



PSigma moves into Emerging Market Corporate Credit

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Tom Becket, CIO of PSigma Investment Management comments on why he is adding the Bluebay Emerging Market Corporate Bond Fund to the Buy List:

“We believe that this is an exciting new asset class, which could deliver attractive long term returns for our clients and be a complementary investment to our current fixed interest investments.

The Asset Class: Whether or not “Emerging” is an appropriate term for many of the economies into which this fund invests is a moot point, especially given the better secular growth trends of many of these economic powerhouses. However, “Emerging” is certainly appropriate for this asset class itself. Whilst EM sovereign bonds are a tried and tested asset class in the wider market, EM corporate bonds are relatively much newer and the domain only of adventurous investors and some selective EM sovereign funds, whose mandates allow them to invest in this space. **We believe that Bluebay are the best in the business at this asset class, for reasons I shall set out below.**

The Emerging Market credit universe is still relatively small at about \$600bn in size. Despite the small scale of the asset class, it is extremely well diversified across sectors and countries, allowing fund managers decent alpha generating opportunities. It is also relatively unknown and the lack of dedicated analysts allows plenty of advantages to dedicated investment professionals.

Why Do We Like It?: The EM story has been regurgitated so many times that it has become extremely well known, if still very exciting. Given the high economic growth and evolutionary consumption shift we expect in Emerging Markets over the next decade, coupled with existing low levels of leverage, the potential for profits growth and improved credit ratings is very strong. At the same time, **EM corporate bonds are trading at double the spread of similar rated companies in the Developed Markets, despite the fact they have similar capital structures, higher growth potential and lower leverage. This to us presents attractive opportunities for early investors.**

We also like EM corporate credit because of its lack of duration and interest risk. As you all are fed up hearing, **we do not like conventional sovereign bonds or investment grade credit because of our expectations for interest rates and bond yields to be driven up from ultra-low levels, spurred on by fears over sovereign credit risk and inflation expectations. Relative to government bonds and high quality corporate debt, where there is significant sensitivity to higher rates and where coupon income is currently very low, the 6-8% income from EM credit in a rate insensitive asset class is very attractive.** We believe this will also cause investors who are currently holed up in swollen Developed World credit funds to start examining and flocking to EM credit. We also believe that in an environment of low real rates coupled with macro uncertainty, the attractiveness of the high yields available from EM corporate credit becomes increasingly obvious on a relative value basis.

There are of course risks aplenty, especially with the uncertain future we are currently facing. Of primary importance there are the knock-on pressures from Sovereign Debt risk. With the “Acropolis Now” situation in Greece and the potential for a “domino effect” through the Periphery of Europe all the way to the UK, US and Japan, it is worth paying heed to the issues facing fixed interest investment at present. However, our view is that the relative attractiveness of EM corporate credit, issued by stable, low leveraged companies, generating big profits and paying decent coupons, will be attractive to long term investors.

Bluebay is a hugely impressive fixed interest house, which was founded in 2001 and they currently run over \$34bn AUM. They also have the biggest and most experienced EM corporate credit team, behind which they have committed a great deal of resource and have spent heavily to gain a leading player advantage. They have been investing in EM corporate credit since 2002 and have now built up a dedicated EM team, with 6 portfolio managers and 5 analysts. Bluebay’s long presence in the asset class (2 of them

were some of the first analysts in the asset class) has allowed them to develop long-standing and trusted relationships with both companies and local investment houses, which gives them an extra insight and trading advantage. The team is also able to leverage off of the experience and knowledge of the rest of Bluebay's investment department, which helps to provide a wider understanding of what is going on in global bond and credit markets.

The investment process of Bluebay features around bottom up credit analysis. The team spends a lot of the time on the road, meeting companies and grilling managements. They also focus upon balance sheets, credit term sheets and other documents relating to the company. The meeting with the fund manager, Polina Kurdyavko, was impressive and she spoke passionately about the development of her team and the opportunity they saw in the asset class.

In terms of risk, we believe that this fund should be considered higher risk than developed world corporate bonds and on a par with High Yield credit. This is entirely debatable, however, and it is noticeable that EM corporate bonds held up significantly better than many of their developed world cousins in the miserable days of 2008-9.

In Conclusion, we believe that this is a suitable addition and diversifier to our Fixed Interest / Corporate Bond portfolios. Although the asset class might be extremely volatile for periods, especially after a very strong period of performance, **we believe that this “asset class of tomorrow” could deliver excellent long term returns, whilst also delivering a healthy yield.** We expect this asset class to become increasingly in favour and there is already a great deal of money being raised to chase existing assets. This will encourage new companies to come to the market, allowing experienced and skilled managers a great deal of opportunities to glean performance. **Finally, we believe that this is an enticing way to play long term EM growth, with lower volatility than EM equities.”**

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About PSigma

PSigma Investment Management was established in 2002 by a team of highly experienced investment managers. The business has grown quickly and has been extremely successful in attracting assets under management of £1bn from private clients, charities and self-administered pension schemes. Much of this success is due to PSigma Investment Management being uniquely positioned to utilise the skills of the consulting businesses within the Punter Southall Group, to help it design specific solutions for its clients rather than shoe-horning them into inflexible standard products. PSigma Investment Management is a trading name of PSigma Investment Management Limited which is authorised and regulated by the Financial Services Authority and a member of the IMA. Registered in England and Wales No. 5374633. FSA Registration No: 478840. Registered office: 126 Jermyn Street, London, SW1Y 4UJ. A Punter Southall Group Company.

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