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Baring High Yield Bond Fund

Barings Asia Regional Conference 2015

October 2015

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Why Barings for High Yield

- Global high yield product
  - US, Europe and emerging markets
- Combining top down scenario approach with bottom up dedicated credit analysis
- Disciplined risk management
- Proven long term investment track record

Investment process

Why global high yield?

Total return (%)	US HYB	European HYB	EM HYB	Sterling HYB
2009Q2	22.5	29.1	26.3	34.8
2009Q3	14.5	21.5	17.8	28.7
2009Q4	5.8	4.1	3.4	11.1
2010Q1	4.8	8.3	9.0	14.3
2010Q2	0.0	-2.7	-0.8	-0.4
2010Q3	6.7	9.3	8.6	12.2
2010Q4	3.0	0.2	2.0	-4.5
2011Q1	3.9	3.9	3.1	6.2
2011Q2	1.0	0.5	1.4	0.2
2011Q3	-6.2	-10.6	-11.7	-11.0
2011Q4	6.2	4.6	7.0	2.8
2012Q1	5.0	12.8	9.4	12.8
2012Q2	1.9	-0.6	-0.3	1.1
2012Q3	4.6	7.2	7.5	10.7
2012Q4	3.2	6.6	5.5	8.8
2013Q1	2.8	1.5	1.7	3.5
2013Q2	-1.4	0.8	-4.9	-0.7
2013Q3	2.3	3.8	1.5	4.3
2013Q4	3.5	4.0	2.6	4.1
2014Q1	3.0	3.0	2.1	3.4
2014Q2	2.5	2.3	5.5	2.5
2014Q3	-1.9	-0.6	-2.2	-1.6
2014Q4	-1.1	0.8	-7.1	1.1
2015Q1	2.5	3.1	3.1	3.6
2015Q2	-0.04	-1.1	5.0	0.2
2015Q3	-4.9	-2.2	-5.0	-0.8

Top

Above average

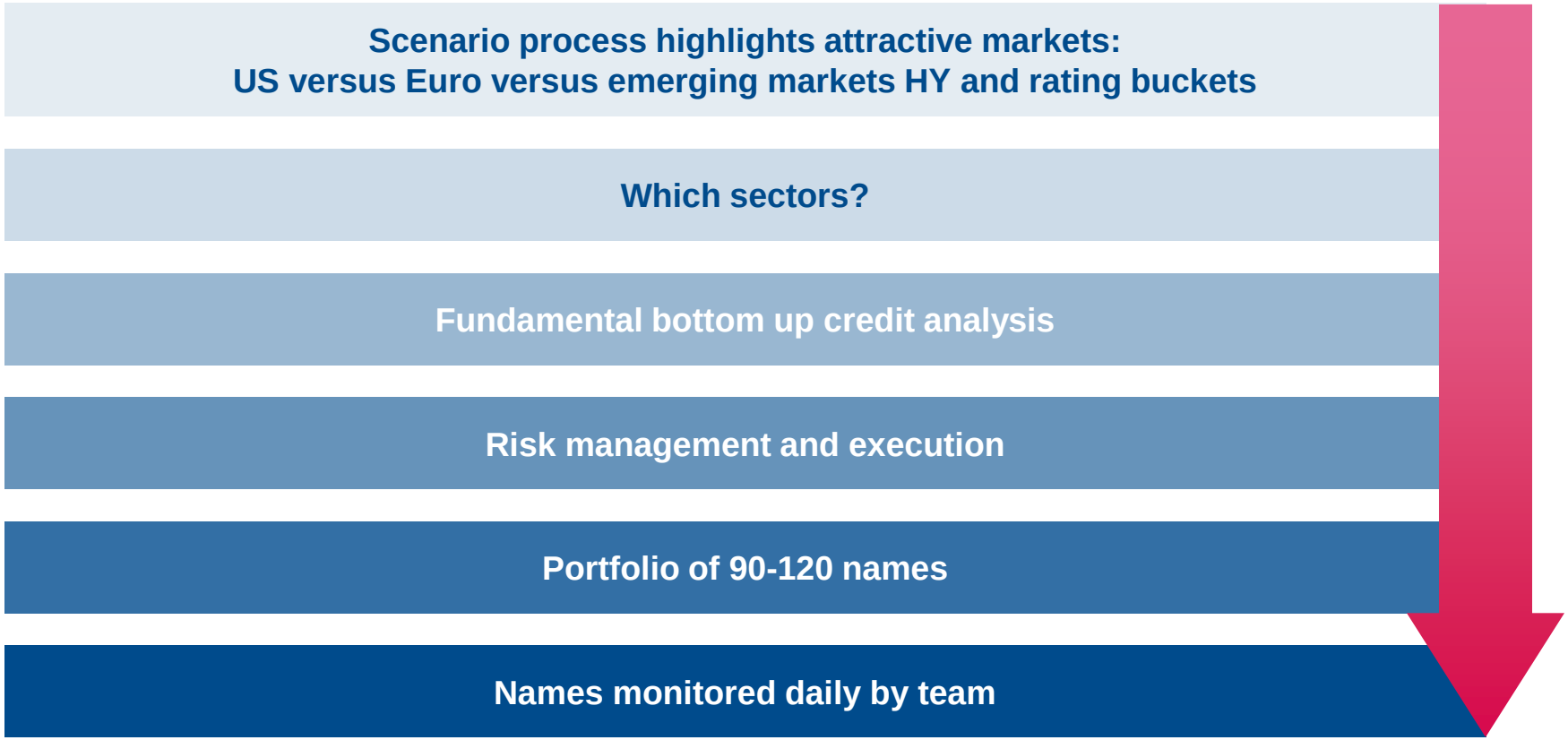
Below average

Bottom

Important to choose the right market at the right time

Source: Bloomberg、all index from BOA-ML HY Bond Index, Local Currency as of September 30, 2015

Investment process
Overview



Source: Baring Asset Management, August 2015

Current scenarios

Scenario 1	**Chinese-led competitive devaluation and rising disinflation**
Scenario 2	**Eurozone joins in global growth upswing**
Scenario 3	**Monetary policy slips behind the curve**

Source: Baring Asset Management, September 2015

Current scenarios

Scenario 1 Chinese-led competitive devaluation and rising disinflation

- The theme of this scenario is predicated upon the emergence of a period of global instability, caused by the outbreak of a currency war as central banks embark upon mutually reinforcing episodes of easy monetary policy. The cumulative effect of these serial policy orientations prevents those economies that would essentially benefit most from their deployment (on a unilateral basis) being able to sustain an adequate differential in monetary policy conditions, relative to their key trading partners.
- Currencies are influenced by the removal of expectation of widening interest rate differentials to the US and some pressure for non-USD currency appreciation is initially seen. However, with global financial conditions deteriorating, global trade volumes declining and persistent demand-deficient disappointments leading to activity and growth levels falling short of market expectations, commodity prices remain weak (negatively affecting G-10 commodity currency valuations). Furthermore, as easier monetary policy conditions are developed elsewhere there is some notable success by policy makers leaning against what otherwise would be a catalyst for USD depreciation. Emerging markets' currency valuations retreat with some stabilisation potential evident in energy deficit countries.

Scenario 2 Eurozone joins in global growth upswing

- This scenario is themed upon a continued recovery in the Eurozone economy under the influence of the plentiful supply of monetary policy accommodation and upon a less aggressive schedule of fiscal consolidation. Constraining factors that ensured that Eurozone economic performance trailed that of the rest of the global economy in 2013/4/5 are removed and the region's recovery becomes much more self-sustaining than previously had been the case.
- Even whilst stronger activity levels are seen and inflation begins to rise, the ECB remains committed to its program of monetary policy easing, through to the end of Q3 2016, in line with its prior communication strategy. Whilst the ECB starts to guide towards expectations of tighter policy being required by the end of 2016, there is no move to actually change monetary policy conditions during the forecast period.

Source: Barings as at September 2015

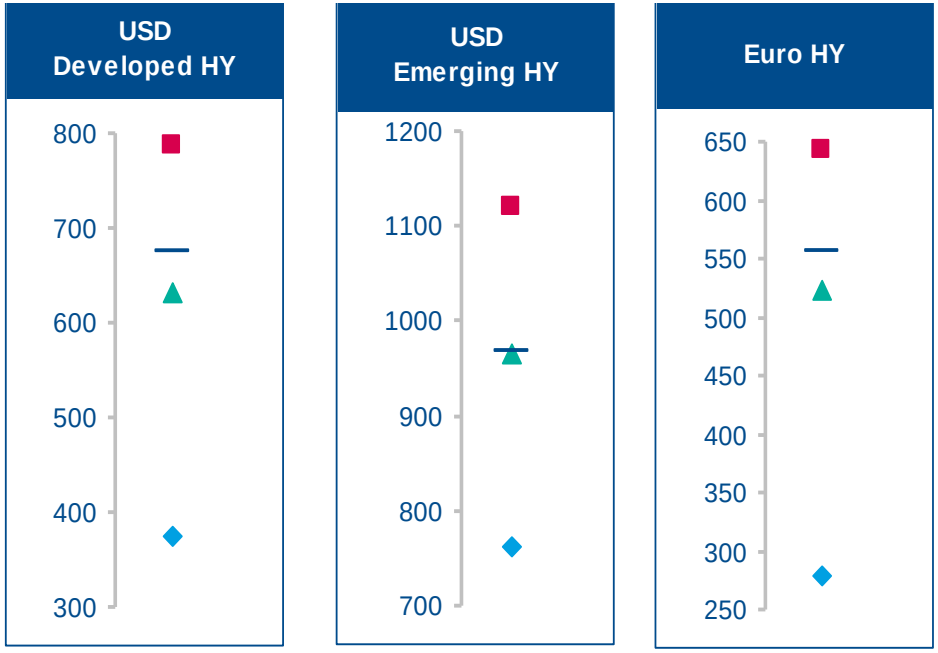
Current scenarios

Scenario 3 Monetary policy slips behind the curve

- This scenario describes a reticent start to the Federal Reserve's upcoming interest rate tightening program: an initial hike is delayed so that it occurs towards and the end of the forecast period and, after a pause, a further hike is possibly delivered. However, the speed of response is too slow to fully counter the growing inflation threat presented by the tightening of the labour market. Whilst the US economy does not develop into an inflationary boom, the prevailing level of nominal GDP growth that is established contains a greater proportion of inflation and a lower level of real growth, relative to current consensus.
- The Federal Reserve eventually charts a new path towards rates normalisation by adopting a more hawkish bias, suggesting that the pace of policy tightening that will continue in the period beyond the forecasting horizon will be more aggressive than that discounted by the market at the point when tightening commences. In the meantime, the US Treasury curve steepens to reflect the market's expectations of a deterioration in inflation risk premia.
- A period of market stress emerges as monetary policy is, for a transitory period, inappropriate for the developing economic conditions. Growth and inflation in Europe and Japan stabilise given that these economies start to benefit from their relatively helpful, easier, monetary and fiscal policy conditions, variously established in the prior period.

Source: Barings as at September 2015

Investment process
High yield credit spreads



- **Scenario 1:** cyclical downturn leads to continuation of easy policy
- **Scenario 2:** Eurozone joins in global growth upswing
- **Scenario 3:** monetary policy slips behind the curve
- **Current**

Identifying the right market and credit rating

Source: Barings, September 2015

Investment process

Fundamental issuer analysis: high yield corporate as an example

Global high yield universe is large**; 2,100 sizeable issues**

- Step 1: Current scenarios forecast positive total returns for **USD denominated credit** in 2 out of 3 scenarios. Opportunity set narrowed down to 1,700 issues. We then filter to remove **emerging market issuers.** We have a preference **'B' rated** credit. Opportunity set narrowed down to 450 **issues**

- Step 2: Favoured sectors are t**elecoms, media and healthcare.** Opportunity set narrowed down to 130 issues from 55 **bond issuers**

- Step 3: These 50 issuers are **screened for valuation and financial liquidity**. Opportunity set narrowed down to **three issuers**: Level 3, Univision and Valeant

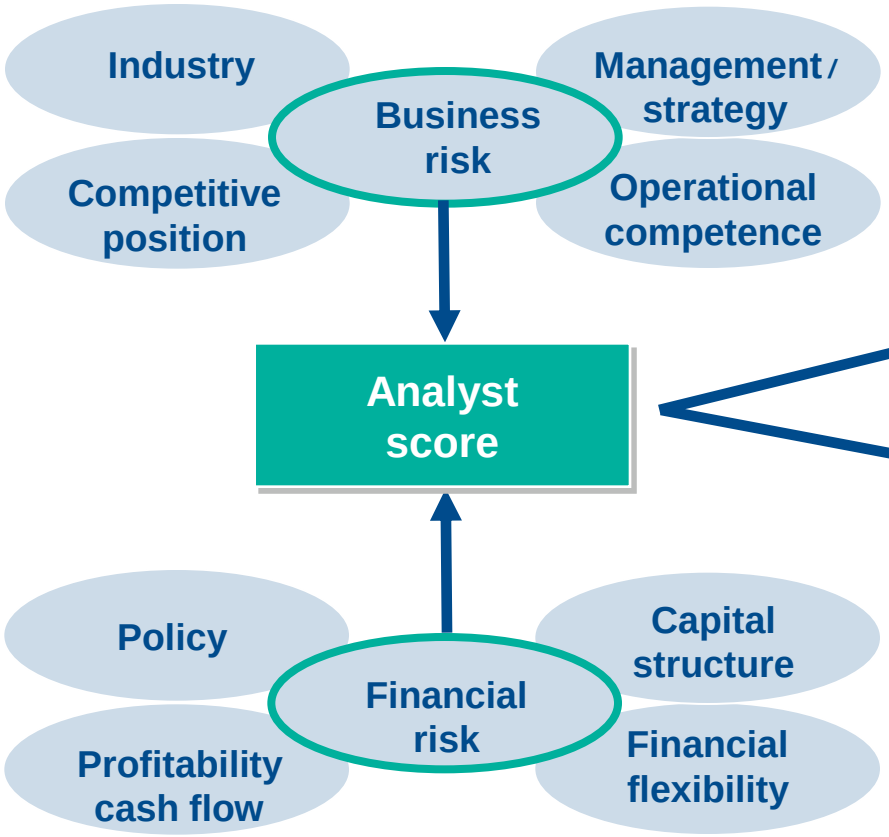
- Step 4: Thorough **bottom-up credit research** conducted on the **three issuers** and discussed at a credit committee. A buy decision followed on Valeant and Univision

Source: Barings, as at September 2015. Please refer to the Important Information Section.

Investment process

Fundamental issuer analysis: high yield corporate

How we research individual companies



Rising				Falling
Credit worthiness				
1	2	**3**	4	5
Corporate quality				
A	**B**	C		
Good				**Bad**

Examples		
Goodyear	2B	BUY
FMG	4B	SELL
Tenet Healthcare	3C	HOLD

Identifying attractive issuers

Source: Baring Asset Management 8 September 2015
Please refer to the Important Information Section

The investment case for high yield
Key considerations

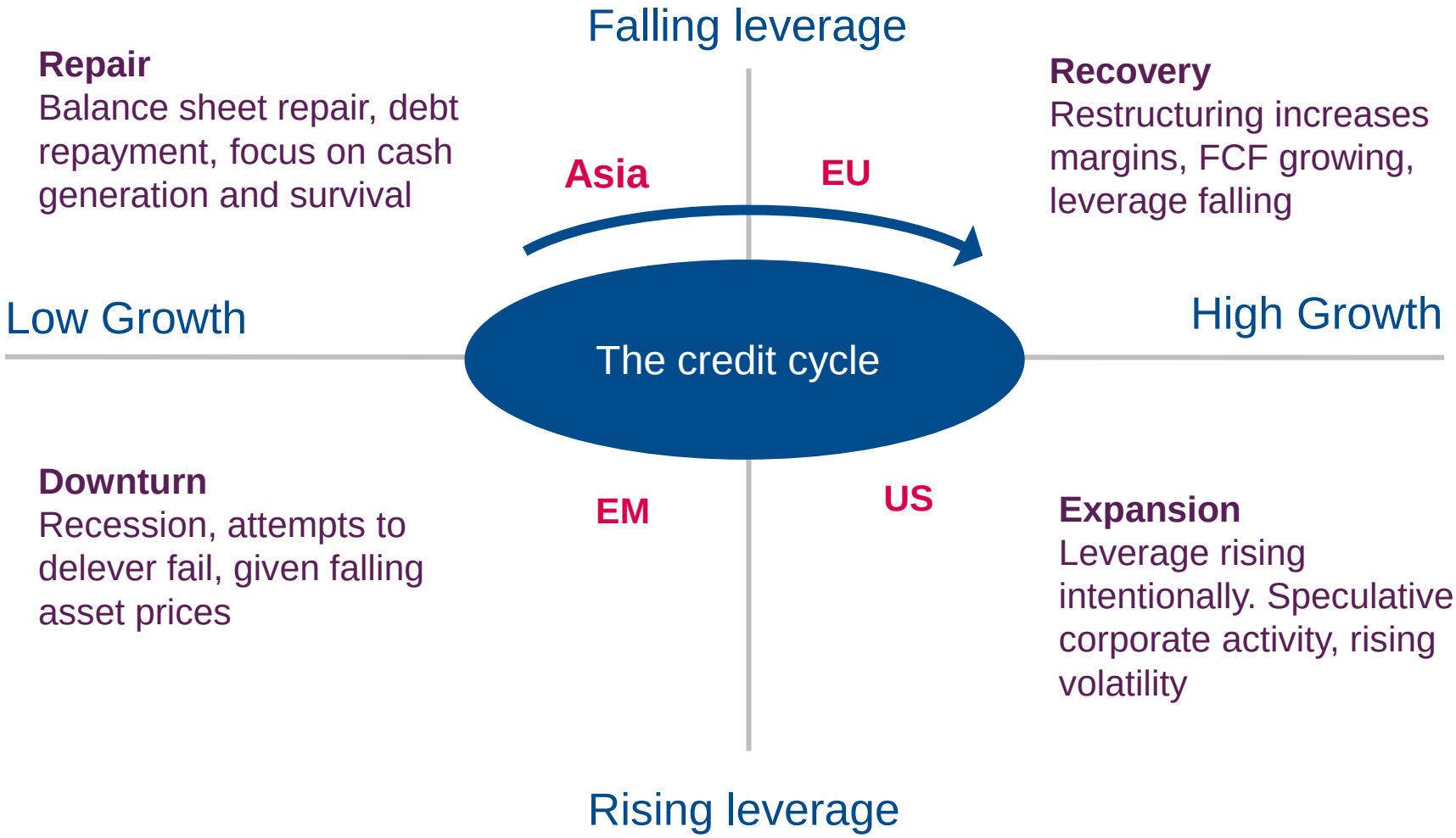
1. **Fundamentals:** balance sheets generally healthy, leverage on the rise but manageable, strong interest coverage, default rates to remain low

2. **Valuations:** yields attractive, with potential for spread tightening

HY remains attractive based on good fundamentals and valuations

Fundamentals

Global credit cycles are not synchronised

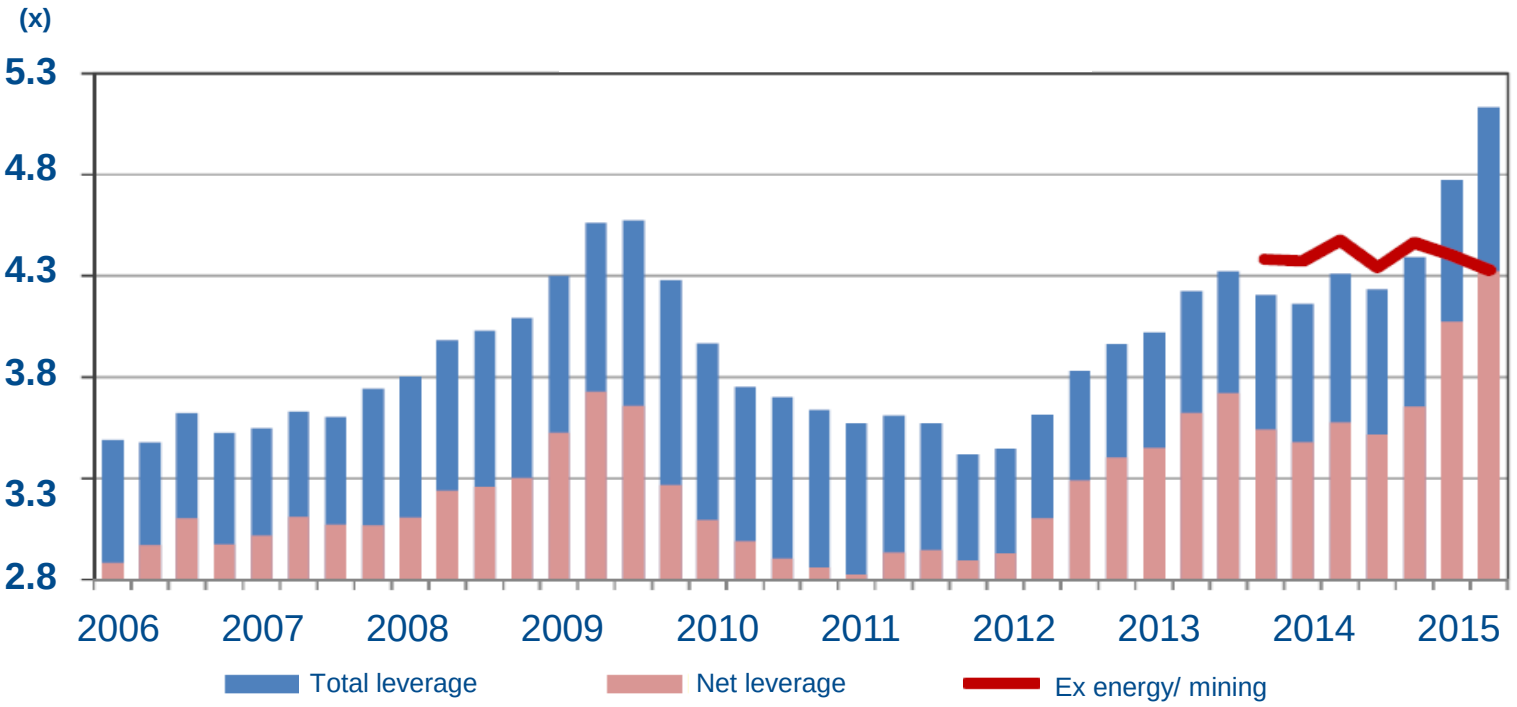


Source: Morgan Stanley Research, Leveraged Finance Strategy - The Yield Book 8 September 2015

Fundamentals
Leverage remains manageable

Gross leverage

(Total debt/ LTM EBITDA, x)

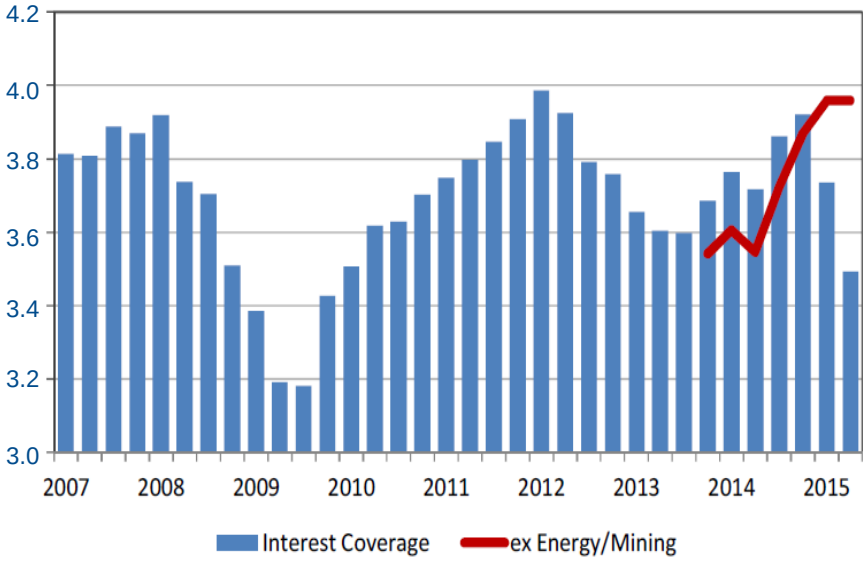


Leverage on the rise, however manageable

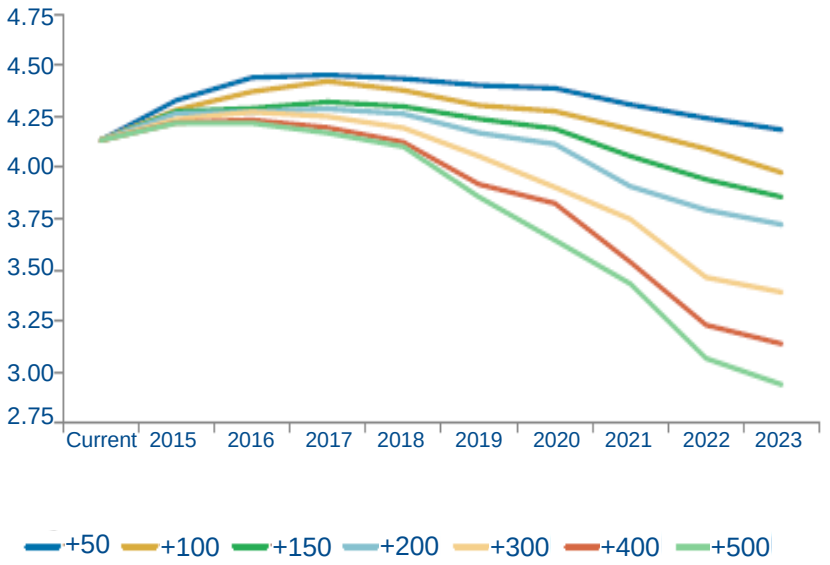
Source: Deutsche Bank, US Corporate Credit Strategy - September 2015

Fundamentals
Strong interest coverage

Interest coverage
(LTM EBITDA/ Net LTM interest expense, x)



HY interest coverage
Over time with shock in rates (x)



Strong interest coverage ratios

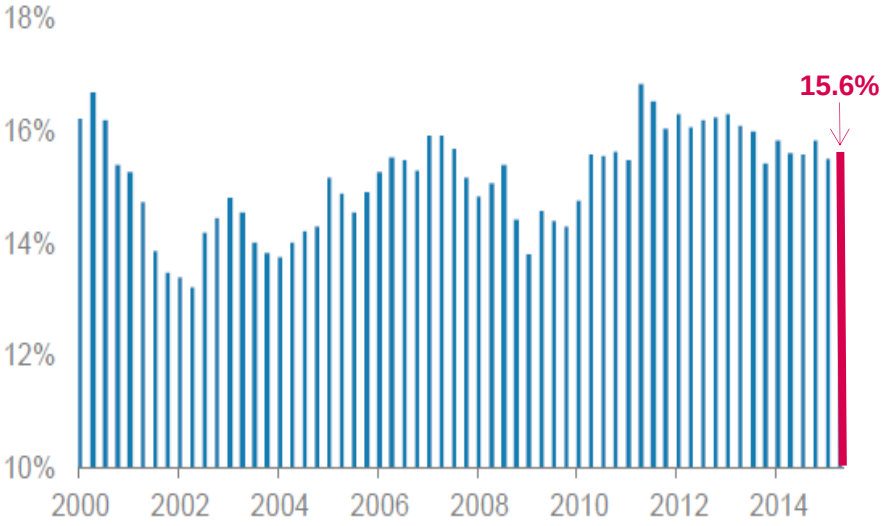
Many years for interest coverage to decline even if rates rise significantly

Source: Deutsche Bank, US Corporate Credit Strategy - September 2015, Morgan Stanley Research, Leverage Finance Chartbook 14 September 2015

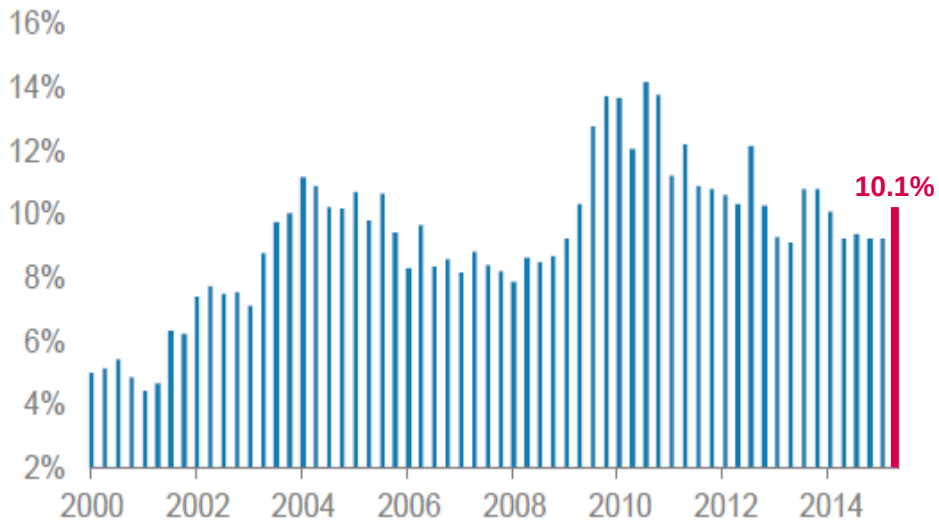
Fundamentals

Margins healthy, cash on balance sheet high

LTM EBITDA margins
(EBITDA/ Total revenue)



Cash/ debt
(Cash on balance sheet over total debt)



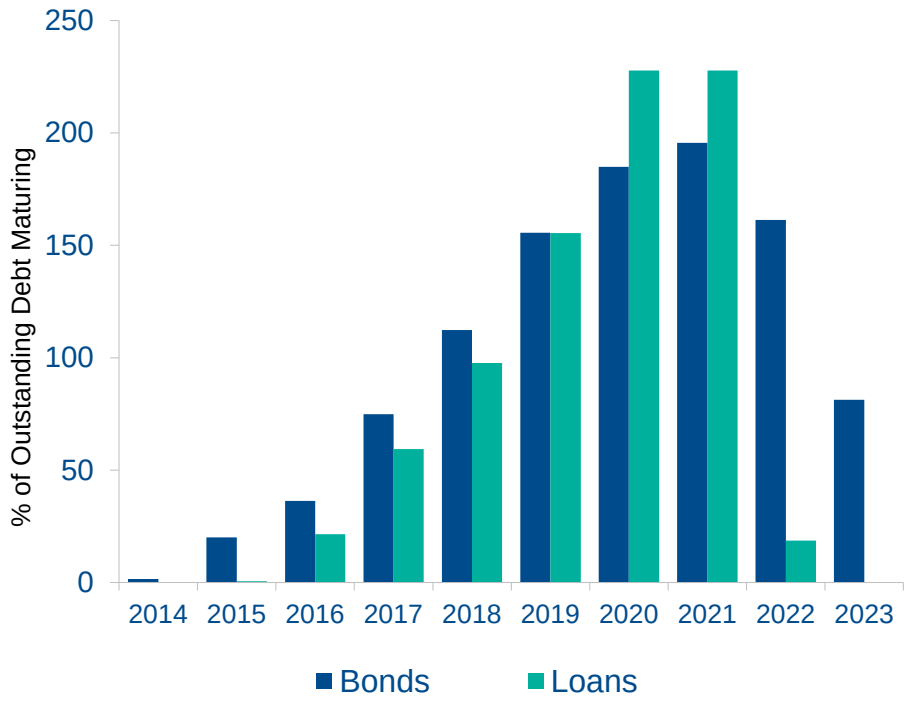
Margins healthy
Ample cash on balance sheets

Source: Morgan Stanley Research, Leverage Finance Chartbook 14 September 2015

Fundamentals
Refinancing not a near term concern

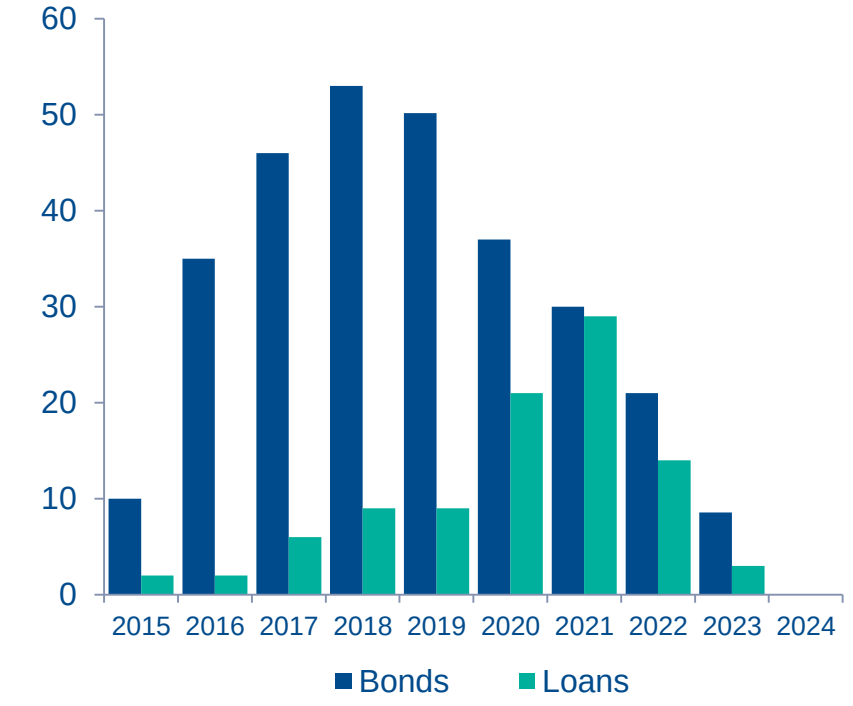
United States

Maturities ($bn)



Europe

Maturities (€bn)



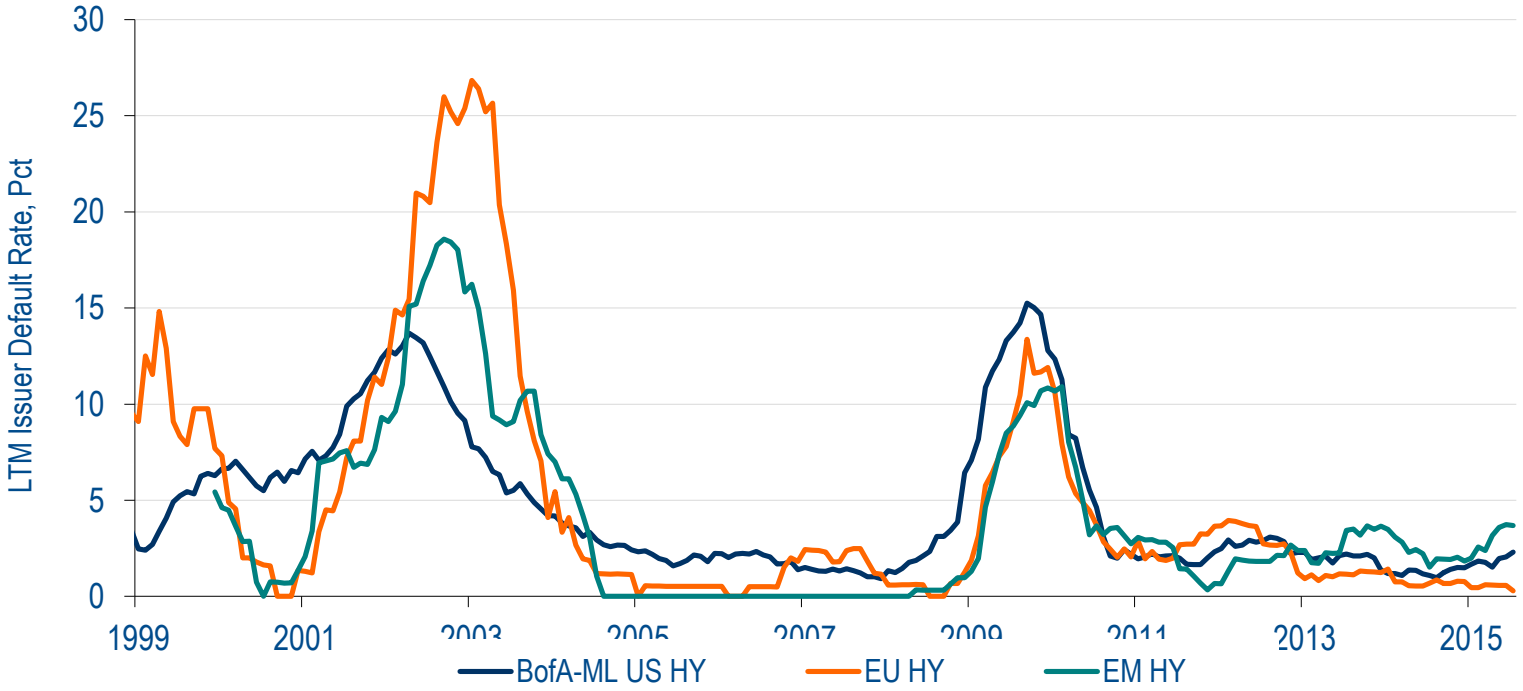
Companies do no have much to refinance near-term

Forecasts are not guaranteed to come to pass
Source: BoA/Merrill Lynch/Bloomberg, 31 August 2015

Fundamentals
Low default rates

Trailing 12 month default rate 2.3% (June 2015)

Moodys projects 2.6% (end 2015)

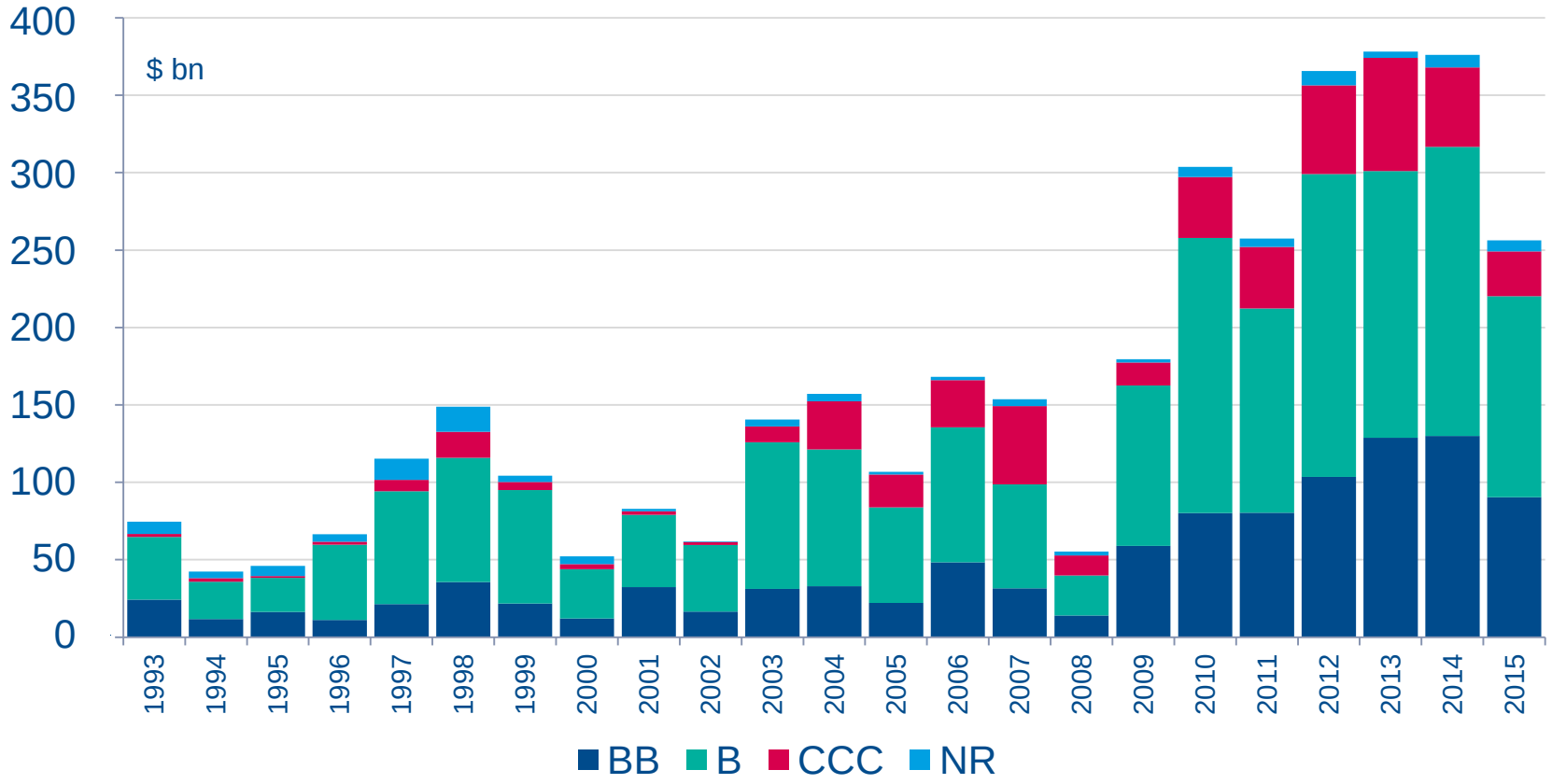


Global default rates to remain low and below average

Source: Bloomberg/BofA Merrill Lynch Global Research, 11 August 2015

Fundamentals

Record high yield issuance

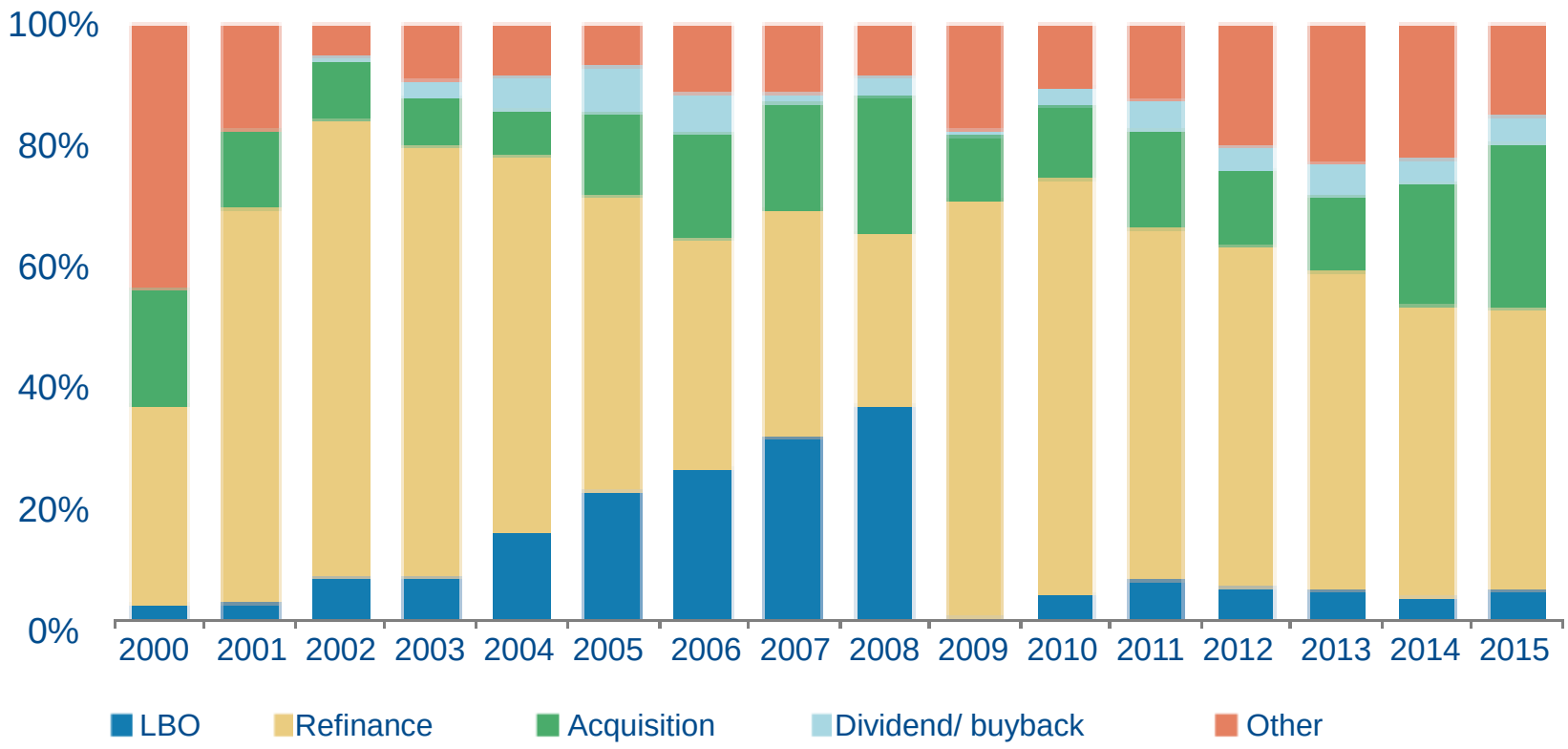


Record high issuance in last three years: mostly in B area, 2015 $256bn

Source: BofA Merrill Lynch Global Research/Bloomberg, 18 September 2015

Fundamentals
New issuance

High yield issuance: use of proceeds

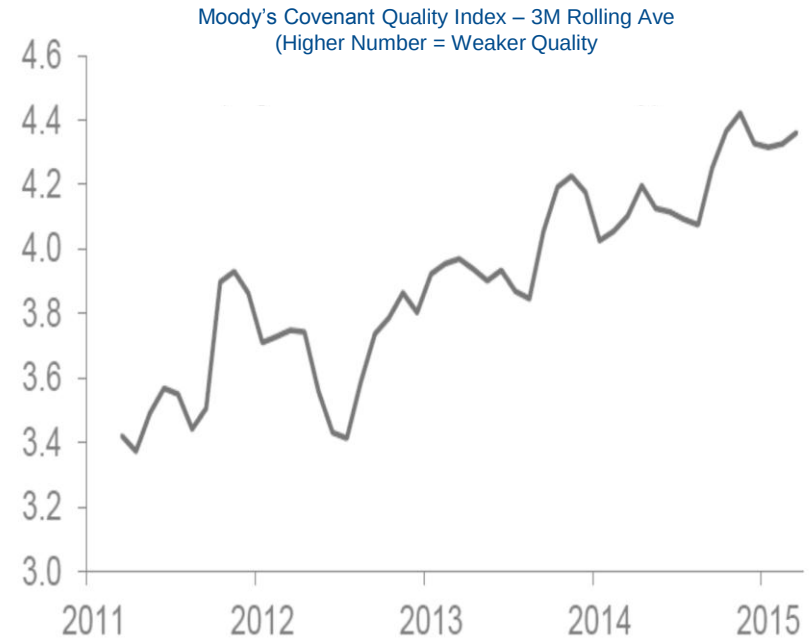


Use of proceeds has been to refinance debt

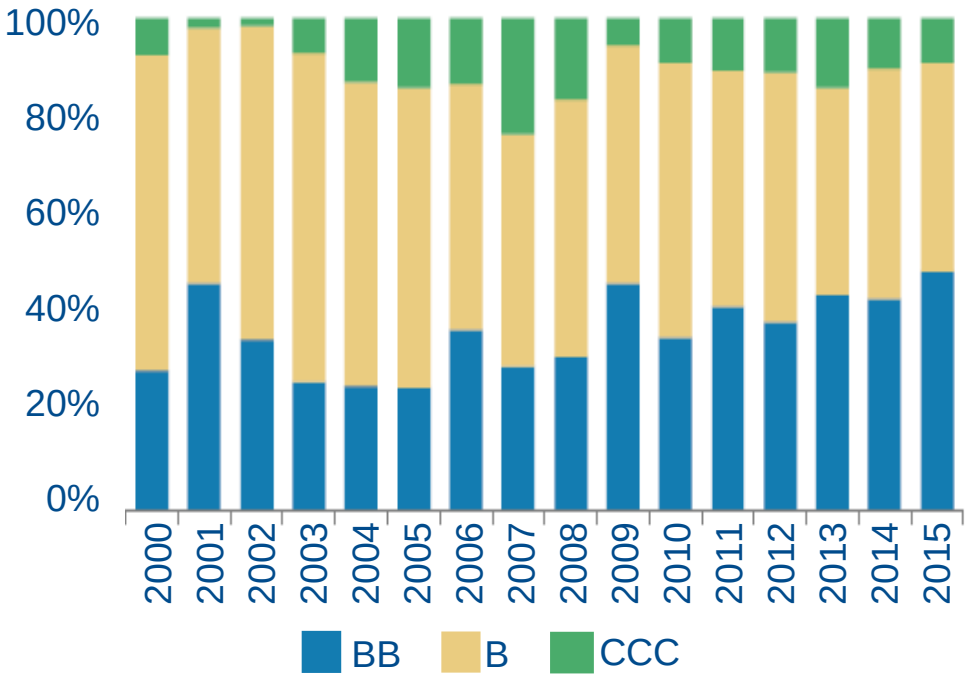
Source: Morgan Stanley Research, Leverage Finance Chartbook 14 September 2015

Fundamentals
Deterioration in quality

High yield covenant quality has weakened



High yield issuance by rating category



Low quality issuance should eventually lead to higher defaults

Source: Morgan Stanley, Leveraged Finance Insights, as at 24 April 2015 / Morgan Stanley Research, Leverage Finance Chartbook 14 September 2015

Valuations

Fixed income menu: yields on offer

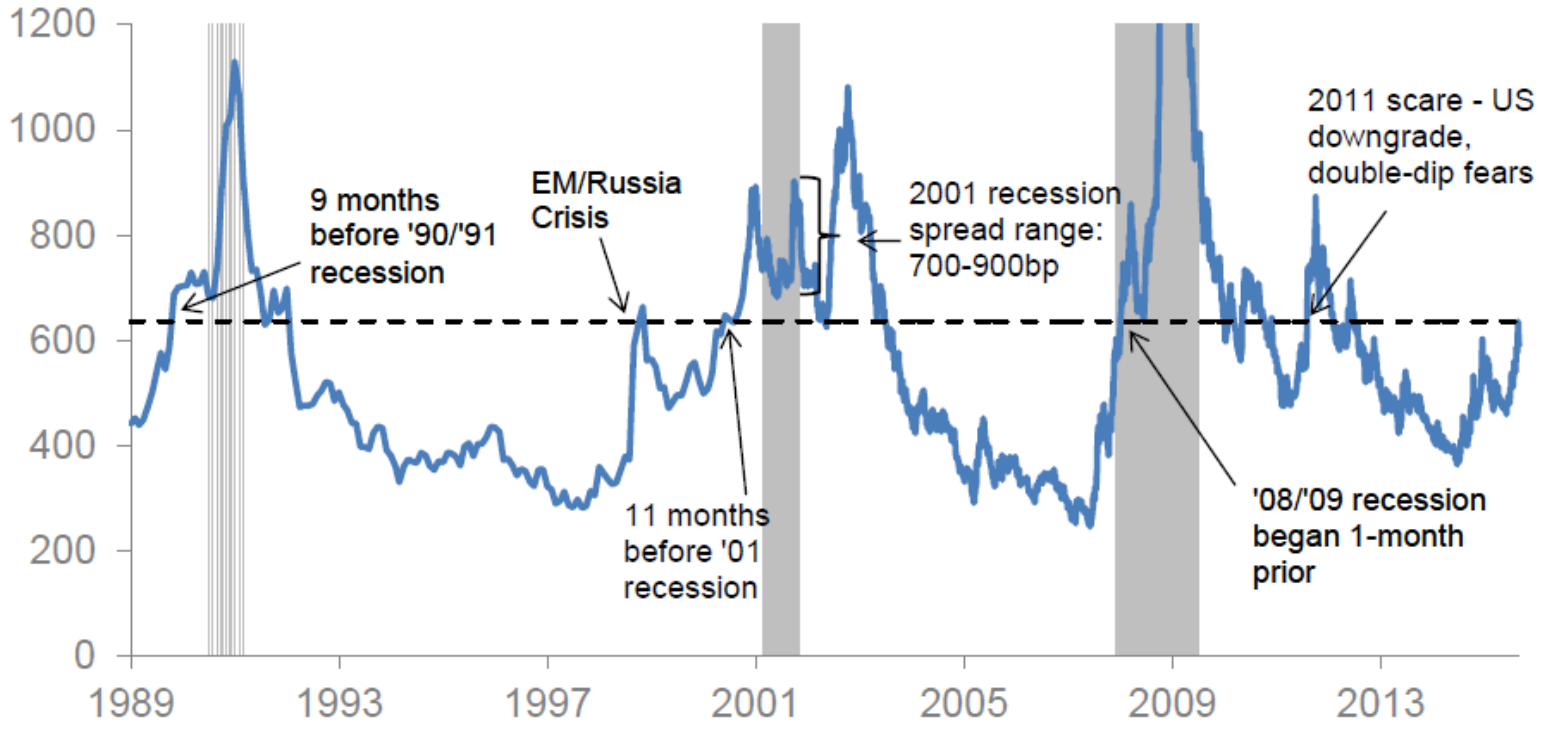
Asset class	YTW (%)	Duration (years)
EM HY	10.1	3.7
US HY	7.9	4.4
Europe HY	5.6	3.7
US IG	3.4	6.8
EUR IG	1.5	5.0
US TSY (5yr)	1.4	4.8
German Bund (5yr)	0.0	5.0

High yield attractive

Source: Bloomberg, as at 29 September 2015

Valuations

Periods in time high yield traded around 600bp while spreads were widening

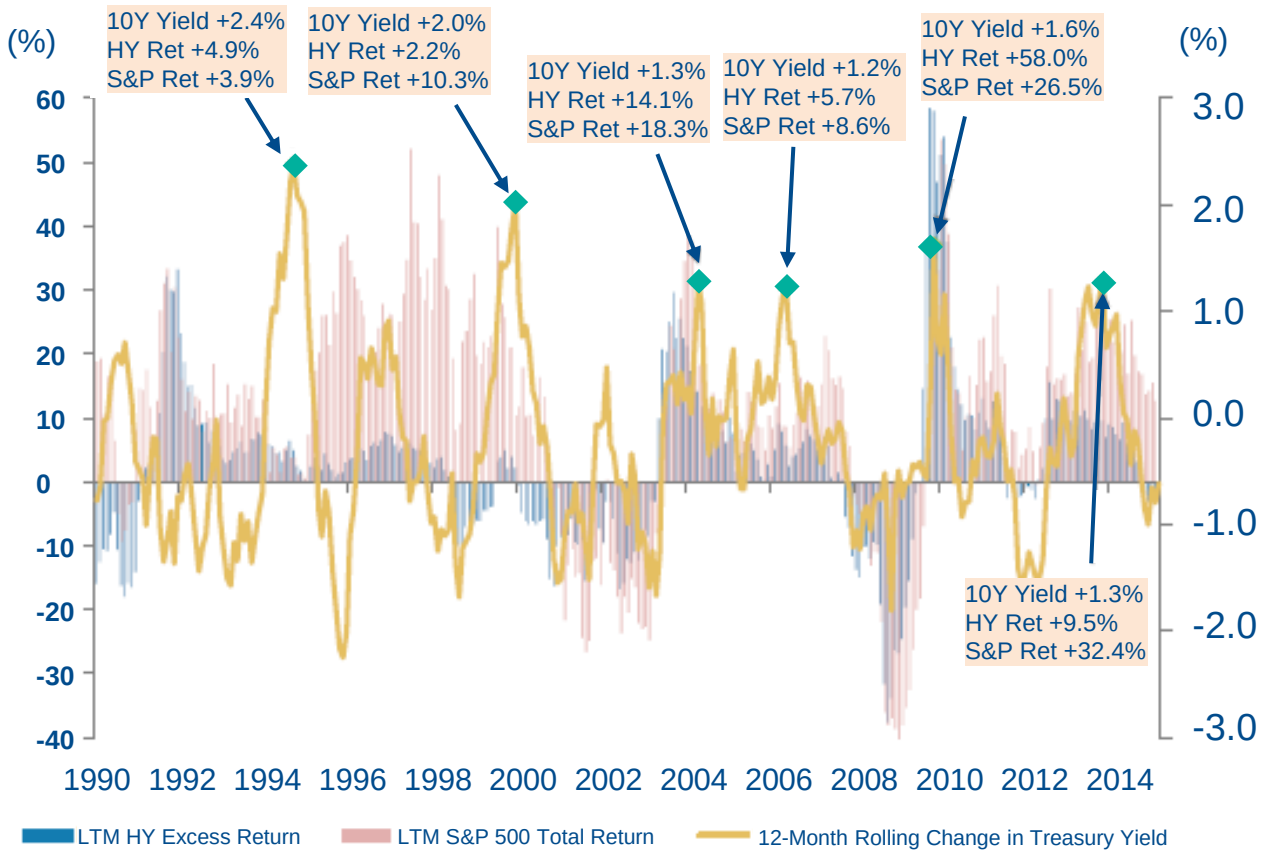


Valuations now much cheaper than in past rate hike cycles: versus 450bps (June 04) and 350bps (Feb 94)

Source: Morgan Stanley, Leveraged Finance Strategy Book, as at 8 September 2015

Valuations

High yield credit and S&P 500 returns in rising rate environments



Rising rates historically not a big issue for high yield

Source: Morgan Stanley, Leveraged Finance Strategy Book, as at 8 September 2015

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Section 4

Positioning for 2015

1. US
2. Emerging markets
3. B
4. Stabilisation in energy valuations

1. US high yield

US HY – EUR HY OAS

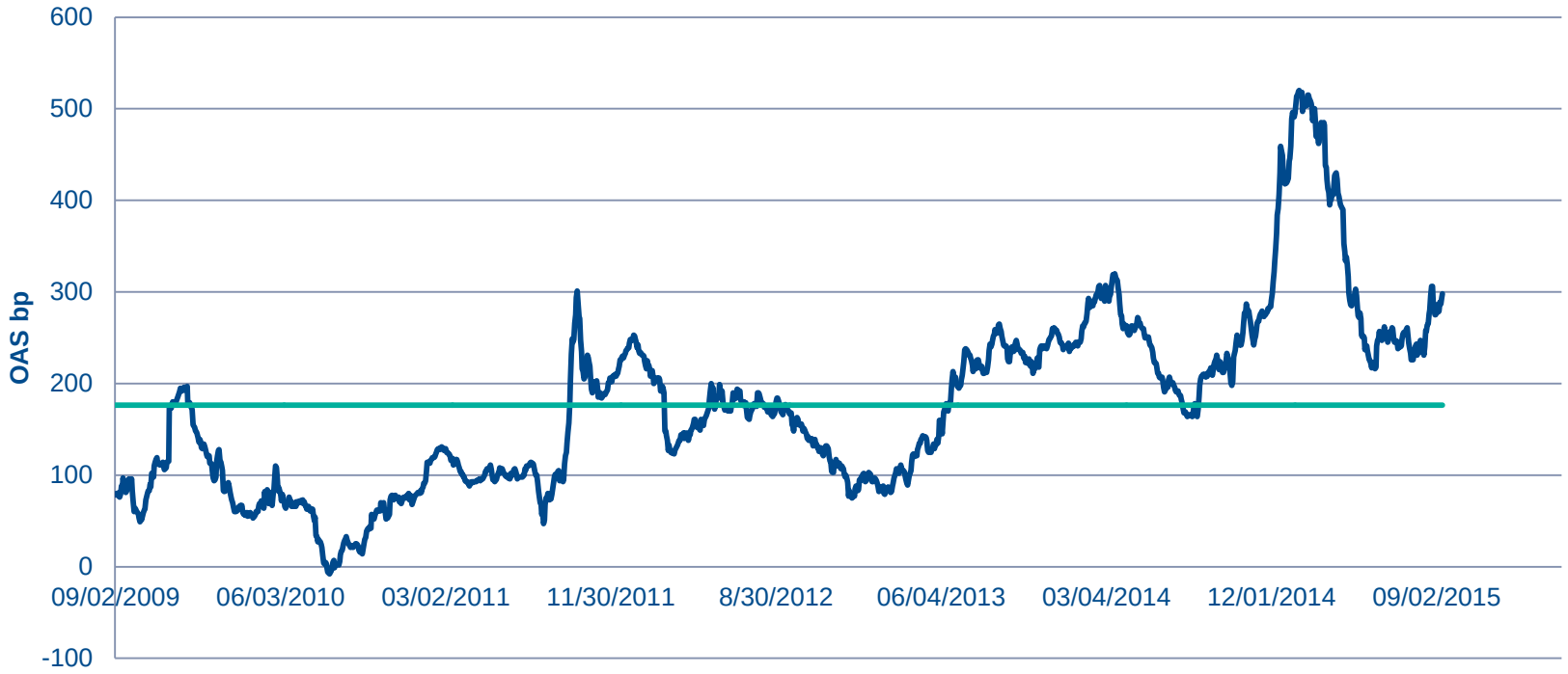


US offers value relative to Europe
Differential close to extreme levels

Source: Barings/Bloomberg, as at 11 September 2015

2. Emerging markets high yield

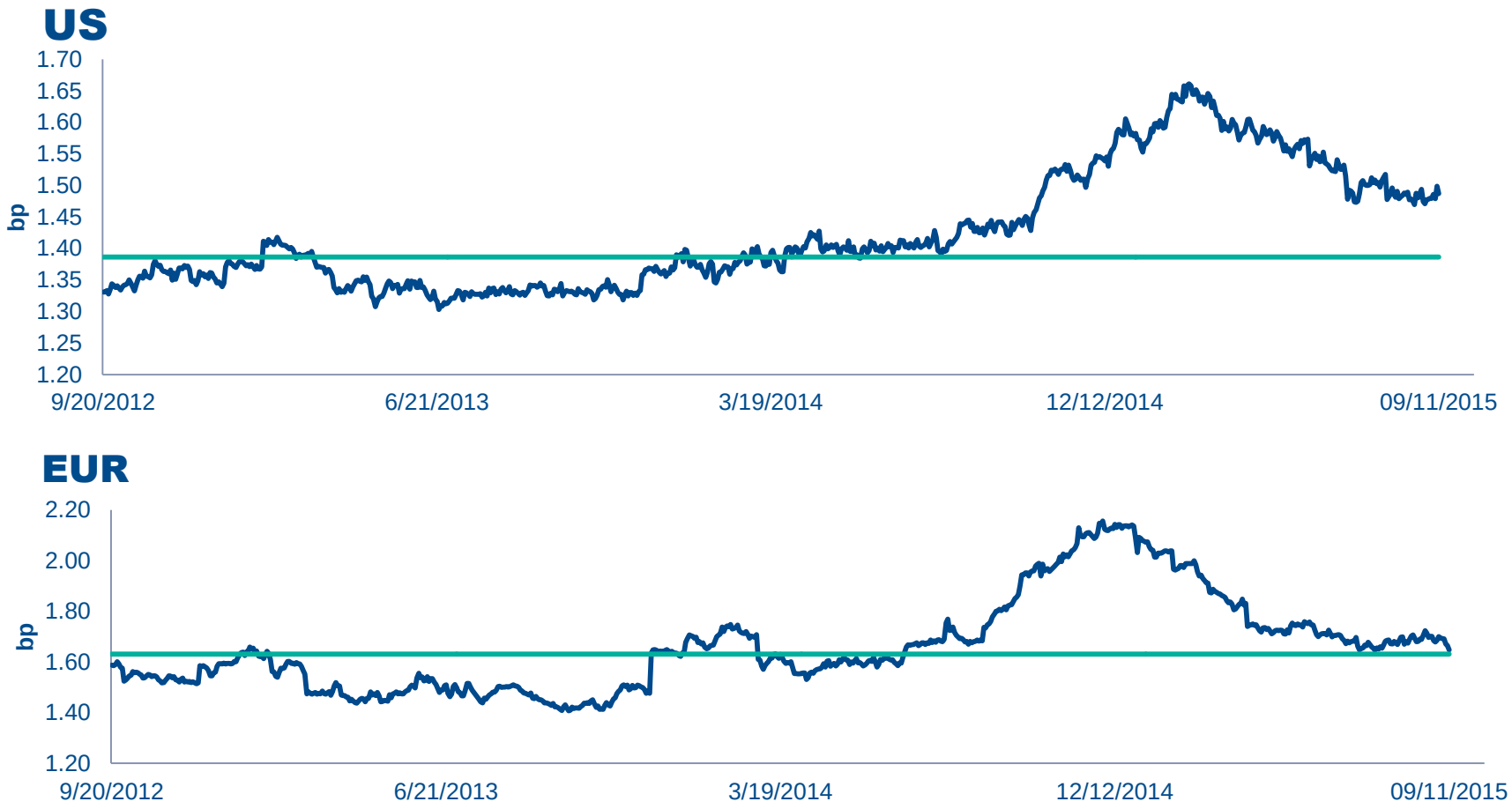
OAS: EM versus US



Emerging high yield valuations still at attractive levels, despite recent recovery

Source: Barings/Bloomberg, as at 11 September 2015

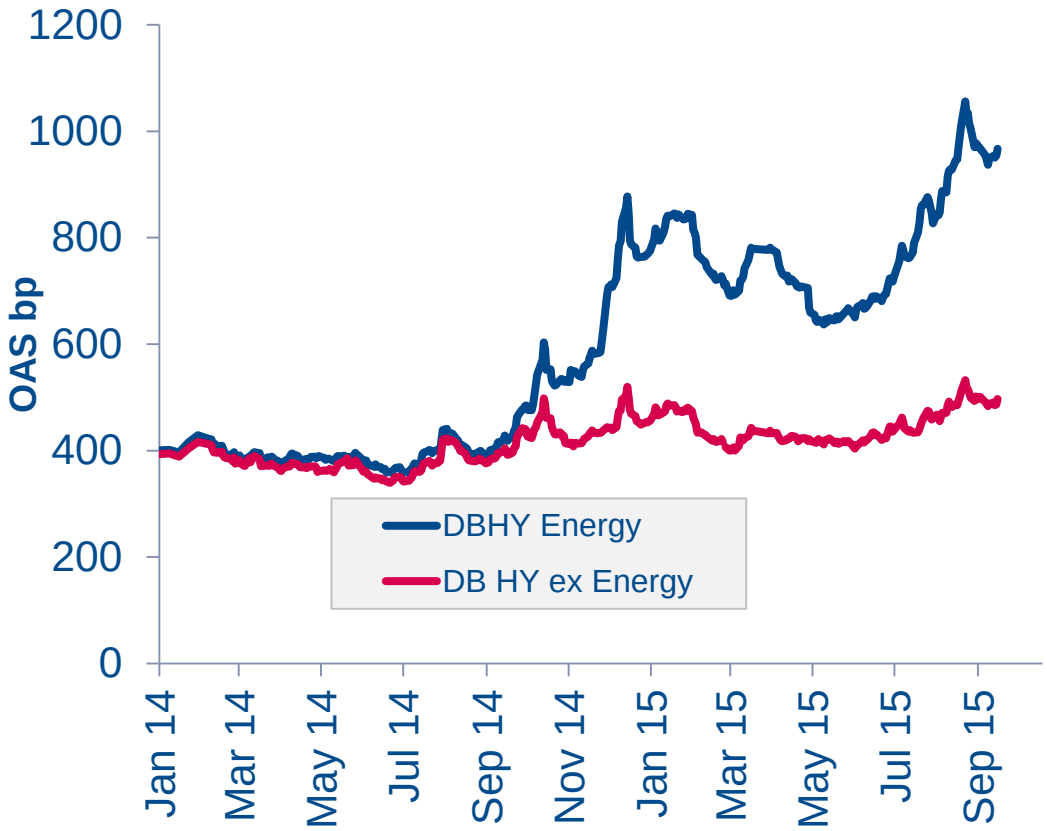
3. B versus BB OAS



Single B rated in the US looks good value with room for outperformance

Source: Barings/Bloomberg, as at 11 September 2015

4. Energy - valuation



- Valuations in energy at distressed levels
- Many companies have hedged oil price for 2015, problems more likely in 2016
- Default rates in energy will rise
- We are comfortable with the names we hold

There will be winners and losers

Source: Bloomberg, as at 17 September 2015

4. Energy - what are spreads pricing in?

Implied sector 5 year cumulative default rate

Assumed recovery rate	High yield energy spread										
	650bp	700bp	750bp	800bp	850bp	900bp	950bp	1,000bp	1,050bp	1,100bp	1,150bp
10.0%	16.6%	18.9%	21.2%	23.3%	25.5%	27.6%	29.6%	31.6%	33.6%	35.5%	37.3%
15.0%	17.6%	19.9%	22.3%	24.6%	26.8%	29.0%	31.1%	33.2%	35.2%	37.2%	39.1%
20.0%	18.6%	21.1%	23.5%	25.9%	**28.3%**	**30.5%**	**32.8%**	**34.9%**	**37.0%**	**39.1%**	41.1%
25.0%	19.7%	22.3%	24.9%	27.4%	**29.9%**	**32.3%**	**34.6%**	**36.9%**	**39.0%**	**41.2%**	43.3%
30.0%	21.0%	23.8%	26.5%	29.2%	**31.7%**	**34.2%**	**36.6%**	**39.0%**	**41.3%**	**43.5%**	45.6%
35.0%	22.4%	25.4%	28.3%	31.1%	**33.8%**	**36.4%**	**38.9%**	**41.4%**	**43.8%**	**46.1%**	49.3%
40.0%	24.1%	27.3%	30.3%	33.3%	**36.1%**	**38.9%**	**41.5%**	**44.1%**	**46.6%**	**49.0%**	51.3%
45.0%	26.0%	29.4%	32.7%	35.8%	**38.8%**	**41.7%**	**44.5%**	**47.2%**	**49.8%**	**52.3%**	54.6%
50.0%	28.3%	31.9%	35.4%	38.7%	41.9%	45.0%	47.9%	50.7%	53.4%	55.9%	58.4%
55.0%	31.0%	34.9%	38.6%	42.2%	45.5%	48.8%	51.8%	54.7%	57.5%	60.2%	62.7%
60.0%	34.3%	38.5%	42.5%	46.2%	49.8%	53.2%	56.4%	59.4%	62.3%	65.0%	67.5%

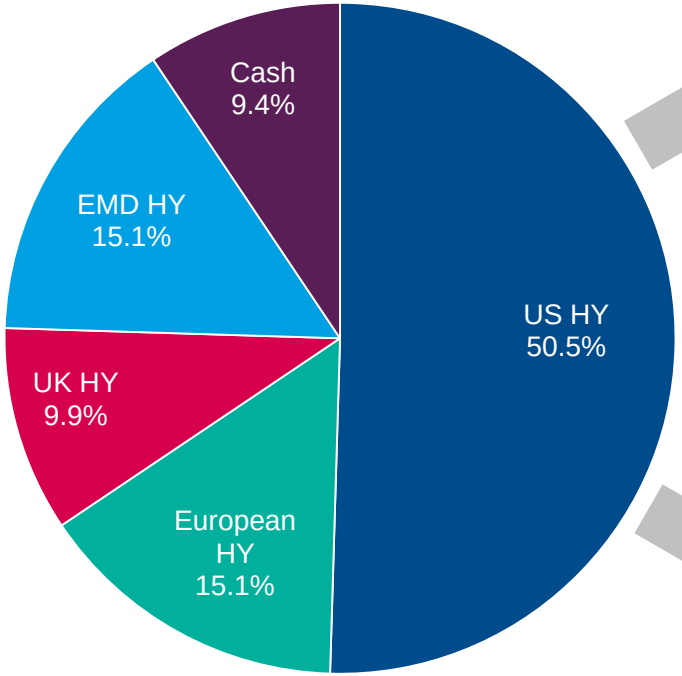
Currently energy spreads are 1100bps*, pricing in 50% default rates excessive

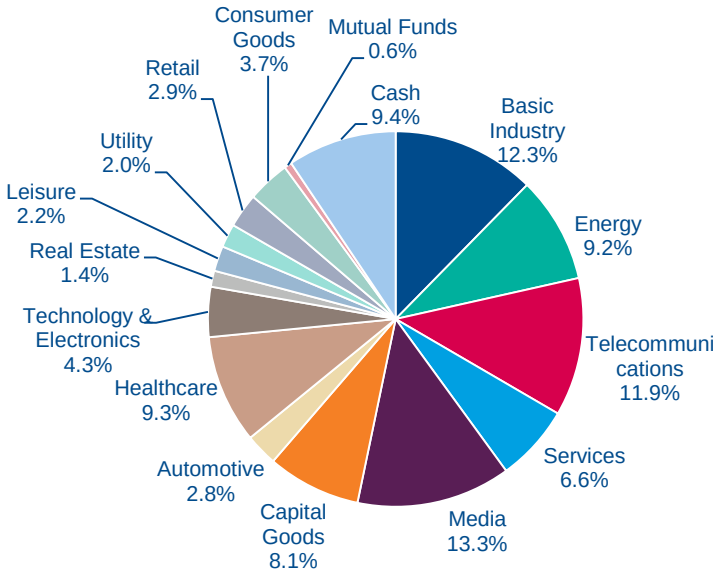
Source: Bloomberg/Deutsche bank , as at 10 August 2015
*Current Energy Spread Rate as at 28 September 2015

Fund allocation by sector and credit rating
30 September 2015

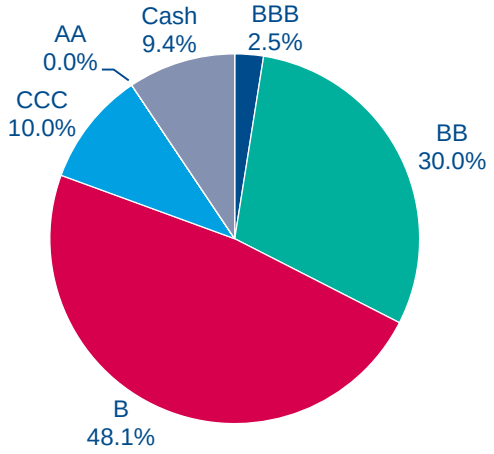
Fund Size: $679 million
Duration: 3.7 years
Holdings: 106

By sector



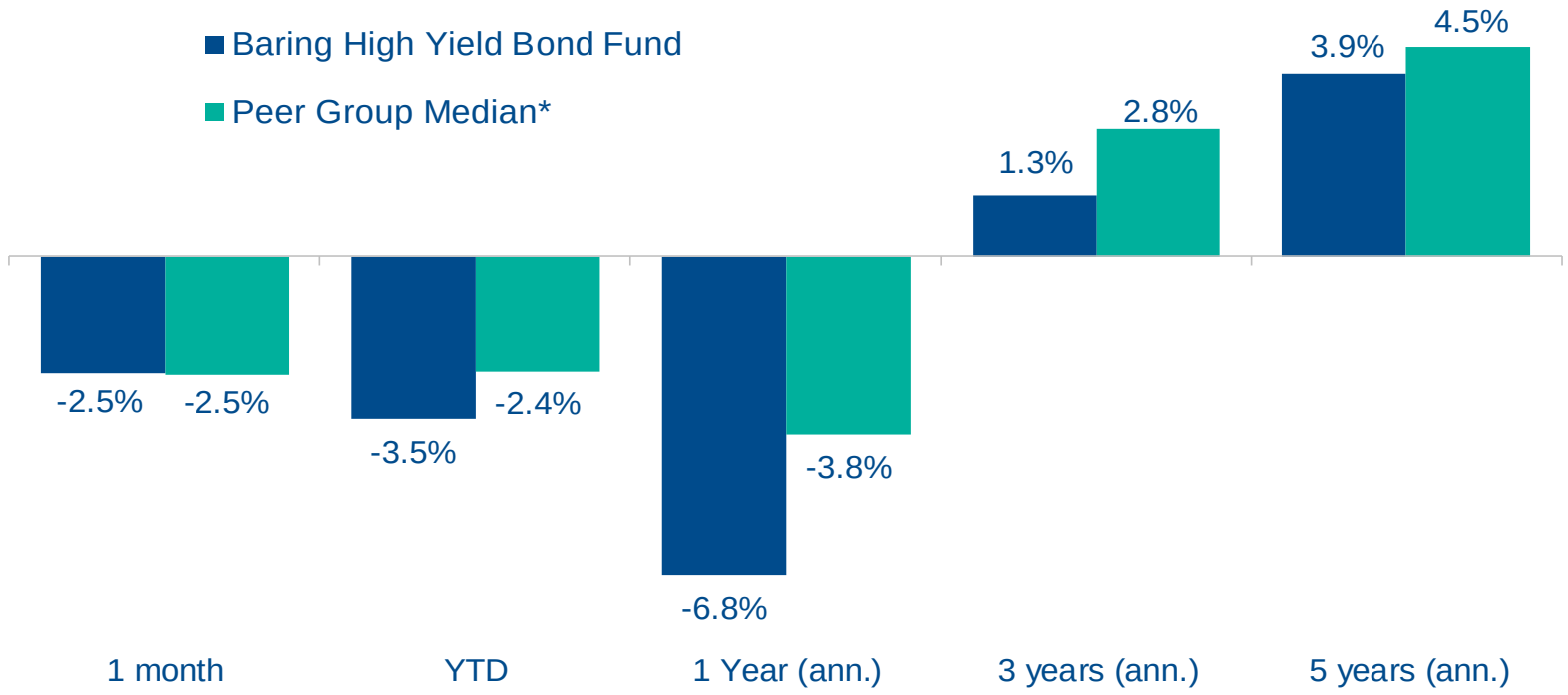


By credit rating*



Source: Baring Asset Management: 30 September 2015
*Credit Ratings show the highest rating between S&P and Moody's. Source: Barings / customised
Allocations are subject to change

Baring High Yield Bond Fund
30 September 2015



Past performance is not a guide to future performance

Source: Morningstar / Barings, 30 September 2015. Fund Performance is in US Dollars on a NAV per unit basis, with gross income reinvested, Net of fees. Inception July 1993. A USD Inc. Share Class.
* Morningstar GIFS Fixed Income Global High Yield Peer Group - Customised Peer Group.

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