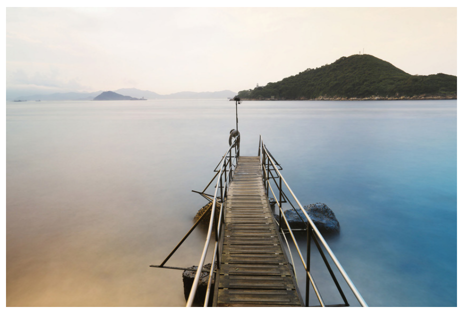
For professional investors only*

EMERGING MARKET DEBT – QUARTERLY NEWSLETTER

First quarter 2018



Market Review and Outlook[1]

Highlights for EM Debt

- Emerging and frontier markets performed well in 2017, taking advantage of the broad-based world economic expansion and favorable commodity prices
- Many idiosyncratic credit stories will continue to make headlines. However, developments in 2017 showed that these events can cut two ways, and that contagion risk has diminished
- Solid opportunities in 2018: in particular, hard currency assets that trade wide to the major EM hard currency indices and EM local markets with high real yields and contained inflation

Emerging and frontier markets generally performed well in 2017, taking advantage of the broad-based world economic expansion and favorable commodity prices. This backdrop set the stage for relatively benign inflation dynamics as well as narrower fiscal and external balances. These positive economic fundamental trends were reflected in strong performance of EM assets – even against the background of gradual moves toward monetary policy normalization in advanced economies. Emerging markets debt generated numerous opportunities across the hard currency, local rate, and foreign exchange sectors.

Emerging Markets Debt Performance

	Total Return (%)		Spread/Yield Change (bps)		OAS (bps)/ Yield (%)
	Q4	2017	Q4	2017	31.12.2017
EM Hard Currency	1.16	10.26	–2	–57	285
EM Local (hedged)	0.03	3.68	15	–65	6.14
EM FX	2.00	11.54	–42	–109	3.54
EM Corporates	0.68	7.96	–3	–47	260

Source: J.P. Morgan as of December 31, 2017. **Past performance is not a guarantee or reliable indicator of results. An investment cannot be made directly in an index.**

On the back of improving fundamentals, such as narrower current account deficits, falling inflation, and growing central bank reserves, we expect that EM growth (ex-China) will accelerate from 3.5% in 2017 to 3.8% in 2018, far exceeding our estimated growth of 2.3% across the developed world.

Although macro risks remain on the horizon – e.g. the ongoing removal of developed market monetary stimulus, led by the Federal Reserve's contracting balance sheet and prospects for three to four rate hikes in 2018 – some of these concerns may be remnants of the volatility surrounding 2013's taper tantrum. In fact, during the last sustained Fed hiking cycle between 2004 and 2006, emerging market hard and local currency debt returned 25% and 29%, respectively.

Many idiosyncratic credit stories – Venezuela, Argentina, Brazil, Mexico, Ukraine, and Russia, among others – will continue to make headlines. Yet developments in 2017 again showed that these events can cut two ways, and that the sector's resilience to macro and idiosyncratic events (as observed in the following chart) and the performance of individual country assets continues to differentiate it.

The Dimishing Contagion Risk in EM

Source: PGIM Fixed Income, J.P. Morgan as of November 9, 2017.

*** investing for their own account – according to MiFID definition**

1) Views from PGIM Fixed Income Emerging Markets Team. PGIM Limited is the investment sub-manager of the Nordea 1 – Emerging Market Bond Fund and Nordea 1 – Emerging Market Bond Opportunities Fund.

Even though hard currency spreads tightened steadily in 2017, they still remain well wide of 2007's historical tight of 166 bps, when only one-third of the market carried investment grade credit ratings. At today's wider spreads, nearly half of the market carries investment grade ratings. As 2017 concluded, we maintained overweights in higher-yielding sovereigns and quasi-sovereigns with wider spread levels, and we generally expect spreads to be supported by low developed market rates and solid global growth. Our top overweights include Argentina, Brazil, Ukraine, and Mexico. In regard to our Mexico positioning, we will be closely monitoring potential volatility in Mexican assets over the first half of the year as the July presidential election approaches.

We'll also watch developments in Argentina closely to see if it can maintain positive momentum and deliver on fiscal reforms through 2018 and 2019. Argentina's political climate and related improved policy mix of late should continue to boost investment and capital inflows into the country, which will likely approach high single-B to low-BB valuations if the strategy proves successful. We believe its provincial and euro-denominated bonds currently offer the best value, but are waiting for more pronounced signals from the central bank to add more strategic FX positions.

In terms of Brazil, its economic recovery should become more tangible in 2018, which is also an important election year. The election outcome will partially determine how Brazilian assets perform over the medium term as we get more clarity on its commitment to market-friendly and debt-stabilizing reforms, along with policies to improve investment. Pension and continued micro reforms are among those steps needed to stabilize Brazil's debt dynamics. Spreads on Brazilian sovereign debt look fair relative to other EM BB-rated issuers but the country enjoys relatively low levels of external indebtedness and high FX reserves compared to many of those credits. This should help limit potential downside from current levels. Against this backdrop, select quasi-sovereigns appear attractive, and so do local bonds in nominal and real terms compared to other local EM markets. The Brazilian real could also benefit from a healthy stream of foreign direct investment over the longer term. As Brazil's political cycle heats up next year, bouts of volatility may provide attractive points to add risk.

Elsewhere in hard currency debt, we continue to seek opportunities to add alpha from exposure to select frontier names. The credit profiles of many of these countries, including, but not limited to, Ecuador, Angola, Ghana, Iraq and Mongolia, are improving with many benefitting from IMF programs. Because these issuers are lower rated and higher risk, we prefer 5- to 7-year issues where we believe spreads are attractive. Prices in this segment of the curve also tend to be less volatile, and there is more visibility that debt will be repaid, notwithstanding potential idiosyncratic or broader market concerns.

Turning to local rates, the real yields across a number of countries—Brazil (4.5%), Indonesia (4%), Mexico (3%), and Colombia (2.5%)—remain attractive. Furthermore, on a nominal basis, the opportunities across the local rates market are reflected by yields that were more than 400 bps higher than the five-year U.S. Treasury yield as of late 2017. We'd note that the exception to our favorable real yield outlook would be certain central and eastern European countries, including Hungary, that carry negative real yields. Our local rates strategy consists of maintaining long duration and curve flattening positions in select yield curves with our top local rate overweights set in Mexico, Brazil, Indonesia, and Malaysia.

The performance of the local rates market will undoubtedly be influenced by EMFX, where we also have a constructive outlook for the coming year. When EMFX hit some volatility in the second half of 2017, we noted that during prior selloffs that occurred under similar market conditions – relatively strong global growth and tightening Fed policy – the market declined by a maximum of only 5% during those spans. The most recent EMFX selloff, which began in mid-September 2017, represented a 5% decline, and the correction began to reverse course as of mid-November. With that backdrop, we recently added to EMFX risk based on strong growth and relatively low inflation rates. Our top EMFX overweights going into 2018 include the Indian rupee, Indonesian rupiah, and the Brazilian real, though we are keeping our eyes open to more tactical positioning in this segment over the first half of the year.

As we consider the EMD sector more broadly, we believe it should continue to provide solid opportunities in 2018. In particular, we would point to hard currency assets that trade wide to the major EM hard currency indices and to EM local markets with high real yields and contained inflation. In an environment of a stable-to-declining U.S. dollar, EM currencies stand to benefit as EM economic growth continues to outpace developed markets. Macro and idiosyncratic risks abound, however, making research and security selection crucial components of the investment process.

Nordea 1 – Emerging Market Bond Fund

Performance Q4 2017

Nordea 1 - Emerging Market Bond Fund (BP-USD)	1.59 %
Nordea 1 - Emerging Market Bond Fund (BI-USD)	1.71 %
Benchmark[2]	1.16 %

Source: Nordea Investment Funds S.A. Period under consideration: 29.09.2017 – 29.12.2017. **The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested.** 2) JP Morgan EMBI Global Diversified.

Overweights to Ecuador, Argentina, Iraq, Angola, and El Salvador along with an underweight to Poland drove performance. Argentina was up on the back of primary election results that provided the current government much anticipated local victories with the hope that it can continue with its reform agenda. El Salvador outperformed as oil rallied and after S&P raised its outlook to positive. An overweight to Venezuela offset some of these gains. Venezuela was the big underperformer of the quarter amid sanctions imposed by the U.S. and the heightened economic and political crisis. An underweight to Uruguay was also a small detractor.

Sovereign positioning in Venezuela, Argentina, Colombia, Hungary, and Kazakhstan contributed to performance. Quasi-sovereign positioning in Venezuela (PDVSA) was the major driver of positive issue selection. Very short maturity bonds maturing around this time period significantly outperformed other Republic and PDVSA issues even as longer-term uncertainty increases with the selective default. Positioning in Peru (SCCO) and Malaysia (PETMK) also contributed while positioning in Brazil and Kazakhstan (KZOKZ) was a small detractor.

The fund's largest overweights are Argentina, Brazil, and Ukraine, and the largest underweights Poland, China, and Chile. The largest positioning changes during the quarter were Venezuela (–0.54 %), Russia (–0.32 %), and Mexico (–0.32 %).

Nordea 1 - Emerging Market Bond Fund: Top 10 Country Exposure

	Portfolio (%)	Benchmark[3] (%)	Difference (%)
Argentina	6.31	3.37	2.94
Mexico	5.99	5.19	0.81
Brazil	5.53	3.34	2.19
Indonesia	4.74	4.34	0.40
Turkey	4.67	3.79	0.88
Ukraine	4.47	2.70	1.77
Russia	4.12	3.61	0.50
South Africa	3.44	2.76	0.68
Ecuador	3.12	2.59	0.53
Lebanon	3.01	2.52	0.49

Source: PGIM Ltd. as of December 31, 2017. Note: Figures based on the model portfolio allocation and can deviate from official fund data. 3) JP Morgan EMBI Global Diversified.

Nordea 1 – Emerging Market Bond Opportunities Fund

Performance Q4 2017

Nordea 1 - Emerging Market Bond Opportunities Fund (BP-USD)	0.82%
Nordea 1 - Emerging Market Bond Opportunities Fund (BI-USD)	0.95 %
Benchmark[4]	1.00 %

Source: Nordea Investment Funds S.A. Period under consideration: 29.09.2017 – 29.12.2017. **The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested.** 4) 50 % JP Morgan EMBI Global Diversified and 50 % JP Morgan GBI-EM Global Diversified.

In hard currency, overweights to Argentina, Ecuador, Ukraine, El Salvador and Iraq drove performance. An overweight to Venezuela offset some of these gains. Hedged local rates returned +0.03% in Q4 2017. An overweight to Indonesia along with underweights to Czech Republic, Romania and Chile contributed to performance. An overweight to Mexico along with underweights to Russia and Hungary detracted from performance.

Sovereign positioning in Indonesia, Colombia, and Argentina contributed to performance. Quasi-sovereign positioning in Venezuela (PDVSA) was the major driver of positive issue selection. Corporate and quasi-sovereign positioning in Brazil (ODBR) was a small detractor. Local rates positioning in Hungary added to performance, while positioning in Brazil, Mexico, Turkey, Indonesia and South Africa detracted from performance.

Emerging market currencies were stronger during the quarter, posting a total return of +2.00% measured by the JP Morgan ELMI+ Index. Many idiosyncratic developments outside the U.S. led to the USD trading weaker against G10 and Emerging Market currencies. Steady long end rates in the U.S. also helped set the weaker dollar tone. Exposure to the Turkish lira, Brazilian real and Mexican peso detracted from performance. Exposure to the Russian ruble, Indian rupee and Czech koruna contributed to performance.

The fund's largest hard currency over/underweights and changes throughout the quarter were similar to the ones seen in the hard currency portfolio (see above). In local rates positioning changes, the fund reduced Mexico (–0.05 years), Brazil (–0.02 years), and Turkey (–0.02 years) and added to South Africa and Malaysia (+0.02 years each). In FX, the fund increased overweights to the Colombia peso, Russian ruble, and Malaysian ringgit, while reducing the South African rand, Indonesian rupiah, and Mexican peso.

Nordea 1 - Emerging Market Bond Opportunities Fund: Top 10 Country Exposure

	Portfolio (%)	Benchmark[5] (%)	Difference (%)
Brazil	9.31	6.67	2.64
Indonesia	8.86	6.98	1.88
Mexico	8.04	7.40	0.63
South Africa	6.80	5.57	1.23
Turkey	6.26	5.49	0.77
Malaysia	4.95	4.13	0.82
Argentina	4.19	2.15	2.04
Poland	3.85	5.80	-1.95
Colombia	3.81	4.94	-1.13
Ukraine	3.25	1.35	1.90

Source: PGIM Ltd. as of December 31, 2017. Note: Figures based on the model portfolio allocation and can deviate from official fund data. 5) 50% JP Morgan EMBI Global Diversified and 50% JP Morgan GBI-EM Global Diversified.