

**BANQUE DE LUXEMBOURG**  
**FUND RESEARCH**  
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**INVESTMENT**  
**METHODOLOGY**  
**BONDS**

# Investment Methodology Bonds

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Our investment process involves a top-down approach. This sets the macroeconomic framework with the ultimate aim of defining the portfolio's sensitivity to changes in interest rates (or modified duration) as well as the positioning of various issuers on the euro zone on the yield curve. The portfolio uses the JPMorgan Global Government Bond EMU Local Currency as a benchmark.

### **Step 1: Defining the macroeconomic scenarios**

The analysis of the macroeconomic environment defines the overall framework and determines the correct duration for the portfolio. Rather than using historical or current data, the investment strategy is based on economic forecasts.

#### a) Government bonds:

- Economic growth
- Inflation
- Foreign exchange markets
- Monetary policies

The emerging market bond portfolio is managed externally. Macroeconomic and geopolitical criteria are used to evaluate the outlook for this asset class.

#### b) Corporate bonds

The corporate bonds portfolio is also managed externally. Internal analyses are used to determine the attractiveness for this asset class:

- Situation in the debt reduction cycle
- State of the economy
- Current dynamics (e.g.: increased mergers and acquisitions activity)
- Activity on the primary market

### **Step 2: Determining the state of the market**

On a tactical basis, economic fundamentals will be confirmed by the observation of technical criteria. These criteria help to take advantage of sporadic opportunities and guide the positioning of the portfolio on a short to medium-term horizon (ranging from a few weeks to a few months)

- Level of bond yields in real terms (current level vs. historical average)
- Steepness of the yield curve (current situation vs. historical average)
- Corporate and emerging market spreads

### **Step 3: Building a portfolio**

The portfolio construction is the result of the following steps:

- Taking into account the decisions in terms of Asset Allocation
- Taking into account the portfolio constraints
- Strict selection of securities (selection of the most recent issues, relative valuation, specificities of the various issuers in the euro zone), etc

### **Step 4: Implementation of active management strategies**

The daily management of the bond portfolio is conducted based on the interpretation of the information detailed above and the integration of various short, medium and long-term views.

- Application of the active management model (integration of technical and fundamental criteria)
- Managing the positioning on the yield curve
- Adapting the average modified duration to take account of changes

### **Step 5: Performance attribution by the Risk Management department of Banque de Luxembourg**

