360°

Rates, recovery or recession?

Fixed Income Quarterly Report

Q3 2022

Federated Hermes Limited

www.hermes-investment.com
For professional investors only

Contents

Authors

Fraser Lundie
Head of Fixed Income – Public Markets

Silvia Dall'Angelo
Senior Economist

Audra Delport, CFA
Head of Corporate Credit Research

Anna Chong
Deputy Head of Corporate Credit Research

Vincent Benguigui
Senior Credit Portfolio Manager

Mark Dove
Junior Credit Portfolio Manager

Nachu Chockalingam
Senior Credit Portfolio Manager

Filippo Maria Alloatti
Head of Financials (Credit)

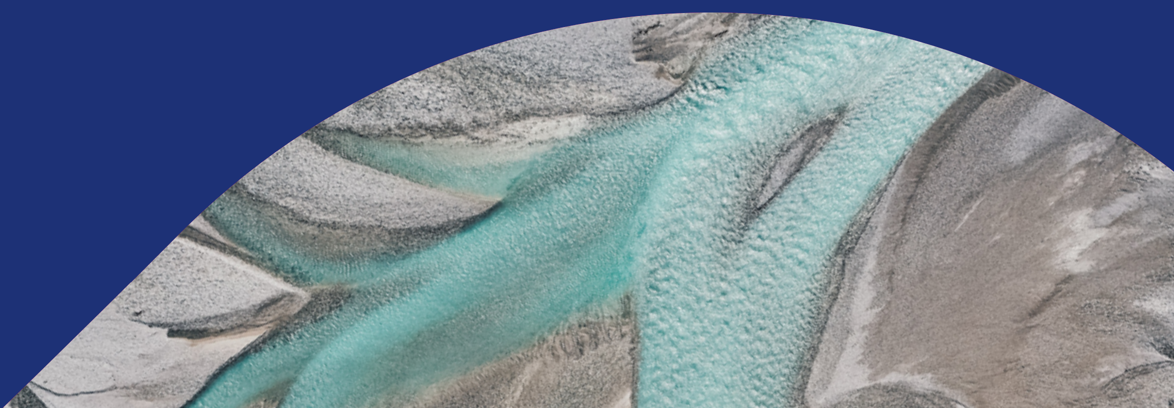
Robin Usson
Senior Credit Analyst

Andrew Lennox
Senior Portfolio Manager

Emeric Chenebaux
Portfolio Manager, Specialist Credit

Orla Garvey
Senior Fixed Income Portfolio Manager

Oba Adelaja
Senior Portfolio Manager



Fraser Lundie
Head of Fixed Income – Public Markets

Commentary

Old adages and proven approaches to the fore

When confronted with unprecedented situations, I take comfort in old adages that have passed the test of time. The market environment this year has proven tricky to navigate, and uncertainty may provide temptation to tinker with the tried and tested. However, it is precisely while weathering this storm that we, as long term, fundamentally driven investors, must hold to proven approaches and processes.

In this latest edition of the 360° report, we seek to summarise our market thinking through the lens of our Multi Asset Credit Strategy Meeting, or MACSM. This view benefits from some of the most experienced and respected professionals in the market, many of whom have worked together at Federated Hermes for many years. I take pride and comfort in this, and in the fact that this framework has been in use since I joined the firm in 2010. The road ahead is undoubtedly uncertain, and economic data – the referee in the inflation vs growth match-off – will remain volatile. The path of growth and inflation will be heavily influenced by fiscal policy, monetary policy, and energy prices.

Bonds in a bear market? Yes, it can happen – but not often. The 'Worst year in history for asset as inflation bites' has been a consistent headline in recent weeks. As I write this, global bonds have lost a fifth of their value in a year. The unambiguously hawkish message to markets during August's Jackson Hole symposium was the trigger to end the summer rally, and we are now firmly back in the territory of defending an asset class that emphasizes stability and reliable returns.

> **"Cheer up mate, it might never happen!" – Unattributed**

The asset class's reputation is well founded. From 1990 to its peak in January 2021, a period spanning much of a generation-long bull market in bonds, the global index had delivered an aggregate total return of nearly 470%.[1] But the recent drawdown is more than double any previous peak-to-trough decline going back to the 1970s, severely testing the narrative as well as the '60:40' bond equity portfolio which forms a bedrock for many asset allocators.

The drawdowns have drained sentiment and conviction levels of market participants. Bond and currency markets have seen more severe and more persistent deterioration in liquidity conditions this year relative to other asset classes, with little signs of reversal. It may be fair to say that bearish bond momentum is approaching extreme levels.

Evidence of this feeding into credit fundamentals remains slow to materialise, with Q3 earnings surprising to the upside. Some lead indicators, including housing market and car sales, are starting to show signs of rolling over, while recent data has mostly also been negative. But is it enough to see a 'Fed pivot'?

> **"If you don't like the weather in New England / Glasgow now, just wait a few minutes." – Mark Twain / Billy Connelly**

The pain is not being felt equally across sectors; our corporate credit analysts point to concerns in homebuilding, retail and technology. Furthermore, credit strength going into this period is particularly important when managing cost and labour inflationary pressures and margin deterioration. Even in Europe, where headwinds are strong due to the energy crisis, companies are arriving with strong credit metrics and balance sheet health supported by low leverage, high interest coverage, and a term structure of liabilities back ended after proactive refinancing activity last year. This backdrop generally leads us to see a lower default rate through the cycle than historically witnessed.

[1] Source: Bloomberg, as at 31 August 2022. **Past performance is not a reliable indicator of future results.**

The constructive argument can be bolstered by the value side – hiking cycles are well priced in developed markets for the rest of this year and central banks appear joined up in their desire to tackle inflation for now. We have likely seen the peak in US inflation already, with Europe and the UK peaking in Q1 2023, in that order. Credit spreads now price a moderate recession, while yields in many parts of the market are at multi-year highs, including some areas that we particularly like right now: subordinated financials, corporate hybrids, and certain parts of structured credit.

Asian markets have suffered less, aided by China's debt, as the central bank eases policy to try and turn around the world's second-largest economy. At the start of Q3, investment-grade dollar bond spreads narrowed last month by the most since 2020, driving them tighter than those of US peers, something that has happened only a few times in the last decade. With all that has been going wrong in this region, this supports the importance of thinking in terms of probabilities and 'what's in the price?'.

"Nothing ventured, nothing gained." – Unattributed

So, the policy mix is likely to stay unfriendly for quite some time. A sustained move downward in inflation requires two key ingredients: slower growth and restrictive monetary policy, neither of which are supportive of risk appetite. But the market is focused on fiscal spending and higher energy prices right now. As we move into Q123, this will likely give way to a focus on falling inflation and growth, and central banks will have less cover for higher rates even if core inflation remains sticky. If this transition plays out slowly, the value of time, or theta, increases – something we think plays into credit markets favourably. Ultimately, we may look back on this as more of a necessary correction from a period of unsustainably ultra-low yields, and one that is mostly done at this point.

Fundamentals

Economic outlook

In our latest quarterly update, we consider the outlook for the global economy amid the ongoing war in Ukraine, mounting inflationary pressures and fears of a recession. As the old adage goes, we hope for the best, but are prepared for the worst.

Since our last edition of this report, the outlook has deteriorated. This is largely due to three key factors:

- First, the European energy crisis, which intensified in recent months, as Russia cut its gas provisions to Europe. The shock from high energy prices is likely to tip the region into a recession this winter, with risks skewed to the downside given the possibility of the price shock morphing into a quantity shock.
- Second, inflation has continued to surprise to the upside across the board, proving even higher and stickier than expected even just a few months ago. This has resulted in a faster pace of monetary policy tightening – now likely to be maintained through the end of the year – which will drag on aggregate demand, with a lag.
- Third, the Chinese economy has performed poorly, due to the persistence of zero-Covid policies and an ongoing correction in the property sector.

PMI surveys suggest the global economy stalled in Q3. The global composite PMI came in at 49.3 in August, down from 50.8 in July, falling below the 50-threshold for the first time since mid-2020. A broader information set including national surveys and hard data on industrial production, consumption and labour markets confirms the picture of a broad-based economic slowdown, although there are significant differences across regions and countries.

Against this backdrop, the US economy has continued to outperform, probably reflecting the long-lasting impact on aggregate demand from the outsized Covid-related fiscal stimulus. While the US labour market has continued to add jobs at a fast pace in recent months, several sectors of the economy have lost momentum, reflecting the impact of inflation on real incomes as well as intensifying monetary and fiscal tightening.

Activity in the US housing sector has contracted by about 40% since early 2021 according to the MBA purchase index, due to a sharp rise in mortgage rates over the same period (see Figure 1). Consumption growth has slowed in recent quarters and is likely to weaken further going forward. In our base case, the US will experience a mild recession around the middle of next year.

The view from Europe

While the euro zone economy started off 2022 on a strong footing, the Russian invasion of Ukraine and the related energy crisis cast a shadow over the outlook for the balance of the year and 2023.

European future gas prices have increased to about €200/MWh recently, about ten-fold their levels in mid-2021, reflecting severe disruptions to supply[2]. Gas supply from Russia (accounting for almost 40% of the total before the conflict) has fallen to a trickle following the closure of the NS1 pipeline in early September (see Figure 2) and is unlikely to be resumed.

A 15% reduction in gas demand in line with the EU target and elevated gas inventories (at about 80% of capacity across the EU) should allow the EU gas market to balance during the winter. However, gas prices are likely to remain elevated, with gas expenditure set to account for 5% GDP this winter, compared to 1% GDP in 2021. This will likely lead to a recession between Q4 2022 and Q1 2023.

In our baseline scenario, we envisage euro zone GDP growth of ~3% in 2022 and ~0.2% in 2023. However, in the worst-case scenario (i.e. severe winter and lack of coordination across EU countries), the energy price shock would morph into a quantity shock, implying energy rationing and an even more severe recession.

The Chinese economy has recovered only slowly from its contraction in Q2 2022. The zero-Covid policy has remained in place, with recurring and protracted lockdowns across the country probably impairing the effectiveness of existing stimulus measures.

Meanwhile, the property sector continues to drag, with a correction process still having far to run. Policymakers will likely stick to a measured and targeted approach to stimulus, which will mainly focus on infrastructure investment. We expect the Chinese economy to grow by about 3% this year, well below the government's official target of 5.5%. However, we believe growth could bounce back to ~5% in 2023, reflecting the likely easing of the zero-Covid policy at the end of this year, after the crucial National Party Congress in October-November.

[2] Source: Bloomberg, September 2022.

The broader outlook

More generally, monetary and fiscal policies appear to be constrained in the current circumstances – and this is a key component of the difficult outlook. Central banks are in aggressive tightening mode across the board, as they focus on fighting elevated inflation. Add in the prospect of a price-wage spiral against the backdrop of a tight labour market and their actions come as no surprise.

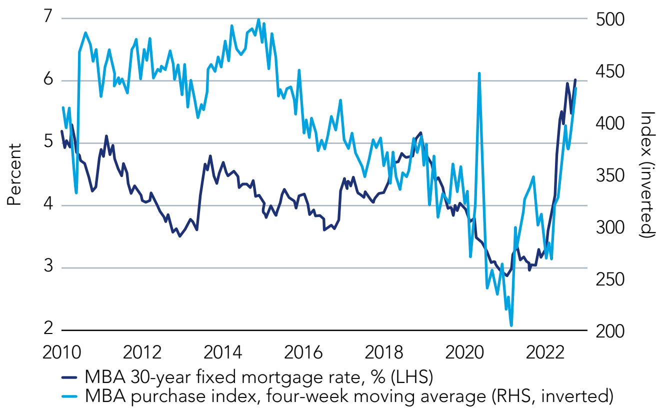
In addition, there is probably a recognition that the supply constraints that played a significant role in pushing inflation high are likely to be protracted, hence demand needs to be re-aligned to contain price growth.

Demand destruction – also induced by monetary tightening – is one of the key drivers of lower inflation in our forecasts for next year. Meanwhile, governments have limited fiscal space, following large Covid-related stimulus.

So far, EU governments have resorted to targeted measures to respond to the energy crisis – support to households and businesses has been worth between 1% and 2% GDP over the last year across the largest eurozone countries.

While the EU aims at raising €140bn (~1% of GDP) from taxing power producers, the UK has put forward an aggressive energy support plan that will be mainly funded with additional public borrowing. In the US, prospects for fiscal easing are virtually non-existent, as the mid-term elections this Autumn are likely to result in a divided government.

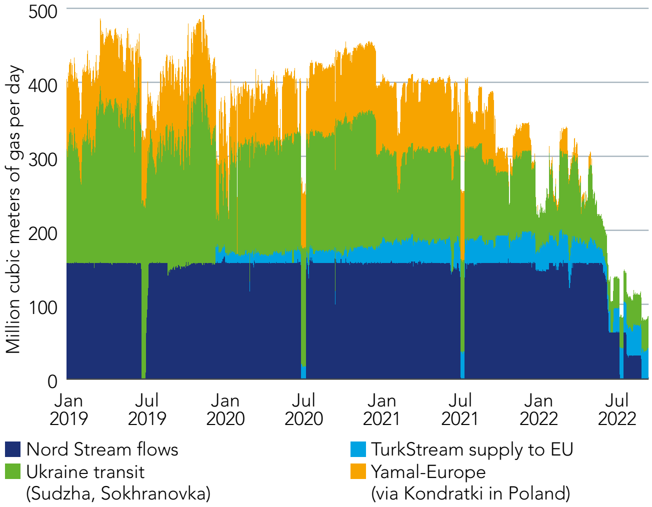
Figure 1 – A sharp cooling of the US housing sector



Source: Refinitiv Datastream, September 2022.
Past performance is not a reliable indicator of future returns.

> **In the worst-case scenario (i.e. severe winter and lack of coordination across EU countries), the energy price shock would morph into a quantity shock.**

Figure 2 – Gas flows from Russia to Europe have fallen to a trickle



Source: Bloomberg, September 2022.
Past performance is not a reliable indicator of future returns.

We predict that data will remain volatile over the coming months, as the direction of growth and inflation continue to be influenced by both fiscal and monetary policy and rising energy prices. Indeed, the more the macroeconomic adjustment comes through higher employment vs. fiscal spending, the less central banks will be required to hike rates, and vice versa. This, however, is still an unknown and so will likely bring with it a continuation of market and political volatility in the short term.

Figure 3: Yield curve score

		UK	US	Bunds	Italy
Duration	2s	0	0	0	0
	5s	-1	-1	-1	-1
	10s	-2	-1	-1	-1
	30s	-2	0	-1	-2
Curve	2s5s	-1	-1	-1	-1
	5s10s	-1	-1	0	-1
	10s30s	0	0	0	-1
MOVE		-1	0	-1	

Duration	Curve	Vol
0	-1	-1
	(-1 = steeper)	(-1 = higher)

Source: Bloomberg, Federated Hermes Limited, as at 8 September 2022.
Past performance is not a reliable indicator of future returns.

Figure 4: Basis point move in rates year-to-date

	US	UK	Eurozone	Italy	Australia	Canada	Japan
2y	4.28	4.20	1.75	2.87	3.31	3.79	-0.05
5y	4.09	4.38	1.96	3.89	3.66	3.33	0.06
10y	3.83	4.08	2.10	4.51	3.89	3.17	0.24
30y	3.78	3.82	2.09	4.33	4.07	3.09	1.38
2y YTD Change bps	354.67	353.50	238.20	293.78	293.78	284.03	4.15
5y YTD Change bps	282.80	356.86	242.04	347.46	347.46	207.14	15.30
10y YTD Change bps	231.98	311.69	228.66	333.85	333.85	174.69	17.25
10y YTD Change bps	187.51	270.43	189.39	233.95	233.95	141.60	69.55

Source: Bloomberg, as at 7 September 2022.
Past performance is not a reliable indicator of future returns.

Corporate fundamentals

From an earnings perspective, the corporate credit outlook for the second half of the year remains challenging. On a brighter note, balance sheets appear to be in good shape.

In our Q1 update, we explained the reasoning behind our move from a positive view on corporate credit fundamentals in 2021, towards a more cautious approach to the asset class in early 2022. Suffice to say, as we look ahead for the remainder of the year and beyond, our stance remains largely unchanged.

Indeed, the main takeaway from the most recent quarter is that the outlook for earnings will become steadily worse. According to JPM research[3], while 38% of HY companies beat expectations in Q2, 20% of companies missed forecasts.

The earnings season has been particularly noteworthy in the following key sectors:

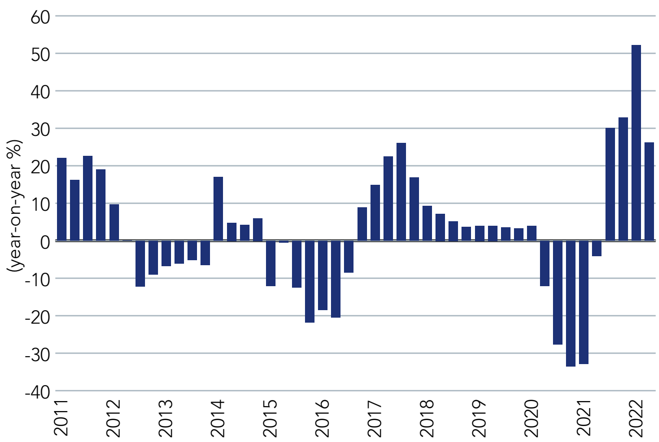
- **Homebuilders:** With rates rising, order books have fallen substantially and cancellation rates are on the rise, meaning that earnings are likely to be pressured going forward.
- **Retail:** Several companies have lowered guidance on the back of weaker consumer spending. Some of these companies have said demand began to soften in June and this carried into July, which could suggest the possibility of additional downside risk.
- **Technology:** Similarly, a number of companies in the information technology space have lowered guidance, with one company citing lower-than-anticipated consumer demand for storage and another flagging a slowdown in both consumer and enterprise spending.

Most companies are experiencing cost and labour inflationary pressures and, as a result, margins have been impacted. This is most visible in Europe, which makes sense given the surge in energy prices on the continent. Several industrial firms have also announced plans to halt production in response.

In aggregate, sales and EBITDA are still growing, however we note at a decelerating rate, as shown in Figure 5 below. On a positive note, strong credit metrics are offsetting this deteriorating sales environment.

Encouragingly, balance sheets continue to be in good shape and leverage levels are still relatively low, as seen in Figure 6. Companies do not have large amounts of loans or debt maturing in the near future, and as a result interest coverage ratios remain strong. That said, as earnings become more challenged over the next quarter, it is likely that credit metrics will begin to deteriorate. Overall, we maintain our conservative stance towards corporate fundamentals.

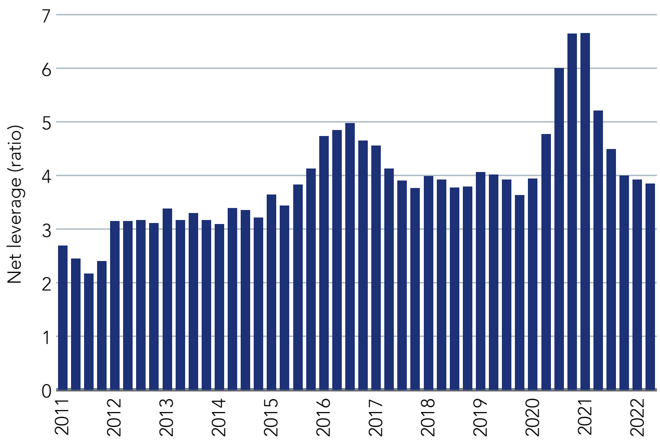
Figure 5: EBITDA growth is slowing (year-on-year %)



Source: Deutsche Bank, Federated Hermes as at 30 June 2022.
Past performance is not a reliable indicator of future returns.

[3] JPM High yield earnings tracker, as at 19 August 2022.

Figure 6: High yield net leverage is still trending down



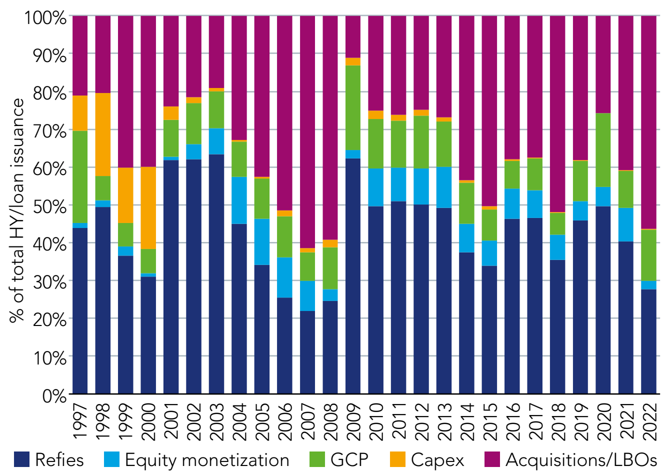
Source: Deutsche Bank, Federated Hermes, as at 30 June 2022.
Past performance is not a reliable indicator of future returns.

Elsewhere, we have seen some signs of companies engaging in creditor friendly behaviour. However, where balance sheets are in decent shape, we continue to witness news-flow around M&A, capex plans, share buybacks and dividends. A large proportion of new HY/loan issuance continues to be used to finance LBOs/acquisitions, as demonstrated in the graph below, but covenant-lite issuance is trending lower. This is perhaps best explained by light issuance levels, with companies less likely to come to market to refinance existing debt unless the situation demands it, given the increase in coupons, as well as limited refinance requirements in the high yield space.

The main takeaway from the most recent quarter is that the outlook for earnings will become steadily worse

While we have seen tenders and/or continued debt paydowns from companies with stretched balance sheets, outright 'creditor friendly' behaviour is yet to be evidenced on any scale. However, if we see a meaningful deterioration in economic conditions, we would expect to see a greater shift in this direction.

Figure 7: HY and loan new issue uses of proceeds, face values ($m equivalents)



Source: BofA, Merrill Lynch Global Research, as at August 2022.
Past performance is not a reliable indicator of future returns.

Sentiment, technicals and relative valuation

An overview of the factors feeding into recent market performance offers a mixed picture on current risks and rewards

i) Sentiment

Fear trumps confidence as negative sentiment takes hold

To better assess market sentiment, the Federated Hermes credit team routinely considers several indicators across rates, equities, and credit. One such indicator is the MOVE index, a yield-curve-weighted index of the normalized implied volatility on one-month Treasury options.

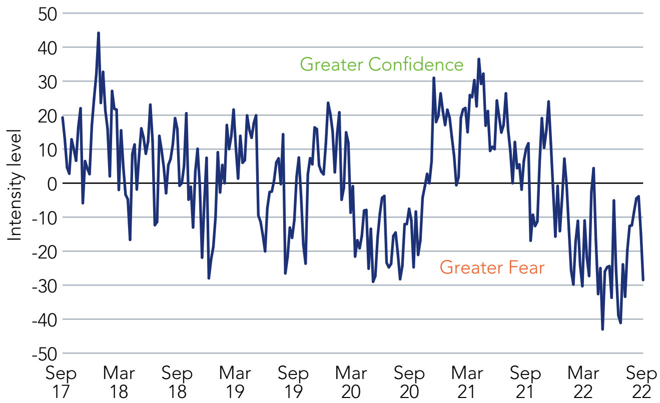
As the graph below illustrates, the index remains in elevated territory. In our view, this is a crucial leading indicator, since rates are the first asset class to move before volatility is carried through into other portions of the market, such as credit.

Figure 8: MOVE Index remains elevated

Source: Bloomberg and Ice Baml, as at 6 September 2022.
Past performance is not a reliable indicator of future returns.

Outside of rates, the bull versus bear market continues to show a cautious output, with bears outpacing their bull counterparts. This trend, which started at the beginning of the year, shows no sign of slowing, and even the summer rally has not been enough to move this survey back to positive territory, as illustrated below.

Figure 9: AAIIBULL – AAIIBEAR (survey, stock investors view over 6m)



Source: Bloomberg and the American Association of Individual Investors (AAII), as at 6 September 2022.
Past performance is not a reliable indicator of future returns.

The credit market itself is also showing signs of concerns. One of our preferred indicators is the Fear and Greed Index. Among the five subsections (implied volatility, skew, momentum, ETF premium and CDS strength), three of the subsections are currently trading above their 80th percentile, as demonstrated in the table below.

Figure 10: Fear and Greed Index

	VTRAC-X	Skew	Momentum	ETF premium	CDS Strength
EUR IG	95%	23%	84%		84%
EUR HY	90%	19%	82%		98%
EUR FIN	91%	16%	81%	74%	
USD IG	76%	53%	84%	67%	
USD HY	90%	53%	80%	71%	
TOTAL	89%	31%	82%	71%	87%

Source: JPM, as at 1 September 2022.
Past performance is not a reliable indicator of future returns.

To sum up, numerous key indicators are pointing towards a fearful environment, despite the relief rally experienced during July and the first half of August. Even so, we believe there is room for a contrarian take on current sentiment and remain marginally risk-off.

ii) Technicals

A pause in new issuance is the underpinning to weak net supply

Credit has faced outflows since the start of the year, with the high yield market most affected and a milder impact on investment grade flows. More recently, however, this trend has slowed with high yield beginning to see some encouraging (albeit moderate) inflows, which we consider a positive.

On the supply side the picture is challenging, with net supply at its weakest in over a decade year-to-date. This has proved a negative (more redemptions than new issuances) for the high yield segment on both sides of the Atlantic, leaving an overall smaller market. More positive, however, is that the average cash balance in funds remains elevated, and investors may be ready to invest in new issues once market conditions turn. Encouraged by this, we maintain risk neutral.

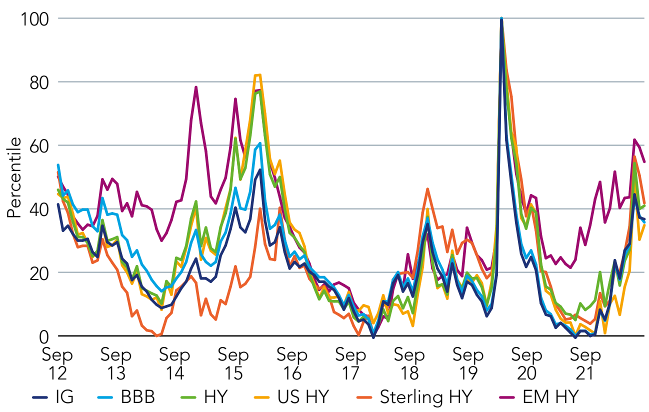
iii) Relative Value:

Differentiation is key but a favourable convexity profile in the broader market suggests a constructive view on valuations

Valuation remains attractive on the credit market, but not all sub asset class screen in the same way.

On a pure spread basis[4], the market is now trading around its historical average level, as seen below.

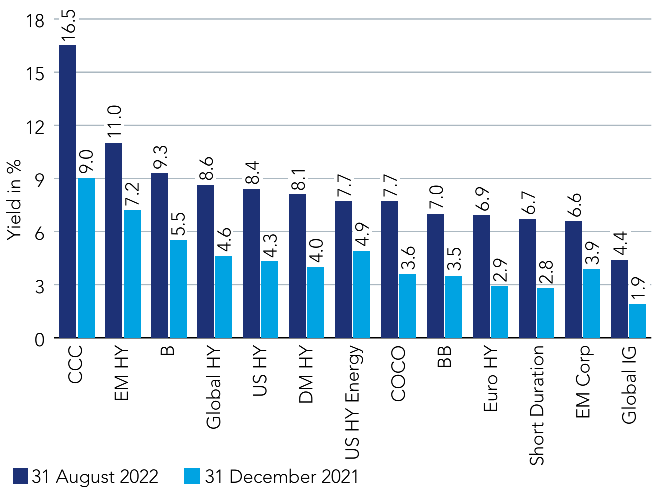
Figure 11: Credit spread percentiles



Source: Factset and Ice Baml, as at 1 September 2022.
Past performance is not a reliable indicator of future returns.

However, when looking at valuation on an all-yield basis, the picture changes and becomes more attractive.

Figure 12: Credit, yield to worst

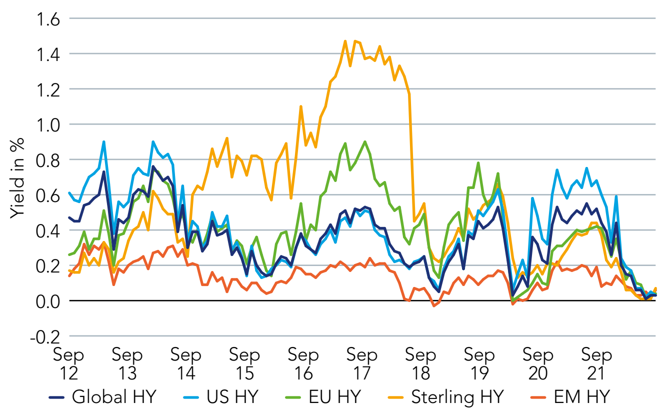


Source: Ice Baml, as at 1 September 2022.
Past performance is not a reliable indicator of future returns.

Another way to gauge the attractiveness of the credit market is through convexity levels[5]. As we can see from the figure below, the current convexity profile on the market is as favourable as it can be, creating a constructive value proposal[6].

Overall, then, we view credit valuations as attractive, and we therefore adopt a marginally positive view.

Figure 13: Yield to maturity, yield to worst (convexity)



Source: Ice Baml, as at 1 September 2022.

Source: Ice Baml, as at 1 September 2022.
Past performance is not a reliable indicator of future returns.

[4] That being said, the data alone is somewhat misleading as this chart does not incorporate total yield.
[5] Most high yield bonds are callable, meaning their issuer can redeem them before their final maturity and therefore reduce the total return. A negative convexity profile occurs when the trading level is above the call price, and when the call option is already available or close to being so, which creates risk for the end investor. By way of contrast, a positive convexity situation means the bond is not constrained and so can continue to perform.
[6] **Past performance is not a reliable indicator of future returns.**

Catalysts

Is a global recession fully priced in? Are there other factors that could derail or improve the current outlook for bond investors?

Following a tumultuous start to the year, the main tail risk catalyst we have identified – and to which we assign a high probability – is that of a global recession, driven by the energy crisis in Europe and exacerbated by a cost of living crisis and other inflationary pressures.

While a 'light' recession is likely already present on many market participants' minds, we believe the market backdrop is yet to fully price in the prospect of this more severe global turndown.

Additional key downside catalysts include the Chinese economy underperforming, due to a combination of extended 'zero-Covid' lockdowns, energy supply issues, or prolonged stress in the real estate sector. We view this as a medium impact but high probability catalyst. High and persistent inflation, and an escalation of geopolitical tensions, are other key China-related downside catalysts highlighted by the team.

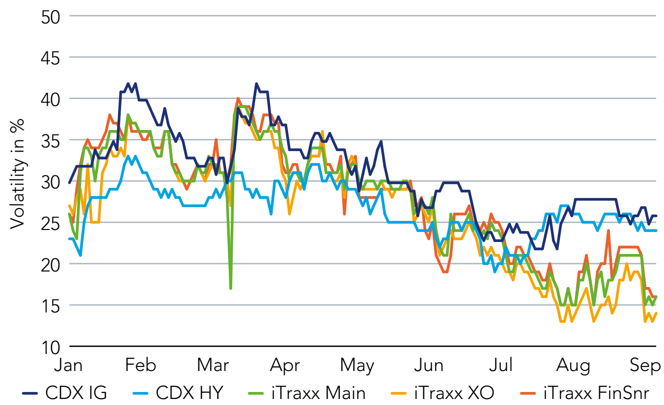
On a more positive note, we see the main upside catalyst coming from policy, either fiscal support, or a dovish pivot from central banks – driven either by success in taming inflation, or by the need to respond to the deteriorating macro backdrop.

Another key positive catalyst we see could come from some improvement to the natural gas crisis in Europe, possibly from weakening political resolve around Russian sanctions, or a ceasefire in the conflict between Russia and Ukraine.

One further upside catalyst includes a recovery in the Chinese economy, again, driven by additional stimulus.

Despite this multitude of possible headwinds, the cost of tail hedging remains on the cheaper side. For instance, volatility skew[7] is now trading at multi-months flat, illustrating a relatively low level of appetite for tail hedging.

Figure 14: Volatility skew history



Source: Citi Velocity, as at 5 September 2022.
Past performance is not a reliable indicator of future returns.

We believe there are two key explanations behind this:

- Already-elevated spread levels make a call for tail risk hedging less relevant, although there are some potential external scenarios that could still impact the market.
- The very light investor positioning reduces the need for hedge hunting, as highlighted in the table below.

In line with this, we assign a marginally risk-off view on the current market.

Figure 15: Investors positioning

	1yr Percentile	3yr Percentile
Main	63%	63%
Cross	92%	97%
SenFin	75%	92%
SubFin	100%	100%
CDX.IG	53%	48%
CDX.HY	48%	83%

Source: DTCC and Barclays, as at 2 September 2022.
Past performance is not a reliable indicator of future returns.

[7] Defined as the volatility difference between an option trading at the money and another one out of the money.

Credit relative value

i) Intra-credit opportunities

With yields remaining well above long term averages, both the investment grade and high yield segments are likely to attract flows. Here, we drill down further to explore our preferences for risk allocation in detail.

Global investment grade: In this segment of the market we have a preference for Europe over the US, given that the latter is now trading more than two standard deviations rich from the former, over a three-year look-back period.

That said, when considering US issuers and curves, we view the belly as being far more interesting than the long end right now. Some long-end bonds are currently trading at lower levels (i.e. in the 60s and 70s) even for high quality issuers. We are looking to improve the convexity profile of our funds, but not all low cash price bonds offer attractive spreads. For us, a low cash priced bond must also have spreads at close to its recent wides for it to be attractive.

Global high yield: In this segment, the US trades rich to Europe and emerging markets, but we know there are some pressures in the latter two regions given the impact of recessionary fears and energy pricing.

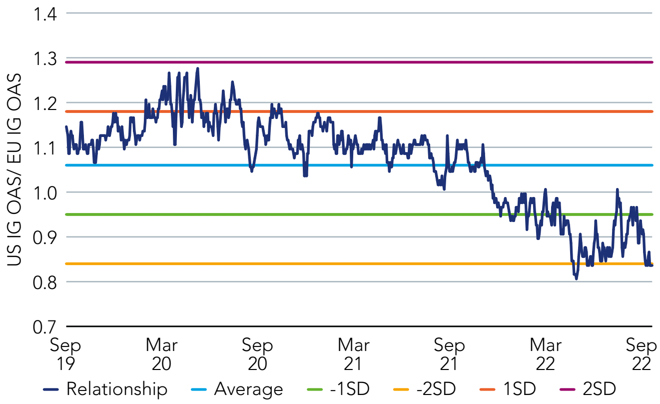
Our preference is to add exposure to quality issuers whose fundamental and sustainability theses we like, since we think that stress will pick-up in the low-quality segment of the high yield market and spread dispersion will increase. We also note that current secured versus unsecured spreads are at average levels, meaning there is less temptation to take a step down in issuers' capital structures.

The charts below illustrate the relative cheapness of Europe versus the US for both global investment grade and global high yield . Both European segments are at least two standards cheap currently against their US counterparts on a three-year look-back period, signifying some of the highest dispersion levels we have seen in recent years.

Figure 16: High yield, US vs. EU

Source: Source: BofA Global Research, ICE Data Indices, LLC, as at August 2022.
Past performance is not a reliable indicator of future returns.

Figure 17: Investment grade, US vs. EU



Source: Source: BofA Global Research, ICE Data Indices, LLC, as at August 2022.
Past performance is not a reliable indicator of future returns.

- In emerging markets, we prefer corporates over sovereigns and our sweet spot from a valuation perspective are strong EM BB issues.
- From a sector perspective, we prefer defensive over cyclical, with homebuilders, consumer cyclicals and technology being key sectors we are wary of right now, given their demand profile and potential for margin erosion over the coming quarters. Sectors where we believe value is particularly present right now include TMT, packaging and healthcare. The former two sectors are higher rated and recent cheapness has been driven by rates volatility. The latter sector is driven by specific stress situations.

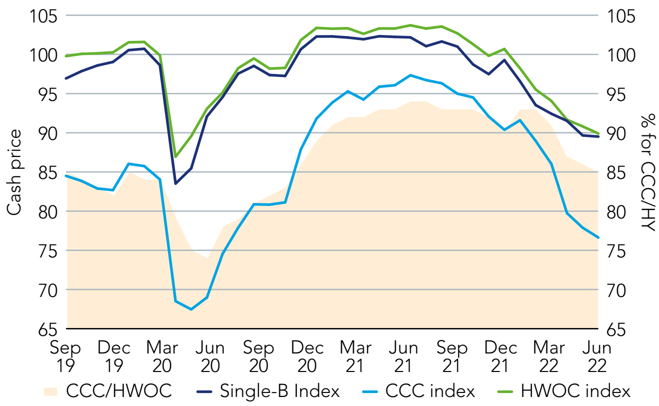
We remain active in our security selection with regards to the issuers we like, and at present the two key areas of focus are: (i) cash to CDS switches where the positive basis is meaningful, and (ii) reverse Yankee switches i.e. selling US$ bonds of issuers to buy EUR or GBP bonds of issuers for meaningful spread pick-ups for the same underlying credit risk.

ii) Stressed, distressed and special situations

CCCs remain within one standard deviation of the US HY index so, despite recent underperformance, are still not looking cheap.

We have seen some signs of dispersion, but as a ratings class, CCCs are still not looking particularly good value. Cash prices have gone sideways over the last couple of months, and CCC index cash prices are not significantly cheapening up versus the wider HY index, hovering around 82%-84% since June of this year. This is still relatively high when compared with the recent Covid-19 sell-off (see chart below).

Figure 18: Relative OAS of US CCC index vs. US HY



Source: Federated Hermes Limited, Bloomberg, as at September 2022.
Past performance is not a reliable indicator of future returns.

Figure 19: US CCC vs US high yield

Source: BofA Global Research, ICE Data Indices, LLC, as at August 2022.
Past performance is not a reliable indicator of future returns.

On a spread basis, CCCs are still within one standard deviation of the US HY index, so are still not looking particularly cheap, despite some recent underperformance.

The proportion of the Asia USD HY index trading below 80 continues to rise, indicating a significant proportion of distressed credits in this part of the market. This is backed up by intra-EM distressed data, which shows that EM Asia HY ratios continues to climb while LatAm and EMEA EM are more stable.

CCC dispersion levels are rising, but well below the peaks seen in previous cycles. We note that the distressed cohort of the HY index have relatively low refinancing risk, with low near-term maturities. This may prolong the amount of time credits remain distressed without defaulting, as it removes immediate refinancing risk, but ultimately does not solve the issue of negative free cash flow (FCF).

> **CCC dispersion levels are rising, but well below the peaks seen in previous cycles.**

Speculative grade default rates remain low, but there are signs that defaults are slowly creeping up. Moody's pessimistic forecast has defaults rising to over 15% in 2023, but the baseline forecast has defaults remaining below 5% in the first half of 2023.

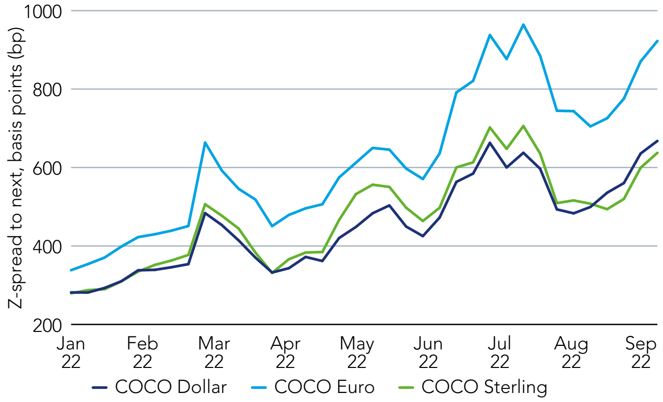
iii) Financials

2022 has cemented itself as a particularly challenging year for financials thus far, with the Russia/Ukraine conflict casting a long shadow over the economic outlook in the context of higher energy prices and other supply issues.

With the UK and Western Europe headed for recession, the outlook remains difficult. Higher rates are likely to continue to lead to wider spreads, while the case year-to-date, and the shutdown of Nordstream 1, will weigh on the market. Although there were tentative signs of US inflation peaking in August, inflation in Europe continues to remain elevated, and entrenched.

The market is driven by macro themes, with the new mantra of 'higher for longer' rates. That said, credit spreads are already relatively wide, and have been pushed wider yet by recent heavy issuance, meaning that in many cases we are at multi-year wides (excluding the Q1 2020 Covid wides). This may suggest that there is a fair amount in the price. The credit spreads of the deeply subordinated debt in the three main currencies are illustrated in the chart below.

Figure 20: AT1 YTD Z-spread evolution by currency



Source: Credit Suisse Index Plus, as at 6 September 2022.
Past performance is not a reliable indicator of future returns.

On balance collateral, values are holding. The future is uncertain, but not as gloomy.

The outlook remains challenged, with Europe increasingly looking headed for recession. Despite this, central banks will continue to raise policy rates to combat inflation, increasing the risk of a stagflationary backdrop. As such, the macro headline risk will likely remain high from a range of sources, including gas shut down, energy rationing risk, Purchasing Managers Index (PMIs), FX, and rates volatility. Against this backdrop, financial fundamentals remain sound.

This could be a different type of downturn. We are not expecting an elevated level of unemployment in contrast to previous crises, given the tightness of labour markets. UK unemployment is forecast to peak at 5% (from 3.8%), which is low by historic standards, while unemployment in parts of Europe is forecast to improve in the short term.

Importantly, learning from the forced deleveraging during the global financial crisis, authorities during the pandemic made effective use of forbearance to encourage banks to keep lending to the 'real economy'. It worked. We do not think they will act differently.

Financials preserve reassuring prudential metrics – capital and solvency, leverage, and liquidity. Non-performing loans will likely go up, but from a low base (1.9% in Q122 as per EBA). On balance collateral, values are holding. The future is uncertain, but not as gloomy.

iv) Corporate hybrids

Year-to-date, corporate hybrids have underperformed compared to other fixed income sub-asset classes on a beta-adjusted spread basis.

Relative to senior instruments, under our *Investment Grade vs. Hybrids Relative Value Framework*, Sub-Senior Spreads (SSS) peaked at ~520bps early July, and after rallying as tight as ~345bps in August, are now at around ~390bps.

This remains significantly wider that the ~125-150bps trading range in 2021. The Hybrid-Senior Spread Ratio (HSSR) peaked at ~3.6x and is now around 3.05x vs. 2.5-2.75x in 2021, suggesting decent value to be found in the hybrid sub-asset class versus senior debt.

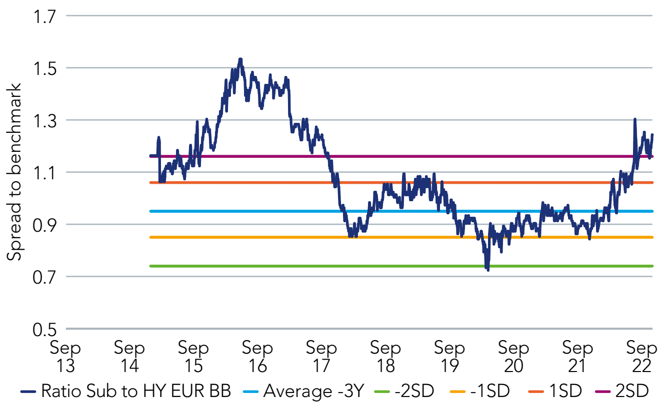
Figure 21: Ratio of corporate hybrids spreads to EUR senior debt spreads

Source: Bloomberg, Federated Hermes, Credit Suisse Indices, as at 13 September 2022.
Past performance is not a reliable indicator of future returns.

Relative to European High Yield BB-risk, under our *High Yield versus Hybrids Relative Value Framework*, corporate hybrids now yield around 0.6% more. They possess a similar risk profile, but a different risk composition – as explained in our recent paper, Finding opportunity in mispriced corporate hybrids. This has only happened twice previously: (1) in a pre-CSPP[8] world between 2014-2016 when the sub-asset class had not yet matured, and (2) in H2 2018 from the taper tantrum induced sell-off.

[8] The Corporate Sector Purchase Programme (CSPP) is a component of the European Central Bank's bond-buying programme, launched in response to the Global Financial Crisis.

Figure 22: Ratio of corporate hybrids spreads to EUR high yield BBs spreads



Source: Bloomberg, Federated Hermes, Credit Suisse Indices, as at 13 September 2022.
Past performance is not a reliable indicator of future returns.

Investment grade investors comprise the bulk of the investor base for corporate hybrids, which is, in our view, the main reason behind such value disconnects versus BB-risk, as investment grade investors tend to be sellers of beta in a volatile rate and monetary policy tightening environment.

In fact, rates volatility remains at present the biggest technical pressure to our constructive view on the sub-asset class, as rate volatility morphs into wider sub-senior spreads.

Interestingly, rating compensation (BBB- to BB+) in corporate hybrids are at an all-time high right now. Investors can pick up ~160bps in Z-spread terms on average by moving from a BBB- rated corporate hybrid into a BB+ rated corporate hybrid. This compares with a ~20-80bps on average spread throughout 2017-2021[9].

We believe liability management could become a central theme in H2 2022.

Lastly, we believe liability management could become a central theme in H2 2022. In a risk-off market, corporate hybrid issuers can take advantage of the S&P 10% hybrid stock reduction rule, which allows a corporate hybrid issuer to redeem and not replace 10% of its hybrid capital each year without impacting its equity content.

We also think some selected hybrid issuers could arbitrage their cost of equity and cost of hybrids by raising equity and conduct liability management exercises of their hybrid capital to improve their credit metrics, as discussed in our commentary from mid-August Goodbye share buybacks, hello bond buybacks.

v) Convertible bonds

Amid the deteriorating macroeconomic picture, we have seen continued weakness across the global convertible bond universe for most of 2022.

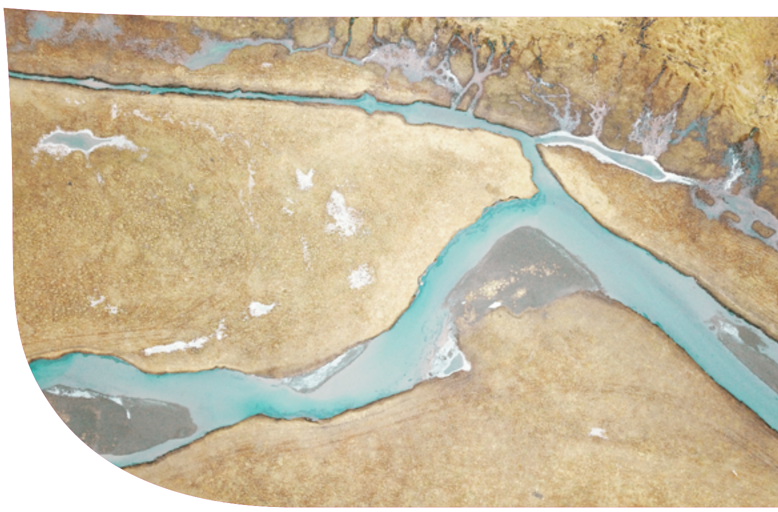
The performance of convertible bonds issued by more growth-dependent and consumer/tech-focused corporates has continued to surprise to the downside, given their vulnerability to higher inflation and tightening financial conditions.

The picture began to look a tad brighter as we arrived at the second half of the year, with converts rallying alongside risk assets through the summer. However, this reversed towards the end of August, following the Jackson Hole summit with its hawkish forward guidance from the Federal Reserve Chair.

Mirroring the theme we have seen in high yield and some other pockets of credit, convertible bond primary market issuance has remained anaemic this year, compared with the heavy levels of prior years. Companies had taken a breather from deployment to adjust to the new environment of elevated debt financing costs and lower share prices.

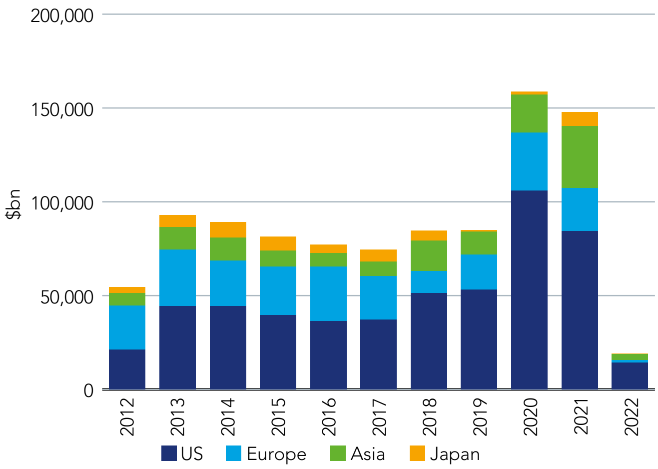
Convertible bond primary market issuance has remained anaemic this year, compared with the heavy levels of prior years.

August, however, marked the reversal of this recent trend. Here, we saw the strongest period of issuance in the year-to-date, with around $6.8bn of new supply, as more corporates appeared to be willing to take the plunge. We are now witnessing a handful of opportunistic issuers taking advantage of post-bear market rally conditions to acquire cheaper financing (versus straight bonds) through selling options to lower coupon payments; perhaps a prelude to a new trend that issuance volumes will follow going forward.



[9] Source: Bloomberg, Federated Hermes, Credit Suisse Indices, as at 13 September 2022.

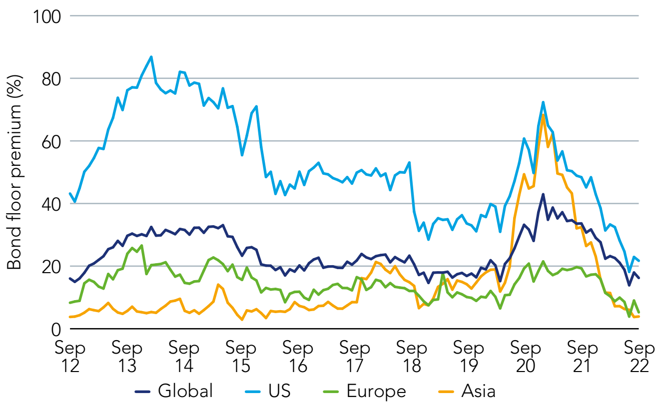
Figure 23: Global convertibles, issuance pace over the past decade



Source: Source: BofA Global Research, ICE Data Indices, LLC, as at August 2022.
Past performance is not a reliable indicator of future returns.

In the current setting, we continue to see a growing set of interesting opportunities in convertible bonds. This is particularly evident within the busted domain as bond floor premiums have fallen. Over 25% of the global convert universe is now trading below 80% of par[10], and relative valuation continues to screen well with many of these bonds trading in-line, if not at a discount, versus comparable vanilla bonds from the same issuer.

Figure 24: Convertibles, bond floor premium over the past decade



Source: BofA Global Research, ICE Data Indices, LLC, as at August 2022.
Past performance is not a reliable indicator of future returns.

We continue to believe that convertibles remain an attractive lever to play within the fixed income spectrum, and favour lower-delta convertibles with options deeply out of the money, given the fact their convexity profiles have become more attractive.

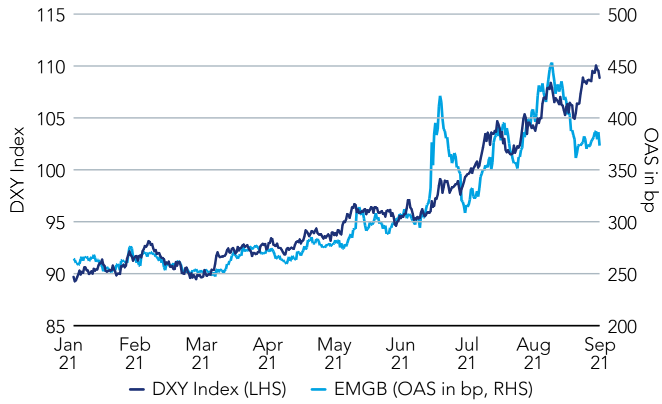
vi) Emerging markets

Emerging market corporates and sovereigns have experienced a tumultuous 2022 – far underperforming their respective developed market counterparts.

The brutal sell-off that emerging market credit experienced in the middle of August, and accelerated post Jackson Hole, took a pause in September. Nonetheless, the focus by core central banks on fighting inflation, with higher rates for longer and weaker growth tolerated, provides, we think, a continued difficult backdrop for EM assets and policymakers.

The headwinds from the strong US dollar are still being felt deeply by EM assets, as depicted in the chart below. To make matters worse, we now have a bleaker growth outlook from China, driven by a deeper and longer property contraction, exacerbated by mortgage boycotts, and intensified by Covid-19 lockdowns ahead of the upcoming National Congress, slowing external demand, and power shortages.

Figure 25: US$ strength and the impact on EM sovereign credit spreads



Source: Bloomberg, as at September 2022.
Past performance is not a reliable indicator of future returns.

The recent reversal in commodity prices is unlikely to significantly impact growth, but we believe it will affect public finances and current account positions. We predict that manufacturing exporters (typically commodity net importers) will see a decline in imports, and for commodity exporters, the H1 2022 windfall gains and export earnings will reverse.

Emerging market inflation momentum has started to ease, which indicates that headline inflation is approaching its peak.

Emerging market inflation momentum has started to ease, which indicates that headline inflation is approaching its peak (core inflation, however, will peak later and will remain stickier). The loss of growth momentum, and the coming disinflation, will grant EM central banks room to calibrate the last phases of their tightening cycles.

[10] Source: BofA Global Research, ICE Data Indices, LLC, as at August 2022.

The outlook for EM issuance for the rest of this year and next is dependent upon issuer and investor acceptance of the current paradigm – year-to-date EM corporate supply, for example, is down 60% when compared with the same period 2021. Higher rates and spreads have caused many issuers to hesitate to lock-in long-term financing at current yields. Also, volatile markets have made investors reluctant to buy new issue bonds, which can often be obtained at significant price discounts in the secondary market. However, we believe a recovery in early 2023 is now essential to allow issuers to meet their 2024 refinancing requirements.

A key event we will be following closely is the upcoming presidential elections in Brazil. Both Lula and Bolsonaro are well known to markets, so perhaps this election will not be as eventful as past ones. Currently, Brazilian pollsters are expecting a Lula win, although the voting intention gap is likely to narrow in the coming weeks. Regardless of the outcome, our forecast is for foreign investors to price in a high probability of a 'muddle through' scenario that will encapsulate some moderate fiscal weakening, and a partial reversal of Brazil's recently strong fiscal performance. This improved fiscal inheritance of the incoming administration should reduce the market sensitivity to the outcome of the election, or reasonable changes to the fiscal rule. As such, Brazilian assets should exhibit far less volatility than we have seen in other recent Latin American elections, such as the recent Colombian elections.

From a valuation point of view, hard currency EM corporates trade slightly rich to EM sovereigns, having been at fair value in Q1/Q2 of this year. Our view is that the sweet spot right now, from a valuation perspective in hard currency EM credit, is BB-rated corporate issues. They trade cheap relative to their DM and EM counterparts that are higher (i.e. BBB) and lower (i.e. B and lower) rated. Our focus is on investing in national champions and EM exporters who will benefit from their local currency weakness relative to a strong US dollar. We continue to be underweight to the Chinese property sector given the inherent weaknesses found here and the slow implementation of policy measures designed to help it.

vii) Leveraged loans

Despite headwinds, European leveraged loans continue to outperform high yield bonds this year.

Since the beginning of 2022, the S&P European Leveraged Loan Index (ELLI) has outperformed the ICE BofA Euro High Yield Index by returning -3.84%, compared with -12.54%[11].

Negative performance was driven by the unstable politic environment and concerns around elevated inflation but has been mitigated by the attractiveness of floating rate instruments limiting rate risk.

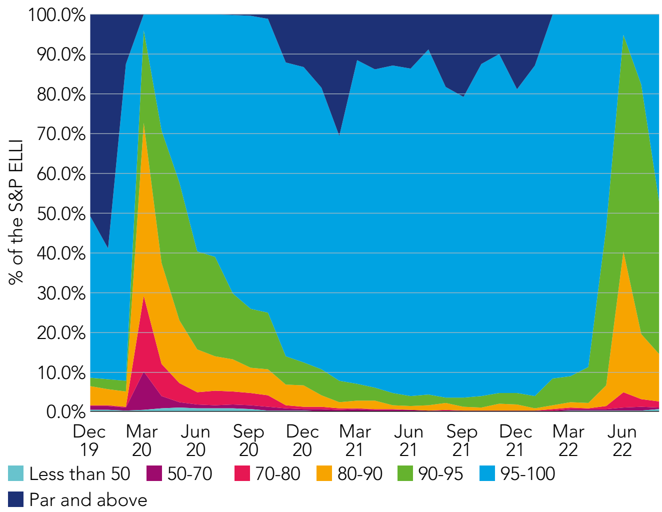
In the secondary market, the S&P ELLI is currently trading at 92.40 from 89.65 at the beginning of July – a level not seen since June of 2020[12].

Given the current economic backdrop, we view loan indicators as optimistic, particularly when comparing with levels reached after the Covid-19 outbreak.

The ELLI distress ratio (or the percentage of names trading below 80) was 2.69% at the end of August 2022 versus 29.09% at the end of March 2020.

- The level of CCC (names rated at CCC+ or lower on the index) was 3.82% at the end of August 2022, versus a March 2021 peak of 8.72%. At the end of February 2020, the level was 2.47%, and refinancing conditions were tighter than they are today (the average TLB[13] spread was 348bps vs. 475bps at the end of July 2022).
- Finally, the level of default remains low at 0.72% (by principal amount) at the end of August 2022, versus 2.61% at an October 2021 peak. S&P anticipated a default rate of 3.0% for June 2023.

Figure 26: S&P European Leveraged Loan Index (ELLI) price distribution, December 2019-August 2022



Source: S&P, as at August 2022.
Past performance is not a reliable indicator of future returns.

Given our view that loans are overpriced in the current environment, we would favour a tilt towards structured credit to mitigate the idiosyncratic risks. We believe this method offers better diversification and protection in the event of a default or rating downgrades. We would also favour a longer duration profile and a preference for newer deals to avoid underlying refinancing risk.

[11] Source: S&P, as at August 2022.
[12] Ibid.
[13] Term B Loans (TLBs) are often referred to as mezzanine debt or subordinated debt in transactions governed under English law.

viii) Structured credit

Despite weathering the worst of the macro headwinds, spreads in structured credit have widened over recent months in sympathy with wider market sell-offs.

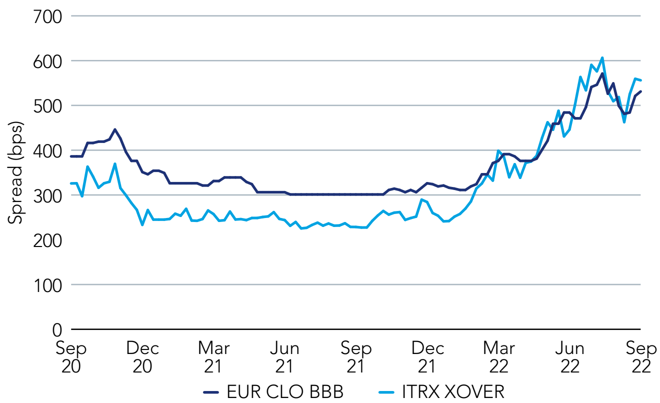
Primary markets for both asset-backed securities (ABS) and collateralised loan obligations (CLOs) were subdued over the summer, and while the pipeline has started up again, we are yet to see the volumes we would normally expect by this time of the year.

In ABS, the primary market has seen the re-emergence of club-like deals where a select group of investors is wall-crossed on a deal so that distribution and allocations can be more certain[14]. In CLOs, we saw a number of deals being pulled after marketing had begun, though not resulting from a lack of demand. Rather, the levels at which loans were trading versus the spreads on the liability stack of the CLO bonds meant the economics did not work to print the deal.

Our multi-asset-credit investment style leads us to view structured credit in the context of broader credit markets, including high yield and investment grade corporates. This is particularly the case when looking at CLOs (which are portfolios of leveraged loans to corporates, and so, therefore, ultimately linked to the high yield and investment grade markets).

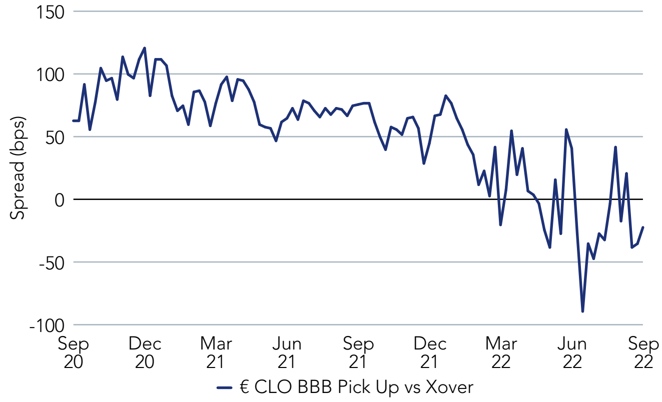
Having tracked the relationship of BBB CLOs against HY corporates ¬– here represented by the iTraxx Crossover index (ITRX XOVER) – CLOs have shown a pick up for quite some time, as illustrated in the charts below. However, over the course of 2022, the increased volatility in credit markets has broken that typical relationship and has, at times, resulted in more nuanced opportunities for trading in and out of CLOs.

Figure 27: EUR CLO BBB & ITRX XOVER spreads



Source: Citi (CLO) and Bloomberg (XOVER), as at 7 September 2022.
Past performance is not a reliable indicator of future returns.

Figure 28: EUR CLO BBB pick up vs. XOVER



Source: Citi (CLO) and Bloomberg (XOVER), as at 7 September 2022.
Past performance is not a reliable indicator of future returns.

As actively managed portfolios of leveraged loans, we expect the sector to weather the deterioration of credit fundamentals over the coming months. S&P forecasts the default rate in European leveraged loans to reach 3% by summer 2023. However, Fitch have stressed European CLOs to a scenario where 30% of issuers are downgraded and the default rate reaches 5% by the end of 2023, and almost all tranches retain their current assigned ratings.

While any credit deterioration has some way to run before ABS tranches are impacted, we keep a close eye on the performance of a range of factors including collateral pools, the use of credit cards, increasing credit card balances, monthly payment rates and mortgage delinquencies (especially in UK non-conforming).

It will be interesting to see whether the stressed consumer looks to pay their mortgage each month, or whether the increased forbearance measures we have seen arise in the past 15 years since the GFC mean that people look to pay off other debts ahead of their mortgage.

[14] 'Wall-crossed' refers to a situation where the flow of information between dealmakers is restricted through the use of 'Chinese walls'.

The value of investments and income from them may go down as well as up, and you may not get back the original amount invested. Any investments overseas may be affected by currency exchange rates. Past performance is not a reliable indicator of future results and targets are not guaranteed.

For professional investors only. This is a marketing communication. It does not constitute a solicitation or offer to any person to buy or sell any related securities, financial instruments or financial products. No action should be taken or omitted to be taken based on this document. Tax treatment depends on personal circumstances and may change. This document is not advice on legal, taxation or investment matters so investors must rely on their own examination of such matters or seek advice. Before making any investment (new or continuous), please consult a professional and/or investment adviser as to its suitability. Any opinions expressed may change. All figures, unless otherwise indicated, are sourced from Federated Hermes. All performance includes reinvestment of dividends and other earnings. Please consider all fund characteristics when investing and not just ESG characteristics.

Issued and approved by Hermes Investment Management Limited which is authorised and regulated by the Financial Conduct Authority. Registered address: Sixth Floor, 150 Cheapside, London EC2V 6ET. Telephone calls may be recorded for training and monitoring purposes. Potential investors in the United Kingdom are advised that compensation may not be available under the United Kingdom Financial Services Compensation Scheme.

Federated Hermes refers to Federated Hermes Limited ("Federated Hermes"). The main entities operating under Federated Hermes are: Hermes Investment Management Limited ("HIML"); Hermes Fund Managers Ireland Limited ("HFMIL"); Hermes Alternative Investment Management Limited ("HAIML"); Hermes Real Estate Investment Management Limited ("HREIML"); Hermes Equity Ownership Services Limited ("EOS"); Hermes Stewardship North America Inc. ("HSNA"); Hermes GPE LLP ("Hermes GPE"); Hermes GPE (USA) Inc. ("Hermes GPE USA"), Hermes GPE (Singapore) Pte. Ltd ("HGPE Singapore"), Federated Investors Australia Services Pty Ltd. ("FIAS") and Federated Hermes Japan Ltd ("FHJL"). HIML, HAIML and Hermes GPE are each authorised and regulated by the Financial Conduct Authority. HAIML and HIML carry out regulated activities associated with HREIML. HIML, Hermes GPE and Hermes GPE USA are each a registered investment adviser with the United States Securities and Exchange Commission ("SEC") and HAIML and HFMIL are each an exempt reporting adviser. HGPE Singapore is regulated by the Monetary Authority of Singapore. FHJL is regulated by Japan Financial Services Agency. FIAS holds an Australian Financial Services Licence. HFMIL is authorised and regulated by the Central Bank of Ireland. HREIML, EOS and HSNA are unregulated and do not engage in regulated activity. In the European Economic Area ("EAA") this document is distributed by HFMIL. Contracts with potential investors based in the EEA for a segregated account will be contracted with HFMIL.

Investments in emerging markets tend to be more volatile than those in mature markets and the value of an investment can move sharply down or up.

Where the strategy invests in debt instruments (such as bonds) there is a risk that the entity who issues the contract will not be able to repay the debt or to pay the interest on the debt. If this happens then the value of the strategy may vary sharply and may result in loss. The strategy makes extensive use of Financial Derivative Instruments (FDIs), the value of which depends on the performance of an underlying asset. Small changes in the price of that asset may cause larger changes in the value of the FDIs, increasing either potential gain or loss.

In Argentina: These materials and the information contained herein does not constitute and is not intended to constitute an offer and accordingly should not be construed as such. The products or services referenced in these materials may not be licensed in all jurisdictions, and unless otherwise indicated, no regulator or government authority has reviewed these materials, or the merits of the products and services referenced herein. These materials and the information contained herein has been made available in accordance with the restrictions and/or limitations implemented by any applicable laws and regulations. These materials are directed at and intended for institutional investors (as such term is defined in each jurisdiction in which these materials are being marketed). These materials are provided on a confidential basis for informational purposes only and may not be reproduced in any form. Before acting on any information in these materials, prospective investors should inform themselves of and observe all applicable laws, rules and regulations of any relevant jurisdictions and obtain independent advice if required. These materials are for the use of the named addressee only and should not be given, forwarded or shown to any other person (other than employees, agents or consultants in connection with the addressee's consideration thereof).

In Australia: This Strategy Document relates to potential offer of financial products or investment opportunities in Australia (Investment opportunities). Both Hermes Investment Management Ltd (HIML) and Federated Investors Australia Services Ltd. ACN 161 230 637 (FIAS) are the distributors of the Investment opportunities. HIML does not hold an Australian financial services licence (AFS licence) under the Corporations Act 2001 (Cth) ("Corporations Act"). HIML operates under the relevant class order relief from the Australian Securities and Investments Commission (ASIC) while FIAS holds an AFS licence (Licence Number – 433831). The offer of Investment opportunities only made in circumstances under which no disclosure is required under Chapter 6D and Part 7.9 of the Corporations Act. Nothing in this Strategy Document is, or purports to be, an offer to a person to whom disclosure would be required under Chapter 6D or Part 7.9 of the Corporations Act. This Strategy Document is not a disclosure document under Chapter 6D of the Corporations Act or a product disclosure statement for the purposes of Part 7.9 of the Corporations Act. This Strategy Document has not been and will not be lodged with ASIC and does not contain all the information that a disclosure document or a product disclosure statement is required to contain. The distribution of this Strategy Document in Australia has not been authorised by ASIC or any other regulatory authority in Australia. In addition, the Fund is not a registered managed investment scheme, as defined in the Corporations Act. This Strategy Document is provided for general information purposes only and is not intended to constitute, and does not constitute, the provision of any financial product advice or recommendation and must not be relied upon as such. This Strategy Document is not intended to influence a person in making a decision in relation to a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products. This Strategy Document has been prepared without taking account of your objectives, financial situation or needs and you should obtain independent professional financial advice that considers your circumstances before making any financial or investment decisions.

In Bahrain: This document has not been approved by the Central Bank of Bahrain which takes no responsibility for its contents. No offer to the public to purchase the strategies will be made in the Kingdom of Bahrain and this document is intended to be read by the addressee only and must not be passed to, issued to, or shown to the public generally. In Brazil: The strategies may not be offered or sold to the public in Brazil. Accordingly, the strategies have not been nor will be registered with the Brazilian Securities Commission – CVM nor have they been submitted to the foregoing agency for approval. Documents relating to the strategies, as well as the information contained therein, may not be supplied to the public in Brazil, as the offering of strategies is not a public offering of securities in Brazil, nor used in connection with any offer for subscription or sale of securities to the public in Brazil. In Brunei: This document is intended for distribution only to specific classes of investors as specified in the Order and must not, therefore, be delivered to, or relied on by, a retail client. The Autoriti Monetari Brunei Darussalam is not responsible for reviewing any documents in connection with these strategies. Prospective purchasers of the strategy should conduct their own due diligence.

In Canada: HIML is not registered in Canada as a dealer, adviser or investment fund manager under applicable Canadian securities laws. Except for the provinces of Alberta, British Columbia, Ontario, Quebec and Nova Scotia, HIML does not engage in the business of, and none of its activities should be construed as holding itself out as engaging in the business of, advising anyone in any Canadian jurisdiction with respect to investing in, buying or selling securities. In the provinces of Alberta, British Columbia, Ontario, Quebec and Nova Scotia, HIML relies on the international adviser registration exemption pursuant to section 8.26 of National Instrument 31-103– Registration Requirements, Exemptions and Ongoing Registrant Obligations. Prior to carrying on any investment advisory or portfolio management services for a client located in a Canadian jurisdiction other than Alberta, British Columbia, Ontario, Quebec or Nova Scotia, HIML will first need to take certain steps to either obtain the appropriate registration or rely on an available exemption from registration.

In Chile: Federated Hermes is not registered or licensed in Chile to provide managed account services and is not subject to the supervision of the Comisión para el Mercado Financiero of Chile ("CMF"). The managed account services may not be publicly offered or sold in Chile. In China: This document does not constitute a public offer of the strategies in the People's Republic of China (the "PRC"). The strategies are not being offered or sold directly or indirectly in the PRC to or for the benefit of, legal or natural persons of the PRC. Further, no legal or natural persons of the PRC may directly or indirectly purchase any of the strategies or any beneficial interest therein without obtaining all prior PRC's governmental approvals that are required, whether statutorily or otherwise. Persons who come into possession of this document are required by the issuer and its representatives to observe these restrictions.

In Columbia: This document does not have the purpose or the effect of initiating, directly or indirectly, the purchase of a product or the rendering of a service by Federated Hermes ("investment adviser") to Colombian residents. The investment adviser´s products and/or services may not be promoted or marketed in Colombia or to Colombian residents unless such promotion and marketing is made in compliance with decree 2555 of 2010 and other applicable rules and regulations related to the promotion of foreign financial and/or securities related products or services in Colombia. The investment adviser has not received authorisation of licensing from the Financial Superintendency of Colombia or any other governmental authority in Colombia to market or sell its financial products or services in Colombia. By receiving this document, each recipient resident in Colombia acknowledges and agrees that such recipient has contacted the investment adviser at its own initiative and not as a result of any promotion or publicity by the investment adviser or any of its representatives. Colombian residents acknowledge and represent that (1) the receipt of this presentation does not constitute a solicitation from the investment adviser for its financial products and/or services, and (2) they are not receiving from the investment adviser any direct or indirect promotion or marketing of financial products and/or services.

In Hong Kong: The contents of this document have not been reviewed by any regulatory authority in Hong Kong. You are advised to exercise caution in relation to the offer. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice. The strategies are not authorised under Section 104 of the Securities and Futures Ordinance of Hong Kong by the Securities and Futures Commission of Hong Kong. Accordingly, the distribution of this document, and the placement of interests in Hong Kong, is restricted. This document may only be distributed, circulated or issued to persons who are professional investors under the Securities and Futures Ordinance and any rules made under that Ordinance or as otherwise permitted by the Securities and Futures Ordinance.

In Israel: This document has not been approved by the Israel Securities Authority and will only be distributed to Israeli residents in a manner that will not constitute "an offer to the public" under sections 15 and 15a of the Israel Securities Law, 5728-1968 ("the Securities Law") or section 25 of the Joint Investment Trusts Law, 5754-1994 ("the Joint Investment Trusts Law "), as applicable. The strategies are being offered to a limited number of investors (35 investors or fewer during any given 12 month period) and/or those categories of investors listed in the First Addendum ("the Addendum") to the Securities Law, ("Sophisticated Investors") namely joint investment funds or mutual trust funds, provident funds, insurance companies, banking corporations (purchasing strategies for themselves or for clients who are Sophisticated Investors), portfolio managers (purchasing strategies for themselves or for clients who are Sophisticated Investors), investment advisors or investment marketers (purchasing strategies for themselves), members of the Tel-Aviv Stock Exchange (purchasing strategies for themselves or for clients who are Sophisticated Investors), underwriters (purchasing strategies for themselves), venture capital funds engaging mainly in the capital market, an entity which is wholly-owned by Sophisticated Investors, corporations, (other than formed for the specific purpose of an acquisition pursuant to an offer),with a shareholder's equity in excess of NIS 50 million, and individuals in respect of whom the terms of item 9 in the Schedule to the Investment Advice Law hold true investing for their own account, each as defined in the said Addendum, as amended from time to time, and who in each case have provided written confirmation that they qualify as Sophisticated Investors, and that they are aware of the consequences of such designation and agree thereto; in all cases under circumstances that will fall within the private placement or other exemptions of the Joint Investment Trusts Law, the Securities Law and any applicable guidelines, pronouncements or rulings issued from time to time by the Israel Securities Authority. This document may not be reproduced or used for any other purpose, nor be furnished to any other person other than those to whom copies have been sent. Any offeree who purchases strategies is purchasing such strategies for its own benefit and account and not with the aim or intention of distributing or offering such strategies to other parties (other than, in the case of an offeree which is a Sophisticated Investor by virtue of it being a banking corporation, portfolio manager or member of the Tel-Aviv Stock Exchange, as defined in the Addendum, where such offeree is purchasing strategies for another party which is a Sophisticated Investor). Nothing in this document should be considered investment advice or investment marketing as defined in the Regulation of Investment Counselling, Investment Marketing and Portfolio Management Law, 5755-1995. Investors are encouraged to seek competent investment counselling from a locally licensed investment counsel prior to making the investment. As a prerequisite to the receipt of a copy of this document a recipient may be required by the Issuer to provide confirmation that it is a Sophisticated Investor purchasing strategies for its own account or, where applicable, for other Sophisticated Investors. This document does not constitute an offer to sell or solicitation of an offer to buy any securities other than the strategies offered hereby, nor does it constitute an offer to sell to or solicitation of an offer to buy from any person or persons in any state or other jurisdiction in which such offer or solicitation would be unlawful, or in which the person making such offer or solicitation is not qualified to do so, or to a person or persons to whom it is unlawful to make such offer or solicitation.

In Japan: Federated Hermes Japan Ltd is registered as a Financial Instruments Business Operator in Japan (Registration Number: Director General of the Kanto Local Finance Bureau (Kinsho) No. 3327), and conducting the Investment Advisory and Agency Business as defined in Article 28 (3) of the Financial Instruments and Exchange Act ("FIEA"). Federated Hermes Japan Ltd is acting as agent or intermediary between affiliated companies within the Federated Hermes group and Japanese licensed discretionary investment managers, trust banks and other Japanese financial institutions. Federated Hermes Japan Ltd is a member of Japan Investment Advisers Association (JIAA).

In Kuwait: This document is not for general circulation to the public in Kuwait. The strategies have not been licensed for offering in Kuwait by the Kuwait Capital Markets Authority or any other relevant Kuwaiti government agency. The offering of the strategies in Kuwait on the basis of a private placement or public offering is, therefore, restricted in accordance with Law No. 7 of 2010 and the bylaws thereto (as amended). No private or public offering of the strategies is being made in Kuwait, and no agreement relating to the sale of the strategies will be concluded in Kuwait. No marketing or solicitation or inducement activities are being used to offer or market the strategies in Kuwait.

In The Sultanate of Oman: The information contained in this document neither constitutes a public offer of securities in the Sultanate of Oman as contemplated by the Commercial Companies Law of Oman (Royal Decree 4/74) or the Capital Market Law of Oman (Royal Decree 80/98), nor does it constitute an offer to sell, or the solicitation of any offer to buy Non-Omani securities in the Sultanate of Oman as contemplated by Article 139 of the Executive Regulations to the Capital Market Law (issued by Decision No.1/2009). Additionally, this document is not intended to lead to the conclusion of any contract of whatsoever nature within the territory of the Sultanate of Oman.

In Peru: All content in this presentation is for information or general use only. The information contained in this presentation is referential and may not be construed as an offer, invitation or recommendation, nor should be taken as a basis to take (or stop taking) any decision. This presentation has been prepared on the basis of public information that is subject to change. This information may not be construed as services provided by Federated Hermes, Inc. within Peru without having the corresponding banking or similar license according to the applicable regulation. In South Africa: This document is not intended and does not constitute an offer, invitation, or solicitation by any person to members of the public to invest. This document is not an offer in terms of Chapter 4 of the Companies Act, 2008. Accordingly this document does not, nor is it intended to, constitute a prospectus prepared and registered under the Companies Act.

In South Korea: Hermes Investment Management Limited is not making any representation with respect to the eligibility of any recipients of this document to acquire the strategies therein under the laws of Korea, including but without limitation the Foreign Exchange Transaction Act and Regulations thereunder. The strategies have not been registered under the Financial Investment Services and Capital Markets Act of Korea, and none of the strategies may be offered, sold or delivered, or offered or sold to any person for re-offering or resale, directly or indirectly, in Korea or to any resident of Korea except pursuant to applicable laws and regulations of Korea.

In Spain: This document is issued by Hermes Fund Managers Ireland Limited, Branch in Spain, with Fiscal Identity Number W0074815B, registered in the Mercantile Registry of Madrid, – Volume 40448, Book 0, Sheet 16, Section 8, Page M-718259, first registration, with domicile at Paseo de la Castellana 18, 7° planta, 28046 Madrid – Spain, and registered in the Comisión Nacional del Mercado de Valores with official registration number 36.

In Thailand: The document has not been approved by the Securities and Exchange Commission which takes no responsibility for its contents. No offer to the public to purchase the strategies will be made in Thailand and this document is intended to be read by the addressee only and must not be passed to, issued to, or shown to the public generally.

In United Arab Emirates (Excluding Dubai International Financial Centre and Abu Dhabi Global Market): This document, and the information contained herein, does not constitute, and is not intended to constitute, a public offer of securities in the United Arab Emirates and accordingly should not be construed as such. The strategies are only being offered to a limited number of sophisticated investors in the UAE who (a) are willing and able to conduct an independent investigation of the risks involved in an investment in such strategies, and (b) upon their specific request. The strategies have not been approved by or licensed or registered with the UAE Central Bank, the Securities and Commodities Authority or any other relevant licensing authorities or governmental agencies in the UAE. The document is for the use of the named addressee only and should not be given or shown to any other person (other than employees, agents or consultants in connection with the addressee's consideration thereof). No transaction will be concluded in the UAE and any enquiries regarding the strategies should be made to Hermes Investment Management Limited in London.

In Uruguay: These materials and the information contained herein does not constitute and is not intended to constitute an offer and accordingly should not be construed as such. The products or services referenced in these materials may not be licensed in all jurisdictions, and unless otherwise indicated, no regulator or government authority has reviewed these materials, or the merits of the products and services referenced herein. These materials and the information contained herein has been made available in accordance with the restrictions and/or limitations implemented by any applicable laws and regulations. These materials are directed at and intended for institutional investors (as such term is defined in each jurisdiction in which these materials are being marketed). These materials are provided on a confidential basis for informational purposes only and may not be reproduced in any form. Before acting on any information in these materials, prospective investors should inform themselves of and observe all applicable laws, rules and regulations of any relevant jurisdictions and obtain independent advice if required. These materials are for the use of the named addressee only and should not be given, forwarded or shown to any other person (other than employees, agents or consultants in connection with the addressee's consideration thereof).

In the United States of America: For a full list of all affiliated companies please see the relevant Form ADV. Certain affiliates have cash solicitation arrangements under which they receive compensation for referring prospects for advisory services.

US Offshore: The Shares have not been and will not be registered under the US Securities Act of 1933, as amended (the "1933 Act") or the securities laws of any of the states of the US. The Shares may not be offered or sold directly or indirectly in the US or to or for the account or benefit of any US Person.

BD010646

Federated Hermes Limited

Federated Hermes

Federated Hermes is a global leader in active, responsible investing.

Guided by our conviction that responsible investing is the best way to create long-term wealth, we provide specialised capabilities across equity, fixed income and private markets, multi-asset and liquidity management strategies, and world-leading stewardship.

Our goals are to help people invest and retire better, to help clients achieve better risk-adjusted returns, and to contribute to positive outcomes that benefit the wider world.

All activities previously carried out by Hermes Investment Management are now undertaken by Federated Hermes Limited (or one of its subsidiaries). We still offer the same distinct investment propositions and pioneering responsible investment and stewardship services for which we are renowned – in addition to important strategies from the entire group.

Our investment and stewardship capabilities:

- **Active equities:** global and regional
- **Fixed income:** across regions, sectors and the yield curve
- **Liquidity:** solutions driven by four decades of experience
- **Private markets:** real estate, infrastructure, private equity and debt
- **Stewardship:** corporate engagement, proxy voting, policy advocacy

For more information, visit **www.hermes-investment.com** or connect with us on social media: