Global Asset Management

BlueBay Emerging Market Absolute Return Bond Fund – CAD Hedged

Q3 2017

Quarterly Report

Performance

As of September 30, 2017	Three Month (%)	Year to Date (%)	One Year (%)	Three Year (%)	Five Year (%)	Since Inception* (%)
BlueBay Emerging Market Absolute Return Bond Fund - CAD Hedged	3.40	7.17	5.98	2.55	1.86	2.39

Series F performance, net of fees.
**Inception date is February 2012.*

Market Review

Emerging market (EM) fixed income continued to perform well in the third quarter, against the spectre of rising rates and modest U.S. dollar resurgence. As tensions on the Korean peninsula subsided and the impact of the devastating storms in the Caribbean and Florida was digested, developed government bond yields rose late in the quarter. Despite these core market trends, higher core yields resulted in tighter spreads rather than emerging market price corrections, but did act as a slight headwind to the quarter end.

The new issuance market remained healthy, and September proved to be a busy month of supply in both sovereign and corporate markets. In the corporate space, U.S.$54 billion of paper came to market in September alone, from Asia in particular, including a U.S.$7.3 billion deal from the Postal Bank of China. We will continue to look to participate in these deals on an opportunistic basis in an effort to take advantage of new issuance premia to enhance returns.

While the news flow was dominated by global geopolitical and environmental events, numerous country-specific developments provided investment opportunities. In Argentina, the primaries for the mid-term elections resulted in a significant rejection of Kirchnerism/Peronism, and President Macri's party (Cambiemos) polled well, which is a vote of confidence for the continuation of reforms despite the weak growth of the past two years. This is an important signal that the Argentine people are moving further from the temptations and perils of Peronism, an important development for the medium-term health of the country. These developments had a positive impact on Argentinean sovereign, provincial, and corporate credits.

Another key country focus later in the quarter was South Africa, where President Zuma survived a no-confidence vote, though the defection of between 25 and 30 African National Congress MPs painted the picture of a leader whose power base is gradually eroding. We believe the weak growth and inflation outlook will lead the South African Reserve Bank to cut rates again before year end.

Portfolio Performance

The fund posted strong results this quarter, returning 3.40% as emerging markets continued to enjoy positive market sentiment.

Positive returns were predominantly driven by our high-yielding hard currency sovereign credit exposure, while our local rates, EMFX, and hard currency corporate positions also added to returns. Our short positioning in general detracted from performance over the period, including our macro duration hedges. At a country level, the key contributors from a predominantly sovereign perspective were Argentina, Ukraine, and Egypt.

On the FX side, our positioning in EM currencies and our underweight to core rates also contributed positively, but to a lesser extent. We re-established a short position in the Chinese renminbi during the quarter given the change in the U.S. dollar trend, and maintained a long U.S. dollar, short Asian FX position.

In Argentina, our long positioning was expressed predominantly in sovereign and quasi-sovereign securities. These performed well due to the results of the Argentine primary elections, where a strong showing from President Macri’s Cambiemos party helped ease market concerns over a step back towards Peronism, as noted above.

Over the course of the quarter we significantly reduced our exposure to Turkey. We have been consistently long Turkish sovereign credit and local markets throughout most of 2017, but a combination of increasing concern about the regional security implications of the Kurdish independence referendum and disappointing trade and inflation data has caused us to change this view. We are currently flat Turkish risk for the portfolio. If anything, from here we expect Turkish lira weakness and are looking for potential opportunities to short the currency.

The main detractors from performance this quarter were predominantly short positions in FX, with short positions in the Turkish lira, Mexican peso, and Russian ruble detracting. Positions in CDS were also negative for performance, with positions in Colombia, Mexico, Qatar, Russia, and Saudi Arabia detracting from returns.

Market Outlook

As we enter the fourth quarter, we believe that the trends that have driven strong EM performance for most of the year – namely, strong EM growth and low global inflation – are still in place. The short-term uncertainties that have held sway more recently may do so for a little longer, and we will look to increase exposure should any further price weakness reach attractive levels.

In summary, despite the geopolitical excitement, global economic activity remains on a solid if unexciting trend and global inflation remains low. The upcoming Federal Reserve Symposium at Jackson Hole will give us another glimpse into the thinking of global central bankers, but we expect them to confirm that the quantitative easing exit in Europe and balance sheet reduction in the U.S. will be conducted in a very gradual and transparent manner. Any news on who is likely to replace Janet Yellen as Fed chair could be a market mover, as well as any progress on Capitol Hill toward tax reform. That said, we remain cautiously optimistic and believe emerging market assets have scope for further outperformance.

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