AXA IM PRIME
Hedge Fund Strategy Overview
Q4 2024

Informative document based on the views of AXA IM Prime, however this is not an investment recommendation, nor advice to buy or sell a specific instrument.

Investment Managers

Prime

Hedge Fund Strategy Overview

Strategy Outlook Dashboard

Strategy	Q2-23	Q3-23	Q4-23	Q1-24	Q2-24	Q3-24	Q4-24
Event Driven	Neutral	Neutral	Positive	Positive	Positive	Positive	Positive
Quantitative	Positive	Positive	Positive	Positive	Positive	Positive	Positive
Stock Picking	Positive	Positive	Positive	Positive	Positive	Positive	Positive
Multi-Strategy	Positive	Positive	Neutral	Neutral	Neutral	Neutral	Neutral
Global Macro	Positive	Positive	Positive	Positive	Positive	Positive	Positive
Managed Futures	Neutral	Neutral	Neutral	Neutral	Neutral	Neutral	Neutral
Fixed Income Arbitrage	Positive	Positive	Positive	Positive	Positive	Positive	Positive
Convertibles Arbitrage	Positive	Positive	Positive	Positive	Positive	Positive	Positive
Credit/Distressed	Positive	Positive	Positive	Positive	Positive	Positive	Neutral

Hedge Fund Strategy Overview

Event Driven

Definition

Event Driven funds aim to profit from significant events affecting a company where the uncertainty regarding the outcome creates an opportunity. They generally combine long and short positions across all asset classes they view to be mispriced, often in an arbitrage type trade.

Approaches are split between those who try to predict events and those that only get involved once events are announced, such as mergers and corporate actions. Once the team has predicted the outcome of the event and has determined an investment horizon, they analyse the securities available and select the best tool to profit, usually ranging across credit and equity. At the same time, they consider the potential risks, in terms of: volatility, liquidity, market and sector risks. Usually, the most significant risk is the potential of the event not happening. Finally, they must determine how to close the position, and the probability of each of the possible outcomes.

Sub-Strategies

Merger Arbitrage

Merger Arbitrage strategies exploit inefficiencies in merger transactions by capturing the spread between the offered price and the traded price of a given security being acquired. The spread reflects the risk of the deal not going through.

Key success factors include the ability to assess deal risk, trading around the spread, properly working out the hedging ratio for complex transactions, and using options as a return enhancer or in order to mitigate risk. The best environment for the strategy is one with plenty of M&A deals, low deal breaks and wide spreads which is driven by interest rates levels, riskiness of deals and liquidity

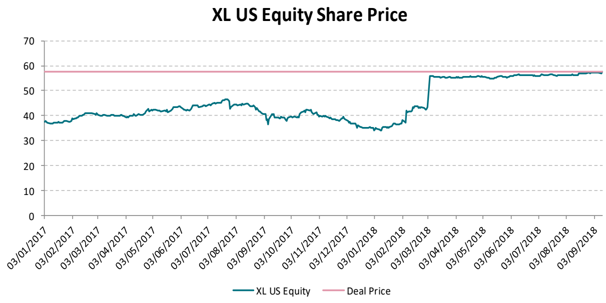
Equity Special Situations

These funds target targeting companies involved in actions such as corporate transactions, management changes, share buy backs, special dividends or restructurings. Funds will take positions based upon announced and pre-announced events and some managers may also become activist, engaging with companies to encourage catalysts. The strategy works best in benign equity markets with ample liquidity.

Distressed Securities

Funds in this space invest in companies facing financial or operational issues such as bankruptcy or capital restructurings. These securities tend to trade below their intrinsic value, creating an opportunity for managers who combine fundamental analysis of the company with their deep understanding of the restructuring or bankruptcy process to determine whether a distressed company is a worthwhile investment.

Trade example



Source: Bloomberg 09/03/18

AXA made an offer to acquire XL in March 2018. The deal was seen by the market as being likely to go through and so XL's share price jumped to near to the deal price following the announcement. Merger arbitrage funds were able to take advantage of the closing of the spread by analysing the likelihood of the deal closing and taking a position accordingly. Although the spread was relatively small, funds used leverage to amplify returns

Key Risks

Deal breaks: managers, especially merger arbitrage specialists, are exposed to confirmed deals collapsing for unexpected reasons.

Rival event: catalysts can be rendered irrelevant by a different catalyst, causing spreads to move unpredictably.

Market beta: although usually event trades have very reduced beta, in times of market stress there can be a lack of buyers and higher beta.

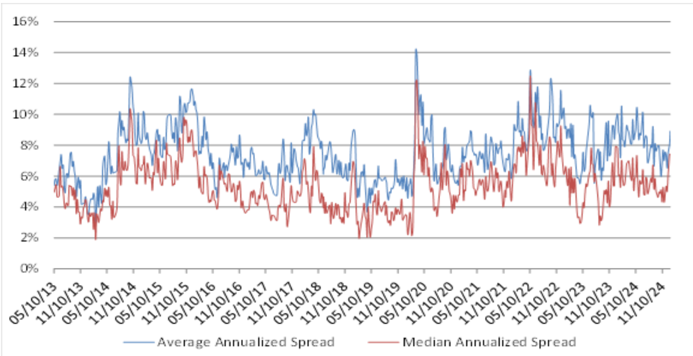
Hedge Fund Strategy Overview

Event Driven

Q4 Performance Drivers

- Event strategies performed well during the quarter, helped by the positive backdrop for global equities.
- The HFRI Event Driven TR Index was up +1.1% for the quarter bringing it to +8.7% YTD.
- The HFRI Merger Arbitrage Index was up +2.1% for the quarter bringing it to 5.9% YTD.
- There was some volatility caused by Sinopharm's bid for China TCM lapsing in October; and Revance Therapeutics accepting a reduced bid from Crown Labs in December. The same month President Biden confirmed he would block Nippon Steel's bid for US Steel, a move widely seen as an abuse of power, and both entities condemned the move and filed lawsuits. Strategy returns were driven by high profile deals tightening such as Chevron/Hess.
- Global deal flow was steady in Q4 with volumes of $1.12tn (compared to $1.15tn in Q3) bringing the total to $4.19tn YTD (compared to $3.65tn in 2023).
- Larger deals included Abu Dhabi National Oil's $16bn bid for Covestro; and Charter Communications' $18bn offer for Liberty Broadband.
- The HFRI Special Situations Index was down -1.5% for the quarter bringing it to +7.2% YTD. Risk-off behaviour put pressure on the complex, highlighted by the weak performance of Vivendi following its four-way split.
- The Equity IPO market saw a continuation of Q3 levels with 407 new issues raising $26bn, according to Bloomberg ($111bn YTD). Secondary activity picked up, with 2,620 deals raising $151bn.

Average Deal Spread (0-30%)



Source: UBS 16/01/25

Outlook

- Global M&A activity picked up in 2024, but was still 16% below the $5.0tn average for the last 10 years. An expected surge in H2 did not materialize, despite the rally in equity and corporate credit allowing easy access to capital and enabling deal flow.
- Uncertainty around the US elections prompted corporations to move at a slower pace, with the effect of pushing the backlog from the 2022-23 down-cycle into 2025, creating a positive backdrop for the year ahead.
- Strategic deals remain the focus of activity, but Private Equity has built up a war chest of $4tn of dry powder and we expect this to be a significant contributor to volumes in 2025.
- Median merger spreads moved slightly wider to 7.4% – broadly in line with the long-term average. Offset by a cut in US interest rates to 4.50%, this leaves implied yields broadly unchanged in the low-teens.
- The positive backdrop for equities creates a fertile environment for Special Sits, with fund pre-positioning for anticipated deals in focus.
- IPO activity has picked up from cyclical lows but volumes were still around half the 10-year average in 2024. Investment banks indicate a full pipeline leading to expectations for a resurgence in 2025.
- Secondary and Follow-On deal flow remains robust, with $516bn of issuance in 2024, a 23% improvement on 2023 and just nudging above the $514bn average for the last 10 years. We expect volumes to accelerate in 2025 and for this to remain a key driver of returns.

Rating: Positive

Investment Managers **/ Prime**

Hedge Fund Strategy Overview

Quantitative

Definition

Quantitative Equity Market Neutral funds use systematic processes in order to build portfolios of long and short equity positions in equal proportions.

Returns can be driven by statistical, factor or fundamental analysis, with the aim to isolate intended risk factors from market beta. This can take the form of tight pair trades or broader longs and shorts that are uncorrelated. Positions are often an amalgamation of multiple alpha signals.

Leverage tends to be an important factor as alpha can be low on an absolute basis, leading to highly diversified portfolios. Additionally, there is often the need for extra hedging in order to ensure that all unintended risks are eliminated.

Sub-Strategies

Multi-factor Quantitative Equity Market Neutral:

This system uses a series of style factors to analyze and predict stock movements. Some of the most common factors used are Value, Growth, Quality, and Momentum. Funds may look to allocate statically across these factors or to combine style factors into an overall alpha signal. Additionally, managers will generate their own, proprietary, style factors based on either statistical or fundamental drivers.

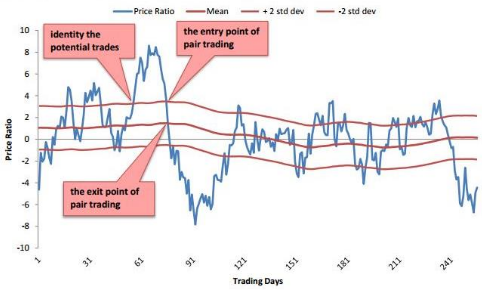
This model usually involves significant risk management to ensure that hedges are correctly positioned to strip out beta and highlight alpha signals. These models can combine different time horizons to enhance the alpha signals.

Statistical Arbitrage

This system uses statistical relationships between stocks to generate trades. Usually this takes the form of pair trading based on the relationship between two stocks or a basket of stocks. Usually, analysis is built solely on price action and involves some form of mean reversion or break-out analysis.

These strategies are designed to be run very tightly within pre-defined pairs or baskets so less hedging is needed. The alpha signals can be limited in absolute size and significant leverage is required.

Trade Example



Source: AXA IM PRIME 01/07/24

In this example we see an example of a pair trade based on price ratios. Here, alpha signals are driven by longer term rolling price ratios combined with standard deviation bands. When the price ratio gets outside of the expected bands, a signal is generated. The other consideration for this trade is momentum of the spread; trades are only entered when a trend has been established as moving back to the mean.

Key Risks

Model deterioration: over time models produce less alpha as competitors discover the opportunity.

Transaction costs: some models may rely on marginal gains and frequent trading, if spreads widen or costs rise alpha can be wiped out.

Crowding: deleveraging can have a significant impact, especially those with reactive risk management.

Investment Managers

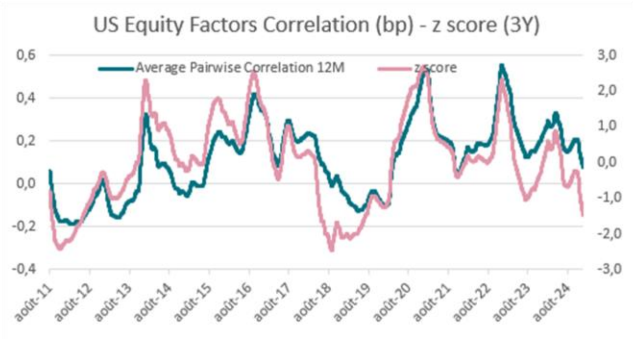
Prime

Hedge Fund Strategy Outlook

Quantitative

Q4 Performance Drivers

- The HFRI Equity Market Neutral Index was up +2.8% in Q4 and +10.9% in 2024.
- Equity factor correlations dropped down materially helping generate alpha.
- Growth was the best contributing factor up +15% over Q4 and 23% for the year. In contrast Value was the worst factor both for the quarter (-9%) and for the year (-14%) with the spread between both reaching extreme levels. Quality and Momentum contributed more muted returns while Size was flat on the quarter.
- We noticed a number of managers deleveraging ahead of US elections as short books got penalized by stocks exposed to the Trump policy agenda. Portfolios leverage increased back up towards the end of November. At the strategy level, performance was evenly distributed, with both fastest and slowest books gaining equally.
- China remained a bright spot. From a model's perspective, all top-line insight groups posted positive returns, with the Macro Thematic insight group being the largest contributor. The Sentiment and Fundamental insight groups were also additive. Within the Fundamental group, Value was flat, while the Quality signal family was the major contributor to the gains. Mutual fund herding signals continued to be the top-performing signals, while industry leadership insights also stood out.



Source Bloomberg data, AXA IM PRIME calculation 16/01/25

Outlook

- Elevated stock dispersion and low factor correlation should continue to support cross sectional multifactor quantitative models, while stat arb strategies could benefit from an elevated level of uncertainty.
- The environment for Quantitative strategies continues to improve in China as Quant funds AUM has dropped by 50% to 100bn$ in 2024. They now account for 5% of daily equity turnover from 20% a year ago leaving room for bigger alpha opportunities.
- Our preference goes to diversified QEMN funds which can benefit from a diversified stream of uncorrelated strategies over various investment horizons (statistical arbitrage to fundamental models) and across multi asset classes.
- Innovation in QEMN has led to the emergence of pure Machine Learning funds that have the potential to identify complex relationships in Financial Markets. Dispersion in this group of managers has increased making it harder to identify sustainable opportunities.

Rating : Positive

Hedge Fund Strategy Overview

Stock Picking

Definition

Discretionary Equity Long/Short funds look to take advantage in movements in the equity markets by taking long and short positions in individual stocks. Typically decisions are made based on fundamental work undertaken by analysts and portfolio managers.

Funds in this space can have varying beta exposure to market, and that exposure can be relatively static or vary considerably. Typically, one can expect leverage to be inversely proportional to net exposure. Some managers are also more concerned with hedging out style, country and sector exposure than others. Investment time horizons can vary greatly, whilst some managers are also active in trading around positions frequently.

Funds can usually be split into a number of broad investment styles. Value managers look for mispriced assets and liabilities. Growth managers look for mispriced growth and potential growth. Momentum managers look for improving or deteriorating trends, usually in earnings. GARP (Growth At a Reasonable Price) managers try to combine value and growth strategies. Company financial accounts and earnings statements are usually the key areas that managers focus on, although there can be an element of technical analysis to highlight entry and exit points.

Sub-Strategies

Trading

Some managers invest based mostly on price action, flows and perhaps only a surface level knowledge of the underlying company. Turnover tends to be high, with tight stop losses and an overall opportunistic approach to investing. Additionally, gross and net can be very variable, driven by the day-to-day opportunity set.

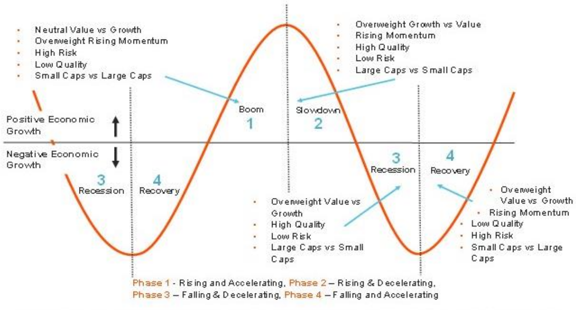
Earnings Predictions

Some managers are focused on correctly predicting earnings surprise, either positive or negative. This tends to mean that their investment time horizon is until quarter end, at which point they have an event, the earnings announcement, that either confirms or refutes their investment thesis. In practice they can hold positions over multiple quarters, but they will re-underwrite each time.

Buy and Hold

Some managers look to undertake significant due diligence on a company before investing in a stock, with the aim of holding on to the position over a multi-year time horizon. Typically, these managers are more agnostic to short term "noise" such as style factors, sector and country biases, and beta exposures. Typically, they expect returns to be driven by a combination of earnings enhancement and, more importantly, multiple re-rating as the company realizes the potential they see.

Trade Example



Source: Source: BofAML European Quant Strategy | Backtesting period from Dec 1992 to Dec 2003. Actual Performance Jan 2004 to Dec 2010.

This chart shows how difference style factors can drive stock prices at different points in a market cycle.

Key Risks

Beta Risk: Managers in this space can be heavily exposed to style, country, sector and market risks

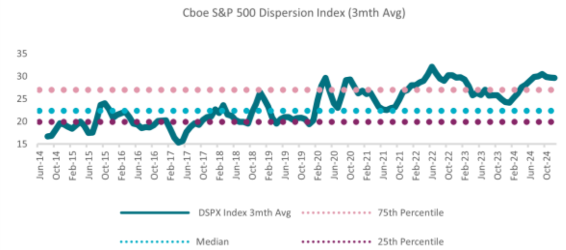
Financial risk: Risk derived from the financial position of a company and its capital structure. This could include liquidity and credit risk, inconsistent earnings or high levels of debt.

Business risk: Internal issues effecting the efficiency of a firm as well as poor management and procedures can have a great impact on the price of a firm's shares.

Hedge Fund Strategy Overview
Stock Picking

Q4 Performance Drivers

- The HFRI Equity Hedge Index added 1.7% in Q4, bringing 2024 returns to 12.3%. The MSCI World index performed -0.2% over Q4 and 18.7% YTD.
- Q4 was dominated by the U.S. presidential election, which resulted in a decisive victory for President Trump. This outcome triggered significant market movements across various industries, most notably, Software & Services, Tech Hardware, Regional Banks, Aerospace & Defense. Equity long/short managers were among top performers in November from these industries boosted by positive expectations of Republican policy priorities, including tax cuts, deregulation, and business-friendly initiatives.
- Managers had begun positioning for these "Trump Trade" sectors early in Q4, increasing their exposure after the election results. On the other hand, Healthcare stocks experienced significant downside volatility in December after President Trump announced RFK's appointment to lead HHS, with markets responding negatively due to uncertainty surrounding RFK's controversial stance on vaccines.
- Asian markets experienced strong performances across major indices: HK/China HSI (+18%), Taiwan TAIEX (+28%), and Singapore STI (+23%). However, Q4 saw some profit-taking that tempered market sentiment. While Japan continued to rise on the back of corporate reforms and increased foreign investment, investors remained cautious about China's consumer stimulus and India's valuations.



Source Bloomberg data, CBOE, AXA IM PRIME calculation 16/01/25

Outlook

- Japan's market momentum appears sustainable, underpinned by its corporate governance initiatives and structural reforms. However, regional dynamics present a more complex picture, with U.S.-China diplomatic relations emerging as a critical market driver in which managers will have to navigate.
- The post-election landscape in the US presents a particularly conducive environment for active stock selection, characterized by the potential for significant regulatory reform and heightened M&A activity. This environment favors investment approaches that leverage deep fundamental analysis while identifying multiple value creation catalysts, including corporate restructuring, operational turnarounds, and strategic transactions.
- Looking ahead, AI still presents compelling opportunities. Managers anticipate significant opportunities in companies driving fundamental technological breakthroughs, especially those with proven commercial applications and strong intellectual property positions. However, a selective approach remains crucial. While market leaders with sustainable competitive advantages offer attractive long positions, there are substantial short opportunities in overvalued companies lacking clear paths to profitability or those facing increasing competitive pressures. This bifurcation in the AI space creates an ideal environment for a disciplined long/short strategy.

Rating: Positive

Hedge Fund Strategy Overview

Multi-Strategy

Definition

Multi-Strategy funds combine multiple investment strategies to create a diversified portfolio. Strategies tend to be managed separately and capital is allocated between them based upon the risk appetite and return target. The aim is to provide broadly uncorrelated strategies that dampen volatility.

Usually, there is a central figure or committee that oversees risk management and capital allocation, either through a discretionary decision-making process or through a model driven approach derived from correlations and quality of returns. Often, portfolio managers are deployed in silos with limited overlap between strategies, although this can vary.

The largest multi-strategies can look more like complete asset management companies, offering access to multiple return streams either on an individual or combined basis with hundreds of portfolio managers.

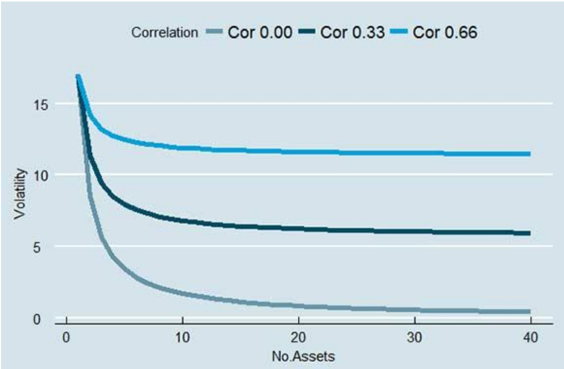
Characteristics

Diversified Returns:
Multi-strategy funds can offer a diversified return by allowing smaller managers with more niche strategies to gain access to established infrastructure. These managers may be unable to perform as stand-alone strategies but, with the processes and capital a multi-strategy fund could have access to they can get off the ground and provide a differentiated return stream for the fund as a whole.

Flexibility:
There can be a greater degree of flexibility as allocations between strategies can be manipulated more frequently based on opportunity set and performance.

Risk Management:
There is often an emphasis on centralised, robust risk management processes. Specialist risk teams will monitor the individual strategies and the portfolio as a whole and ensure that stringent guidelines are adhered to.

Investment Teams and Greater Talent Development:
Analysis of multi-strategy funds tends to pay particular attention to the internal workings of the fund and how the individual strategies work together. Rather than maintain poor performing managers, multi-strategy funds are often focused on refreshing talent to improve the quality of overall returns.



Source AXA IM PRIME illustration 01/07/24

By employing strategies that are uncorrelated, the benefits of diversification can be amplified to reduce risk.

Key Risks

Talent Retention: There is significant competition for portfolio managers within multi-manager shops.

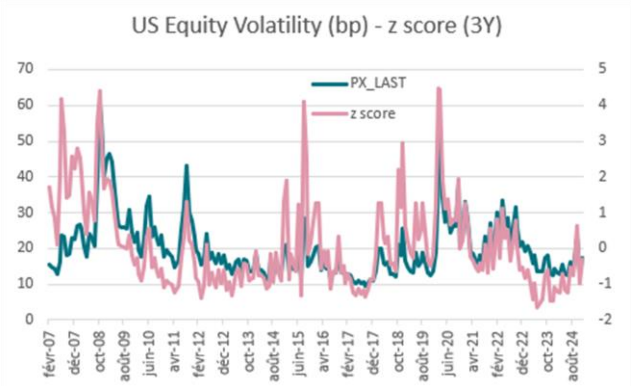
Fees: Some funds charge full pass-through costs, which can lead to very high expense ratios.

Diversification: Over-diversifying into non-core areas can be difficult, sometimes leading to muted or negative returns as new strategies bed in.

Hedge Fund Strategy Overview
Multi-Strategy

Q4 Performance Drivers

- The HFRI RV Multi-Strategy Index was up +1.7% in Q4 and +7.1% in 2024.
- Strong gains were generated in Equity strategies with Healthcare, Technology and Financials leading. Managers continues to add risk to US portfolios while exposures outside the US remained more challenging for alpha generation.
- Commodity strategies in Precious Metals and Energy contributed the most as inflationary pressures pushed gold higher while energy prices were impacted by a colder winter. Europe is facing supply issues which could impact prices for the next 12 months before going into surplus in 2026 as more US gas is shipped.
- Fixed Income allocations benefited from Bond basis trading and Directional Rates and Macro.
- Fundamental credit continued to tighten while convertible bonds benefited from a dynamic new issue market and the chepening of bonds.
- Quantitative strategies performed strongly driven by equity strategies.



Source Bloomberg data, AXA IM PRIME calculation 16/01/25

Outlook

- Top Tier funds are annualizing at low to mid teen returns as they continue to attract and retain most of the talent. Second Tier firms generated most of their gains in equities but have generally found it more challenging outside of equities and a few niche strategies.
- Most Top Tier funds are closed to new capital, making it difficult to increase allocations and diversifying into second tier firms comes with its own challenges.
- Equities which have been the main driver of performance last year could prove more challenging as the market navigates through tariff uncertainty.
- FX offers plenty of opportunities, with funds generally long USD and JPY and short EUR, GBP.
- Commodities is an area where competition for talent has heated up with opportunities in the Energy sector still plentiful.
- Rates could see opportunities outside the US as most of the action at the front end might be behind us in the US while the ECB could tighten further, Brazil might reverse last year's hikes and Japan might raise rates.
- We continue to maintain a NEUTRAL rating.

Rating : Neutral

Hedge Fund Strategy Overview

Global Macro

Definition

Global Macro funds focus on macroeconomic factors, taking positions according to the changes they see in the economic environment. They tend to make their profit from early identification of market moves in either direction.

Macro investing is very different from the investment strategies applied by other hedge fund managers, as it is more an overall approach than a precise strategy. Most funds will implement a top-down view and develop a global picture of markets to take advantage of opportunities when they appear across multiple asset classes. Once they have identified an interesting trade, they will often use a bottom-up approach in order to determine the most effective way to express their view.

Macro funds can use both quantitative and qualitative approaches at any stage of the investment timeline. They analyse economic cycles, political events and a variety of other indicators, often through interaction with policy makers and economists. Whilst some funds may base their top-down view on a manager's sentiment, others could apply models to notify them when a set of factors has moved and are likely to lead to a mispricing.

Sub-Strategies:

Relative Value

Relative Value managers seek to reduce their directional exposures to asset classes and instead exploit spreads between related securities. These could include trades of bonds of the same tenure but issued by different governments or intra-curve trades, trading bonds issued by the same government but of different maturities. Equally, managers could look to capture spreads between different asset classes exposed to the same economic risks that they believe are priced differently.

Directional

Directional managers aim to have positions based on their broader assessment of the market. This requires a strong conviction and tends to come on the back of deep fundamental work to understand a multitude of potential drivers and risks. These managers tend to take longer term, structural type views and trade through noise to enhance risk/reward profiles.

Quantitative

Quantitative Macro managers use systematic processes to identify the same types of trades implemented by discretionary macro traders. These can be trend based, more like a CTA, based on factors such as momentum, carry or value, or arbitrage trades based more on price action.

Trade Example

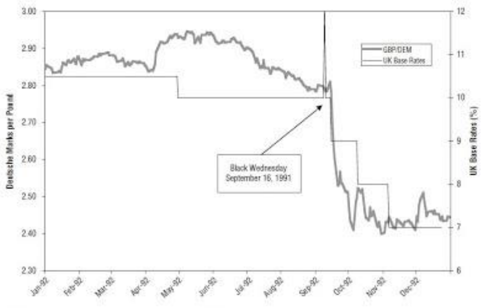


FIGURE 2.5 Sterling/Mark and UK Base Rates, 1992
Source: Bloomberg.

Source Bloomberg 1992

In this famous trade, George Soros correctly predicted that the Bank of England would be unable to maintain GBP inside the ERM, shorting the currency for a significant profit.

Key Risks

Choppy trends: managers tend to trade with momentum, if no trends establish themselves the can get whipped around.

Concentration: many managers employ concentrated positions, which increase risk.

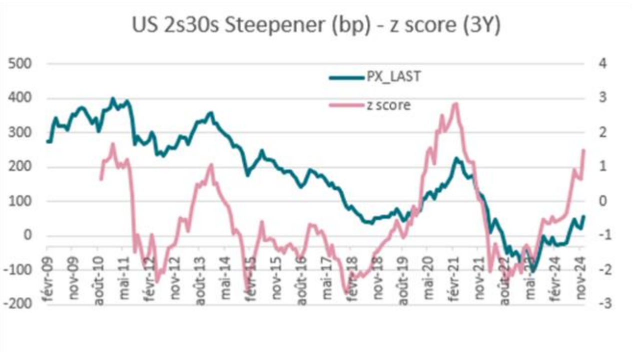
Stagnant policy: managers struggle without changes in macroeconomic conditions and policies in major global economies.

Hedge Fund Strategy Overview

Global Macro

Q4 Performance Drivers

- The HFRI Macro Total Index was up +0.8% in Q4 and +5.7% in 2024.
- Macro managers experienced significant dispersion over Q4 with markets digesting the likelihood and implication of a Trump win.
- US election trades proved very profitable and long USD positions were the main profit centre over Q4.
- In Rates, gains came from long EU rates at the front end driven by disinflation and lower growth expectations and curve steepeners in EU and US.
- EM proved more challenging. USD vs China was profitable but the massive 100bps hike in Brazil detracted from performance.
- Gains were generated in December on the back of a hawkish cut by the Fed. Long positions at the front end of the curve against 5Y and 10Y points performed strongly. Short equity positions performed well around the Fed meeting together with long USD against most major currencies.



Source Bloomberg data, AXA IM PRIME calculation 16/01/25

Outlook

- 2025 will see significant divergence in economic trends that should translate in numerous trade opportunities.
- Trump coming in power comes with potential tariff increases, a curb on immigration and potential fiscal policy changes through more tax cuts. The combination of reshoring, strong US growth and higher inflation could further boost US exceptionalism and few managers have risked shorting equities yet. Long dollar and steepeners are some of the favorite trades in the US.
- Europe is facing political crisis in France and Germany which will accelerate the divergence in economic fortunes. Short EUR against USD and JPY and long duration positions have been introduced as Europe could potentially face imported deflation from China.
- In Japan all indicators point to a continuation of higher inflation. This should translate into more rate hikes from the BOJ and provide a positive backdrop for the banking and consumer sectors further boosting equity markets.
- Emerging Markets have been challenging throughout 2024 with managers being burnt in Brazil. The Central Bank aggressive intervention in December has stabilized the currency near its lows and could provide significant value both in Rates and FX for when the fiscal situation stabilizes. China continues to rebalance its economy away from exports and towards investment and consumption. Any aggressive move on tariffs from the US could significantly weaken the currency which remains a short position.

Rating : Positive

Hedge Fund Strategy Overview
Managed Futures

Definition

Managed Futures funds, also known as Commodity Trading Advisors (CTAs), are a group of funds which employ a systematic, non-discretionary strategy to invest in liquid futures contracts. Strategies typically employ leverage as they invest in unfunded instruments.

The signals used in the strategies are predominantly based on momentum or trend following strategies using techniques such as weighted moving averages and Relative Strength Indicators. This strategy can take either long or short positions in a particular market and there is no inherent long or short bias.

CTAs usually invest across a broad range of markets such as Equities, Fixed Income, Commodities and FX in order to benefit from diversification. Strategies are spread across markets as well as time-frames i.e. they employ signals which can have a horizon ranging from intraday to several months.

Sub-Strategies

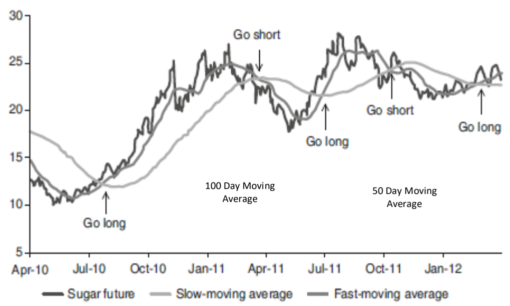
Trend Following
Mathematical models identify patterns or trends in market movements and take positions on the assumption that these trends will continue. Based on historical data, a set of criteria will be established and, once met, a position will be taken. When the criteria cease to be met, the position is closed and the information fed into the model is updated.

Moving Averages
When the short-term moving average or price of a contract crosses the bounds of a longer- term one, it can trigger a buy or sell signal. Not only does this technique identify current trends but it can construct an entry/exit strategy.

Trend Reversal
These funds look to benefit from inflection points in price trends. They tend to be shorter-term and take positions once a reversion has begun to gather momentum.

Contrarian:
Funds applying this strategy seek to identify the inflection points themselves, aiming to buy at the trough and sell at the peak. They are often betting against immediate market sentiment in order to capture the greatest difference and maintain tight stop losses.

Trade Example



Source AXA IM PRIME illustration 01/07/24

In this example, signals to buy are trigerred when the 50 day moving average price cuts the 100 day moving average from below, indicating positive price momentum. A sell signal is activated when the opposite is true.

Key Risks

Volatile Markets: If trends struggle to gain traction in markets that are frequently reverting, funds can get caught offside

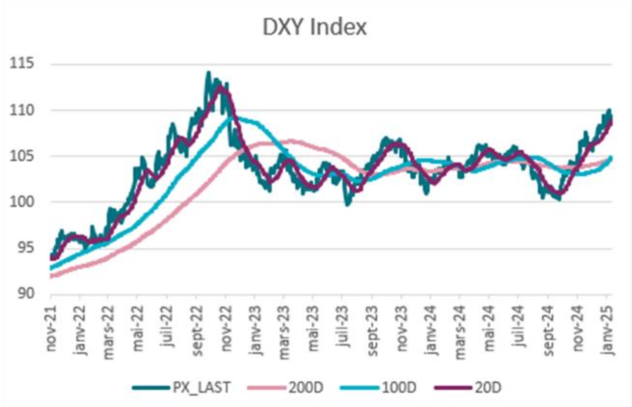
Flat Markets: Without significant enough trends for a fund to catch onto or position themselves against, CTAs will have a limited number of opportunities. In such a case, short positions can generate losses from cost of carry factors.

Crowding: Positions can get crowded by similar market participants, which can amplify reversals.

Hedge Fund Strategy Overview
Managed Futures

Q4 Performance Drivers

- The HFRI Macro Systematic Diversified was up +0.1% in Q4 and +4.1% in 2024.
- Trend following was up +0.2% in Q4 but got whipsawed throughout the quarter.
- October started with a loss on the back of a potential Trump win and inflationary pressures leading to a rally in longer term Rates and the Dollar (both long positions). Equities also mean reverted towards month end (long positions). The strategy benefited marginally from commodities, with short Natural Gas and long Gold positions.
- Post US elections, equities and dollar rallied. Net long positioning across equities along with long dollar positioning across currency pairs contributed positively. After an initial rise, Rates normalized over the month with net long duration exposure leading gains. Commodities contributed negatively, driven by the rise in Nat Gas prices.
- December performance was driven by the sticky inflation outlook along with the hawkish remarks by the FED around the potential for a longer rate cutting cycle that anticipated, leading to equities underperforming while US 10y yields increased. CTA fund lost on both having been long equities and short Rates. CTAs also lost in the significant reversal in energy prices which started to rise. On the positive side the comments from FOMC led to the Dollar continuing its rising streak over Q4 24.



Source Bloomberg data, AXA IM PRIME calculation 16/01/25

Outlook

- 2024 has been marked by the strong outperformance of long term trend following strategies while short term CTAs got whipsawed in Rates and Commodities.
- Current signals indicate:

  Equities: bullish US, Japan & EU, neutral UK & Small caps, bearish Latam & Kospi

  Rates: bearish most markets, bullish Korea

  Credit: bullish across the board

  Currencies: bullish USD & EMEA FX, bearish G10 FX, especially Commo FX

  Commodities: bullish Precious & Energy, bearish Industrials & Aggs. Managers switched aggressively to long positions on Energy after the December reversal.
- Most CTAs now employ a mix of Trend and Non-Trend strategies. The addition of strategies across Carry, Seasonality, Curve Trades and Mean Reverting strategies have the potential to diversify risk in the absence of trending markets.

Rating : Neutral

Hedge Fund Strategy Overview
Fixed Income Arbitrage

Definition

Fixed Income Arbitrage funds aim to exploit perceived mispricing amongst and between fixed income instruments and their derivatives. Often, opportunities for these relative value strategies are the result of capturing temporary anomalies in price relationships between fixed income instruments while keeping an overall market neutral exposure. This strategy typically requires large amounts of leverage in order to exploit these small pricing discrepancies.

Opportunities for Fixed Income Arbitrage trades can arise for both fundamental and technical reasons. Many investors prefer unfunded products, such as futures, as part of their hedging strategies, which can cause dislocations versus the underlying cash market, especially during times of market stress. At these times investors prefer futures due to better liquidity and lower funding costs/balance sheet impact as witnessed during the 2008/9 period.

Technical reasons that can generate opportunities for Fixed Income Arbitrage investments can be large amounts of issuance of Fixed Rate Bonds, which issuers want to swap back into floating, and can lead to potential tightening of swap spreads. Fundamental spreads exist between fixed income instruments related to the same underlying asset but with different durations or conditions, which can lead to an opportunity for those that can successfully model and hedge the risks.

Sub-strategies

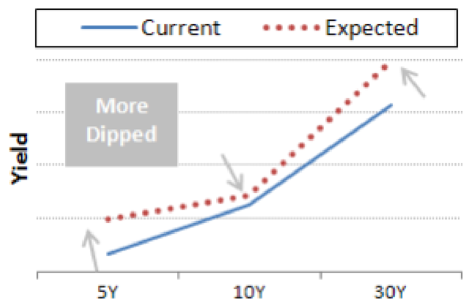
Yield Curve Arbitrage:
Funds seek arbitrage opportunities across different sections of a yield curve, i.e. where one section is overpriced relative to fundamental value and another is under-priced. Yield Curve steepeners/ flatteners/ butterflies are commonly used strategies in intra-curve arbitrage. In each case, the fund will take long and short positions where they believe the shape of the yield curve is likely to change.

Cash vs Futures Basis
In this case, funds aim to take advantage of the price discrepancies between a futures contract and the securities deliverable at expiry.

Issuance Driven Trades
Funds look to profit from distortions in the price of securities with very similar maturities based on their issuance. Predominantly this means trading the On-The-Run bond vs Off-The -Run bonds.

Swap Spread Trades:
Funds may take positions in both the fixed and floating sides of an interest rate swap with the intention of benefitting from predicted widening or tightening of the spread.

Trade Example



Source AXA IM PRIME illustration 01/07/24

The example above is a yield curve butterfly. The fund believes that the yield will increase in the 5 and 30Y sectors but decrease in the 10Y. As such they would go short the 5Y and 30Y securities (the wings) and long the 10Y (the belly).

Key Risks

Cost of Carry: Short positions in a fixed income security require the holder to pay the interest. In such a case, rising rates can make holding a short position very expensive.

Prepayment Risk: Within asset backed sub-strategies, an early return of principal means that future interest payments aren't paid to a fund.

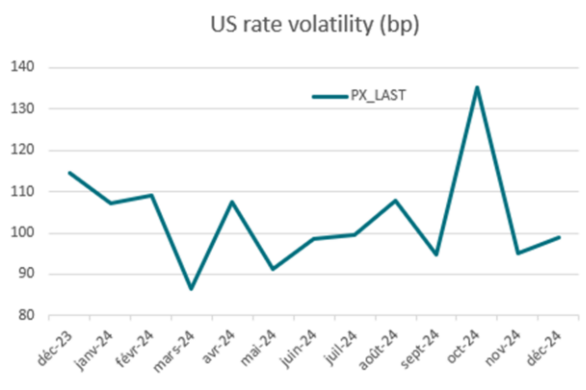
Liquidity and Borrowability: Given that fixed income funds tend to employ a lot of leverage, lack of available balance sheet makes borrowing more expensive.

Hedge Fund Strategy Overview
Fixed Income Arbitrage

Q4 Performance Drivers

- The HFRI Relative Value Fixed Income Sovereign Index finished the year up 9.7%.
- In the US the Trump election put bond volatility back on the agenda, as his proposed policies of higher tariffs, tax cuts and reduced immigration created an uncertain outlook. These potential actions could be inflationary, just as the Fed is looking to dovish positioning. The MOVE Index, a proxy for bond volatility, surged to 136 from 94 at the beginning of the quarter, only to drop to 82 by December.
- At the same time central banks outside of the US contended with increasing doubts that economic growth would continue, despite a backdrop of a lower rate environment. This situation, combined with increasing geopolitical uncertainty such as the collapse of Germany's governing coalition, increased borrowing costs in regions such as the United Kingdom. The decorrelation of productivity projections made for difficult bond auctions. Additionally the divergence of increased yields and cheapening currencies against the US Dollar created profits for funds who typically limited trades to rates.

Rates volatility picked up over Q4



Source: Bloomberg 16/01/25

Outlook

- Bond markets will be a moderate opportunity because of the uncertain crosscurrents of problems that need resolution:
- Lack of leadership in many large GDP countries, prospects of accelerating economies and structurally driven slowdowns, fluctuating currencies/inflation, bond buyers who are very reactive to weak fiscal policies and unusually extended American Exceptionalism
- Heavily scrutinized Trump inflationary policies on tariffs and immigration, matched with a target of maintaining the USD as the global reserve currency
- The diverging economic outlooks across various geographies will likely open investment opportunities on a global basis. On the one hand countries such as Japan and the US will be more hawkish versus 2024, others such as Europe will contend slowing growth.
- Stagflation scenario may occur where inflation remains above target and economic growth stalls, with outcomes exacerbated by the ability of governments to boost their economies.
- These differences will be a good environment for flexible and dynamic RV positions across regions; however central bank decision-making remains dependent on short-term data and can remain unpredictable. Additionally, bond issuance could be volatile as investors reflect their skepticism of government stability via bond pricing.
- Trading a steepening/flattening yield curve was a focus for 2024, and we expect the same conditions to exist in 2025. For example, spiking bond yields reflect concerns that fiscal spending will remain elevated, at the same time that Trump is planning tax cuts – so much so that Trump has been referred to as "the human steepener." Adding to the uncertainty is whether tariff proposals will have an impact on offsetting the tax-related drop in revenues.

Rating : Positive

Investment Managers

/ Prime

Hedge Fund Strategy Overview

Convertibles Arbitrage

Definition

Convertibles Arbitrage is a relative value strategy, focused on the relationship between a convertible bond and the underlying equity. The vanilla convertible arbitrage trade is going long the convertible bond and short the underlying stock, as to the upside, the positive convexity in the bond results in the gains exceeding losses on the short stock hedge, and the opposite applies in a downside scenario as the short stock position acts as a hedge against the long convertible position. Convertible Arbitrage managers seek to provide equity participation to the upside and principal protection to the downside, whilst monetizing convexity through market equity volatility and extracting alpha from special situations and events.

Convertible arbitrageurs will generally seek CBs that exhibit high equity volatility, low conversion premium, high gamma, high liquidity and that are trading cheap versus theoretical fair value. Returns are driven by carry (the income earned from the coupon on the CB), monetization of market equity volatility through gamma trading, and new issues, which typically trade cheaply to fundamental fair value.

CBs can behave as yield instruments (bond-like in nature, sensitive to credit spreads), total return instruments (moderate yields, balanced with relatively high gamma which enables dynamic hedging of the underlying stock) and equity alternatives (high theoretical deltas, low yields – these are in the money and equity-like in nature)

Sub-strategies

Synthetic Put Options:

The convertible is trading close to its parity value (the value of the underlying shares if investors convert). The conversion option is in the money and the conversion premium is low – this is a high delta, equity-like trade. By going long the convertible bond and short the underlying equity, you can generate P&L in a significant equity sell-off as the returns on the short stock position will exceed losses on the convertible (these losses will be capped as the bond can be sold 'put' at the bond floor).

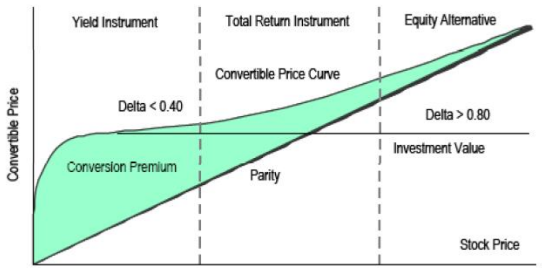
Balanced Arbitrage

The vanilla convertible arbitrage trade. The option embedded in the convertible bond is close to its strike price, so gamma (how much the option delta changes for a given change in the underlying equity) is at its maximum. This is a long volatility position, generating P&L via gamma trading.

New Issuance Driven Trades

Funds look to profit from new issues trading cheaply to theoretical fair value, as these convertibles typically quickly revert (richen) to theoretical fair value, providing opportunity for P&L generation through holding the position over a short period.

Convertible Bond Profile



Source AXA IM PRIME illustration 01/07/24

Convertible bonds are bonds yielding regular coupon payments but can be converted into a pre-determined number of common shares at certain times over the life of the bond, usually at the discretion of the bondholder.

Key Risks

Credit: Given much of the market is non-rated, valuations may be impacted by a flight to quality.

Interest Rates: Convertibles could underperform in a rising rate environment.

Market stagnation: If volatility is suppressed and the new issuance calendar is sparse, generating returns could prove challenging.

Hedge Fund Strategy Overview
Convertibles Arbitrage

Q4 Performance Drivers

- Performance continued its positive run through Q4 boosted by rising equities and credit grinding ever tighter. Equity vol notched up one point but there were sharp rises in interest rates which tested hedges, with the US 10-year 79bps higher on the quarter.
- The HFRI RV Fixed Income Convertible Arbitrage Index returned +1.6% for the quarter, bringing it to +11.1% YTD.
- The Barclays Global Converts Hedged TR index (long-only, currency hedged) gained +2.3% over the same period bringing it to +11.3% YTD.
- The big driver of returns in 2024 has been new issues, with hedge funds profiting both from the discount on issue as well as the retiring bond being taken out at a premium.
- Issuance surged to $42bn in Q4, up from $25bn in Q3. 2024 saw a total of $128bn raised, up 42% from the $90bn in 2023. Asia saw the biggest pickup with a +170% increase, driven by AI capex needs. In contrast Europe shrank by 50% and was one of the weaker spots.
- The positive dynamics pushed valuations higher across regions, with Japan joining the US in the slightly rich category, while Europe and Asia ex-Japan moved closer to fair value.

Convertible Valuations

Source: Jefferies 16/01/25

Outlook

- The convertibles market witnessed a resurgence in 2024 with tailwinds coming from rallying equities, tightening credit, bouts of volatility and strong trading volumes.
- The rally in credit was most pronounced in the weakest credits, driving returns, but reducing the opportunity set in stressed names as sub-Investment Grade paper tightened during the year.
- We now expect volatility and gamma trading to be the key driver of returns. Hedge fund participation has increased and now represents more than 60% of market ownership, driving trading volumes to new peaks and opening up the opportunity set.
- Issuance, in many cases linked to the exchange of a maturing HY bond or convert, also remains a theme coming into 2025, and we expect the trend of corporations looking to the CB market as a cheaper alternative to HY to continue.
- Sectors likely to see increased activity include Healthcare (US), AI/Semis (Asia) and Travel (airlines, lodging). Crypto has been a surprise component of performance helped by the Trump rally.
- An anticipated increase in Merger activity should add to performance, either through take-outs of existing bonds a deal or leading to new issues to fund acquisitions.

Rating : Positive

Investment Managers

Prime

Hedge Fund Strategy Overview

Credit/Distressed

Definition

Credit Managers look to profit by investing in debt or debt-like instruments related to individual companies, employing some combination of directional, relative value and arbitrage strategies.

The corporate credit space is delineated through structure and rating: from Investment Grade to High Yield and Junk. Additionally, there are various structures that managers can utilize, from plain vanilla bonds through to CoCos and CLOs. Managers can specialize in one area or move actively across different strategies. These complexities can make it difficult for non-specialists to correctly understand and value individual instruments, creating investment opportunities.

Net exposure amongst managers can vary considerably, with some managers looking to strip out market direction via active shorting or arbitrage plays, whilst other managers are more focused on carry and value opportunities. Typically, a manager will take a view on a bond based on a fundamental approach that identifies mispricing, for example if earnings or debt repayments are ahead/behind schedule.

Sub-Strategies:

Credit Long Short

Managers look to build portfolios of long and short corporate credit positions based on their opinion of the fundamentals of the company and their analysis of their ability to repay their bonds. Shorts may take the form of alpha generative trades or be more pure hedges to strip out market beta

Credit Relative Value

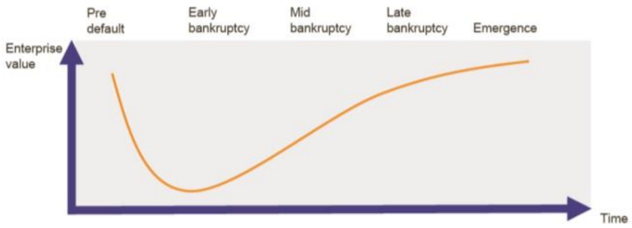
Managers look to capture the relative mispricing between two credit instruments. Trades can be expressed by going long or short cash vs synthetic bonds, senior vs subordinated debt, debt vs equity and term structure.

Distressed

Distressed debt investing involves looking at companies which are in distress or already defaulted and whose debt is trading at severely impaired level. This involves taking a view on the recovery value of the debt through a detailed understanding of the capital structure and enterprise value of the company after the restructuring process.

Later, in in the early to mid-bankruptcy stages, the fund may purchase bonds they view as cheap. In the late-emergence stages, the fund could substitute their loans for either, or a combination of, new bonds or post-reorganization equities in the restructured firm.

Trade Example



Source AXA IM PRIME illustration 01/07/24

This graph shows a typical distressed cycle for a company undergoing bankruptcy and then recovering. Managers can enter and exit the trade at various times based on their analysis of the likelihood of recovery.

Key Risks

Credit risk: This is the risk of borrower default and failing to make the required repayments. This can lead to the loss of both the principal and the intermediate coupon payments.

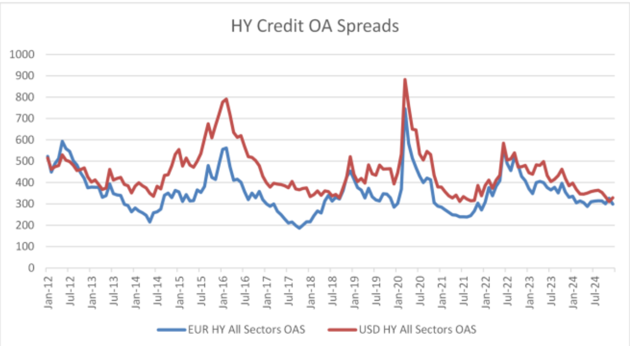
Cyclical factors: Depending on the stage of the business cycle, firms may struggle repaying creditors as a result of decreased demand.

Liquidity Risk: Bonds can become illiquid in stressed markets.

Hedge Fund Strategy Overview
Credit/Distressed

Q4 Performance Drivers

- Credit was positive over the quarter but experienced cross-currents, with the US out-performing Europe in spreads and vice versa in rates. Credit volatility was stable with VIXIG flat at 28, and VIXHY +9 at 141.
- The nomination of Donald Trump for a second term, saw US CCC paper rally -118bps on the quarter making it one of the best performing assets of 2024. Europe initially saw a similar move but political turmoil in France and Germany caused a late sell off and CCCs tightened -62bps.
- The 5-year US Treasury yield meanwhile sold-off +82bps, reversing Q3 and offsetting Q4 spread gains in the US.
- The Barclays US Corporate HY index rose +0.2% for the quarter to end +8.2% YTD; Europe was +2.0% (+9.1%YTD). The CS Leveraged Loan Index, (mainly floating rate) rose +2.3% over the same period, leaving it up +9.1% YTD.
- The HFRI RV: Fixed Income-Corporate Index gained +1.5% for the quarter, taking it to +9.7% YTD. The HFRI ED: Distressed / Restructuring Index rose +1.9% over the same period leaving it +10.5% YTD)
- Carry remains an attractive component of returns with all-in yields on High Yield bonds in the US moving up from 6.84% to 7.49%. in Europe HY yields fell from 6.21% to 5.83%. Levered Loan yields rose to 8.8%.



Source: Bloomberg data, AXA IM PRIME calculation 16/01/25

Outlook

- Credit is now priced near perfection with IG and HY spreads at cyclical tights. This reflects positive economic headlines in the US, with full employment, moderate inflation and robust growth.
- The inauguration of Donald Trump to the White House has added to the positive outlook, reflected in the sharp moves higher in US rates as well as the snap-back in CCC spreads.
- The rise in all-in yields means that HY credit still offers a higher yield (7.5%) compared to the implied earnings yield on US stocks (3.5%). Carry is most pronounced in Levered Loans, which offer 8.8%.
- Key questions now are, how much of the good news is in the price? And where are we in relation to the top of the cycle. In the near-term we expect the new administration to ignite the economy, but there is little room for mistakes at these levels.
- It is worth noting that Leverage Loan defaults (incl distressed exchanges) have risen to a 4-year high, and US corporate bankruptcies and credit card defaults hit their highest levels since 2010, so there are signs of weakness at the margin.
- In structured credit we continue to like CMBS, where ongoing stress is expected to extend for 1-2 years. Tighter conditions have allowed higher quality assets to refi leading to a wave of SASB issuance with AAAs yielding S+600bps.
- US Agency mortgages also remain one of the areas of better value with basis roughly unchanged during 2024 and offering opportunities to pick up carry and trade the ranges. Mortgage derivatives offer an attractive way to gain exposure with returns in the low teens available with limited leverage.

Rating : Neutral

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AXA IM Prime: January 2025

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