAML Global High Yield Constrained, ICE BofAML 0-5Y US HY Constrained.

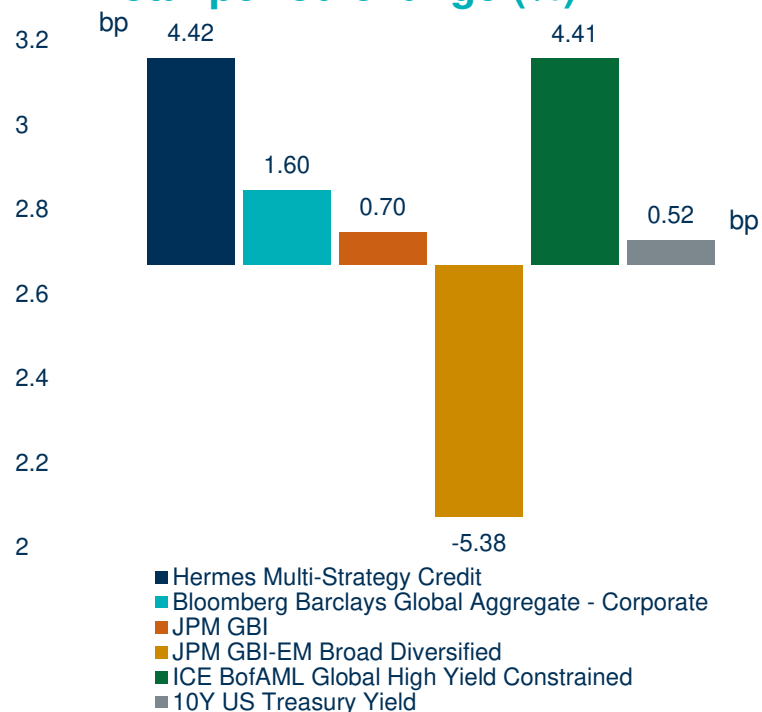
Case study – Taper Tantrum

Downside protection in periods of market stress

Composite returns over Taper tantrum



Total period change (%)



Past performance is not a reliable indicator of future returns.

Performance shown is based on the representative fund upon which the Hermes Multi-Strategy Credit Strategy is based.

Source: Evestment. Performance over the Taper Tantrum (between 30 June and 31 December 2013) in USD, gross of fees. Data is supplementary to GIPS® Presentation that follows. As fund inception date is May 2014, composite data used here. Indices used (from top to bottom): Bloomberg Barclays Global Aggregate – Corporate, JPM GBI, JPM GBI-EM Broad Diversified, ICE BofAML Global High Yield Constrained, ICE BofAML 0-5Y US HY Constrained.

Summary

- ▶ Correlation and rate levels make duration dependency a risk
- ▶ High conviction approach allowing for credit selection to be a major component of returns
- ▶ Seeking downside protection through multiple avenues
- ▶ Truly global approach
- ▶ ESG integration is a valuable tool for both downside protection and alpha generation through engagement on key issues that can impact the enterprise value and cash flows

Hermes Multi Strategy

GIPS® Composite

Composite: **Hermes Multi Strategy Credit Hedged to USD**

Creation date: **01 June 2013**

Inception date: **01 June 2013**

All information is quoted in USD

Year	Gross of Fees Return	Net of Fees Return	Benchmark Return	Composite 3-Yr St Dev (%)	Benchmark 3-Yr St Dev (%)	No of Portfolios	Composite Dispersion	USD Total Composite Assets (Million)	% Total Firm Assets
2018	-1.7	-2.4	-	2.7	-	<5	-	1086	3.4
2017	6.3	5.6	-	3.0	-	<5	-	1315	3.8
2016	10.1	9.4	-	3.5	-	<5	-	866	3.0
2015	1.0	0.4	-	-	-	<5	-	767	2.7
2014	6.1	5.4	-	-	-	<5	-	360	0.9
2013*	4.4	4.0	-	-	-	<5	-	40	0.1

*Partial Year Returns for Composites and Benchmark

Hermes Fund Managers Limited claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS® standards. Hermes Fund Managers Limited has been independently verified for the periods 1 January 1998 through 31 December 2018. The verification report is available upon request. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS® standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS® standards. Verification does not ensure the accuracy of any specific composite presentation.

For the purposes of compliance with GIPS®, the firm is defined as Hermes Fund Managers Limited ("Hermes"), an asset management group consisting of a number of subsidiary or affiliate companies. As of 31 December 2009 the Hermes Fund Managers Limited firm definition was broadened to better represent the full range of investment strategies offered. Hermes Investment Management is the brand name for the Hermes group including Hermes Fund Managers Limited. Information about changes is available upon request. Gross of fees returns have been calculated gross of management, custodial fees and reclaimable withholding taxes, but after all trading commissions.

The composite includes all discretionary portfolios following the Hermes Multi Strategy Credit Hedged to USD strategy run by the Hermes Credit team and has an inception date of 1 Jun 2013. The objective of the strategy is designed to target a

return similar to High Yield credit with significantly less overall volatility. The strategy may invest in a broad range of assets, either directly or through the use of derivatives, (including, but not limited to, equities, equity-related securities, eligible CIS and/or financial indices, futures, options, swaps, debt, fx and money markets). The strategy through its investments in FDIs may be leveraged. The composite does not have a benchmark as it is an absolute return strategy. Performance returns shown in USD. The Composite base currency is USD.

The management fee schedule for this strategy is 0.65% per annum.

The standard fees are shown in Part 2A of its Form ADV. For historical fees, please contact Hermes. Net results reflect the above-mentioned fee schedules, actual results may vary for each individual portfolio.

Composite descriptions, along with additional information regarding policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. Where appropriate, composite dispersion is calculated as the asset weighted standard deviation of the annual returns of the constituent portfolios. If a composite consists of less than five portfolios for the full year then no measure of dispersion is shown. The three year annualised standard deviation measures the variability of the composite and benchmark returns over the preceding 36 month period. Standard deviation measures are not shown where there are less than 36 monthly observations available. Standard deviation measures are not required for periods prior to 2011.

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Hermes Investment Management

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Our goal is to help people invest better, retire better and create a better society for all.

Our investment solutions include:

Private markets

Infrastructure, private debt, private equity, commercial and residential real estate

High active share equities

Asia, global emerging markets, Europe, US, global, small and mid-cap and impact

Credit

Absolute return, global high yield, multi strategy, unconstrained, real estate debt and direct lending

Stewardship

Active engagement, advocacy, intelligent voting and sustainable development

Offices

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