INVESTMENT PROCESS

Janus Henderson Euro High Yield Bond Strategy

Published May 2017

For professional investors only

Key differentiators

Global insight: Janus Henderson's credit team has been built up into a global team that allows them to contextualise value in European credit and be aware of cross-regional factors that affect individual credits.

Multiple levers of return: Investment in an expanding universe of issuers, complemented by interest rate management, tactical off-benchmark opportunities and selective use of derivatives. Janus Henderson was an early adopter of credit derivatives and has a strong implementation track record.

Commercially-driven analyst structure: Janus Henderson's credit analysts focus on supplying active buy and sell recommendations, rather than simply replicating rating agency research notes.

High-conviction approach: 75-150 issuers selected with a strong emphasis on credit analysis, with the ability to access smaller, less liquid credit issuers while actively managing the portfolio to reflect market changes.

Overview

The Janus Henderson Euro High Yield Bond Strategy seeks to capture the total return potential of the European high yield bond universe through a conviction portfolio, yet one that is diversified in terms of issuers, sectors and geography.

Security selection is the primary driver of returns, so emphasis is placed on assessing company metrics, corporate strategy, and bond covenants while taking into account the credit cycle and market conditions.

Management team

Stephen Thariyan, Tom Ross and Thomas Hanson jointly manage the strategy. They have strong track records as credit managers, with a combined 55 years of industry experience.

(at 31 March 2017)

The portfolio managers harness the strengths of Janus Henderson's highly experienced credit team of portfolio managers, analysts and traders. They work with colleagues globally, who have expertise across investment grade, high yield, secured credit and emerging market debt, as well as cross-collaboration with the equity teams.

Investment philosophy

The high yield market is diverse. It ranges from large publicly-listed household names that have been downgraded from investment grade to smaller private companies that are first-time issuers. By definition, the sub-investment grade market is populated by companies where questions exist over earnings direction and balance sheet strength. Given that high yield is an area where strong credit analysis is rewarded, the investment philosophy is based upon three key elements:

Market inefficiency	Price inefficiencies exist that create attractive relative value opportunities across issuers due to size, credit quality and geography
Research driven	Forward-looking credit research aims to identify issues ahead of time and to allow expression of high conviction views
Flexibility	Ability to access smaller, less liquid credit issuers while retaining ability to exit positions on a change of view

Past performance is not a guide to future performance. The value of an investment and the income from it can fall as well as rise and investors might not get back the amount originally invested.

Janus Henderson
—KNOWLEDGE. SHARED—

Janus Henderson Euro High Yield Bond Strategy

Investment universe

At least 70% of the portfolio's net assets must be invested in sub-investment grade corporate debt securities with a credit rating of BB+ or lower and denominated in euros or sterling. Investment is primarily in cash bonds, although derivatives may be used to gain exposures or hedge positions.

Process overview

1. Focus the universe

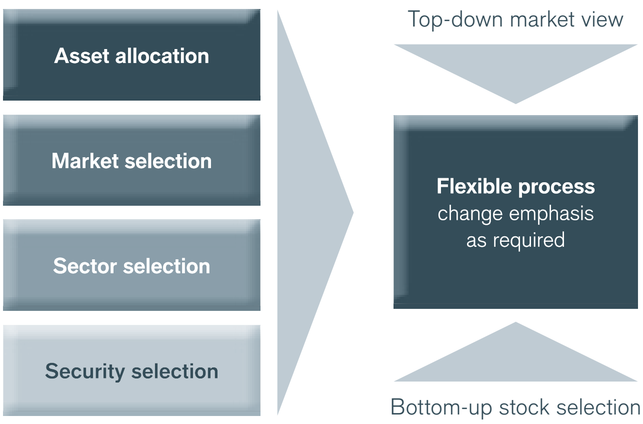
The European high yield universe includes approximately 300 issuers and the initial stage of the process is to focus on the areas of the market with the most attractive risk/return profiles. A combination of internal and external research and analysis is used to determine the final 75-150 issuers to be included in the portfolio[2]. A key strength of Janus Henderson is the team's expertise in assessing smaller issuers and those lower down the ratings spectrum, given that mispricing is often most pronounced in these areas of the market.

[2] Illustrative range only and may be subject to change - correct at 31 March 2017

2. Idea generation

Ideas are assessed based on a rigorous four-factor decision framework that covers: **macroeconomics**; **corporate health**; **market dynamics**; and **valuations**. In this way, top-down macroeconomic analysis is blended with bottom-up credit selection to inform analysis.

Research and analysis – targeting the strategy



Top-down

Asset allocation: The credit portfolio managers meet each month to formulate the team's macro outlook. This includes a review of credit sub-asset classes using the four-factor decision framework. In addition to macroeconomic factors, the team reviews each sub-asset class based on the fundamental health of balance sheets, supply and demand technicals, and relative value compared to other credit opportunities.

Market selection: Based on the macro view, credit sub-asset classes are ranked in order of preference based on their potential to offer the best returns in the coming months. This provides the portfolio managers with an overlay for portfolio construction for each strategy. While the managers are able to deviate from this higher level view if bottom-up opportunities merit it, justification must be provided and the reasons endorsed at the monthly portfolio review meeting with the wider team.

Seasonal factors can be important within high yield, thus particular attention is paid to the deal pipeline and flows, all of which can have a bearing on high yield valuations.

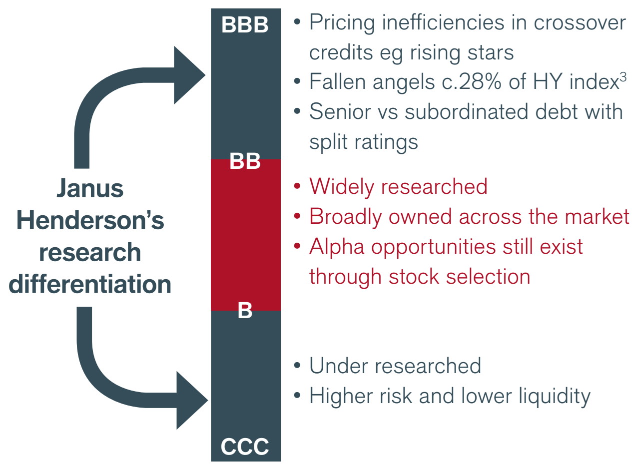
Bottom-up

Sector selection: Analysts are responsible for analysing specific sectors and the securities within those sectors across the full capital structure. Each month the analysts score their respective sectors based on the same four-factor decision framework. They pay particular attention to credit improvement/deterioration and the likelihood of default.

Security selection: Analysts provide a continuous stream of unconstrained buy/sell ideas, focusing on value and the catalysts that drive price performance in a bond. The team's analysts stand out for their 'publishing-lite', commercial approach to generating trade ideas, and are remunerated based on the success of these ideas.

The key question for the analysts is which companies offer value or are best avoided, since price movements tend to be more acute in high yield than investment grade. As well as identifying near-term catalysts for returns, the analysts often propose bonds from companies that are in the early stages of credit improvement. Over time, these can offer significant ratings upgrades, even to the point of gaining investment grade status, so-called 'rising stars'. Similarly, value may be present in bonds recently downgraded from investment grade, so-called 'fallen angels'.

Exploiting the opportunity set



[3] Source: Market value of BofA Merrill Lynch Euro Fallen Angel High Yield Index (HEFA) as a percentage of BofA Merrill Lynch Euro High Yield Index (HE00) at 31 March 2017.

Janus Henderson Euro High Yield Bond Strategy

Direct meetings with company management allow for a deeper understanding of an issuer's corporate strategy and whether this is bondholder-friendly. The credit analysts also liaise closely with their colleagues in the equities department to develop a broader viewpoint, identify inconsistencies in future expectations and assess areas of potential conflict among stakeholders. Analysis of sustainability and corporate governance is incorporated in recognition of the importance that management, quality of earnings and the regulatory environment can have on long-term corporate success.

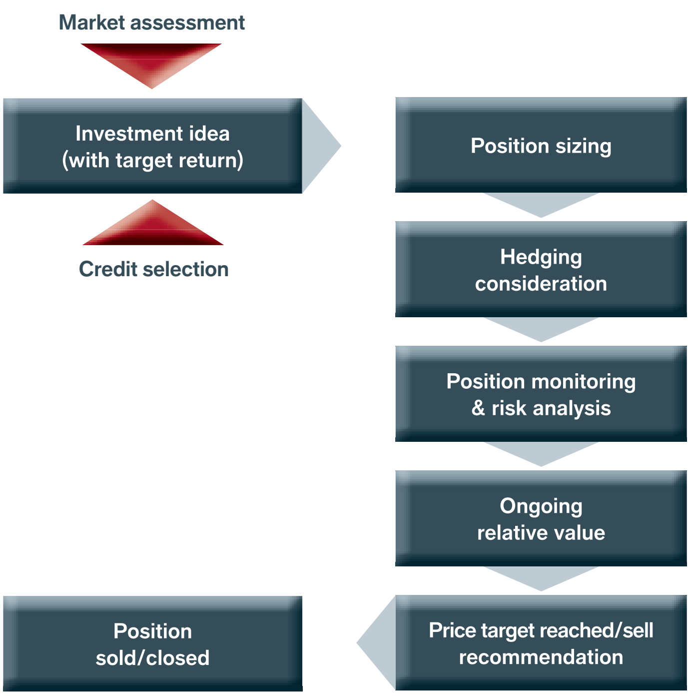
3. Portfolio construction

Idea adoption
Each portfolio manager assesses investment ideas that arise from the decision framework. While the macro view provides a basis for construction, the individual managers implement the ideas that best meet the objective of their specific strategy. These ideas could be at a sector level (eg, a strong directional view) or individual security level (either outright or relative value).

The analyst recommendation is made with a proposed target return and anticipated impact on portfolio risk. The portfolio managers will use measures such as duration contribution, tracking error and factor analysis to assess the recommendation. They also overlay a qualitative view, which contributes to position sizing, taking into account factors such as liquidity and expected recovery value should the bond default.

An idea selected by the portfolio managers may be implemented using either cash bonds or credit derivatives. Credit analysts, portfolio managers and Janus Henderson's dedicated credit traders sit on adjacent banks of desks and have ongoing dialogue that helps optimise the execution of trades.

Investment lifecycle
The lifecycle of an investment made by the credit team is ever changing and has key checks applied. Although this process is not linear, the chart below gives an indication of the various stages it goes through.



Tom Ross, CFA
Portfolio Manager

> "In a world of low interest rates, high yield corporate bonds offer attractive income. Our goal is to enhance total returns and manage downside risk through our credit research."

Sell discipline

Each active position has an investment rationale, target return and risk level, determined by the credit analyst and portfolio managers at the outset. These are then subject to continued monitoring, with revisions as new information is received. Typical triggers for a sell recommendation include:

Relative value

- Initial performance target achieved
- Superior investment opportunity elsewhere
- Spread per unit of leverage insufficiently attractive
- Cross-market currency mismatch in bonds from same issuer

Anticipated near term negative credit event

- Earnings risk (issuer specific or peer group)
- Releveraging (debt financed M&A, distribution to shareholders)
- Change in strategy/senior management
- Liquidity concerns
- Potential covenant breach

While the strategy provides investors with access to many of the smaller issuers that comprise a large part of the high yield market, the managers tend to avoid bond issues that are below €100 million in size due to liquidity.

Derivatives
Janus Henderson's credit team has employed derivatives within portfolios for more than a decade. Derivatives are used for hedging purposes, to alter exposures in the strategy or to undertake synthetic short positions. Credit derivatives may be used to take advantage of relative value discrepancies between bonds and derivatives, or to take a short position in a single issuer through credit default swaps if a security is deemed to be overvalued. Derivative transactions are made with one or more counterparties and counterparty risk is spread in accordance with strategy directives.

Duration positioning
Duration in high yield portfolios tends to be lower than investment grade because of the relatively short maturities and higher coupons. As a result, duration tends to be a secondary consideration, although it is taken into account when assessing relative value and market sentiment towards different areas of the fixed income market.

Currency hedging
Currency exposure is hedged back to the euro (the benchmark currency) through FX forward contracts and then, if necessary, to the required currency of the mandate.

Janus Henderson Euro High Yield Bond Strategy

4. Risk management

Risk management is embedded throughout the process via performance attribution, risk budgeting, liquidity analysis, stop-losses, strict sell disciplines and concentration limits, together with monitoring of performance, volatility/tracking error and net/gross exposures.

Janus Henderson's oversight structure includes an Investment Risk Team that is independent from the portfolio managers. This team works closely with the portfolio managers and senior management to ensure all risks taken in the portfolios are intended, ie, they accurately reflect the managers' core views and are in line with client expectations.

Third party risk models such as RiskMetrics and UBS Delta are employed to provide a comprehensive decomposition of risks in the portfolio. This allows for reviews of risk and for stress testing and scenario analyses to be undertaken. Dashboards are updated daily so that portfolio managers and the investment risk team are quickly alerted to any developing risks.

Each quarter the Investment Risk Team meets the portfolio managers for a formal risk review of the portfolio and may be required to attend additional fixed income oversight meetings on a rotational or as required basis.

Portfolio Managers

Stephen Thariyan
Head of Global Credit
Stephen Thariyan joined Henderson in 2007 as Head of Credit and is in charge of the 33-strong London-based global credit team. Prior to this, Stephen was a portfolio manager at Rogge Global Partners, following five years as Head of Credit Reserach. Before that he was director and senior analyst at NatWest Markets' credit unit. He started his career as an accountant at Ernst & Young in 1988 and later moved to become senior auditor at Chevron Corporation.

Tom Ross, CFA
Portfolio Manager
Tom joined Henderson in 2002 and has been co-managing absolute return credit funds since 2006. In August 2015 he was appointed co-manager of a number of European and global bond portfolios. Prior to fund management, he specialised in credit trading on Henderson's centralised dealing desk, where he was able to build strong relationships with market participants in order to gain flow and positioning information to supplement credit views.

Thomas Hanson, CFA
Portfolio Manager
Thomas Hanson joined Henderson in October 2015 as a Portfolio Manager. Prior to joining Henderson, Thomas was a Senior Credit Portfolio Manager at Aerion Fund Management. He co-managed the sterling investment grade corporate bond portfolio for the National Grid pension scheme, totalling £4.9bn. Thomas started his career at Lazard Asset Management, where he spent 14 years, and became the lead portfolio manager for all sterling fixed income strategies and a senior portfolio manager for European investment grade and high yield funds. Thomas is a CFA charterholder.

Janus Henderson Investors

Henderson Global Investors merged with Janus Capital Group in May 2017.

Past performance is not a guide to future performance.
The value of an investment and the income from it can fall as well as rise and investors may not get back the amount originally invested.

Contact us
General enquiries: **+44 (0)20 7818 5228**
Email: **institutionalsupport@janushenderson.com**
Website: **janushenderson.com/institutional**

Janus Henderson
—KNOWLEDGE. SHARED—

H029214/0417