Ostrum ASSET MANAGEMENT

FUNDING YOUR TOMORROW

SHORT-TERM INVESTMENT STRATEGIES

Short-term strategies could make the difference in a context of interest rates uncertainties

MAY 2018

Since 2011, due to the very accommodative monetary policy of Central Banks around the world, investors have been facing low interest rates, particularly in Europe.

In this context, investors may want to consider short term strategies, if they believe that:

- 2018, will be a year of transition in the financial markets, before entering a new investment cycle and the possibility of re-building of risky assets premiums, or
- Central Banks will accelerate the normalization of their monetary policies, due to higher inflation expectations.

In other words, even if the path and timing remains ambiguous, we could face some spikes in volatility in 2018. In that scenario the question should not be what was a portfolio's investment record, but rather how will performance be achieved now, in this new cycle?

In the case where the world doesn't change in 2018, investors will continue to have to live with low interest rates and will want to find alternatives to very low money market rates (EONIA index stands at -0.35% as of end of May 2018).

Over the past years, short duration strategies have elicited growing investor interest. On one hand, the extremely low level of money market rates has incited corporate treasurers to consider extending their investment horizons so as to access incremental yield. On the other hand, longer term investors must also contend with the fact that rates have reached historically low levels and should be expected to rise at some point. For such portfolios reducing the average maturity of investments is one way to try to protect capital.

Thus, investors willing to accept some principal fluctuation in exchange for yields that significantly outpace money market investments, with far lower volatility than long term bonds, might consider reducing their portfolio's maturity structure to minimize interest rate risk, over a two-year horizon.

We offer short term strategies to meet the needs for lower modified duration and a lower historical volatility. We classify these into three categories: Floating Rate Notes, Short-Term Credit Strategies, Absolute Return Strategies.

- **Floating Rate Notes strategies** to significantly reduce modified duration
  This is not a linear relationship; the lower the duration, the greater the decline in sensitivity to interest rates.
  Here we deal with a modified duration close to zero in order to minimize interest rate risk.

- **Short Duration Credit strategies** to reduce volatility
  Next to reducing interest-rate sensitivity, short term credit strategies are also appealing for their partial buffer against rising rates, as well as against steepening yield curves. Duration or sensitivity to interest rate change, is naturally lower for shorter maturities and higher coupons. Short maturities can offer a measure of principal preservation thanks to the pull to par effect and thanks to the spread embedded in the yield to maturity, which acts as a cushion helping to absorb volatility effects

- **Absolute Return Strategies** to search for the most attractive instruments
  in changing markets.
  This can be important in an environment where market declines, 'air pockets', and capital losses are increasingly frequent. For example, an absolute-return approach can apply flexibility in duration management; rather than managing, for example, against a short-duration government index.

SHORT TERM STRATEGIES RELEVANT NOW	FLOATING RATE NOTE	SHORT TERM CREDIT	ABSOLUTE RETURN
EURO ABS IG			
ULTRA SHORT TERM CREDIT			
EURO SHORT TERM CREDIT			
SHORT TERM GLOBAL HIGH INCOME			
EURO BONDS OPPORTUNITIES			
CREDIT OPPORTUNITIES			

The strategies presented above are subject to capital loss.

1. FLOATING RATE NOTES:

Euro ABS IG: A floating rate strategy with a high average rating[1]

The investor benefits from returns offered by senior tranches of European securitizations, backed by diversified assets (a.o. auto and consumer loans and residential mortgage backed securities) of high quality: the portfolio has an average rating of "AA" as of 27/04/2018. Due to the fact that these tranches are floating rates, the modified duration of the strategy is close to zero. We do think that the ABS asset class will continue to attract investors in 2018 thanks to its low rate sensitivity, its attractive valuation at similar rating and the new regulatory framework with the new label "STS" for Simple Transparent and Standardized. For 2018, Ostrum Asset Management anticipates a gross performance between 0.10% and 0.30%. The annualized volatility at three years is low at 0.49%[2] as of the end of April 2018 (gross of fees).

Main risks: Capital, Credit, Specific risks associated with investment in securities issued by securitisation vehicles.

2. SHORT TERM CREDIT STRATEGIES:

Ultra Short Term Credit: A strategy with guidelines close to money market funds

The guidelines of the ultra-short-term credit strategy reflect those of European money market funds both in terms of Weighted Average Life ("WAL") and Weighted Average Maturity ("WAM"). Like for European money market funds, no single investment may have a residual final maturity of more than two years. The main difference with money market funds is that the ultra-short-term credit strategy allows investing in both high yield and non-rated bonds for up to 70% of net assets in total in order to enhance returns. Portfolio construction is based on a rigorous security selection. It aims to identify the best investment opportunities maintaining a goal of capital conservation.
For 2018, Ostrum Asset Management, forecasts a gross performance between 0.10% and 0.20%[2]. The annualized volatility at three years is low at 0.40% as of the end of April 2018 (gross of fees).

Main risks: Capital, Credit, Below investment grade securities, Overexposure, Emerging Market, Securitization instruments.

Euro Short Term Credit: A short-term credit bond strategy with a return above of the money market funds.

The strategy, with its core plus process invests in short investment grade credit bonds and benefits from an additional return with an exposure up to 15% on European High-Yield bonds and/or up to 15% on securitization instruments. The average rating of the portfolio is still "BBB" but with a higher yield to maturity than its benchmark with an average modified duration very close to 2 (as of end of April 2018). The driving force of performance comes from the issuer/issue selection. For 2018, we forecast the continuing of the CSPP which will maintain the spread compression. For 2018, Ostrum Asset Management plans a gross performance between 0.50% and 1.00%[1]. The annualized volatility at three years is at 1.01% as of the end of April 2018 (gross of fees).

Main risks: Capital, Credit, Below investment grade securities, Leverage, Securitization instruments.

[1] The Euro ABS IG strategy holds an AA average credit rating as of 27.04.2018.
[2] These forecasts are not a reliable indicator of future performance

Short Term Global High Income, a strategy to benefit from the carry and the diversification on short term high yield bonds.

This strategy invests in short-term high yield bonds from both sides of the Atlantic with contained volatility. The portfolio's average modified duration is below 2 years. The short-term high yield market will still be attractive in 2018 in the two areas thanks to investors yield search, good credit fundamentals and low default rate forecasts in the US and in Europe. For 2018, Ostrum Asset Management anticipates a gross performance between 1.5% and 2%[1] in EUR. The annualized volatility at three years is at 2.22%, as of the end of April 2018 (gross of fees).

Main risks: Capital, Credit, Below investment grade securities.

3. ABSOLUTE RETURN STRATEGIES:

Euro Bond Opportunities 12M: A flexible approach which adapts to changing market conditions.

The Euro Bonds Opportunities 12M strategy uses two active strategies, a carry strategy and a dynamic duration management. Flexible allocation between carry and duration strategies targets enhanced return while minimizing the risk of capital loss or drawdown.
The strategy seeks to make the most of all fixed income market configurations over a 12-month investment horizon while aiming to minimize downside risk. The active security selection aims to deliver the highest available yield in the market through Euro sovereign debt selection, covered bonds and bank bills with the ability to manage the duration from 0 to 4 years. For 2018, Ostrum Asset Management anticipates a gross performance of Eonia +110 bps[1]. The annualized volatility at three years is around 0.74%, as of the end of April 2018 (gross of fees).

Main risks: Capital, Debt securities, Interest rates, Leverage.

Credit Opportunities: A pure credit absolute return strategy that seeks to benefit from positive credit trends and aims to deliver attractive and durable performance through market cycles.

In a context of low returns and low credit spreads with a non-negligible probability of more volatile markets, the credit opportunity strategy has the freedom to go beyond traditional benchmarks with a limited budget of risk.
The Credit Opportunities strategy is a pure credit absolute return strategy that seeks to benefit from positive credit trends, while remaining flexible enough to withstand volatility and try to deliver attractive and durable performance through market cycles.
To that end, the portfolio holds an exposure to credit market on Investment Grade and High Yield with an ability to stay between -2% and +2% in modified duration and, an overlay of global flexible strategies such as long/ short or directional strategies.
The portfolio management team uses an active, discretiona[2]ry and disciplined management process designed to seek durable alpha generation while putting risk first.
The gross performance targeted for 2018 is around EONIA +3.5%[1] within a limited risk budget (targeted VaR 99%, 20 days at 2.5%)

Main risks: Capital, Credit, Interest rates, Leverage, Securitisation, Below investment grade securities.

[1] These forecasts are not a reliable indicator of future performance

Short Term Strategies in a nutshell:

	Strategy	Expected gross performance for 2018*	Recommended investment horizon	Risk and reward profile (SRRI)**	Duration (guidelines)	Average duration***	AuM (M)***	Base cur.	Inception date
Floating Rate Notes	Euro ABS IG	0.10% - 0.30%	1 year	1/7	0 - 0.25	0.13	902	EUR	15/04/2005
Short Term Credit	Ultra Short Term Credit	0.10% - 0.30%	2 years	2/7	0 - 0.5	0.35	872	EUR	01/03/2013
Short Term Credit	Euro Short Term Credit	0.50% - 1.00%	2 years	2/7	0 - 5	2.0	1.382	EUR	30/09/2011
Short Term Credit	Short Term Global High Income	1.5% - 2% (en EUR)	3 years	3/7	2 years max	1.8	93	USD	25/10/2011
Absolute Return	Euro Bonds Opportunities 12M	Eonia + 1.10%	1 year	2/7	0 - 4	1.4	197	EUR	01/09/2009
Absolute Return	Credit Opportunities	Eonia + 3.50%	2 years	4/7	- 2 - + 2	0.35	65	EUR	15/04/2012

* This data should not be interpreted as having any contractual value. It is produced for information purpose only. There can be no assurance that developments will transpire as may be forecasted in material. Natixis Asset Management will not be held responsible for any decision taken on the basis of this information. These forecasts are not a reliable indicator of future performance.'anticipés. Ostrum Asset Management ne saurait être tenue responsable des décisions prises sur la base de ces informations. Ces prévisions ne constituent pas un indicateur fiable des performances futures
**The risk-return indicator is presented on a scale ranging from 1 to 7. The numbers correspond to increasing levels of risk and return, allowing for a better understanding of a mutual fund's performance potential in comparison to its associated risk. The general method for calculating this regulatory indicator is based on the fund's historical annualised volatility, which is calculated using weekly returns over a 5-year period. This indicator is periodically reviewed and may change. the indicator is the one applicable at the time of writing of the document.
***Data as of 27/04/2018 (average duration and AuM).

Source : Ostrum Asset Management on 30 April 2018

Written on May 2018

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This non-contractual document has been prepared by Ostrum AM on May 2018.

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Limited Liability Company, Share Capital €50,434,604.76
Regulated by AMF under n°GP 90-009
Company Trade Registration (RCS) Number 329 450 738 Paris

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