"Better Value, Dangerous Technicals"

Lyxor Chenavari UCITS fund up c. +1.26% (gross USD) year-to-date as at Friday 13 March close

Dear investors,

Whilst our usual pace is to laboriously produce investment letters once or twice a year, we believe that the exceptional market conditions in the past two weeks do warrant an update. As NAVs are being finalised, we are presenting below Chenavari's latest gross estimates in USD, the Fund's reference currency. These are meant to provide orders of magnitude rather than final numbers.

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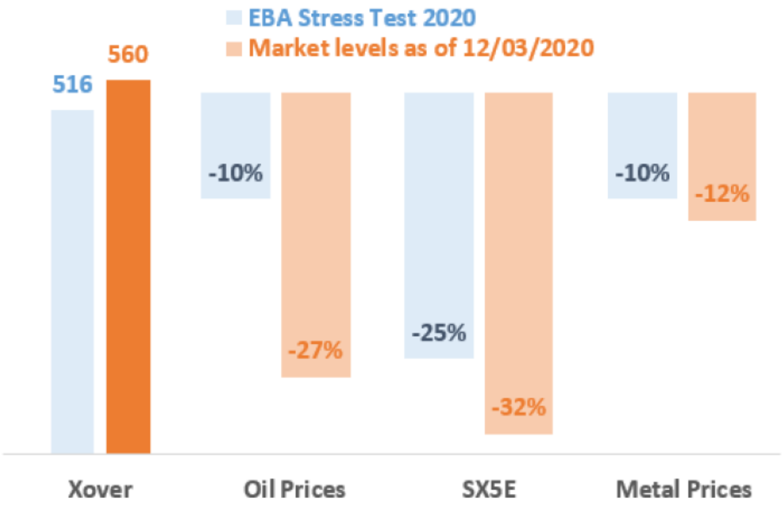
A lot has happened since we issued our last letter on 2 March[1]. A large portion of Europe has woken up to the angst of quarantine, closed schools, atrophied social life, spoiling any potential joy of working from home without guilt. Whilst the direct medical impact of the virus remains somewhat muted as yet (in the crude, cold language of statistics), its indirect effects have already taken a huge toll on communities, people's mental health, – and on the financial markets (see full details on Chart 2, page 3).

To get an order of sense of the market rampage, it is helpful to compare the moves to the adverse scenarios used for the 2020 EBA Stress Tests (which have now been postponed to 2021), as Chart 1 shows.

Chart 1: "When Reality Overcomes Fiction"



Source: BNP Paribas Credit Research, 13 March 2020

[1] https://www.chenavari.com/assets/Uploads/b13276b390/200302-Lyxor-Chenavari-UCITS-Update-EXTERNAL.pdf

The week started with oil carnage; then it was Central banks' showtime. Both the ECB and the Fed failed to reassure. Indeed, this crisis is very much a "real economy" crisis, with many small businesses at risk of defaulting across the world – and larger ones too, potentially triggering a global credit (and social) crisis.

This time, relief may only come from Governments, which will have to step into the economy and unleash major actions such as the ones announced by President Macron in France on Thursday (talking about a "massive" programme including notably the creation of a "solidarity fund" to help businesses affected by the pandemic, as well as credit guarantees to SMEs[2]). The significant move by Donald Trump on Friday night to declare national emergency and release USD50bn is another example of these State-driven actions. One may note that these necessary actions will come at a huge cost – a further increase of public debt levels, which bodes ill for the solidity and margin for manoeuvre of many countries in the decades to come.

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<u>Fund Positioning</u>

In the European credit market, we observed a correction in High Yield over the past week. The IBOXX HY was down 11%, with many bonds dropping more than 20 points. Liquidity contracted sharply as the fear of ETF selling and outflows intensified. The market moves are summarised in Chart 2.

Against that backdrop, the Fund's portfolio was fairly well protected, as we favoured a low levered exposure minimising basis risk (i.e. the vast majority of the Fund's shorts consisted of bonds). The co-PMs dramatically reduced the number of Bonds held (from 37 at the beginning of February to 21 on 13 March). Finally, the convexity strategy played its role as a "buffer", contributing 17bps to the gross performance at the Fund level in March, whilst accounting for 10% of the allocation.

As we write this letter, we are entering the third week of March slightly up year-to-date (circa +1.26% gross according to our estimates), as shown on Chart 3.

[2] Source: Financial Times, "France to close all schools as it braces for 'Italian Scenario'", 12 March 2020

Chart 2: Recent performance of key reference indices (week-on-week changes, MTD and YTD)

	January	*February 2020*					*March 2020*			YTD
	2020	Week 1	Week 2	Week 3	Week 4	MTD	Week 1	Week 2	MTD	2020
Main s32 5y (IG)	+4.8%	-6.1%	-4.6%	+3.5%	+49.8%	+38.9%	+23.4%	+34.0%	+65.3%	+140.7%
XO s32 5y (HY)	+11.3%	-6.6%	-1.7%	+3.6%	+38.2%	+31.5%	+25.3%	+36.1%	+70.4%	+149.5%
SNRFIN s32 5y	+5.3%	-9.7%	-3.8%	+3.8%	+54.0%	+38.9%	+21.2%	+39.9%	+69.5%	+147.9%
SX5E (EUROSTOXX 50)	-2.8%	+4.3%	+1.1%	-1.1%	-12.4%	-8.6%	-2.9%	-20.0%	-22.3%	-31.0%
SPX (S&P 500)	-0.2%	+3.2%	+1.6%	-1.3%	-11.5%	-8.4%	+0.6%	-14.6%	-14.1%	-21.4%
SX7E (EUROSTOXX Banks)	-5.5%	+9.0%	+1.5%	-2.7%	-14.5%	-7.9%	-10.9%	-23.3%	-31.7%	-40.6%

Note: for credit indices, performance is expressed in spread variations (spreads increase as markets fall)
Source: Bloomberg

Chart 3: Lyxor Chenavari UCITS L/S Credit - gross P&L attribution overall and by Strategy (USD)

	January	*February 2020*					*March 2020*			**YTD**
	2020	Week 1	Week 2	Week 3	Week 4	MTD	Week 1	Week 2	MTD	**2020**
Corporate	1.04%	0.15%	-0.03%	0.10%	0.12%	0.34%	-0.32%	-0.48%	-0.80%	**0.58%**
Financials	0.77%	0.34%	0.24%	0.09%	-0.52%	0.14%	-0.37%	-0.44%	-0.80%	**0.11%**
Structured Credit	-0.06%	0.08%	0.06%	-0.05%	0.05%	0.14%	-0.20%	0.37%	0.17%	**0.25%**
Other	0.11%	0.04%	0.03%	0.02%	0.03%	0.12%	0.06%	0.03%	0.09%	**0.32%**
Overall Fund GROSS	*1.85%*	*0.61%*	*0.30%*	*0.16%*	*-0.33%*	*0.74%*	*-0.82%*	*-0.51%*	*-1.34%*	***1.26%***
Net perf SI EUR *	1.21%	0.54%	0.15%	0.05%	-0.35%	0.38%	-0.92%	-0.17%*	-1.09%*	**0.49%***
Net perf SI USD *	1.36%	0.58%	0.18%	0.08%	-0.31%	0.52%	-0.89%	-0.17%*	-1.07%*	**0.80%***

** Net performance from Bloomberg as at 9 March 2020*
Source: Chenavari unaudited estimates, 13 March 2020

In the wake of the market collapse, we would like to make the following two points.

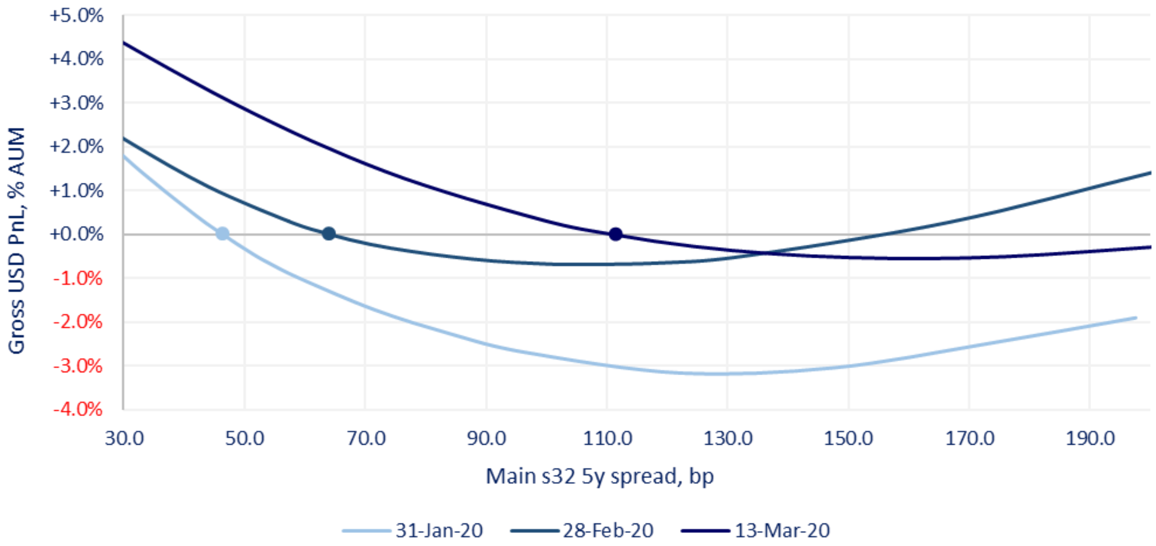
<u>First, value is reconstituting</u>. After many years of super tight levels, we are starting to see “fundamental value” in some areas (the credit spread of the iTraxx Crossover 5 year is now c. 520 bps while it was trading close to 200 bps at the start of the year).

<u>Second, technicals will be king in the short-term</u>. After the brutal sell off, we would expect some of the most exposed funds to start facing redemptions. Depending on the magnitude of those redemptions, and the level of leverage of the funds, we believe that some “half liquid” instruments could be hit by forced selling. This could trigger further dislocation on certain cash instruments, paving the way for very attractive entry points on certain corporate bonds and AT1s.

This thesis of “better value, dangerous technicals” has driven us to build a profile with a slight skew towards synthetic instruments on the long side, in addition to bonds, whilst the shorts are mostly expressed via cash bonds.

Overall, the Fund's positioning remains very flat. We try to limit our maximum drawdown in the scenario of further widening (cf. chart 4: less than 1% drawdown in any scenario, thanks to convexity and options).

Chart 4: Fund level systemic stress as a function of iTraxx Main (S32 5Y) spread (the dot representing the position of the Main index at the time of the Curve)



Source: Chenavari unaudited estimates, 13 March 2020

Chart 5 gives a more precise picture of our exposure by instrument. For the sake of clarity, note that long positions are the lines showing a positive performance in case of a tightening of indices -and short positions the opposite.

In summary, the Fund's long sleeve is quite balanced between bonds and CDS indices. However, shorts are very largely skewed toward cash instruments (expressed via the BondTRS line).

This creates a "long synthetic / short cash" basis, which we are using to play the potential dislocation of certain cash instruments.

It is also important to note that the fund has built a comfortable cash buffer, giving us the ability to buy back some bonds should the potential technical dislocation mentioned above create attractive opportunities. This also means that the Fund's positioning remains very opportunistic and could evolve extremely quickly as the co-PMs see fit. More than ever, the current market conditions call for being agile and opportunistic; the positioning represented above is only a picture at a point in time and could change fast.

Chart 5: Sensitivity of the Fund's portfolio per instrument type on various scenarios of widening / tightening (Corporate and Financials Strategies)

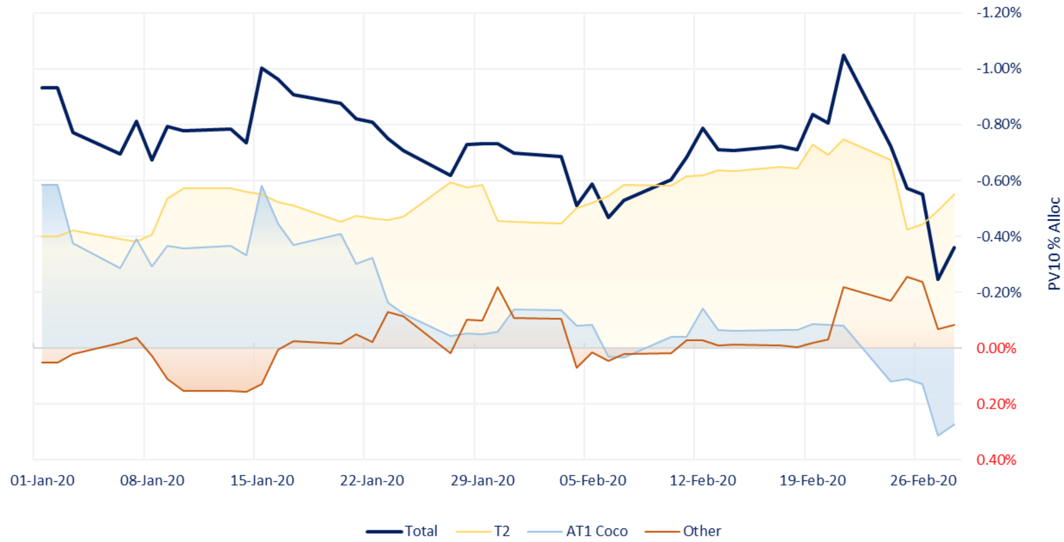
	tightening of indices (%)				widening of indices (%)		
	Stress (5y credit tenor)						
Trade Type	*-50%*	*-20%*	*-10%*	*0%*	*10%*	*20%*	*50%*
CDSIndex (SYNTHETIC)	1.88%	0.71%	0.35%	0.00%	-0.34%	-0.67%	-1.62%
Bond (CASH)	4.15%	1.50%	0.72%	0.00%	-0.67%	-1.29%	-2.92%
BondTRS (CASH)	-4.22%	-1.55%	-0.74%	0.00%	0.70%	1.35%	3.08%
CDS	-0.65%	-0.24%	-0.12%	0.00%	0.11%	0.22%	0.51%
Other	0.01%	0.00%	-0.01%	0.00%	0.00%	0.00%	0.02%
Total	*1.17%*	*0.42%*	*0.20%*	*0.00%*	*-0.20%*	*-0.40%*	*-0.94%*

Source: Chenavari unaudited estimates, 13 March 2020

As an example of our caution on certain instruments, the Fund's exposure to Financials mostly stems from Tier 2 debt, whilst we are net short on the AT1 (or Cocos) universe, as highlighted in Chart 6.

This positioning allowed the Fund to recoup some MTM losses recorded in the first week of March, as most Cocos rapidly repriced to perpetuity at the end of last week. This move was exacerbated by Deutsche Bank's non-call of its $ 6.25% AT1 on Wednesday 11/03.

Chart 6: PV10[3] by seniority and overall as a % of allocated capital, Financials Strategy



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We hope the above helps explain the Fund's positioning in the current environment.

Should you wish to arrange a follow-up discussion, please do not hesitate to contact us:

- vincent.laurencin@chenavari.com
- IR team: Kirstie Sumarno +44 207 245 4677 ir@chenavari.com

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[3] In our view, the best way to discuss the positioning of the Sub-Strategies in detail is to look at the PV10, that is, the theoretical reaction of a given Strategy to a 10% widening of spreads, as measured by our risk team under certain modelling assumptions.

As an order of magnitude, we would reckon that an unlevered Long Only fund invested in single B instruments with a duration of 5 years would have a PV10 of c. -2% (i.e. a drawdown of 2% if spreads were to widen by 10%). A PV10 of zero shows a perfectly market neutral strategy, and a positive PV10 indicates a net short positioning (positive performance if indices were to widen by 10%).

Disclaimer:

Estimations reflect conservative modelling assumptions, but do not reflect the best and worst case scenarios. Estimates are based on the market conditions at the time of modelling and are therefore, subject to change. Stress Tests present a set of hypothetical scenarios that assume changes for one or more market variable in order to assess the effect on the portfolio. The results shown represent estimated gross performance of the Fund under the market conditions stated. Chenavari has made assumptions that it deems reasonable anduses the best information available to calculate the stress test estimates. If a different set of assumptions were used in this calculation, there could be a material difference in the calculated estimates. Please refer to Offering Document for risk parameters.

Hypothetical performance results have many inherent limitations, some of which are described below. No representation is being made that any account will or is likely to achieve profits or losses similar to those shown. In fact, there are frequently sharp differences between hypothetical performance results and the actual results subsequently achieved by any particular trading program.

One of the limitations of hypothetical performance results is that they are generally prepared with the benefit of hindsight. In addition, hypothetical trading does not involve financial risk, and no hypothetical trading record can completely account for the impact of financial risk in actual trading. For example, the ability to withstand losses or to adhere to a particular trading program in spite of trading losses are material points which can also adversely affect actual trading results. There are numerous other factors related to the markets in general or to the implementation of any specific trading program which cannot be fully accounted for in the preparation of hypothetical performance results and all of which can adversely affect actual trading results.