Stratton Street UCITS - NFA Global Bond Fund UI

May 2017

- **Positive month for bond markets: Fund's QDUSD class gained 1.21% and +5.92% YTD**
- **Fed expected to raise rates in June and UST yield curve flattens: Fed 'ahead of the curve'**
- **Treasuries and the Russia holdings amongst the portfolio's top performers**
- **US dollar retreats back to pre US election levels**

Market Comment

May was generally a positive month for bond markets helped by a solid performance from US Treasuries and the VIX index of volatility making what was then new lows albeit with a temporary spike as yet another Brazilian President, this time Michel Termer, faced investigation over bribery allegations. A combination of some mixed US economic data and President Trump's political difficulties dampened expectations for meaningful growth boosting policy initiatives. The US Treasury 10 year yield compressed 8 bps to 2.2% at month end and the Treasury yield curve flattened as a benign inflation picture increased confidence that the Fed is 'ahead of the curve'. The US dollar index retreated 2.15% back to pre US Presidential levels.

The oil price was volatile over the month, rallying ahead of the 172nd OPEC meeting where OPEC and some key non-OPEC countries announced the extension of production cuts; but a lot of hope had built for greater than announced measures and the crude price weakened into month end finishing -2.75% mom. This had little impact on the portfolio's Middle Eastern bonds where most paper remained in demand: the ratings downgrade of Oman by S&P (to BB+) and Qatar by Moody's (from Aa2 to Aa3) had no real impact. China's rating downgrade by Moody's (from Aa3 to A1) also grabbed the headlines briefly but again had negligible impact on pricing.

Portfolio Review

The fund's QDUSD class gained 1.21% net of fees over the month, outperforming the JP Morgan Global Aggregate Bond Index (USD) which gained 0.81% over the same period.

The main contributors to performance came from the fund's holdings in Russia (+0.35%), Qatar (+0.17%), Saudi Arabia (+0.16%) and Mexico (+0.13%). Russian Railways (RZD) 7.487% 2031 was a notable contributor at the individual issuer level adding 0.19% to performance.

The Qatar holdings performed well despite the Moody's downgrade which cited 'a weakening of Qatar's external position and uncertainty of the sustainability of the country's growth model' as the key reasoning. This has not changed our view: we like to look at the asset side of the balance sheet and not just the debt position in isolation hence we look at net foreign assets (NFA) and for us the picture looks a lot less concerning. We remain comfortable with our positions in Qatar as they trade sufficiently 'cheap', even with a downgrade. For example, State of Qatar 6.4% 2040 trades 4.7 notches cheap using an Aa2 equivalent best rating (AA by S&P) and 3.7 notches cheap if we use an Aa3 rating.

In terms of transaction the main changes were to add old favourite quasi-sovereign bonds: Abu Dhabi National Energy Company (TAQA) 6.5% 2036 and Ruwais Power 10.5% 2036. Both A3 rated bonds continue to offer good value with expected returns plus yield in excess of 14%, and the addition of over 2.5 credit notches of protection.

Outlook

For us, June still remains a live meeting for another rate rise. The issue is whether the trajectory for further tightening eases, particularly if the Fed embarks on its gradual balance sheet tightening plan albeit most likely with a data dependent cap on holdings allowed to maturing without reinvestment. May non-farm payrolls were below market expectations but with the unemployment rate at 4.3% the rate of hiring should slow as the labour market slack gets closer to being used up and the Fed is likely to be more concerned about the lack of inflationary pressures. Federal Reserve governor Lael Brainard, a well-established dove, said that 'it will likely be appropriate soon' to adjust the Funds rate but that if soft inflation data persists that it 'would be concerning and, ultimately, could lead me to reassess the appropriate path of policy.' Inflation indicators have so far remained benign: for example, April core PCE is running at 1.5% yoy although the May FOMC statement views inflation as running close to the committee's 2% longer run objective.

In the absence of any detail on Trump's tax reform and fiscal stimulus initiatives and the difficulty of knowing what he can actually get passed by Congress we see little evidence to convince us that US growth can sustainably be boosted back above the 3% level: the structural trends of poor demographics, secular stagnation and elevated global debt levels remain firmly entrenched.

Our view remains that the Fed will remain ahead of the curve and the yield curve will flatten so we continue to favour positioning at the long end. In terms of credit, while spreads in investment grade credit may not tighten significantly from current levels we still see scope for valuation upside by targeting undervalued credits with several notches of credit cushioning versus their rating and which trade on attractive positive yields. The portfolio trades ~3.4 credit notches cheap with a gross redemption yield of 4.15%.

Historical Performance[1]

	2017 %	Inception %
QDUSD	5.92	6.67
QAUSD	5.96	6.46
QDGBP hedged	5.47	6.09
QAEUR hedged	5.11	6.15

Performance Summary[1]

Index	Monthly Return %
Stratton Street UCITS – NFA Global Bond Fund UI QDUSD	1.21
JPMorgan Global Aggregate Bond Index (USD)	0.81

Fund Prices[1]

Institutional Class	Price	Monthly Return %
QDUSD	106.67	1.21
QAUSD	106.46	1.23
QDGBP hedged	106.09	1.12
QAEUR hedged	106.15	1.04

Portfolio Statistics

Gross Redemption Yield	4.15
Gross Running Yield	4.64
Fund NAV (USD Millions)	94.66
Number of holdings	50
Number of countries	14
Duration	9.41

Fund Breakdown

Net Foreign Assets		Entity Type	
Rating	% NAV	Entity	% NAV
7 Star	50.25	Sovereign	26.54
6 Star	14.67	Quasi	55.97
4 Star	13.53	Supra	-
3 Star	18.91	Corporate	14.85
Total	97.36	Total	97.36

Credit Rating	
Rating	% NAV
AAA	3.08
AA	28.67
A	43.01
Baa	22.60
Total	97.36

Portfolio Exposure by Country	% NAV
Abu Dhabi	10.22
Chile	3.06
China	8.92
Hong Kong	1.14
Kuwait	4.05
Mexico	8.25
Norway	2.63
Oman	5.75
Qatar	18.75
Russia	10.47
Saudi Arabia	10.54
Singapore	2.92
United Kingdom	3.92
United States	6.74
Total	97.36

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Share class information

Class	AMC	Minimum Subscription	Subsequent Investment	Front-end load	WKN	ISIN	Bloomberg
QAEUR hedged	0.60%	EUR 500,000	None	Up to 3%	A2AQ20	LU1483930282	SNFAQAE
QAUSD	0.60%	USD 500,000	None	Up to 3%	A2AQ2Z	LU1483930100	SNFAQAU
QDGBP hedged	0.60%	GBP 500,000	None	Up to 3%	A2AQ2Y	LU1483930019	SNFAQDG
QDUSD	0.60%	USD 500,000	None	Up to 3%	A2AQ2W	LU1483929862	SNFAQDU
RDEUR hedged*	1.10%	No minimum	None	Up to 3%	A2AQ22	LU1483930449	TBC

* Class not yet activated but available on demand

Fund Information

Domicile / legal status: Luxembourg / SICAV (UCITS)
Base currency of the Fund: USD
Valuation currency: USD, EUR, GBP (depending on share class)
Valuation/dealing: On every full banking day, which is simultaneously a stock exchange day in Luxembourg, United Kingdom and Frankfurt am Main.
Subscription/withdrawal: 4pm (Lux time) on the business day prior to the relevant Dealing Date
Redemption fee: None
The Company: Stratton Street UCITS
Name of the Sub-Fund: Stratton Street UCITS – NFA Global Bond Fund UI
Asset Manager: Stratton Street Capital LLP
Management Company: Universal-Investment-Luxembourg S.A.
Auditors: KPMG Luxembourg
Custodian: Brown Brothers Harriman (Luxembourg) S.C.A.
Launch Date Fund: 30th November 2016
Launch Date Class: QAEUR hedged & QDGBP hedged 30th November 2016, QDUSD 9th December 2016, QAUSD 13th December 2016

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[1] Source: Bloomberg and Stratton Street calculations. All returns are calculated net of fees and include dividends re-invested, data as at end May-2017.
Past performance is not a reliable indicator of future performance.

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