

CQS Insights

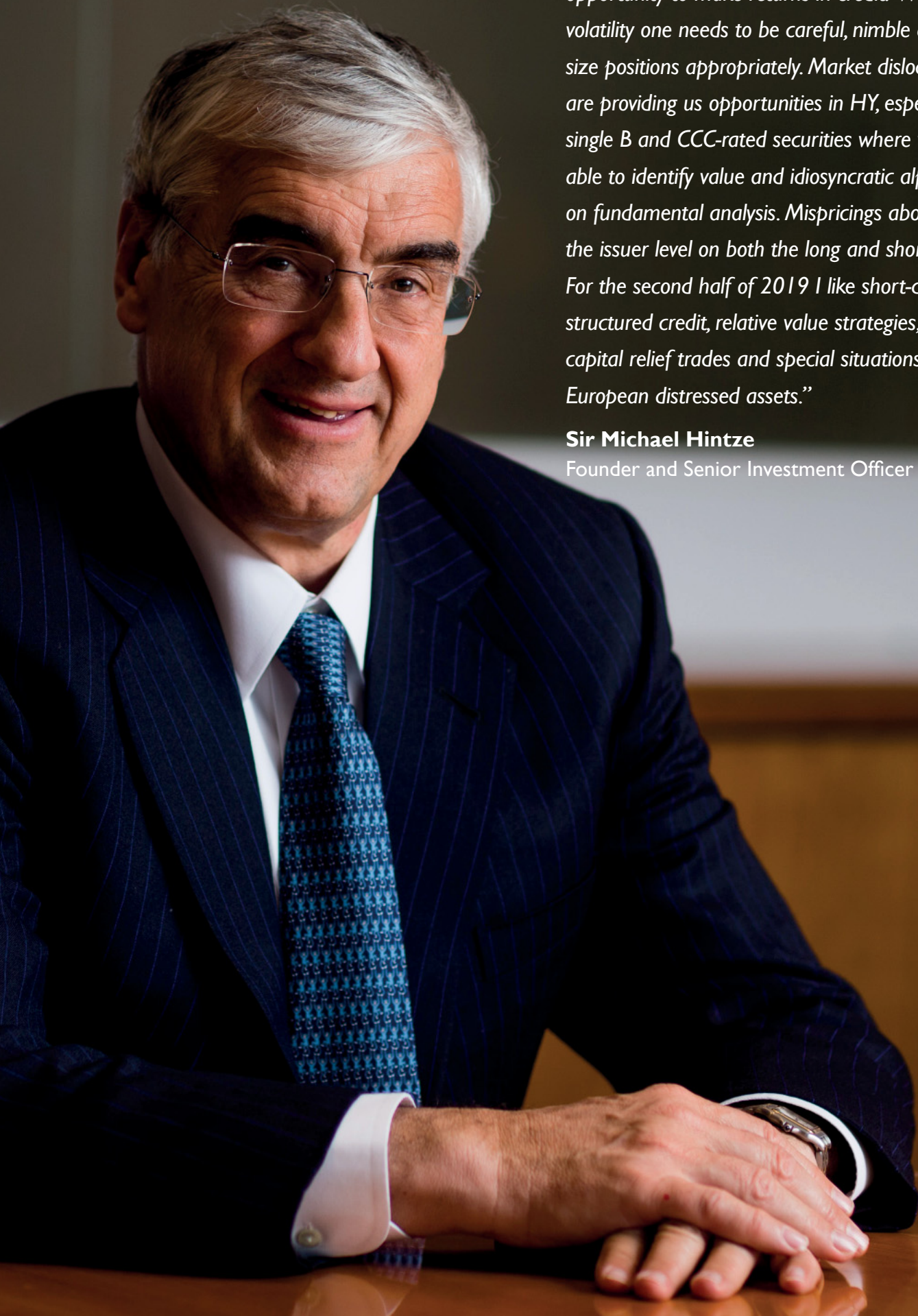
Mid-Year Review 2019

Sir Michael Hintze

JULY 2019

Sir Michael Hintze, Founder and Senior Investment Officer of CQS, presents his views on the credit cycle globally, and the risks and opportunities he sees in markets during the second half of 2019

CQS



“There are significant crosscurrents in markets. Nevertheless, my fundamental thesis is constructive. Dispersion continues to provide substantial opportunity to make returns in credit. With greater volatility one needs to be careful, nimble and right-size positions appropriately. Market dislocations are providing us opportunities in HY, especially in single B and CCC-rated securities where we are able to identify value and idiosyncratic alpha based on fundamental analysis. Mispricings abound at the issuer level on both the long and short side. For the second half of 2019 I like short-dated structured credit, relative value strategies, regulatory capital relief trades and special situations, especially European distressed assets.”

Sir Michael Hintze

Founder and Senior Investment Officer of CQS

Market views

Constructive market view

“I am fascinated by the challenges posed by today’s markets and remain excited about generating returns for clients. I continue to be cautiously constructive and see substantial opportunity both on the long and short sides of the market in a more dispersed world.”

There are a significant number of cross-currents in markets. Nevertheless, my fundamental long-term thesis is constructive. The US is still growing, as too is the Chinese economy. Albeit a limited trade deal would be well received by markets, the tariff issues may now not be fully resolved, but my view is that this will, at worst, realign global growth rather than destroy it totally. In the short term, global growth could decrease to around 2.25%, but I do not see it turning negative. There is just too much fiscal and monetary stimulus in China and in the US for it to do so.

The great strategic rivalry between the US and China will continue in the tech space for decades to come. It could even cause a Cold War Mark II. Unlike the Cold War between the US and the Soviet Union which was based primarily on the ideology of two systems, the rivalry with China has material economic dependencies that were absent between the US and USSR. However, the existence of economic interests should mean it will not be overly destructive to long term growth since it will be more nuanced and fought along the lines of technology rather than ideology.

Dispersion and idiosyncratic opportunities will be more prominent. Market structure will also lead to more violent short-term moves which should subsequently correct. As far as the credit cycle is concerned, we are well into it, as I have discussed before. However, I do not see any short-term catalyst to end it. At the end of last year, concerns about global growth led to a sharp market correction. In November and December of 2018, we aggressively added risk. In March 2019, in portfolios I manage, we began to put on hedges as valuations rose and credit spreads tightened. More recently, I have taken off some of these hedges as central banks have communicated further accommodation. Defaults remain relatively low, and increased volatility in H2 2019 should allow us to selectively add to risk, especially on idiosyncratic widening in credits that we like. That said I am mindful that in the longer-term, especially in 2022–2024, there is a significant need to refinance the Investment Grade (‘IG’) universe (absent substantial refinancing prior to that). Additionally, US Treasuries issuance will be exacerbated by the structural deficit that is being run in the US. As a result, we expect further volatility, especially 3 - 5 years from now.

I am pleased to report that the strategies we manage have, by-and-large, performed well and I believe there are excellent investment opportunities for the second half of the year. The market is concerned about growth, the quality of cash flows and leverage. In credit, this has led to the relative outperformance of the higher end over the lower end of the capital structure. This dislocation is providing us opportunities in High Yield (HY), especially in single B and CCC-rated securities where we are able to identify value and idiosyncratic alpha based on fundamental analysis. For the second half of 2019 I like short-dated structured credit, relative value strategies, regulatory capital relief trades and special situations, especially European distressed assets. Convertible bonds are also enabling us to benefit from the inherent attractive convexity of their return profile. While loans have underperformed broader credit indexes in H1 2019, my belief that default rates will remain modest, along with our selective approach, should allow us to generate good risk-adjusted returns in this asset class. The team remains constructive on the global ABS proposition, focusing on stable income profiles with lower correlation to wider markets.

Risks

“Remaining mindful of the ‘known knowns’, while continually striving to identify the ‘known unknowns’, is what most challenges and excites me.”

Of course, one needs to be mindful of what could go wrong, as well as what could go right. There are significant tail risks – the environment, geopolitics, epidemics, an escalation of conflict with Iran that leads to a spike in the oil price and which impacts global economic growth, the challenges facing the European Union, as well as Brexit, and so on. Trade conflict is certainly high up on the list of risk factors. I will not dwell on it here and in particular on the US-China trade negotiations, as I have written extensively on the subject in my previous updates on this rivalry and the geo-tech war, which I alluded to earlier. Nevertheless, it will continue to weigh on markets and result in geopolitically-inspired market volatility. Remaining mindful of the ‘known knowns’, while continually striving to identify the ‘known unknowns’, is what most challenges and excites me. Naturally, it’s the ‘unknown unknowns’ that are truly the ‘black swans’. An example might be an airborne epidemic similar to Spanish Flu in 1918. As unpleasant and devastating as Ebola was, it is a disease spread through contact rather than being airborne, and was consequently regionalized and containable. Other examples might be a nuclear atrocity or solar flares as devastating as coronal mass ejections. Importantly, the challenge of identifying such risks informs our overall investment process and ongoing risk management framework.

Policy Errors, QE and Modern Monetary Policy (MMT)

“But will QE be as effective as it has been in the past?”

“Indeed markets may already be pricing in the prospects of further QE and the actual effect of any announcement may be close to zero.”

Policy errors are another source of risk. This is especially true today when central bank independence is under growing political pressure in many countries, and where QE and Modern Monetary Theory (MMT) could still be regarded as experimental. A loss of faith in the system could also be potentially catastrophic.

In the context of weakening economic data, the prospects of further central bank easing via lowering overnight rates and additional QE have driven market performance over the last few months. But will QE be as effective as it has been in the past? There is academic evidence that QE’s effect is diminishing¹. Given the present level of inflationary expectations and rates, the effects are likely to be more muted. Indeed, markets may already be pricing in the prospects of further QE and the actual effect of any announcement may be close to zero. The timing and size of the ECB’s re-launch of QE is uncertain. Speculation is that it could be as early as Q4 2019 or Q1 2020, and be in the range of €45bn or greater per month. The Fed has turned dovish and forward rates are suggesting rate cuts of 50bps this year. But the notion of a central bank policy error cannot be dismissed.

In this post GFC, QE-dominated environment, it seems to me something has changed. There’s been a transformation in this Dynamic General Stochastic Equilibrium (DGSE) world. For example, what now happens in a MMT world is that the Treasury can issue bonds through the banking system creating excess reserves and where the ultimate repository of those bonds is the central bank. Remember, most Reserve Banks are not owned by the government, they are independent entities. So, liquidity is being

Source: ¹QE No Longer Works: Deutsche Bank research July 2019.

“... they are all behaving in ways that confound their historical relationships...”

created, not cash, as such. Liquidity is so abundant that it actually decreases inflation; it increases the supply of money to the point where you have negative interest rates. It's an intriguing world we now occupy.

Some commentators have rubbished MMT. While I am not a theoretical macro-economist, what I currently see are the counterintuitive outcomes. Whether that's the Phillips Curve or the Keynesian Supply/Demand curve, they are all behaving in ways that confound their historical relationships and explanations are being sought for this. It's all very well to dismiss MMT, but in academic literature there is a view that forward expectations of inflation matter more than the actions of a central bank, hence the focus on DGSE. When I started at Salomon Brothers in 1982, we all used to wait on the Trading Floor for the Federal Open Market Committee to act. Now it doesn't matter. Now what we're waiting for is the governor of a central bank's words; it's about what they say; it's about forward guidance. They're parsing and counting words, not money. Market participants are hanging on every word and their nuance.

The inverted US yield curve

“There are good technical reasons why the US yield curve has flattened.”

The inversion of the US yield curve has garnered a great deal of attention given its historic relationship as a reliable recession indicator. However, I believe this inversion may have more to do with technical factors, rather than presaging a recession.

There are good technical reasons why the US yield curve has flattened. Issuance due to a ballooning US deficit has been high. The increased issuance by the US Treasury is focussed on short-term bills, whereas the Fed has been buying further out the yield curve, in the 10-year plus point. Accentuating this is that the Fed could be buying USD 100bn in T-bills in 2020, or around half of net issuance, and even more beyond that. From October 2019, the Fed will reinvest principal payments from its MBS holdings into Treasuries in the secondary market, and around 15% into T-bills.

Negative yields in Germany and Japan due to Quantitative Easing (QE) have left US debt comparatively attractive, further compressing term premium. Furthermore, low inflation expectations in the US pension funds' funding ratios have steadily improved largely due to the stock market rally as well as increased contributions following the corporate tax break in September 2018. This has resulted in demand for duration as pensions switch into Treasuries from equities

These technical, rather than fundamental, factors have driven the yield curve to invert. In fact, if the Fed soon eases, the yield curve may begin to steepen back out.

As an aside, the EU's Solvency II Directive's impact on markets is a concern as it obliges insurance companies to gravitate towards highly rated, often government paper. In today's market, that can mean buying EU government securities at a negative yield. Is it rational to pay a government treasury to own its bonds? Is this the right way to preserve principal? It seems irrational to me. Is the world really that risky?

Market structure: Stronger banks, but more fragile markets

Market structure and liquidity have changed significantly. Consequently, we will continue to see lower levels of overall volatility punctuated by gapping markets and rapid mean reversion. There are three primary reasons for this – bank regulation, passive funds and algo trading. In a period of low or high volatility, fundamental risks may not change and these traders will typically follow GARCH-style driven models, resulting in quicker mean reversion. Right-sizing positions and managing portfolio liquidity to be able to take advantage of gapping markets and mark-to-market volatility is a key focus for us. Q4 2018 and the subsequent rally in Q1 this year illustrates this point, namely that current market structure can provide dislocations for us to capture alpha.

What this means for investors

Clearly, timing an entry and exit point is important, but very difficult to execute properly. Many of our clients debate whether assets will continue to generate the income and growth that they are targeting to meet their liabilities. With global nominal GDP of about USD80tn and investable assets of around USD300tn, how does one generate long term returns of 5%, 6% or 7%, or more, particularly in a world with \$12tr of negative-yielding bonds?²

Real economy assets typically have a lower volatility, akin to M1, but at what multiple is one buying such an asset, and is the return sufficient? If one invests in assets such as equities and credit, which are akin to M3, the volatility profile typically rises. Hence, it's a question of a client's willingness to tolerate mark-to-market volatility. However, to achieve significant returns without commensurate volatility is largely incongruous. Longer lock structures can mitigate this, and can enable a manager to generate alpha, absent the noise associated with short-term market fluctuation.

We manage a range of strategies with differing liquidity terms and volatility profiles. We take our investment and operational risk management approach very seriously. This is paramount to our organizational framework. As recent well-publicized events have highlighted, matching fund liquidity with the liquidity of its underlying holdings is critical. My belief is that investors pay us to take investment risk to generate sufficient risk adjusted returns, and not expose them to institutional or operational risk.

Source: ²CQS Research as at 28 June 2019.

Asset Class Thoughts and Outlook

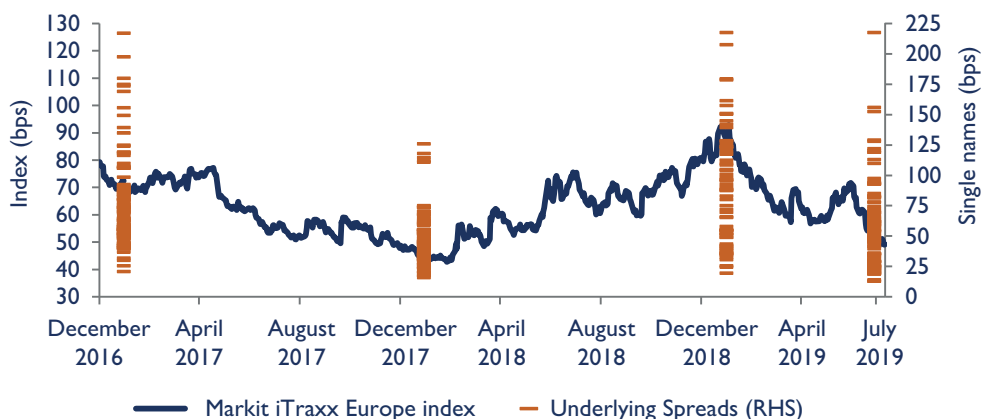
Credit

“I believe the credit cycle has further to run”

As I mentioned, I believe the credit cycle has further to run. In portfolios I manage, I continue to be constructive, seeking to take advantage of volatility and dispersion, and idiosyncratic credit opportunities. 2018 was a year in which credit markets normalised and started to behave in a more ‘healthy’ manner. What I mean by this is that all boats were lifted by the rising QE tide, but in 2018 the tide ebbed. Bad and good news took bonds down or up. The recent credit rally has been driven in part by rate expectations which have driven liquid IG to tighten much more than HY. While IG valuations in particular are not as attractive today as they were at the beginning of 2019, IG Cash, especially BBB-rated, continues to look relatively attractive on an idiosyncratic basis as deleveraging continues to be a focus of many names. US IG BBB spreads have tightened from the wide of close to 230bps in early January to around 170bps now. In part this is due to market expectations of rate cuts reflecting perceptions of a sharply slowing US economy, and a resultant ‘flight to quality’. As I mentioned earlier, tactically I have taken some hedges off because of QE expectations.

In Europe, differentiation and dispersion has returned meaningfully. Figure 1 below illustrates European IG spread (blue line) and dispersion (orange dots).

Figure 1: Growing dispersion in IG³



“In the medium-term, the effect of ECB QE should benefit Italian banks...”

Italian banks dominate the widest names, with Dutch information services firm, a German industrial company and a Telco amongst the tightest. Interestingly, Italian banks may be one of the biggest beneficiaries of ECB QE. They trade at the widest gap to EU banks since 2016. While BTP spreads will be affected by the Italian 2020 budget negotiations, we believe a compromise with the EU will be found. In the medium-term, the effect of ECB QE should benefit Italian banks and we have been adding to positions selectively. The lower-rated parts of HY have lagged. During H1, 2019, in the US, BBs returned 10.8%, whereas B and CCCs rose 9.8% and 8.5%, respectively.⁴ The decompression and then compression suggests we’re in a range-bound volatile trading environment, rich with opportunities. I certainly believe this to be the case.

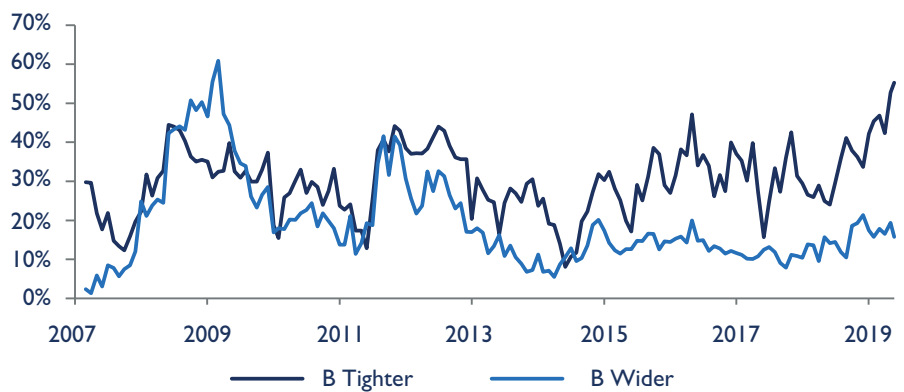
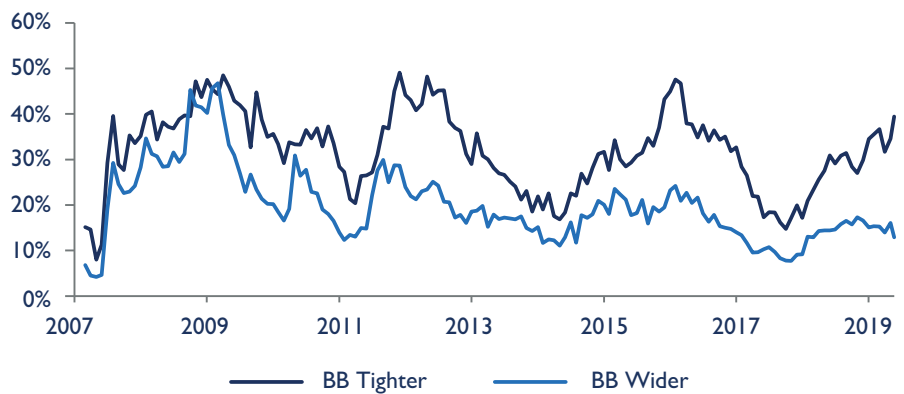
Source: ³Bloomberg and CQS Research as at July 2019. ⁴Bloomberg. Total return, USD, as at 28 June 2019.

“...dispersion is back.”

Figure 2 below illustrates the dispersion in European HY. It shows the proportion of the index trading tighter than the bottom end of the range relative to the proportion trading wider than the top end of the range. Of particular interest to us, as fundamentally-driven investors, is that the proportion of single-B bonds now trading through the index average is over 55%. Based on our fundamental and qualitative analysis, this enables us to identify value both on the long and short sides. Interestingly, it appears to us that there is more relative value and idiosyncratic opportunity in Europe at this time.

“...it appears to us that there is more relative value and idiosyncratic opportunity in Europe at this time.”

Figure 2: Dispersion is back in HY⁵



Source: ⁵Deutsche Bank Research, ‘A closer look at EUR HY dispersion’ and Markit, as at 26 June, 2019.

Special Situations

“Dispersion is growing significantly...”

Dispersion is growing significantly in both the US and Europe. Companies with weaker balance sheets are coming under increased pressure and this has been particularly notable during H1 2019 as the broader market has rallied. US BB-rated bonds have returned 7.9% in terms of capital appreciation, whereas CCC-rated bonds, adjusting out for the 35+ points rally in PetSmart, have only rallied 3%.⁶ In Europe, the dispersion is also stark, greater than the 2016 highs according to some measures. As a result, there is an increasing opportunity set for us in Special Situations strategies.

Figure 3: Distressed ratio rising⁶

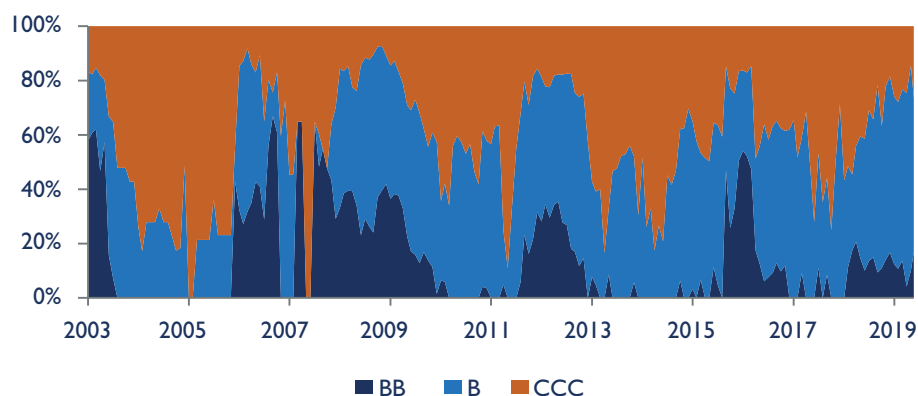


Figure 3 shows the rating makeup of the distressed ratio by rating. The chart shows the proportion of the index trading wider than 1000bps. While there is little evidence of any extreme systematic distress, the ratio has been steadily rising during H1 and is now back above 7%. The notional face value of B-rated debt within the distressed ratio (>€12bn) is at its highest level since the European sovereign crisis.⁷ Some of the notable drivers include indiscriminate selling by real money accounts in sectors such as Consumer Discretionary, Oil & Gas and Telcos, as well as Brexit uncertainty. Some notable European underperformers include Boparan, Lecta, Interlot, Thomas Cook, CMA, Tereos, Moby, Casino and Rallye. In the US, the list is understandably dominated by Oil & Gas with names such as Sanchez, Weatherford, Rowan and Chesapeake. Telcos have also come under pressure with Windstream filing for Chapter 11 and Frontier weakening dramatically.

“...many businesses which have otherwise sound business models have come under pressure and present us with idiosyncratic opportunities.”

Continued uncertainty surrounding the course of Brexit in the UK and the future path Europe will take, is creating on-going opportunities. Consumer and business confidence has been hit. Alongside disruption from on-line competition, the Retail and Travel & Leisure sectors continue to come under pressure, in turn impacting businesses further down the chain such as the commercial real estate they occupy, specialty lenders, banks that provided them with relationship loans, and so on. Given the backdrop, many businesses which have otherwise sound business models have come under pressure and present us with idiosyncratic opportunities to work with management to right size capital structures and stabilize operations.

Source:⁶Bloomberg and CQS Research as of 28 June 2019. ⁷Deutsche Bank Research, ‘A closer look at EUR HY dispersion’ and Markit, as at 26 June, 2019.

Another area of growing opportunity is Liquidation and Litigation strategies. Many of the existing opportunities in Financials are on the back of European governments intervening to restore bank solvency, some in contradiction to the spirit of the EU Bank Recovery and Resolution Directive (BRRD.) Such actions have alienated many creditors, making it in turn even more difficult for weaker banks to attract desperately needed capital, giving rise to lawsuits as investors seek to recoup losses and others seek to identify compelling entry points.

Relative Value Strategies

An environment of higher market volatility is typically accompanied by higher dispersion. We believe such market conditions exist and will likely persist. One of the best ways to express increased dispersion is through Relative Value strategies as pay-offs of volatility/dispersion can be highly asymmetric. In Europe, the ECB's QE activities include asset purchase programmes, which tend to favour IG corporate bonds. At the same time, growing dispersion means bifurcation between higher quality credits and lower quality ones, especially in HY. For example, to 'own' dispersion, we might construct a highly convex, asymmetric pay-off by positioning long senior financial credit and short European HY. Actual construction of such a strategy is far more complex but enables Relative Value strategies to own cheap convexity which benefits from increased dispersion.

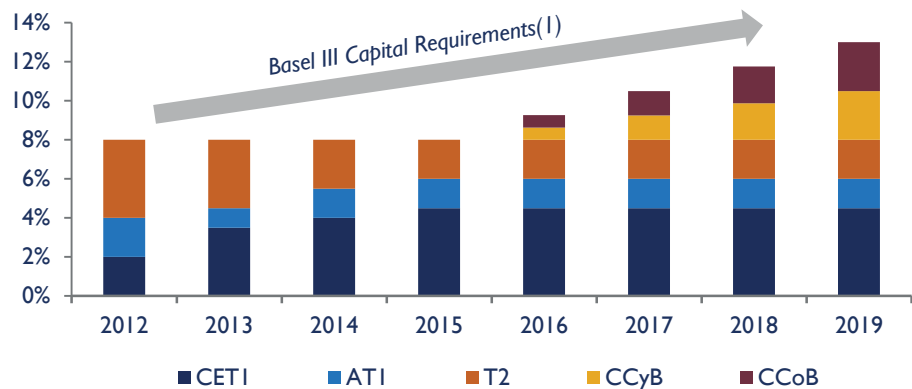
Regulatory Capital Relief (SRT)

As bank regulation evolves, Regulatory Capital transactions, officially termed as Significant Risk Transfer (SRT) by Regulators, will be an important part of a bank's tool kit to manage their capital positions in addition to instruments such as ATIs, CoCos and Contingent Capital. SRT transactions are another potential tool that can help them manage their regulatory capital risk via risk sharing of the loans on their balance sheets with a range of institutional investors. SRTs can offer stable and low correlated returns. These transactions use well established securitisation technology. Unlike traditional securitisations, they are not driven by arbitrage motivations, but rather they are risk sharing transactions where the bank and investors are closely aligned and both benefit in different ways.

“An environment of higher market volatility is typically accompanied by higher dispersion.”

“SRT... are risk sharing transactions where the bank and investors are closely aligned...”

Figure 4: Banks' Regulatory Capital requirements continue to rise⁸



Source: ⁸The New Basel III Framework: Navigating Changes in Bank Capital Management. PwC's FSI, October 2010. ARP Research.

SRT provides an opportunity to work alongside banks, allowing investors to develop close relationships to understand and invest in their core lending businesses, whereby banks use SRT to allow them to retain attractive core lending exposures on their balance sheets to manage the capital of their on-going core business operations where they have a significant market presence and wish to continue to do so. It provides alignment and allows an investor to share risk with a bank in its core loan portfolio, while isolating that investment from general bank risk. The risk-adjusted returns offered by SRT investments are attractive and compare favourably to competing opportunities in adjacent sectors. For example, loss adjusted yields on an SRT transaction are typically in the region of 8 to 12% versus ATIs which typically offer income yields of 4 to 6%.⁹ With SRT issuance projected to be EUR 6-7bn this year, we continued to identify compelling opportunities.

ABS

In recent months, the focus has been on allocating to stable income profiles with lower correlation to wider markets, maintaining liquidity and hence flexibility within the portfolio and to managing any tail risk. During H1 2019 ABS markets generally lagged the performance of credit and equities markets. This divergence in spread performance between ABS and general credit markets has further increased the available spread pick-up we can achieve in our markets, across a range of investment opportunities. This spread basis comes despite the secured nature of ABS and continued strong collateral credit performance.

As a higher and higher proportion of global assets tend to zero or negative returns, ABS sectors from US RMBS to European CLOs offer compelling relative value to their relevant comparatives. One of the most notable is in European CLOs, where new issue single-B is pricing around Euribor+900, with some names as wide as Euribor+975, compared with European HY where the iTraxx XOVER index is trading at a spread of approximately 250 basis points. This is partly driven by the lag in ABS markets and also by supply technicals. Numerous ABS sectors sit near the widens of recent spread ranges. We favour assets with the lower volatility and idiosyncratic sector plays such as Regulatory Capital trades, US Monoline related trades and Consumer ABS. We are also maintaining a lower risk, liquid element in the form of US RMBS. The US housing market remains well supported and we believe US RMBS continues to offer attractive return potential going forward.

Global loans

We continue to like loans. Generically, they have defensive features – attractive current income, floating rate, well diversified, senior and secured – lending themselves to institutional investment. Economic uncertainty, combined with more accommodative monetary policies in the US and Europe, and some concerns over leverage and liquidity, have introduced an element of volatility for specific industries and individual borrowers. We see this as an opportunity to capitalise on the increased dispersion of returns across geographies and between sectors, to generate alpha from asset allocation and

Source: ⁹Bloomberg, as of 28 June 2019.

credit selection. Despite the potential for idiosyncratic volatility, we remain constructive on the overall fundamental landscape in both the US and European loan markets. We currently favour the European loan market over the US due to a more stable technical landscape there is an (absence of daily liquidity retail funds in the EU). The prospects for supportive ECB asset purchasing fixed rate securities should also increase the relative attractiveness of loans.

ESG

The ESG theme is important and it is a key factor that is integrated into our investment process. We view ESG considerations as a growing driver influencing financing costs, valuations and performance, while also acting as a lever to shape and influence the world for generations to come. According to Morningstar, ESG money market funds have risen to \$52bn in the first half of 2019. While still a modest proportion of the \$6tn in the money market sector,¹⁰ it is an indication of ESG's growing importance. My sense is there is growing anecdotal evidence that ESG factors do and will continue to have an impact on companies' cost of capital and performance. As investors, we need to have the tools to monitor and measure the effect of ESG factors as part of our analysis and decision-making process. In addition to ESG being an integral part of our analysis, as a signatory to Principles for Responsible Investment ("PRI") we seek to be an active owner of securities, to incorporate ESG issues into our ownership policies and practice, and seek appropriate disclosures by entities we invest in. We are also aiming to promote acceptance and implementation of the Principles within the investment industry, to work with the PRI Secretariat and other signatories to enhance the effectiveness in implementing the Principles, and to report on our activities and progress towards implementing them.

Geopolitical

Geopolitics is increasingly complex as the US election approaches and this is certainly going to weigh on President Trump's decision making, including on the trade war with China.

Brexit and the EU

There are three things that I find particularly interesting from our work. First is our view that there may be some hope for the new British Prime Minister's negotiations with the EU. The EU have concessions ready which they did not 'spend' on his predecessor because they did not believe Mrs. May could win over MPs. The second is that Italy's 2020 budget is due in October, and Mediterranean migration – as well as vital reform of the EU and Eurozone, will once again rise towards the top of the EU's agenda in the Autumn. Third, not all is well within the EU. There are increasing tensions between Paris and Berlin, with relations between the two capitals at a modern low. This state of affairs could well be exploited by President Trump who appears to us to be

Source: ¹⁰Morningstar and Financial Times, as at 17 July, 2019.

intent on tariffs against German saloon cars, as he pursues trade talks with the EU with nothing off the table – including French agriculture. He could tactically seek to exploit this friction. From a market perspective, a hard Brexit has been largely discounted in the short-term (though perhaps not in the medium-term). Any sentiment that a deal on Brexit might be possible should benefit Sterling and UK assets. Conversely, a sharp downward adjustment of Sterling, such as in the case of no deal, would enable us to buy UK assets. Developments on the trade front between the US and the EU are likely to create volatility in EU markets, which I believe we are positioned to take advantage of.

Iran

And Iran? 20% of the world's oil passes through the Straits of Hormuz, a 21 mile-wide sea corridor, and reaction times between forces at high readiness are short. Much of this is already in the oil price and markets have also grown accustomed to 'noise'. In the short term the chances of an oil shock are high and given the importance of oil to the global economy, we continue to monitor the situation closely.

Summary

There are significant crosscurrents in markets. Nevertheless, my fundamental thesis is constructive. While we are well into the credit cycle, I do not see any short-term catalyst to end it. Dispersion continues to provide substantial opportunity to make returns in credit. It is a credit pickers' market. With greater volatility one needs to be careful, nimble and right-size positions appropriately. Market dislocations such as the one at the end of 2018 and beginning of 2019 is providing us opportunities in HY, especially in single B and CCC-rated securities where we are able to identify value and idiosyncratic alpha based on fundamental analysis. Mispricings abound at the issuer level on both the long and short side. For the second half of 2019 I like short-dated structured credit, relative value strategies, regulatory capital relief trades and special situations, especially European distressed assets.

I would like to thank our clients for the confidence and trust they have shown in us and, as always, we will continue to do our very best to generate attractive returns.

Sir Michael Hintze

Founder and Senior Investment Officer

IMPORTANT INFORMATION:

This document has been issued by CQS (UK) LLP (FRN 400496) which is authorised and regulated by the UK Financial Conduct Authority and/or (as the case may be) CQS (US), LLC which is a registered investment adviser with the SEC. The information is intended solely for sophisticated investors who are (a) professional investors as defined in Article 4 of the European Directive 2011/61/EU or (b) accredited investors (within the meaning given to such term in Regulation D under the U.S. Securities Act of 1933, as amended) and qualified purchasers (within the meaning given to such term in Section 2(a)(51) of the U.S Investment Company Act 1940, as amended).

CQS is a founder of the Standards Board for Alternative Investments ("SBAI") (formerly, the Hedge Fund Standards Board) which was formed to act as custodian of the alternative investment managers' industry best practice standards (the "Standards") published by the Hedge Fund Working Group ("HFWG") in 2008 and to promote conformity to the Standards. SBAI is also responsible for ensuring that they are updated and refined as appropriate. The Standards were drawn up by HFWG which comprised the leading hedge funds (based mainly in London) in 2007 in response to concerns about the industry, including financial stability and systematic risk. The HFWG completed its work in January 2008 and published its report outlining the Standards. By applying the Standards, managers commit to adopt the "comply or explain" approach described in the Standards.

The term "CQS" as used herein may include one or more of any CQS branded entities including CQS (UK) LLP, CQS Cayman Limited Partnership which is registered with the Cayman Islands Monetary Authority, CQS (Hong Kong) Limited which is regulated by the Hong Kong Securities and Futures Commission, CQS (US), LLC which is registered with the US Securities and Exchange Commission, and CQS Investment Management (Australia) Pty Limited which is registered with the Australian Securities & Investments Commission, Australian Financial Services Licence No. 386047.

This document has been prepared for general information purposes only and has not been delivered for registration in any jurisdiction nor has its content been reviewed by any regulatory authority in any jurisdiction. The information contained herein does not constitute: (i) a binding legal agreement; (ii) legal, regulatory, tax, accounting or other advice; (iii) an offer, recommendation or solicitation to buy or sell shares or interests in any fund or any security, commodity, financial instrument or derivative linked to, or otherwise included in, a portfolio managed or advised by CQS; or (iv) an offer to enter into any other transaction whatsoever (each a "Transaction").

Any decision to enter into a Transaction should be based on your own independent investigation of the Transaction and appraisal of the risks, benefits and suitability of such Transaction in light of your individual circumstances. Any decision to enter into any Transaction should be based on the terms described in the relevant prospectus, supplement, offering memorandum, private placement memorandum, subscription documents, trading strategy, constitutional document and/or any other relevant document as appropriate (each an "Offering Document"). Any Transaction will be subject to the terms set out in its Offering Document and all applicable laws and regulations. The Offering Document supersedes this document and any information contained herein.

Nothing contained herein shall constitute or give rise to the relationship of partnership nor shall it constitute a joint venture or give rise to any fiduciary or equitable duties. Any information contained herein relating to any third party not affiliated with CQS is the sole responsibility of such third party and has not been independently verified by CQS or any other independent third party. The information contained herein is not warranted as to completeness or accuracy and no representations are made in such respect, nor should it be deemed exhaustive information or advice on the subjects covered; as such, the information contained herein is not intended to be used or relied upon by any counterparty, investor or any other party. The information contained herein, as well as the views expressed herein by CQS professionals made as of the date of this document, is subject to change at any time without notice.

CQS uses information sourced from third-party vendors, such as statistical and other data, that are believed to be reliable. However, the accuracy of this data, which may also be used to calculate results or otherwise compile data that finds its way over time into CQS research data stored on its systems, is not guaranteed. If such information is not accurate, some of the conclusions reached or statements made may be adversely affected. CQS bears no responsibility for your investment research and/or investment decisions and you should consult your own lawyer, accountant, tax adviser or other professional adviser before entering into any Transaction. CQS is not liable for any decisions made or action taken by you or others based on the contents of this document and neither CQS nor any of its directors, officers, employees or representatives (including affiliates) accept any liability whatsoever for any errors and/or omissions or for any direct, indirect, special, incidental or consequential loss, damages or expenses of any kind howsoever arising from the use of, or reliance on, any information contained herein.

Information contained in this document should not be viewed as indicative of future results as past performance of any Transaction is not indicative of future results. Any investment in any fund or other vehicle managed by CQS (a "CQS Fund") or any of its affiliates involves a high degree of risk, including the risk of loss of the entire amount invested. The value of investments can go down as well as up. An investment in any CQS Fund will involve a number of material risks which include, without limitation, risks associated with adverse market developments, volatility of markets invested in, currency and exchange rate risks, risk of counterparty or issuer default and risk of illiquidity. Any assumptions, assessments, intended targets, statements or other such views expressed herein (collectively "Statements") regarding future events and circumstances or that are forward looking in nature constitute only subjective views, outlooks or estimates and are based on CQS's expectations, intentions or beliefs. The Statements should not in any way be relied upon, and involve inherent risk and uncertainties beyond CQS's control. The Statements should not be assumed to be accurate or complete, now or in the future (including with respect to the composition and investment characteristics of any CQS Fund), and may be subject to change. CQS undertakes no responsibility or obligation to revise or update such Statements. Target returns and volatility targets discussed in this document are high-level, may change with market conditions and are generally used only as guidelines. Target returns reflect subjective determinations by CQS. Performance may fluctuate, particularly over short periods of time. Targeted returns should be evaluated over the time periods indicated and not over shorter periods. Target returns are not intended to be actual performance and should not be relied upon as any indication of actual or future performance. Some of the information contained in this document may be aggregated data of transactions executed by CQS that has been compiled so as not to identify the underlying transactions of any particular CQS Fund.

Any indices included in this document are included to simply show the general market trends relative to the types of investments CQS tends to select for certain CQS Funds for the periods indicated within this document. The indices are not representative of CQS Funds in terms of either composition or risk (including volatility and other risk related factors). CQS Funds are not managed to a specific index.

This document is not intended for distribution to, or use by, the public or any person or entity in any jurisdiction where such use is prohibited by law or regulation. In accepting receipt of this information, you represent and warrant that you have not been solicited, directly or indirectly, by CQS and are receiving this information at your own request. It is your responsibility to inform yourself of and to observe all applicable laws and regulations of any relevant jurisdiction.

(Continued on next page)

CQS (US), LLC is a member of the National Futures Association (the "NFA") and is subject to the NFA's regulatory oversight and examinations. However, you should be aware that the NFA does not have regulatory oversight authority over underlying or spot virtual currency products or transactions or virtual currency exchanges, custodians or markets.

The information contained herein is confidential and may be legally privileged and is intended for the exclusive use of the intended recipient(s) to which the document has been provided. In accepting receipt of the information transmitted you agree that you and/or your affiliates, partners, directors, officers and employees, as applicable, will keep all information strictly confidential. Any review, retransmission, dissemination or other use of, or taking of any action in reliance upon, this information is prohibited. Any distribution or reproduction of this document is not authorized and prohibited without the express written consent of CQS, or any of its affiliates.

AIFMD and Distribution in the European Economic Area: CQS (UK) LLP is an Alternative Investment Fund Manager (an 'AIFM') to certain CQS Funds (each an 'AIF') (as defined in the Alternative Investment Fund Managers Directive (Directive (2011/61/EU) ('AIFMD')). The AIFM is required to make available to investors certain prescribed information prior to investing in an AIF. The majority of the prescribed information is contained in the latest Offering Document of the AIF. The remainder of the prescribed information is contained in the relevant AIF's pre-investment disclosure document, the monthly investor report, and the fund limits document. All of this information is made available in accordance with the AIFMD. In relation to each member state of the EEA (each a "Member State"), this document may only be distributed and shares or interests in a CQS Fund ("Shares") may only be offered or placed in a Member State to the extent that: (1) the CQS Fund is permitted to be marketed to professional investors in the relevant Member State in accordance with the AIFMD (as implemented into the local law/regulation of the relevant Member State); or (2) this document may otherwise be lawfully distributed and the Shares may otherwise be lawfully offered or placed in that Member State (including at the initiative of the investor).

Information required, to the extent applicable, for Distribution of Foreign Collective Investment Schemes to Qualified Investors in Switzerland: The representative in Switzerland is ARM Swiss Representatives SA, Route de Cité-Ouest 2, 1196 Gland, Switzerland. The distribution of Shares of the relevant CQS Fund in Switzerland will be exclusively made to, and directed at, qualified investors (the "Qualified Investors"), as defined in the Swiss Collective Investment Schemes Act of 23 June 2006, as amended ("CISA") and its implementing ordinance (the "Swiss Distribution Rules"). Accordingly, the relevant CQS Fund has not been and will not be registered with the Swiss Financial Market Supervisory Authority ("FINMA"). The paying agent in Switzerland is Banque Cantonale de Genève, 17, quai de l'Île, 1204 Geneva, Switzerland. The relevant Offering Document and all other documents used for marketing purposes, including the annual and semi-annual report, if any, can be obtained free of charge from the representative in Switzerland. The place of performance and jurisdiction is the registered office of the representative in Switzerland with regards to the Shares distributed in and from Switzerland. CQS (UK) LLP (as the distributor in Switzerland) and its agents do not pay any retrocessions to third parties in relation to the distribution of the Shares of the relevant CQS Fund in or from Switzerland. CQS (UK) LLP (as the distributor in Switzerland) and its agents do not pay any rebates aiming at reducing fees and expenses paid by the relevant CQS Fund and incurred by the investors. GMvI.

Index Descriptions: It is not possible to invest directly in an index. The Markit iTraxx Europe index comprises 125 equally weighted credit default swaps on investment grade European corporate entities, distributed among 4 sub-indices: Financials (Senior & Subordinated), Non-Financials and HiVol. The composition of each Markit iTraxx index is determined by the Index Rules. Markit iTraxx indices roll every 6 months in March & September.

CQS (UK) LLP
4th Floor, One Strand
London WC2N 5HR
United Kingdom
Tel: +44 (0) 20 7201 6900
Fax: +44 (0) 20 7201 1200

CQS (US), LLC
152 West 57th Street
40th Floor
New York
NY 10019
United States
Tel: +1 212 259 2900
Fax: +1 212 259 2699

CQS (Hong Kong) Limited
Unit 1207, 12th Floor
No.9 Queen's Road Central
Hong Kong
China
Tel: +852 3920 8600
Fax: +852 2521 3189

**CQS Investment Management
(Australia) Pty Limited**
Level 13
1 Margaret Street
Sydney
NSW, 2000
Australia
Tel: +61 2 8294 4180

clientservice@cqsm.com
www.cqs.com



About CQS

CQS is a credit-focused multi-strategy asset manager founded by Sir Michael Hintze in 1999. Our deep experience allows us to offer solutions for investors across a range of return objectives and risk appetites. We are an active asset manager with expertise across the credit spectrum, including corporate credit, structured credit, asset backed securities, convertibles and loans. We are committed to delivering performance and high levels of service to our investors. CQS has offices in London, New York, Hong Kong and Sydney.