LOMBARD ODIER
INVESTMENT MANAGERS

Investment viewpoint

LO Funds–Convertible Bond Asia celebrates 10 years

For professional investor use only • Convertible Bonds

December 2018

Launched in December 2008, the **LO Funds–Convertible Bond Asia** fund has succeeded in delivering to its investors the promised asymmetrical returns, capturing more of the equity upswings than participating in the downturns.

In a decade which encompasses the end of the great recession, quantitative easing, a great equity bull market and the rising risks of the current economic environment, the fund has delivered on what it set out to do. The aim is to provide investors low volatility exposure to the Asia-Pacific equity markets and outperformance of regional equities, on a risk-adjusted basis.

Looking forward, we expect some clouds to clear in Asia, although the macroeconomic backdrop will remain challenging. In our view, Asian convertible bonds provide a very useful tool for investors to navigate the coming uncertain market environment.

Client Portfolio Manager **Maxime Perrin** outlines the case investing in the Asia-Pacific region in the current climate, while cautioning investors against the associated risks. He also looks at why investors consider the use of Asian convertible bonds to gain exposure to the region.

Maxime Perrin
Client Portfolio Manager

Why the Asia-Pacific region?

1. There are **clear signs that economic growth in the region will be supported** by fiscal and monetary measures in 2019, particularly in China.
   - Chinese policy makers are recognising the downside risks to growth and are easing along multiples axes. Fiscal policy is moving towards stimulus regarding infrastructure investment, lower bank RRR (reserve ratio requirements) and other measures to improve liquidity. President Xi signaled support to private-owned enterprises that included tax and fees reduction and access to financing measures.[1]
   - In the broader region, most Asian authorities have maintained a favorable policy mix, which should enable these economies to maintain stable growth. Moreover, we believe Asian central banks are likely to continue to allow currencies to adjust in response to US rate rises.
   - There is likely to be less pressure from the US dollar going forward.
   - The decline in oil prices eases headwinds and softens inflation for many emerging Asian economies.

[1] Source: Bloomberg, October 2018.

2. **Valuations are attractive** after a sharp correction in both equities and credit.
   - Asian equities in 2018 had their sixth worst year since the 1980s. Our analysis of historical trends point to a likely rebound in 2019.
   - Credit spreads have widened substantially. Corporate yields levels are close to 10-year highs.
3. There remains, however, **substantial risks associated with emerging-market exposure.**
   - Three macro drivers, in our view, will continue to challenge the more bullish views on Asia in 2019. These are:
     i. Slowdown in global economic growth. This is aggravated with further monetary tightening, notably from the Fed.
     ii. Trade war fears. China and the US have agreed on three months of negotiations ending on 31 March 2019. The threats of tariffs and counter-tariffs is expected to continue. Investors can thus expect higher volatility until a clear compromise is found.
     iii. Domestic issues in China. We see some particular threats, including the growth and excessive level of overall credit, as well as consumer sentiment and the relationship between state-owned enterprises and the private sector.

Why use convertible bonds to gain exposure to the region?

1. Asian convertible bonds are appealing for **a defensive-minded approach** to the region in the current market climate.
   - Asian convertibles offer potential opportunities on both sides of the investment spectrum: credit and equity markets.
   - Asian convertible bonds can offer good defense against downturns through its bond component and low equity risk through its poorly valued optionality – yet allow meaningful participation in the event of an upside.
   - Asian convertible bonds appear technically cheap if one expects equity volatility to rise. A higher volatility environment benefits the asset class, as it strengthens the option value of these instruments.
   - In 2018, convertible bonds from the Asia-Pacific region reflected only 30% of the downside of the region's equities (-3.7% for LO Fund–Convertible Bond Asia versus -12.7% for the MSCI Asia ex-Japan index, both USD-hedged[1]).
2. Historically, convertible bonds from the Asia-Pacific region have a track record proving its capacity to deliver low-volatility exposure to regional equity markets.
   - The 10-year track record of our own LO Funds–Convertible Bond Asia fund has a high level of volatility-adjusted performance. It has a Sharpe Ratio of 1.04 versus 0.61 for the MSCI Asia ex-Japan.[2]

Strategy overview[3]

1 Asymmetry	2 Risk/reward	3 Strong convictions	4 Quality names	5 Currency hedged
An objective which reflects the asymmetry of the asset class delivers performance while protecting capital during downtrends	Focusing on **the best reward/risk profiles** of the asset class means investing in balanced convertible bonds	Out-performance is possible when portfolio is structured around **strong convictions** (in regions, sectors, style)	Long-term performance adjusted to volatility is better achieved with a strong bias towards **good quality names**: Minimum B- credit rating	**No currency hedge versus USD** as we bet on local currencies' appreciation in the medium term

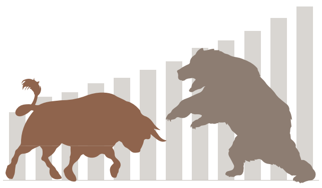
2 Source: LOIM, Bloomberg. Past performance is not a guarantee of future results.
3 For illustrative purposes only.

LO Funds–Convertible Bond Asia

In a nutshell, the strategy is focused on balanced convertible bonds, which generally target a delta of between 30% and 60%, together with a strong bond protection. We do so in order to reflect the asymmetry of the asset class. The fund is dedicated to good quality names, with no investment made below a B- credit rating.

A long-standing franchise at Lombard Odier Investment Managers

A market leader

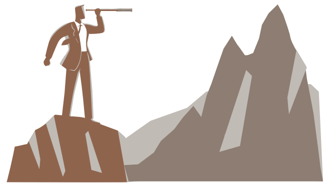


LOIM has been investing in convertible bonds since 1987, building up over three decades of convertible bonds experience across both bull and bear markets.

Established team

The 11-member investment team performs broad and extensive research, leveraging the research and risk management capabilities of LOIM's global platforms.

High conviction



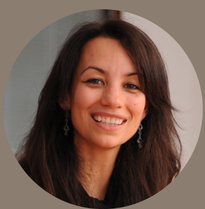
We search for the best quality investments across different regions, sectors and styles, targeting an overall credit rating of investment-grade for the portfolio.

An experienced team

Our team has seen its numbers grow over the past few years with two credit analysts dedicated to Asia joining the team in 2015, based in Singapore, together with our dedicated equity analyst for Asia, Larry Pun.

CONVERTIBLE BONDS TEAM

PORTFOLIO MANAGEMENT



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Head of Convertible Bonds & Fixed Income
22 years' experience

ARNAUD GERNATH
Co-Portfolio Manager
23 years' experience

MAXIME PERRIN
Client Portfolio Manager, 22 years' experience

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Equity analyst
11 years' experience

Larry Pun
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21 years' experience

Maxime Perrin
Equity analyst & Client Portfolio management
22 years' experience

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Louis Boppe
Convertible bond analyst
10 years' experience

Giuliano Mazzoni
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42 years' experience

CREDIT ANALYSTS

Tracy Wang
Asia Credit analyst, CFA
12 years' experience

Kenneth Kwan
Asia Credit analyst, CFA
7 years' experience

Vikki Lindstrom
Credit analyst
22 years' experience

Understanding the risk and reward profile

1 2 **3** 4 5 6 7

Lower risk
Potentially lower rewards

Higher risk
Potentially higher rewards

Understanding the risk and reward profile

This indicator (SRRI) represents the annualised historical volatility of the Sub-Fund over a 5-year period. Where there are less than 5 years' worth of data, missing returns are simulated using an appropriate benchmark. The SRRI may change over time and should not be used as an indicator of future risk or returns. Even the lowest risk classification does not imply that the Sub-Fund is risk-free or that capital is necessarily guaranteed or protected.

The Sub-Fund invests at least two-thirds of its assets in convertible bonds issued by companies in Asia and across all sectors. The investments are focused on balanced convertible bonds with good credit ratings, providing equity exposure and downside protection through the fixed income component of the asset class. The Sub-Fund also takes currency exposure in its non USD investments.

The following risks may be materially relevant but may not always be adequately captured by the synthetic risk indicator and may cause additional loss:

Credit risk: A significant level of investment in debt securities or risky securities implies that the risk of, or actual, default may have a material impact on performance. The likelihood of this depends on the creditworthiness of the issuers.

Liquidity risk: Where a significant level of investment is made in financial instruments that may under certain circumstances have a relatively low level of liquidity, there is a material risk that the fund will not be able to transact at advantageous times or prices. This could reduce the fund's returns.

Operational risk and risks related to asset safekeeping:
In specific circumstances, there may be a material risk of loss resulting from human error, inadequate or failed internal systems, processes or controls, or from external events.

Before taking any investment decision, please read the latest version of the Prospectus, the articles of incorporation, the Key Investor Information Documents (KIIDs) and the latest annual report and semi-annual report. Please pay attention to the Appendix B "Risk Factors Annex" of the prospectus.

IMPORTANT INFORMATION

Lombard Odier Funds (hereinafter the "Fund") is a Luxembourg investment company with variable capital (SICAV). The Fund is authorised and regulated by the Luxembourg Supervisory Authority of the Financial Sector (CSSF) as an Undertaking for Collective Investments in Transferable Securities UCITS under Part I of the Luxembourg law of the 17 December 2010 implementing the European directive 2009/65/EC, as amended ("UCITS Directive"). The Management Company of the Fund is Lombard Odier Funds (Europe) S.A. (hereinafter the "Management Company"), a Luxembourg based public limited company (SA), having its registered office at 291, route d'Arlon, 1150 Luxembourg, Grand Duchy of Luxembourg, authorised and regulated by the CSSF as a Management Company within the meaning of EU Directive 2009/65/EC, as amended. This marketing document relates to "Convertible Bond Asia", a Sub-Fund of Lombard Odier Funds (hereinafter the "Sub-Fund"). This marketing communication was prepared by Lombard Odier Asset Management (Europe) Limited.

The prospectus, the articles of incorporation, the Key Investor Information Documents, the subscription form and the most recent annual and semi-annual reports are the only official offering documents of the Sub-Fund's shares (the "Offering Documents"). The Offering Documents are available in English, French, German and Italian at www.loim.com and can be requested free of charge at the registered office of the Sub-Fund in Luxembourg: 291 route d'Arlon, 1150 Luxembourg, Grand Duchy of Luxembourg.

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France–Centralising agent: CACEIS Bank.

Germany–Paying agent: DekaBank Deutsche Girozentrale.

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