Polar Capital
Global Convertible Team
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Will convertibles continue to outperform?

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Convertibles have outperformed other asset classes over the last year. Below we examine why this has been the case and if the drivers of this outperformance will remain in place for the next 12 months

Over the past 12 months, most risk markets have performed well, as detailed in the table below. Of note is that the larger-cap equity indices (MSCI World; S&P 500) have outperformed smaller caps (Russell 2000) and that high-yield bonds have outperformed investment-grade bonds. However, what is less broadly discussed is that the **Refinitiv Global Focus Convertible Bond Index has outperformed all of them.** Moreover, the Polar Capital Global Convertible Fund has outperformed that benchmark by 132bp.

Asset class performance: 12 months to end May 2025 (US$)

MSCI World Total Return Index	13.7%
S&P 500 Total Return Index	13.5%
Russell 2000 Total Return Index	1.2%
Bloomberg Investment Grade Bond Index	7.0%
Bloomberg Global High Yield Bond Index	10.9%
Refinitiv Global Focus Convertible Bond Index	14.6%
Polar Capital Global Convertible Fund	15.9%

Source: Polar Capital, Bloomberg, as at 30 May 2025. USD I Acc Share Class.

We believe there have been four principal drivers of Convertible outperformance over the past year. Overleaf we discuss if these drivers will remain in place going forward.

Awards & ratings

We believe there have been four principal drivers of Convertible outperformance over the past year.

> Converts have outperformed large and small-cap equities as well as investment grade and high yield bonds

1. Equity markets

AI infrastructure spend and growth

Spending on AI infrastructure has grown materially over the past year with capital expenditure running at unprecedented levels. McKinsey estimates there will be a capex spend of over $5trn between now and 2030 directly related to AI data centres. Simply put, this is one of the most resource and investment-intensive technological revolutions in human history. The convertible universe includes many companies directly benefitting from this investment and capex expenditure.

Strong US earnings and guidance

Despite macroeconomic noise, corporate earnings continue to exceed market expectations. According to FactSet, with essentially all S&P 500 companies having reported Q1 earnings, 78% beat EPS estimates, with an expected 2025 earnings growth rate of 9.1%. Macroeconomic indicators have also improved, making for a fertile environment for the many high-growth companies in the convertible universe.

European defence spending

Impacted by the Russia/Ukraine war and geopolitical uncertainty related to US/NATO relations, anticipated defence spending in the Eurozone will likely balloon in the years ahead. Per the Stockholm International Peace Research Institute, European military spending rose 17% y/y in 2024 alone, the highest since the end of the Cold War. While the convertible universe has limited direct exposure, the fiscal impact will extend beyond the immediate sector.

2. Credit markets

Low leverage

Corporate leverage remains low. According to the US Federal Reserve, Q1 2025 saw the lowest Q1 debt as a percentage of equity market value in recorded history (19%).

Strong cashflows

According to the US Bureau of Economic Analysis, Q1 2025's corporate net cash flows were the highest Q1 on record, increasing 6.1% y/y from 2024.

Refinancing of legacy Covid-era debt

Many companies have successfully refinanced legacy Covid-era debt at manageable rates, reducing near-term refinancing risk and improving maturity profiles.

This financial discipline, combined with continued demand from yield-seeking investors, has provided a strong and stable backdrop for credit markets, contributing to tighter spreads and positive total returns across the asset class. Convertibles have benefitted from these credit trends and are expected to continue to do so.

3. Equity market volatility

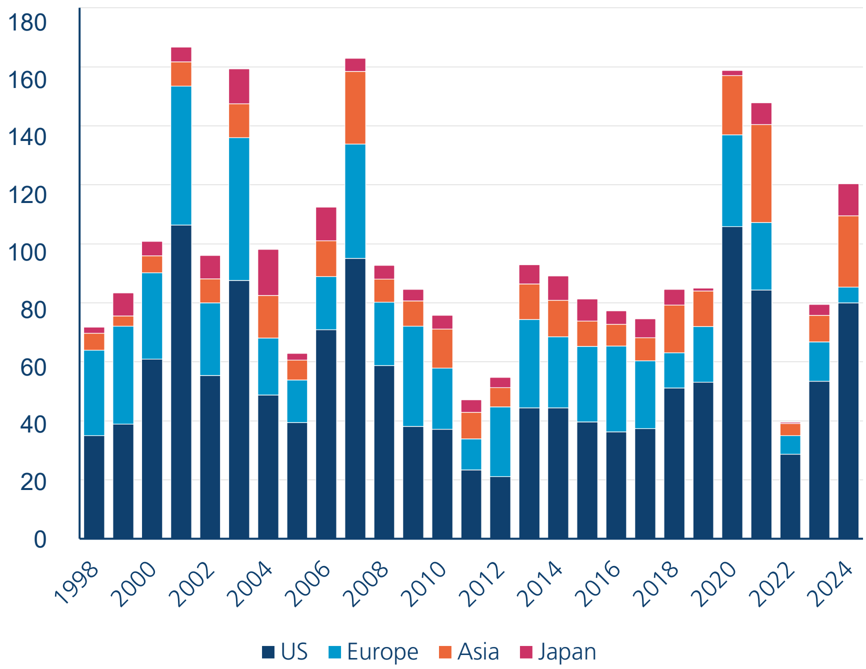
Convertible valuations have benefitted from ongoing equity market volatility over the past 12 months, driven by geopolitical tensions in Europe and the Middle East, renewed trade friction between the US and China and uncertainty surrounding elections across the globe. The latter includes the divisive US political backdrop, the rise of the populist right in France and Germany, the impeachment of the President of South Korea and the surprise ascent of Shigeru Ishiba in Japan's Liberal Democratic Party to become the country's prime minister.

4. Convertible issuance

As we have written about previously, we believed the convertible primary market was set for an acceleration of issuance driven by higher interest rates and companies looking to refinance Covid-era debt both in the high yield and convertible markets. This proved to be the case, with $119bn of convertible debt issued in 2024. We believe the same drivers remain in place for a similar quantum of issuance in 2025.

> We expect significant convertible issuance from a wide variety of issuers in 2025

Global Convertible issuance



Source: Bank of America Merrill Lynch. Date: 31 December 2024.

Outlook

Looking ahead, we believe the backdrop remains robust for convertibles to continue to outperform.

Within equities, we believe valuations may remain supported by a favourable macroeconomic backdrop. Inflation appears to be under control, giving central banks greater flexibility and reducing pressure on interest rates. Solid employment data points to continued consumer strength, while corporate earnings growth remains healthy across key sectors. The risk of a near-term recession has notably diminished, helping sustain investor confidence. Additionally, the easing of tensions and a reduced threat of an all-out trade war between the US and China has alleviated one of the major drivers of a potential sharp decline in risk assets, potentially creating a constructive environment for equity market performance.

The above factors, combined with manageable refinancing conditions, strong corporate balance sheets and cashflow generation equally provides a potentially constructive backdrop for credit markets.

> We believe the outlook for convertibles remains very positive and continue to believe the asset class offers a very real prospect of further outperformance

However, despite the above robust outlook, we do not believe the path forward will necessarily be a straight one. Equity volatility has been evident over the past year, from the August 2024 Japanese rate hike-induced selloff to the end of 2024's US election-driven boost to April's 2025 Liberation Day-related turbulence. With foreign policy (US/China tensions; US/EU tariff cliff in July; Russia/Ukraine; and most recently the escalating Iran-Israel conflict) remaining at the forefront of investors minds, we believe markets will remain volatile with increased periods of heightend uncertainty.

So, will convertibles continue to outperform? We believe convertibles will continue to benefit from a meaningful tailwind of heightened market volatility for the remainder of 2025. We believe company balance sheets are in good shape and will likely continue to be so given the robust earnings outlook and corporate cash flow generation. However, we are more cautious in our outlook for equities given on-going market strength but recognise the three tailwinds discussed above (AI spend, strong US earnings growth and increased European defence spending) remain in place. Finally, we are certain in our view that convertible issuance will remain robust through the remainder of 2025 and so generate many excellent trading and investment opportunities. So, will convertibles continue to outperform? We believe the outlook for convertibles remains very positive and continue to believe the asset class offers a very real prospect of further outperformance.

Polar Capital Global Convertible Team

19 June 2025

The team at Polar Capital manages two convertible funds, each with different objectives and risk profiles.

Polar Capital Global Convertible Fund

- This is a long-only convertible fund seeking to generate capital appreciation through investing in the global convertible markets, together with income generation and capital protection
- The Fund was established in 2013 and is still managed by the original founding portfolio managers
- Top quartile performance since inception[1]
- The Fund has delivered more upside and participated in less downside than its benchmark
- Additionally, the Fund has delivered superior income compared to its benchmark
- **12-month Fund return 15.92%[2]**

Growth	Income	Protection
Target asymmetric, convex returns Identify clear upside catalysts Invest only when risk-adjusted returns are attractive	Target 6% Distribution Yield[3] Seek income without over-reaching Invest globally; geography and benchmark agnostic	Clear focus on limiting drawdowns Macro level: robust portfolio stress testing Micro level: detailed fundamental credit analysis

Polar Capital Global Absolute Return Fund

- This is an absolute return-seeking fund, targeting returns of c6-10% with volatility of returns of c6%
- The Fund was established in 2018 and is still managed by the original founding portfolio managers based in London and Connecticut
- The Fund has never had a loss-making year and builds upon the track record of the ALVA Convertible Arbitrage fund managed by the same team
- Taken together, the Absolute Return and ALVA funds have an enviable 10-year track record of generating excellent risk-adjusted returns, **while never suffering any loss-making years**
- **12-month Fund return 10.31%[2]**

Growth	Income	Protection
Return target 6-10% Volatility target 6% Identify clear return catalysts and target asymmetric returns	Target 5% Distribution Yield[3] Buffer created to smooth distributions	Clear fous on limiting drawdowns Low levels of correlation with other asset classes Low Equity exposure

1. Source: Lipper Global: Bond Convertibles - Global; USD I Acc Share Class; as at 30 May 2025.

2. Polar Capital, as at 30 May 2025. USD I Acc Share Class.

3. Please note that this is the target yield as of 30 May 2025, it is not a guaranteed yield and it is subject to change in the future.

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POLAR CAPITAL

Risks

- **Capital is at risk and there is no guarantee the Fund will achieve its objective. Investors should make sure their attitude towards risk is aligned with the risk profile of the Fund before investing.**
- **Past performance is not a reliable guide to future performance. The value of investments may go down as well as up and you might get back less than you originally invested as there is no guarantee in place.**
- The value of a fund's assets may be affected by uncertainties such as international political developments, market sentiment, economic conditions, changes in government policies, restrictions on foreign investment and currency repatriation, currency fluctuations and other developments in the laws and regulations of countries in which investment may be made. Please see the Fund's Prospectus for details of all risks.
- The Fund invests in equities, convertible and fixed income securities and prices can rise or fall due to several factors affecting global stock markets.
- The Fund uses derivatives which carry the risk of reduced liquidity, substantial loss and increased volatility in adverse market conditions, such as failure amongst market participants. The use of derivatives will result in the Fund being leveraged (where market exposure and the potential for loss exceeds the amount the Fund has invested) and in these market conditions the effect of leverage will magnify losses. The Fund makes extensive use of derivatives.
- The Fund invests in assets denominated in currencies other than the Fund's base currency. Changes in exchange rates may have a negative impact on the Fund's investments. If the share class currency is different from the currency of the country in which you reside, exchange rate fluctuations may affect your returns when converted into your local currency. Hedged share classes may have associated costs which may impact the performance of your investment.
- There may be times where the issuer or guarantor of a fixed income (or convertible) security cannot meet its payment obligations or has their credit rating downgraded, resulting in potential losses for the Fund.
- The Fund invests in emerging markets where there is a greater risk of volatility due to political and economic uncertainties, restrictions on foreign investment, currency repatriation and currency fluctuations. Developing markets are typically less liquid which may result in large price movements to the Fund.

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The Fund promotes, among other characteristics, environmental or social characteristics and is classified as an Article 8 fund under the EU's Sustainable Finance Disclosure Regulation (SFDR). For more information, please see the Prospectus and relevant Fund Supplement.

ESG and sustainability characteristics are further detailed on the investment manager's website: - https://www.polarcapital.co.uk/ESG-and-Sustainability/Responsible-Investing/.

A summary of investor rights associated with investment in the Fund can be found here.

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Benchmark: Polar Capital Global Convertible Bond Fund The Fund is actively managed and uses the Refinitiv Global Focus Convertible Bond Index as a performance target and to calculate the performance fee. The benchmark has been chosen as it is generally considered to be representative of the investment universe in which the Fund invests. The performance of the Fund is likely to differ from the performance of the benchmark as the holdings, weightings and asset allocation will be different. Investors should carefully consider these differences when making comparisons. Further information about the benchmark can be found here. The benchmark is provided by an administrator on the European Securities and Markets Authority (ESMA) register of benchmarks which includes details of all authorised, registered, recognised and endorsed EU and third country benchmark administrators together with their national competent authorities.

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