Quarterly Portfolio Update

*Amundi Funds II – Pioneer Global High Yield**

29 June 2018

BOND COMMENTARY

Market Review

High yield posted a negative return for the quarter with the Bloomberg Barclays Global High yield Index returning -2.17%. U.S. high yield returned 1.03% while European high yield returned -6.17% in U.S. Dollar terms and Emerging Market U.S. Dollar high yield returned -4.86%. In euro, the Pan-European High Yield Index returned -1.17%.

During the month, U.S. corporate BB returned -0.17%, single -B returned 1.42%, while CCC returned 2.87%. In Euro, European high yield BB returned -1.37%, single B returned -0.52%, while CCC returned -1.77%.

While volatility pulled back from the high levels of the first quarter, markets continued to suffer from heightened volatility in the second quarter of 2018, relative to the very low levels of 2017. Concerns about trade wars took centre stage, as President Trump more aggressively pursued tariffs against allies and adversaries.

Structured sectors and high yield assets generally outperformed Treasuries. U.S. high yield corporates enjoyed positive total and excess returns over both the second quarter of 2018 and June 2018, benefiting from their U.S.-focus, their higher yield and low default outlook. They delivered positive total and excess returns of approximately 1%, as spreads remained almost unchanged, ending the period at 371 basis points.

Fears that the new populist Italian government threatened the status-quo of the euro and European Union rose in late May 2018, but subsided as a new government was formed and officials toned down their anti-euro rhetoric.

The unexpected appreciation of the U.S. Dollar, which rose 5.7% from its mid-April 2018 low, as well as a continued rise in oil prices — which have climbed 23% year-to-date, including a 14% increase in the second quarter of 2018 — contributed to a sell-off in emerging markets, along with tighter international liquidity and rising trade tensions, particularly in countries with significant US dollar debt.

The U.S. Dollar appreciated in part due to a more hawkish FOMC, offset by a more dovish ECB. Citing continued strong gross domestic product and employment growth and rising inflation, the FOMC raised rates in both of their March and June 2018 meetings. They brought forward projected rate increases, to include two more increases in 2018. However, they also adopted a symmetric view around their inflation target in June 2018, indicating they would not necessarily take a more aggressive approach to increasing rates, should future inflation exceed target levels for a short time.

Portfolio Review

For the quarter, the Portfolio outperformed its benchmark, the Bloomberg Barclays Global High Yield index.

The underweight allocation to Emerging Markets (EM) was a positive contributor to relative performance, driven mainly by our underweight to sovereigns. Allocations to catastrophe bonds also contributed. Underweight to the Euro and Sterling contributed to performance as the U.S. Dollar rallied vs both currencies. However, exposure to the Argentina peso was a drag on performance, given the general weakness in EM and the specific issues associated with Argentina, which eventually had to approach the IMF for liquidity to stabilize its currency.

Security selection within the Energy sector weighed on performance, driven mostly by our up-in-quality bias within the sector as lower quality credits outperformed. Security selection within EM Basic Industry and International Consumer Cyclicals also detracted from relative returns.

Outlook

Regarding the U.S. Dollar corporate credit markets, U.S. high yield spreads have traded in a 70-80 basis points band year-to-date but were 9 basis point wider

for June while Euro high yield spreads have widened 18 basis points and EM corporate bonds have widened 43 basis points during the month. Euro high yield looks oversold and while EM corporates look cheap we do not anticipate any significant tightening while investors are concerned about risks of a trade war. As for U.S. HY, we expect them to continue to trade within their year-to-date band. If U.S. HY spreads were to widen to north of +400bp/7.00%, which would be higher than the year-to-date range, we would view such a level as cheap. Currently, we believe U.S. HY is a bit wide of fair value.

Supporting spreads of all three subcomponents of the global high yield market has been a light new issue calendar, as many companies prefer to issue leveraged loans instead given their light covenants and lack of prepayment restrictions.

From a positioning perspective, we continue to be overweight Bs and underweight BBs. We have reduced our exposure to CCCs as spreads have tightened. We continue to overweight US HY and underweight Euro HY though we have recently modestly reduced our underweight. We have also modestly reduced our holdings in EM corporates and maintain our underweight to EM sovereigns. While we are generally favourable regarding the fundamentals in Home Building, we do believe that the market levels reflect nearly all the upside and have therefore reduced our exposure. We continue to be overweight Energy.

We believe U.S. gross domestic product growth may accelerate to almost 3% over the year, benefiting from significant tax cuts, deregulation and stronger fixed investment spending.

Solid employment and income growth may continue to support consumption and the housing market. Higher corporate profits, benefiting from strong global growth, tax cuts and the 100% expensing of fixed investment, may also support increased fixed investment.

Globally, we continue to believe the Eurozone and Japan may also enjoy strong growth, benefiting from still supportive monetary policy. Eurozone growth may be lower than that achieved in 2017, as exports may suffer from the lagging effects of a stronger euro. In addition, political risk has risen in Europe, due to the triumph of populists in the Italian elections, as well as union resistance to President Emmanuel Macron's implementation of labour reforms in France. While China's growth may moderate in light of its goals to rein in credit growth, we believe a modest decline in China's growth will not disrupt overall Asia or global gross domestic product growth.

However, global growth could moderate in the face of President Trump's more aggressive protectionist trade policy. While the U.S. and China are negotiating trade imbalances, President Trump has been aggressive against U.S. allies.

We continue to believe that inflation may surprise to the upside on a number of fronts in 2018 and that the FOMC may be behind in raising rates. Emerging signs of wage growth acceleration, service inflation, tighter labour markets in key industries such as homebuilding and more restrictive immigration policies may contribute to higher price levels in the coming year. In addition, producer price indices are already increasing, on the heels of higher oil and metals prices. Fiscal stimulus, including the tax cuts and higher spending from the budget, has the potential to further fuel inflation.
We will continue to employ our active management skills as we navigate the waters of the financial markets, which have become choppier over the last quarter.

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