

Inflation and monetary policy in focus

SKAGEN Tellus had a good quarter in absolute terms but lagged the benchmark slightly. The largest positive contributors to fund performance were our investments in the Czech Republic and the Dominican Republic thanks to both falling interest rates and appreciating currencies. The largest detractors were our investments in Peru and the US driven by weak currencies and rising interest rates. During the quarter we added a short-term USD denominated Italian government bond, a small position in a ZAR denominated long-term bond issued by the European Investment Bank and a COP denominated Colombian government bond.

Intensified inflation debate

The focus and debate around inflation that started in the first quarter only intensified in the second quarter and will likely continue in the coming months. The questions remain as to how transitory the latest price increases are and how sustainable the current monetary and fiscal policies are. The main focus is on the US economy as the price pressures in Europe are milder, but as always US developments will typically trickle through to the rest of the world and especially emerging markets. We still see most of the current price increases as transitory but acknowledge greater inflation risk going forward.

The discussions around inflation also extend to central bank policies. Analysts and commentators scrutinise every word communicated by the Federal Reserve Bank (Fed) in the US, but we seek to maintain a long-term focus and generally pay little attention to a couple of months' difference in the timing of a policy change. The Fed's announcements and

actions often cause large short-term market fluctuations, but we anticipate that monetary policy in the US will remain expansive for some time.

As regards the other central banks, a couple of EM central banks have started hiking interest rates and among them we find the Mexican central bank. In June, the Bank of Mexico raised the policy rate from 4 percent to 4.25 percent and the markets price in an additional four hikes of 25 basis points each in 2021. We find this quite aggressive and have therefore decided to invest in some longer-term bonds in Mexico as the risk of hawkish central bank surprises is slight.

Politics in Latin America

When investing in emerging markets, we must generally accept and expect that political developments will have a greater influence on financial markets than we see in developed markets. Developments of note this quarter were mid-term elections in Mexico and social unrest in Colombia.

The Mexican elections were the largest ever with more than 21 000 seats up for election in both local and federal elections. People's attention was most closely focused on how well the party (Morena) of President Andrés Manuel López Obrador would do. In general, support for Morena and their coalition partners is still strong, but the coalition ended up with a smaller majority in congress than they held before the elections. This was generally the most favoured outcome judging by market movements as this will reduce the President's ability to push through his most controversial reforms.



Photo: Unsplash

Volatility in Colombia

In Colombia the government proposed a new tax reform that proved to be highly unpopular and fuelled large and violent protests. The government is currently working on a revised reform and seems confident that they will reach agreement with the opposition. Even so, the failed reform push resulted in a downgrade to sub-investment grade by two credit rating agencies. This caused some volatility in financial markets with the currency taking the largest hit. Markets have largely calmed down now, and the currency has regained its losses. Colombia was priced as a sub-investment grade country even before the downgrades, so this was not very surprising and has not materially changed our view of the case. Additionally, Colombia is still rated investment grade by Moody's. The direction and impact of political events are difficult to forecast, hence we generally sit through these market fluctuations as long as the events do not materially alter the investment case.



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Outlook

Interest rate levels are still at historically very low levels in developed markets and we anticipate that rates will move higher going forward. In emerging markets, however, the picture is quite different. With the jump in interest rates earlier this year, long-term interest rates in several countries are now higher than their long-term averages. The reason for this comes from differing growth outlooks, inflation dynamics and credit risk, all of which create opportunities for an unconstrained investor such as SKAGEN Tellus. We have increased our exposure to long-term positions in countries such as Mexico and South Africa lately but remain conservative in our overall allocation to duration.

SKAGEN Tellus invests primarily in bonds and certificates issued or guaranteed by governments from around the world.

The fund is suitable for those with at least a three year investment horizon. Investors must be able to tolerate currency fluctuations.

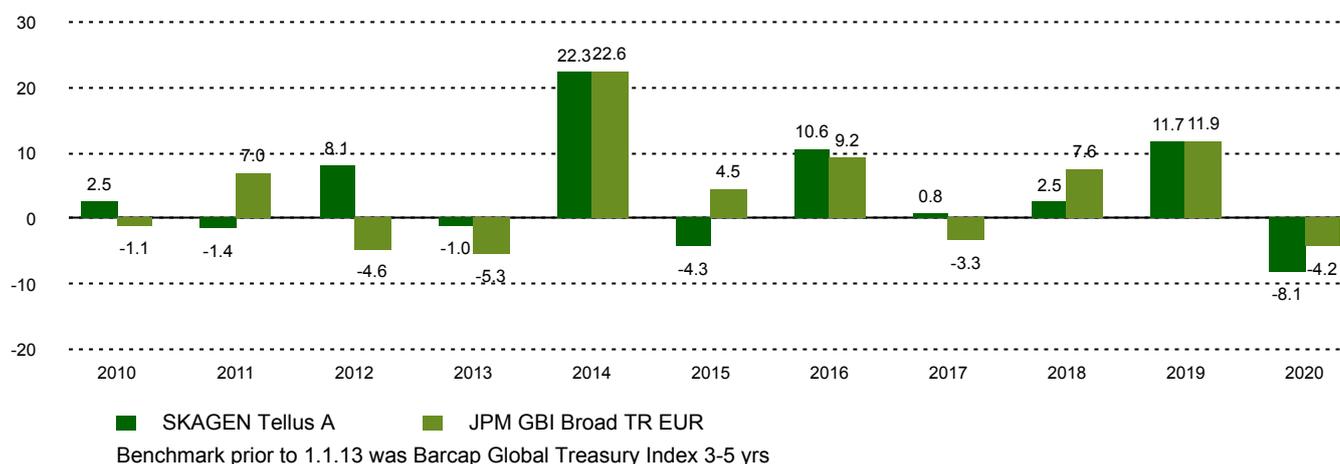
Historical performance (net of fees)

| Period | SKAGEN Tellus A | Benchmark index |
|-----------------|-----------------|-----------------|
| Last month | 1.9% | 2.2% |
| Quarter to date | -1.2% | -0.8% |
| Year to date | 0.5% | -0.1% |
| Last year | -3.2% | -7.9% |
| Last 3 years | -0.1% | 2.1% |
| Last 5 years | 2.0% | 1.9% |
| Last 10 years | 4.2% | 4.4% |
| Since start | 4.4% | 4.4% |

Fund Facts

| | |
|----------------------|--------------------------|
| Type | Fixed income |
| Domicile | Norway |
| Launch date | 29.09.2006 |
| Morningstar category | Global Bond - EUR Biased |
| ISIN | NO0010327786 |
| NAV | 103.77 SEK |
| Fixed management fee | 0.80% |
| Benchmark index | JPM GBI Broad TR EUR |
| AUM (mill.) | 459.10 SEK |
| Duration | 3.58 |
| WAL | 4.55 |
| Yield | 2.45% |
| Number of holdings | 16 |
| Portfolio manager | Sondre Solvoll Bakketun |

Performance last ten years



Contributors in the quarter



Largest contributors

| Holding | Weight (%) | Contribution (%) |
|-------------------------------|------------|------------------|
| Czech Republic Government | 4.98 | 0.28 |
| United States Treasury | 32.00 | 0.24 |
| Uruguay Government | 5.44 | 0.22 |
| European Bank for Recon & Dev | 6.02 | 0.19 |
| Romanian Government | 6.26 | 0.17 |



Largest detractors

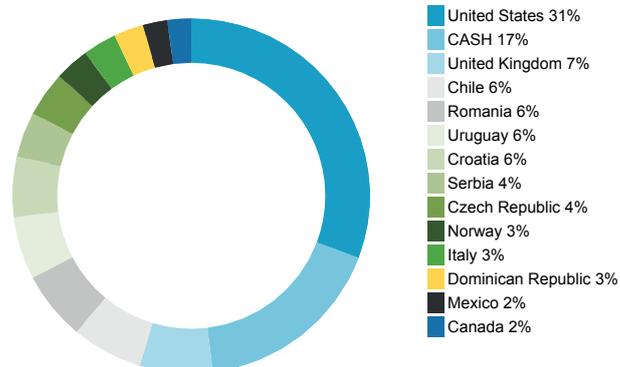
| Holding | Weight (%) | Contribution (%) |
|------------------------------|------------|------------------|
| Peruvian Government | 2.18 | -0.40 |
| City of Oslo Norway | 2.00 | 0.00 |
| European Investment Bank | 0.12 | 0.00 |
| Chile Government | 6.17 | 0.01 |
| Republic of Italy Government | 0.18 | 0.03 |

Absolute contribution based on NOK returns at fund level

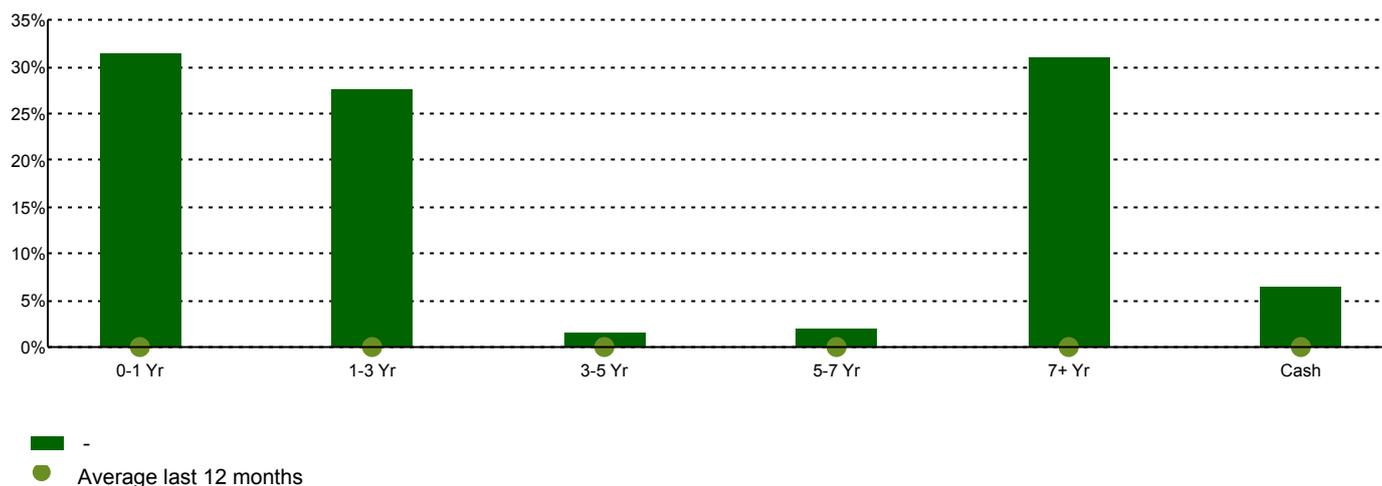
Top 10 investments

| Holding | Percentage of Fund |
|--|--------------------|
| US Government | 30.7 |
| UK Government | 6.6 |
| Republic of Chile | 6.4 |
| European Bank for Reconstruction & Development | 6.4 |
| Romanian Government | 6.3 |
| Oriental Republic of Uruguay | 5.7 |
| Republic of Croatia | 5.5 |
| Republic of Serbia | 4.1 |
| Czech Republic Government | 4.1 |
| International Finance Corp | 3.7 |
| Total | 79.5 |

Country exposure



Maturity structure



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Important information

Unless otherwise stated, performance data relates to class A units and is net of fees. AUM data as of the end of the previous month. Except otherwise stated, the source of all information is SKAGEN AS. Historical returns are no guarantee for future returns. Future returns will depend, inter alia, on market developments, the fund manager's skills, the fund's risk profile and subscription and management fees. The return may become negative as a result of negative price developments. You can download more information including subscription/redemption forms, full prospectus, Key Investor Information Documents (KIID), General Commercial Terms, Annual Reports and Monthly Reports from our local websites or our local representatives. Statements reflect the portfolio managers' viewpoint at a given time, and this viewpoint may be changed without notice. This report should not be perceived as an offer or recommendation to buy or sell financial instruments. SKAGEN AS does not assume responsibility for direct or indirect loss or expenses incurred through use or understanding of this report. Employees of SKAGEN AS may be owners of securities issued by companies that are either referred to in this report or are part of a fund's portfolio.