

In Focus

For professional investors only*

September 2018

Our FFIF risk balanced and flexible approach is back on track and makes a difference

Nordea 1 – Flexible Fixed Income Fund

ISIN: LU0915365364 (BP-EUR) / LU0915363070 (BI-EUR)

- Fixed income markets face many headwinds, which expose investors to higher drawdown
- The search for yield is clearly challenged: our “truly” diversified allocation based on risk balancing principles is now a competitive edge
- Our fund offers investors an effective and liquid tool for capital preservation, decorrelation and flexibility

So far this year, fixed income markets embarked investors in a bumpier road than they were used to, owed to growing political events and as the Fed continued its normalization policy by raising its short-term interest rate. As a result, spreads globally widened, especially Emerging Market Debt (EMD) and within High Yield (HY) space. EMD was moreover affected by a stronger US dollar. In this context, many unconstrained fixed income managers, who in previous years chased yield and thus tilted their portfolios to HY and, or EMD, suffered as markets started to struggle. This is not the case for the Nordea 1 – Flexible Fixed Income Fund (FFIF), which remains true to its philosophy of risk balance and did not take excessive risk in the search for yield and thus is less exposed to downside risk in fixed income markets as well as to liquidity risk.

A diversified global fixed income fund
(correlation vs. peers and asset classes)

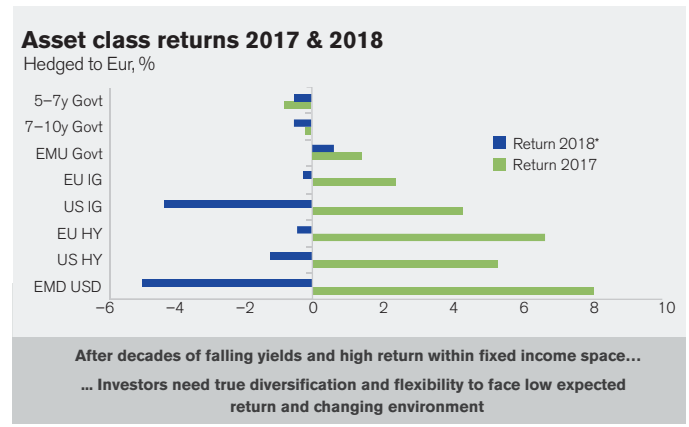
	Nordea 1 – Flexible Fixed Income Fund BI-EUR	Morningstar Peer Group
Nordea 1 – Flexible Fixed Income Fund BP-EUR	1.00	0.50
Morningstar Peer Group	0.50	1.00
US High Yield	0.32	0.73
Euro High Yield	0.33	0.80
Euro Investment Grade	0.49	0.42
US Investment Grade	0.37	0.20
US Treasuries 7–10 years	0.29	-0.01
German Federal Govt 7–10 years	0.38	0.09

The FFIF is able to provide diversification due to its lower correlation to HY markets

Source: © 2018 Morningstar, Inc. All Rights Reserved. Data as at: 30.08.2018. European Open End Funds database, Morningstar EAA OE Global Flexible Bond – EUR Hedged category. Period under consideration: 26.08.2013 – 25.08.2018. Performance in base currency and based on daily observations. **The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested.**

Thanks to its more diversified approach, the **Nordea 1 – Flexible Fixed Income Fund (FFIF)** offers fixed income investors an **effective tool to counterbalance the significant credit risk** embedded in their fixed income portfolios and allocations. On top of that, the Multi Assets Team’s (MAT) focus on flexibility allows to navigate through this challenging environment, by adapting both our credit and duration exposure to evolving markets, and to manage downside risk.

This year drove investors to a new era. Indeed, the White House’s trump card on tariffs and US partners’ retaliatory measures triggered concerns on global economy, further intensified by the crisis of the Turkish Lira, which in August fell 30% over 3 days, leading to EM spreads widening. In the meantime, European Union had to face the effects of the internal political concerns, while credit also struggled. This backdrop saw investors struggle to find positive return within fixed income after a decade of high returns.



Source: Nordea Investment Management AB and Bloomberg. 5–7y (7–10y) Government returns are equal-weighted 5–7y (7–10y) ICE BofAML Govt bond index returns from US, UK, Canada, Germany and Australia. EMU Govt is the JP Morgan EMU Govt Bond Index return, EU IG, US IG, EU HY and US HY are the respective ICE BofAML Index returns and EMD USD is the JP Morgan EMBI Global Diversified Index return. All returns are hedged to EUR. *As of 31.07.2018.

The FFIF’s long term balanced value proposition – amid safe and risky assets (duration and credit) – allowed **the portfolio to be significantly more resilient during drawdowns** than the ones that, in order to chase return, got unbalanced exposure to EMD or HY, which put investors’ capital at risk. This capital preservation feature explains why **the portfolio consistently outperformed its peers during the first part of the year**, without having to take unnecessary or uncompensated risks.

* Investing for their own account – according to MiFID definition

YTD Performance vs Peers



The FFIF has demonstrated its diversification potential as compared to credit tilted peers in 2018 owed to its more balanced approach and its focus on limiting drawdowns

Source: © 2018 Morningstar, Inc. All Rights Reserved as at: 30.08.2018. European Open End Funds database, Morningstar EAA OE Global Flexible Bond - EUR Hedged. Performance in EUR and based on daily observations. Period under consideration: 01.01.2018 - 25.08.2018. **The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested. The value of shares can greatly fluctuate as a result of the sub-fund's investment policy and is not guaranteed.**

Also, in this search for yield, investors have increased their liquidity risk, which is on the rise in this new challenging environment for fixed income. The FFIF is a very liquid investment vehicle. The fund is investing in highly liquid physical bonds (e.g. high quality government bonds like US Treasuries or German Bunds) and uses highly liquid most commonly used plain vanilla derivative instruments to gain access to markets with liquidity constraints or where trading costs are high. This leads to a portfolio with the required high level of liquidity the portfolio management team is looking for to be able to manoeuvre at all times and during all market conditions. In that way the fund's holdings differ from several other flexible bond funds with a heavier tilt towards cash bonds from non core sovereign markets and/or corporate credit markets. The fund's holding structure implies that 100% of the invested assets can be sold within one week and most assets can even be sold within one day at normal or only slightly elevated transaction costs. The focus on liquidity is another distinctive feature of the fund and part of the **different levels of risk monitoring and management which characterize the FFIF.**

On this bumpy road for fixed income, **active risk management and true diversification are keys to protect portfolios against drawdowns, without sacrificing expected return.**

The Nordea 1 - Flexible Fixed Income Fund represents a safety belt in a road full of potholes and is able to provide:

- 1) **Capital preservation**, thanks to its risk balanced approach
- 2) **Decorrelation** (as compared to credit tilted peers)
- 3) **Flexibility**, while still offering positive expected returns
- 4) **Aligned liquidity** with the one of underlying portfolio

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