SKAGEN Credit SEK

All data in SEK as of 30.09.2017 unless otherwise stated.

One way market

Global corporate bonds had another good quarter with generally lower credit spreads. Apart from a slight uptick in August due to the heightened tensions between North Korea and the US, spreads headed lower throughout the quarter. The general reduction in credit spreads so far in 2017 has been a global phenomenon, observed in both developed and emerging markets. The largest spread reduction this quarter was seen in the "High Yield" bond segment where companies rated lower than BBB- are to be found.

Contributors

The largest positive contributors this quarter were three Brazilian companies, namely JBS, Petrobras and Cosan as well as the Indian IT company Rolta. The protein company JBS rose sharply in the quarter following a heavy fall the previous quarter. The question around the majority owner's whereabouts has been put aside and the market has once again turned its focus to the company's business. Good second quarter numbers combined with balance sheet strength helped to push both the equity and bond prices higher.

Petrobras continues to deliver positive news and it looks as though it will reach its very ambitious 2.5x leverage target in 2018. Of special interest is its ongoing asset sale, which is proceeding according to plan, as well as the fact that it is extending its debt maturity profile. One of the two Petrobras bonds in Credit performed particularly well as it was part of a tender offer and bought back by the company.

Only three companies detracted from the fund's performance in the quarter; namely Seadrill, Bombardier and Frontier. In mid-September the drill operator Seadrill presented its long-awaited restructuring plan. The terms of this plan, which is not yet finalised, were not favourable for unsecured bond holders and the 0.2 percent position in the fund almost halved in size. The US Commerce Department has made an initial ruling recommending hefty import tariffs on the jets of Canadian Train & Aeroplane company Bombardier. The tariffs are not final and both Canadian and British politicians have since argued vehemently against them. If the tariffs do end up materialising, this would be a severe setback for Bombardier as it is dependent on increasing the numbers of jets sold.

One of the largest positive contributors this quarter was JBS. Photo: Bloomberg

Petrobras continues to deliver positive news and it looks like it will reach its very ambitious 2.5x leverage target in 2018. Photo: Bloomberg

Low funding costs – improved credit metrics?

A lot of companies borrow money at low rates in the bond market. When both the risk-free rate and credit premiums are at historically low levels, companies naturally take advantage of this and issue bonds. Longer maturities are in general preferred over shorter maturities, and 5-10 year bonds are those most issued. The companies thereby lock in a low funding cost for a rather long period ahead. This is of course very positive for companies in many ways, as it reduces interest rate costs, lowers re-financing risk and in general makes the future more predictable. All this is also good news for us as bond investors, as it reduces the amount of unknowns in the analysis.

One very important question that is not often raised though is what do the companies actually do with all the cheap money? From a credit perspective it is no good if everything is used to just increase dividends, as this does not improve the credit quality. If the companies instead choose to reduce the amount of debt, then the credit metrics instantly improve. What is important in the long run is simply whether the companies have a business that generates an acceptable return. If they don't, then cheap funding is of little importance. On an aggregate level it does not seem as though credit metrics have improved as of late. Hence the low credit spreads in today's market are not a result of improved corporate credit quality. The combination of historically low credit spreads without improvement in credit quality makes corporate bonds in general look rather expensive. It is therefore more important than ever to pick single bonds when investing in this asset class.

Reduced risk

The risk in SKAGEN Credit has been gradually reduced in 2017. Both the average credit quality and the average time to maturity have been altered to reduce the risk in the fund. Changes in credit spreads will therefore have less of an impact on the fund than they had a year ago. The investments are spread between 18 countries and 10 sectors, none of which account for more than 20 percent of the portfolio. The fund is therefore well diversified, even though it is concentrated to around 40 bonds. Risk and return in the fund is generated by bond coupon payments and the bonds' change of credit spreads.

Quarterly Report

SKAGEN Credit SEK

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SKAGEN Credit is our global corporate bond fund.

The fund is suitable for investors who have at least a two year investment horizon.

SKAGEN Credit SEK A is a currency-hedged feeder fund that invests its assets in the master fund SKAGEN Credit.

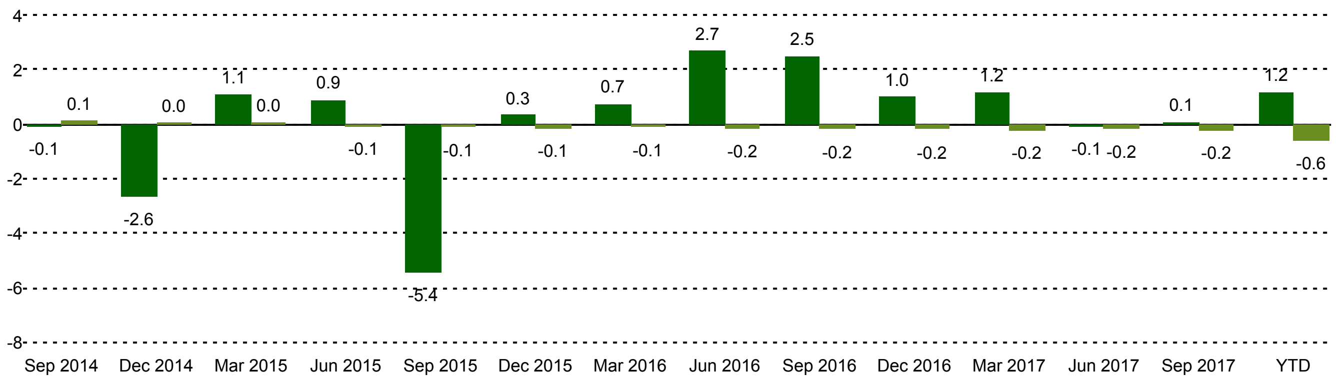
Historical performance (net of fees)

Period	SKAGEN Credit SEK	Benchmark index
Last Month	0.0%	-0.1%
Quarter to date	0.1%	-0.2%
Year to date	1.2%	-0.6%
Last year	2.2%	-0.8%
Last 3 years	0.7%	-0.5%
Last 5 years	n/a	n/a
Last 10 years	n/a	n/a
Since start	0.6%	-0.4%

Fund Facts

Type	Fixed income
Domicile	Norway
Launch date	30.05.2014
Morningstar category	Other Bond
ISIN	NO0010710726
NAV	98.18 SEK
Fixed management fee	0.80%
Benchmark index	NASDAQ OMRX Treasury Bill TR
AUM (mill.)	25.95 SEK
Duration	0.96
WAL	2.27
Yield	-0.42%
Number of holdings	39
Lead manager	Ola Sjöstrand

Quarterly Performance



Contributors in the quarter

Largest contributors

Holding	Weight (%)	Contribution (%)
JBS Investments	2.67	0.25
Rolta Americas	0.25	0.16
Petrobras Global Finance	3.15	0.11
Cosan	2.90	0.07
Glencore	4.42	0.08

Largest detractors

Holding	Weight (%)	Contribution (%)
Seadrill Ltd	0.12	-0.05
Bombardier Inc	2.15	-0.05
Frontier Communications	0.62	-0.04
Danske Bank AS	2.30	0.00
Jaguar Land Rover	3.32	0.00

Absolute contribution based on NOK returns at fund level

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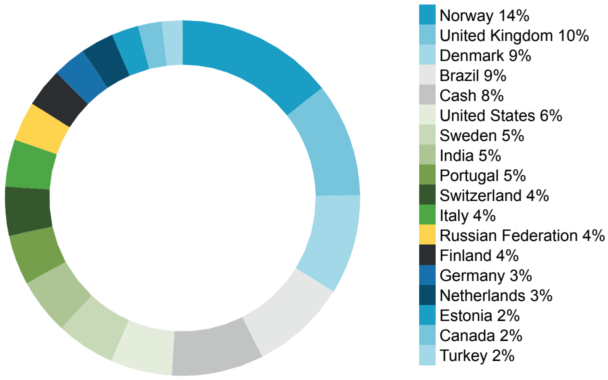
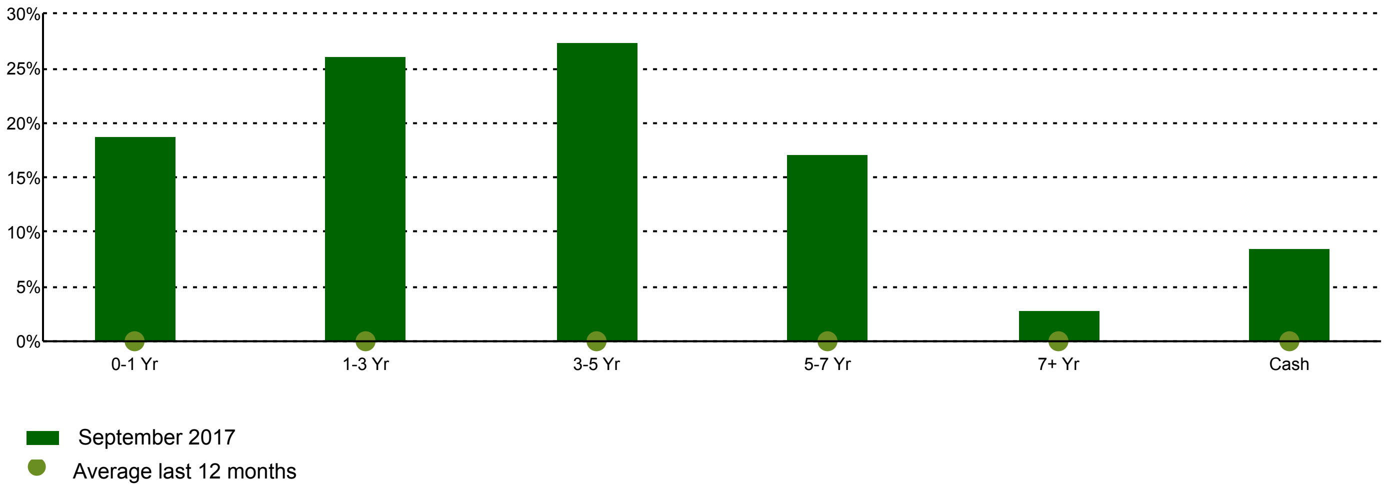
Top 10 investments

Holding	Percentage of Fund
BKK	4.7
EDP Finance BV	4.5
Heathrow Funding Ltd	4.5
Glencore Canada Financial Corp	4.4
Jacob Holm & Sonner Holding AS	3.7
Citycon Treasury BV	3.5
Jaguar Land Rover Automotive Plc	3.3
Schaeffler Finance BV	3.2
Petrobras Global Finance BV	3.2
DSV A/S	3.1
Total	38.2

Country exposure



Maturity structure



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Important information