

EURO CORPORATE BOND FUND A-ACC-EURO

30 SEPTEMBER 2018

Portfolio manager: David Simner

Performance for 12 month periods in EUR (%)

Performance over quarter in EUR (%)

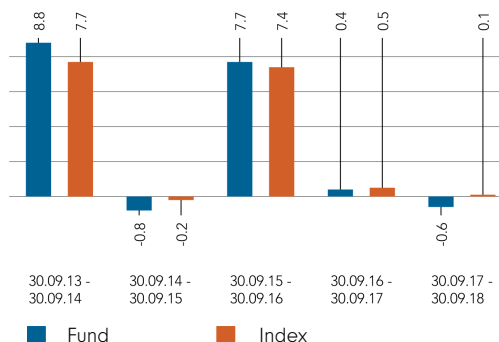
Fund 0.4

Market index 0.0

The BofA ML Euro Corporate Cap Index

Market index is for comparative purposes only.

Source of fund performance is Fidelity. Basis: nav-nav with income reinvested, in EUR, net of fees. Other share classes may be available. Please refer to the prospectus for more details.



Market Environment

European bonds posted mixed returns, with corporate bonds outperforming core government bonds. Demand for European government bonds remained subdued due to concerns around Italy's budget crisis and the trade war between the US and China. Furthermore, most economic parameters in Europe declined, led by inflation and consumer confidence. Consumer confidence slid sharply to -2.9 in September compared to -0.6 at the end of June 2018, the lowest level in more than a year. Meanwhile, lower composite Purchasing Managers' Index (PMI) readings and waning industrial metrics point to a weakness in the economy, which could be exacerbated by the pullback in global demand and uncertainty over the region's trade relationship with the US. On the political front, the prospect of a chaotic Brexit grew following an informal summit in Austria, during which a number of the UK's proposals were dismissed by the European Union. Risk sentiment took a hit towards the end of the quarter as the Italian government announcement that it would maintain its deficit target at 2.4%, well above market expectations. German business confidence fell slightly in September to 103.7, due to mounting concerns over export-oriented companies given the ongoing trade war between the US and China.

Fund Performance

The fund posted positive absolute returns and outperformed the index over the quarter.

Subordinated financials holdings boosted performance

Investor risk sentiment improved as trade tensions between the US and Europe eased. The fund's exposure to risky credit instruments added value. The allocation to subordinated bonds of Assicurazioni Generali, a large Italian insurer, and Credit Agricole, a large French bank, were the top contributors to returns.

High conviction exposure to crossover credits added value

The fund exposure to fundamentally strong high conviction credits added value. For instance, positive bias towards financial name such as UniCredit and Caixabank were among the top contributors to return. Caixabank rallied after the credit posted strong second quarter 2018 results on account of lower loan loss provisions through rationalization of its balance sheet.

Fund Positioning

The turmoil in European bond markets continues, largely due to continued political tensions in Italy. Towards the end of the quarter, the Italian budget failed to meet market expectations. The government's focus on spending rather than productivity enhancing measures is expected to weigh on Italy's long-term debt sustainability, given its reliance on very optimistic growth projections. Consequently, we expect European government bonds to remain volatile. However, corporate bonds should be better able to navigate the volatility. European investment grade spreads have already widened considerably since the start of the year, and should provide a valuable cushion for total returns in the volatile and uncertain period ahead.

Moved to short duration position

The fund reduced duration (measure of its sensitivity to interest rate changes) and is now firmly underweight from a broadly neutral stance at the end of the last quarter, in anticipation of a tighter global monetary policy. The short duration position in core European corporate bonds was retained on concerns around quantitative tightening and the US-led trade war rhetoric. However, we reduced duration in high-conviction credits on account of volatility in the region.

Remain long credit beta; positive bias towards financials

The fund marginally increased its credit beta over the quarter to take advantage of attractive valuations. This gave us the opportunity to add positions at attractive levels, specifically in Renault and Michelin. The fund also remains overweight in financials, with holdings in Generali, UniCredit and Caixabank.

Important Information

Past performance is not a reliable indicator of future results. The fund's returns can be affected by fluctuations in currency exchange rates.

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