JPMorgan Global Convertibles Income Fund

Continuity of approach under new team head

Investment companies

JPMorgan Global Convertibles Income Fund (JGCI) is managed by the convertible bonds team at J.P. Morgan Asset Management (JPMAM), now led by Natalia Bucci following the departure of Antony Vallée in February 2018. Bucci and other members of the team have worked together for many years, and stress the continuity of a process that has been developed collaboratively over time, based on in-depth fundamental security analysis. The portfolio management team has been bolstered with the addition of Paul Levene, who joined JPMAM in 2015. JGCI continues to achieve its target yield of 4.5% and NAV progression has been broadly steady, with the share price having risen by a greater margin over 12 months, following the introduction of a discount management policy in May 2017. The team remains positive on the outlook for the global economy, which supports exposure to more equity-sensitive areas of the convertible bond market.

12 months ending	Share price (%)	NAV (%)	Barclays Global Credit Rate Sensitive (%)	MSCI World (%)	FTSE All-Share (%)
31/05/15	(0.8)	0.5	1.6	16.8	7.5
31/05/16	(8.0)	(1.5)	(3.1)	1.3	(6.3)
31/05/17	14.2	9.2	11.4	32.0	24.5
31/05/18	0.5	1.4	1.3	8.8	6.5

Source: Thomson Datastream. Note: All % on a total return basis in GBP. Inception date is 11 June 2013.

Investment strategy: More flexible approach

JGCI invests mainly within the bond-like and balanced areas of the convertible bond market, with an increased focus on the balanced segment since the team was given the flexibility to take a more total return approach to meeting the fund's 4.5% dividend yield target. Security selection is bottom-up, supported by JPMAM's team of convertible bond analysts, but the process also takes account of top-down factors such as industry fundamentals, the global economy and interest rates. The c 90-name portfolio is diversified by geography, industry, issuer size and credit quality.

Market outlook: More volatile conditions

Having experienced a period of historically low volatility in 2017, global equity markets have been less stable so far in 2018, beset by worries such as the risk of a global trade war, military action in the Middle East and the withdrawal of central bank liquidity. Bond markets also face risks from rising interest rates, and historically tight spreads on high-yield credit leave little room for manoeuvre. However, the macroeconomic backdrop remains relatively benign, which could support risk assets.

Valuation: Discount below medium-term average

At 1 June 2018, JGCI's shares traded at a 2.8% discount to cum-income NAV. This was narrower than the 4.7% average discount over three years but wider than the averages over one year and since launch in June 2013 (2.2% and 1.7% respectively). JGCI's discount widened amid heightened volatility and risk-aversion in 2016, leading to the introduction in May 2017 of a discount management policy aiming to limit the discount to 2% in normal market conditions.

6 June 2018

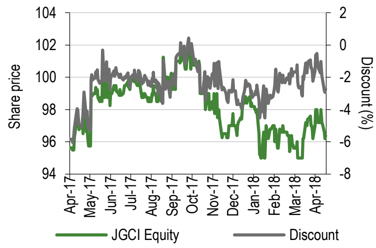
Price	**95.2p**
Market cap	**£146.7m**
AUM	**£165.9m**

NAV*	97.9p
Discount to NAV	2.8%

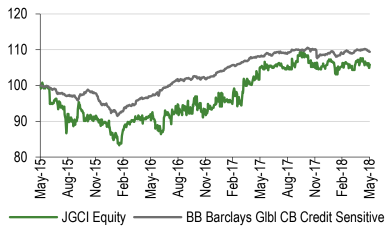
*Including income. As at 1 June 2018.

Yield	4.7%
Ordinary shares in issue	154.0m
Code	JGCI
Primary exchange	LSE
AIC sector	Sector specialist: Debt
Benchmark	Bloomberg Barclays Global Convertibles Credit Rate Sensitive

Share price/discount performance



Three-year performance vs index



52-week high/low	101.8p	94.4p
NAV** high/low	102.7p	97.2p

**Including income.

Gearing

Gross*	1.0%
Net*	2.1%

*As at 1 June 2018.

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Edison profile page

JPMorgan Global Convertibles Income Fund is a research client of Edison Investment Research Limited

Exhibit 1: Company at a glance

Investment objective and fund background

JPMorgan Global Convertibles Income Fund (JGCI) aims to provide investors with a dividend income, combined with the potential for long-term capital growth, from investing in a globally diversified portfolio of convertible securities. The dedicated convertibles team at J.P. Morgan Asset Management (JPMAM) follows a well-developed process that combines equity and credit selection techniques. Capital and income currency exposures are hedged.

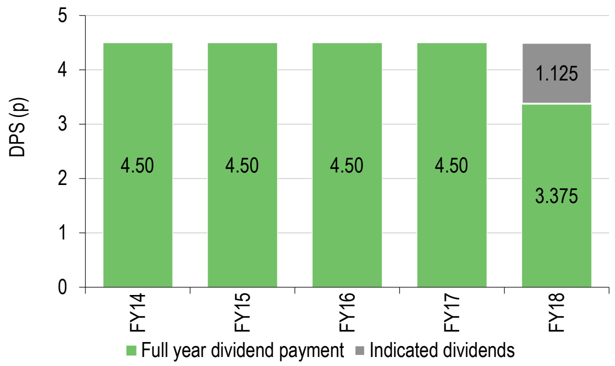
Recent developments

- 15 May 2018: Robin Dunmall, a member of the portfolio management team, to leave JPMAM to pursue other opportunities.
- 30 April 2018: Third interim dividend of 1.125p announced for the year ending 30 June 2018, to be paid on 19 June.
- 22 February 2018: Second interim dividend of 1.125p announced for the year ending 30 June 2018, to be paid on 29 March.
- 15 February 2018: Fund manager Antony Vallée to leave JPMAM. Analyst Paul Levene becomes a named fund manager alongside Natalia Bucci.

Forthcoming		Capital structure		Fund details	
AGM	November 2018	Ongoing charges	0.99%	Group	J.P. Morgan Asset Management
Annual results	October 2018	Net gearing	2.1% (1 June 2018)	Manager	Team-managed
Year end	30 June	Annual mgmt fee	0.75%	Address	60 Victoria Embankment, London EC4A 0JP
Dividend paid	Quarterly	Performance fee	None		
Launch date	11 June 2013	Company life	Indefinite	Phone	+44 (0)20 7742 9995
Continuation vote	Three-yearly, next 2018	Loan facilities	$32m multi-currency	Website	www.jpmconvertiblesincome.co.uk

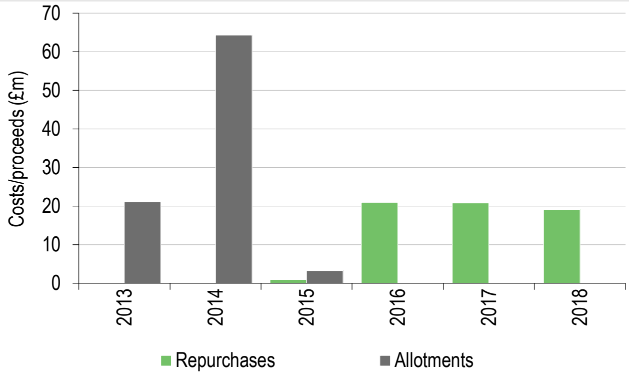
Dividend policy and history (financial years)

In the first year, dividends were paid half-yearly, but moved to quarterly thereafter. The launch target for a gross dividend of 4.5% of the issue price (100p) has been delivered in the first four financial years and is on track to be matched in FY18.

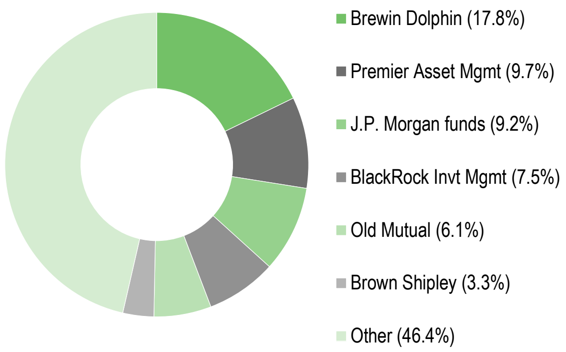


Share buyback policy and history (calendar years)

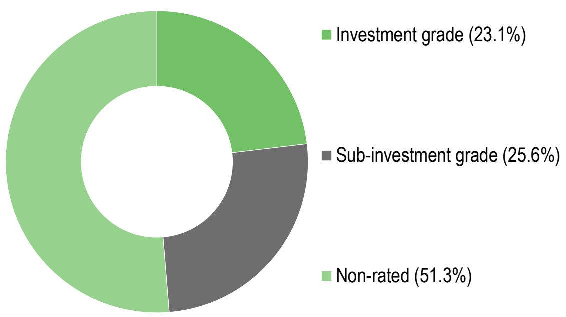
JGCI may buy back up to 14.99% of its issued share capital annually and new shares may be issued under a placing programme. A discount control policy introduced in May 2017 targets a maximum discount of 2% in normal market conditions.



Shareholder base (as at 9 March 2018)



Portfolio breakdown by official credit quality (as at 30 April 2018)



Portfolio characteristics (as at 30 April 2018)

Portfolio yield to best (31/12/17)*	4.3%
Equity sensitivity (delta)	32.4%
Duration (to put)	3.0 years
Number of securities	91
Available cash	0.9%
Bond quality (JPMAM assessment 31 December 2017, includes gearing)	
Internally rated high yield	40%
Officially rated high yield	23%
Officially rated investment grade	17%
Internally rated investment grade	17%

Top 10 holdings (%, as at 31 March 2018)

Issuer	**% of portfolio**
Aabar Investments Fixed 0.5%	4.4
Helical Bar Fixed 4%	2.4
TPK Holding Zero Coupon	2.2
Finisar Call/Put Fixed 0.5%	2.2
St Modwen Properties Fixed 2.875%	2.2
Zhen Ding Technology Putable Zero Coupon	2.2
Remgro Jersey Fixed 2.625%	2.1
J Sainsbury Fixed 1.25%	2.1
OUE Ltd Putable Fixed 3%	2.1
Capitaland Putable Fixed 1.95%	2.1
Top 10 (% of portfolio)	**23.8**

Source: JPMorgan Global Convertibles Income, Edison Investment Research, Bloomberg, Morningstar. Note: *Yield to best: highest yield for each bond with all future put dates treated as possible maturity dates and a yield-to-maturity calculation performed for each date.

Fund profile: UK's only closed-end convertibles fund

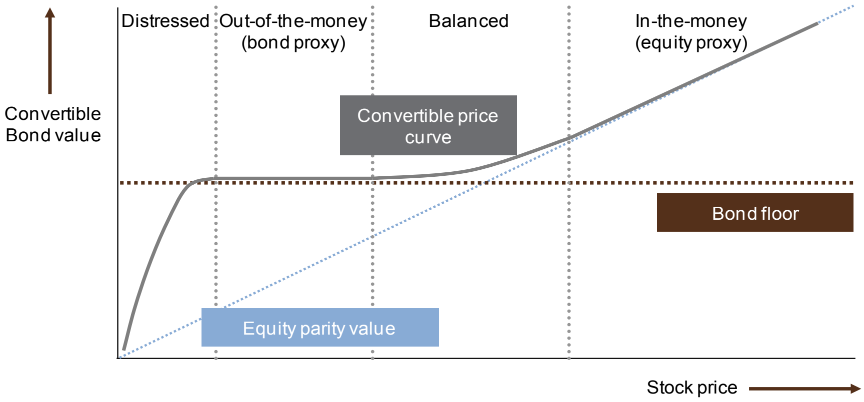
Incorporated in Guernsey and launched in June 2013, JPMorgan Global Convertibles Income Fund is the only London-listed, closed-end investment company specialising in convertible bonds. It is managed by the experienced convertible bonds team at J.P. Morgan Asset Management, now headed by Natalia Bucci following the departure of Antony Vallée in February 2018. The day-to-day management team now comprises Bucci and Paul Levene; a third portfolio manager, Robin Dunmall, left JPMAM in May 2018. Specialist analysts provide global coverage across industry sectors, and the team also has its own dedicated trading desk.

While JGCI's principal aim remains to pay a regular quarterly income (targeting a yield of c 4.5% pa), since late 2015 it has had more flexibility to invest for total return, which has resulted at times in more exposure to balanced convertibles (see below). Gearing is deployed tactically and has broadly ranged between c 6% net cash and c 9% geared in the past 12 months. A new discount control policy introduced in 2017 has helped limit volatility in the share price.

Background to convertible bond investment

Convertible bonds combine the characteristics of a corporate bond with an embedded option allowing them to be converted into the underlying equity at a preset rate or a particular date, normally at a premium to the price of the equity at the time the bond is issued. Like bonds, they can be redeemed at par value at maturity (if they are not converted), and they typically pay a fixed coupon. At issue, the yield on a convertible is generally lower than on a conventional bond, but higher than the dividend yield on the underlying equity. Convertibles rise in value if the price of the underlying equity rises, but because they have a par value at which they can be redeemed, they offer downside protection in a falling share price environment. Conversely, because of the equity participation, convertibles are less exposed to interest rate risk than a conventional bond. Like any bond, however, a convertible bond is exposed to default risk.

Exhibit 2: Interaction of bond and equity components of a convertible bond



Source: JPMorgan Global Convertibles Income Fund

Exhibit 2 illustrates the interaction of the bond and equity components of convertibles at different share price levels. The bond floor represents the par value of the convertible. If the company is in distress, the price of the bond in the secondary market may fall below this floor, effectively increasing the yield if the coupon is fixed. In the out-of-the-money segment, the par value of the convertible is above the underlying share price, meaning there is no incentive to convert; these 'bond-like' convertibles are held purely for income. As the underlying share price rises, the value of the convertible also rises, giving more of a balance of income and potential capital returns. An in-the-money convertible, where the share price of the company is above the par value of the bond, will behave more like an equity, with most of the return coming from capital gains.

The fund managers: Natalia Bucci and Paul Levene

The managers' view: Capturing more equity upside

JGCI's managers currently favour more exposure to the balanced segment of the convertible bond market, which offers more equity upside. This is in light of the continued positive economic backdrop, with a decent level of globally co-ordinated growth, which is good for corporate earnings and risk assets in general. The team's base-case scenario is that the economic environment will continue to support credit. However, having participated strongly in rising equity markets in recent years, spreads on high-yield bonds are now very tight, meaning the scope for further capital gain is limited. Bucci adds that the team maintains its overall focus on income, but wherever possible prefers bonds with lower starting yields and more equity market exposure.

The manager points out that convertible bond valuations behaved well in the recent period of equity market volatility, unlike in past corrections, which saw spreads widen or valuations become cheaper. While the JGCI portfolio sold off somewhat, this was in line with the team's level of modelled equity sensitivity. Because equity valuations fell in the sell-off but credit valuations largely did not, Levene says this points to better value in the balanced segment. Conversely, he says that the more credit-sensitive part of the market, where very tight credit spreads limit the upside, is where cracks could appear if there are any negative surprises from geopolitical and macro risks, such as the withdrawal of central bank stimulus or a possible global trade war. "Our base case is still positive, but if there is a negative event, credit will not be the place to hide, given the tightness of spreads," he adds.

Bucci argues that should credit market conditions turn negative, JGCI's additional investment flexibility should stand it in good stead. "This flexibility gives us the ability to transition the portfolio in an environment where credit might become stressed," she says. "We stay focused on payment of the dividend, but it is up to us as a team how we navigate that through the cycle."

Asset allocation

Investment process: Flexible focus on income and total return

JGCI has been team-managed since launch, and JPMAM is keen to stress the continuity of process (Natalia Bucci has been involved with JGCI from the outset), following the departure of former team head Antony Vallée in February 2018 and portfolio manager Robin Dunmall in May 2018. Bucci now heads the six-strong team, and underlines the importance of the stable of capital structure analysts that has been built up over the years – enabling the managers to take a more bottom-up approach and understand the fundamentals of the underlying companies – as well as the two dedicated convertible bond traders. One of the analysts, Paul Levene, who joined JPMAM in 2015, is now also a named portfolio manager on JGCI. Levene (previously at Ferox Capital) has more than 20 years' experience, spanning credit market cycles. His specialist focus on high-yield and distressed credit is particularly applicable to JGCI, where the majority of investments are rated sub-investment grade.

JPMAM's convertible bonds team sits within the multi-asset Global Investment Management Solutions group, and manages a SICAV as well as JGCI. As shown in Exhibit 2, the team sees the convertible bond market as having three main segments. While the SICAV focuses on the balanced to equity-like segments, JGCI – because of its income focus – is concentrated more in the bond-like to balanced areas. The bond-like segment is less favoured by the majority of convertible bond investors, which means JGCI's managers are often able to find convertibles that are trading at low valuations relative to the theoretical value of the credit plus the equity optionality.

JGCI invests globally, with sector and geographical allocations based partly on where the managers find the most compelling stock-specific opportunities, and partly on their view of the outlook for yields and overall convertible bond market valuations. Fundamental analysis of each issuer and its industry sector are key to the process. Portfolio holdings are rarely held until maturity, with the team preferring to sell as the bonds approach parity with share prices, reinvesting in higher-yielding names.

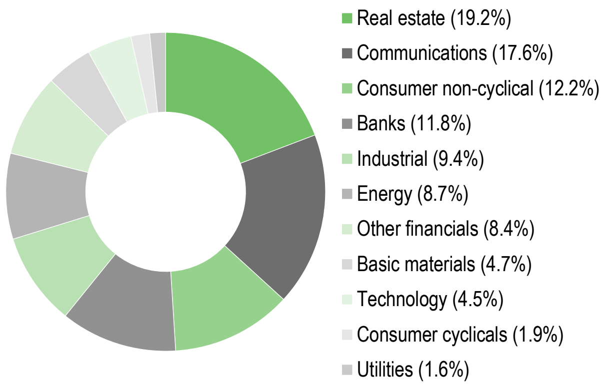
The portfolio is broadly diversified by geography, industry, issuer size and credit quality. As a result of the greater investment flexibility granted to the team in late 2015 (allowing it to target total returns rather than focusing solely on income), there is also a spread of yields, sometimes including zero-coupon convertibles, although at the end of H118 (31 December 2017), all portfolio holdings had positive yields. In terms of credit quality, a lack of ratings agency coverage means many convertibles do not have an official credit rating. However, the JPMAM team assesses and assigns an internal rating to all holdings. The portfolio is tilted to sub-investment grade (BB and below) issuers, with 63% of the portfolio at 31 December 2017 invested in issuers either internally (40%) or officially (23%) rated high-yield. All currency exposures are hedged back to sterling.

Current portfolio positioning

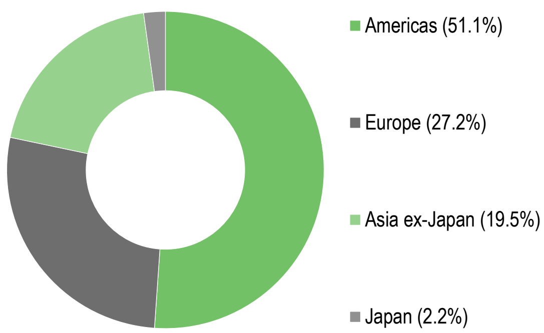
At 30 April 2018, there were 91 names in JGCI's portfolio, the same number as a year earlier. The top 10 holdings made up 23.8% of the portfolio at end-March. The managers are making use of the additional investment flexibility granted in late 2015, which allows them to focus on total return rather than solely on income, and as such the proportion of the portfolio invested in the balanced segment of the market (33% at end-H118) is around the highest it has been since the fund's inception. Because these bonds have lower yields (mainly sub-2%) and higher equity sensitivity, the managers are focusing on defensive large-cap names that should be more robust in the event of an equity market correction. Higher-yielding bonds (those on yields above 6%) are towards the lower end of the historical range; in this area, the managers prefer self-help situations where companies are taking steps to improve their credit quality.

Exhibit 3: Sector and geographic portfolio analysis as at 30 April 2018

Portfolio analysis by sector



Portfolio by region



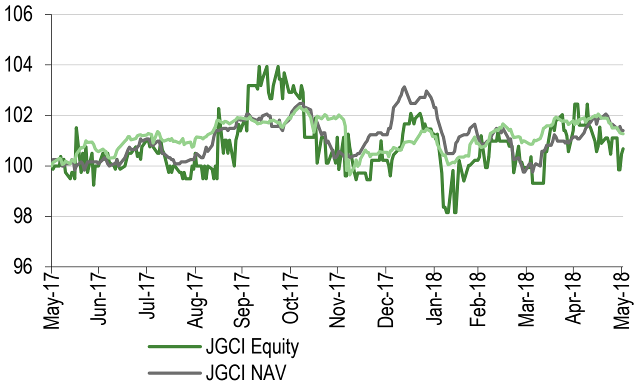
Source: JPMorgan Global Convertibles Income Fund, Edison Investment Research

As shown in Exhibit 3, the portfolio is broadly spread by industry and geography. Real estate is the largest sector weighting, with the exposure having shifted away from the US (where interest rates are rising more aggressively, which tends to be negative for real estate), and towards Asia ex-Japan (principally China and Singapore), where many companies trade at a significant discount to NAV. Levene comments that the team has also been finding opportunities in attractively valued Chinese banks. Exposure to Japan is largely through a new instrument, asset-swapped convertible option transactions (ASCOTs). These are geared instruments that offer considerable equity upside for limited premium expense. The US is the largest single geographical exposure, supported by the positive macro backdrop – corporate earnings are benefiting from the impact of tax cuts – as well as individual company fundamentals. At 31 March 2018, the largest single position was in Aabar Investments, an Abu Dhabi-incorporated investment company (see Exhibit 1).

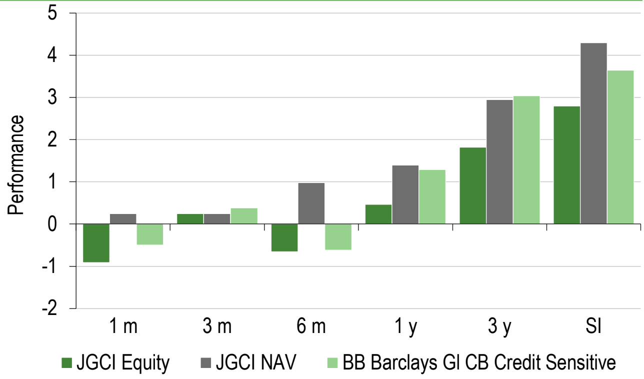
Performance: NAV outpaces share price return

Exhibit 4: Investment company performance to 31 May 2018

Price, NAV and benchmark total return performance, one-year rebased



Price, NAV and benchmark total return performance (%)



Source: Thomson Datastream, Edison Investment Research. Note: Three-year and since inception (SI, 11 June 2013) performance figures annualised.

Having been boosted by the introduction of a new buyback policy in May 2017, JGCI's share price performance over the 12 months ended 31 May 2018 was relatively flat. NAV performance was better and was slightly ahead of the benchmark (Exhibit 4). Positive NAV performance in recent months came from some energy stocks such as Premier Oil, which benefited from rising oil prices and was sold at well above par value, while detractors included Carillion and South African consumer-focused investment company Brait. The fund has lagged the performance of equity indices (Exhibit 5), which have bounced back strongly from a period of volatility earlier in the year, during which JCGI outperformed, demonstrating the defensive characteristics of convertible bonds. Performance relative to the official benchmark, the Bloomberg Barclays Global Convertibles Credit Rate Sensitive index, has been more volatile over the past six months (Exhibit 6) compared with the previous 18 months; JGCI's NAV total return is broadly in line with or ahead of the index over all periods shown since the fund's inception.

Exhibit 5: Share price and NAV total return performance, relative to indices (%)

	One month	Three months	Six months	One year	Three years	SI*
Price relative to Barclays Glbl CB Cr Rate Sensitive	(0.4)	(0.1)	(0.0)	(0.8)	(3.5)	(4.0)
NAV relative to Barclays Glbl CB Cr Rate Sensitive	0.7	(0.1)	1.6	0.1	(0.3)	3.2
Price relative to MSCI World Index	(5.0)	(3.0)	(4.4)	(7.7)	(27.5)	(39.6)
NAV relative to MSCI World Index	(3.8)	(3.0)	(2.8)	(6.8)	(25.0)	(35.1)
Price relative to FTSE All-Share	(3.6)	(6.7)	(6.9)	(5.7)	(15.1)	(24.0)
NAV relative to FTSE All-Share	(2.5)	(6.7)	(5.4)	(4.8)	(12.2)	(18.3)

Source: Thomson Datastream, Edison Investment Research. Note: *SI = since inception, 11 June 2013. Data to end-May 2018. Geometric calculation.

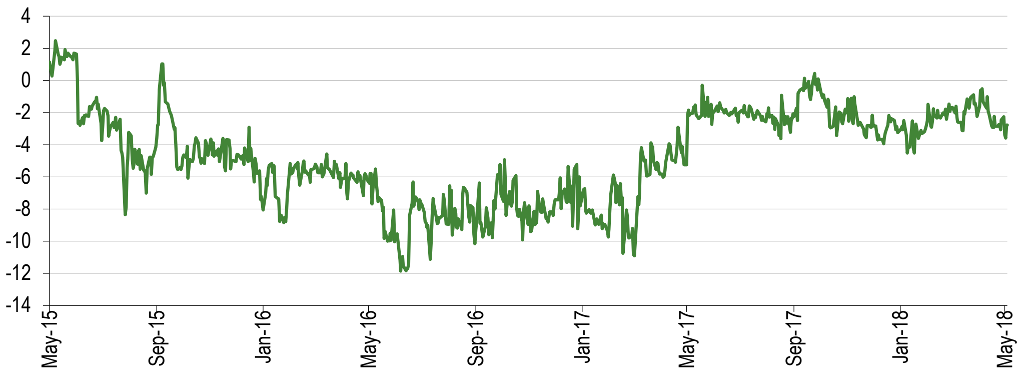
Exhibit 6: NAV total return performance relative to benchmark over three years

Source: Thomson Datastream, Edison Investment Research

Discount: More stable under new buyback policy

Having traded at an average premium for its first two years of existence, JGCI's shares moved to a discount to NAV, which widened from mid-2015 until the introduction in May 2017 of a new buyback policy, aiming to maintain the share price between a 2% discount and a 2% premium to NAV in normal market conditions. Under the new policy, 19.6% of the shares have been bought back into treasury in the past 12 months (to 1 June). The current discount of 2.8% compares with average discounts of 2.2%, 4.7% and 1.7% respectively over one and three years and since inception.

Exhibit 7: Share price premium/discount to NAV (including income) over three years (%)



Source: Thomson Datastream, Edison Investment Research

Capital structure and fees

Incorporated in Guernsey as a closed-end investment company, JGCI is listed on the London Stock Exchange, with 154.0m shares in issue at 1 June 2018. This was a reduction of 37.7m shares compared with 12 months earlier, following an increase in share buybacks under a newly introduced discount policy that aims to maintain the share price between a 2% discount and a 2% premium to NAV. The cost of the repurchases was £37.0m.

JGCI has a $32m borrowing facility with Scotiabank. This was undrawn at end-H117 (net cash of 5.6%) but has been partly deployed more recently, with net gearing standing at 2.1% at 1 June 2018. Gearing is limited to a maximum of 20% of NAV, with the current facility equating to available gearing of c 13%. The managers use gearing tactically and in the last 12 months the level has ranged from 8.6% geared to 6.2% net cash.

JPMorgan Funds receives an annual management fee of 0.75% of net assets, with no performance fee. For FY17, ongoing charges were 0.99% (FY16: 1.02%).

Dividend policy and record

Since launch in 2013, JGCI has targeted and paid a dividend of 4.5p per year (a 4.5% yield on the issue price of 100p). Originally paid in two instalments, since FY15, dividends have been paid quarterly. So far in FY18, three interim dividends of 1.125p have been declared. Revenue returns per share in the six months ended 31 December 2017 were 2.01p, meaning H118 dividends were slightly uncovered by income on an annualised basis. However, JGCI has the ability to use capital as well as income returns to fund the dividend; it also had revenue reserves of 0.75p per share at 31 December 2017 (total of £1.3m, up from £89,000 y-o-y). While the fund has moved to a more total return focus with a greater exposure to balanced convertibles, all holdings at end-H118 had positive yields. Based on the current share price, JGCI has a dividend yield of 4.7%.

Peer group comparison

As JGCI is the only dedicated, UK-listed, closed-end convertibles fund, it does not have a ready-made peer group. Exhibit 8 below shows a group of funds with broadly similar investment approaches (an income focus and some degree of investment in convertible bonds). The Advent Claymore fund is a US-listed, closed-end fund with a high level of gearing, while the Polar Capital and Salar funds are open-ended. JGCI's NAV total returns rank it second over one, three and four years, and third over two years. It is the smallest of the four funds. Ongoing charges are the lowest in the group, and there is no performance fee. Gearing is low compared with the Advent fund, and the discount to NAV is also lower. JGCI has the joint-highest yield in the group.

Exhibit 8: Selected peer group as at 5 June 2018*

% unless stated	Market cap/ fund size £m	NAV TR 1 year	NAV TR 2 year	NAV TR 3 year	NAV TR 4 year	Ongoing charge	Perf. fee	Discount (ex-par)	Net gearing	Dividend yield (%)
JPMorgan Global Convertibles Income	**147.0**	**2.2**	**11.5**	**10.1**	**11.7**	**1.0**	**No**	**(2.5)**	**106**	**4.7**
Advent Claymore Cnvt Secs&Inc II	167.6	(1.0)	27.4	21.7	34.4	2.1	No	(10.6)	188	4.7
Polar Capital Glbl Convert £ Hedged**	485.56	7.6	13.1	8.6	--	1.2	Yes			4.5
Salar Fund £ Hedged**	1,037.25	(0.7)	6.1	2.7	10.2	1.3	Yes			1.0
Peer group average	**459.4**	**2.0**	**14.5**	**10.8**	**18.7**	**1.4**		**(6.6)**	**147**	**3.7**
JGCI rank in peer group		**2**	**3**	**2**	**2**	**4**		**1**	**2**	**1=**

Source: Morningstar, Edison Investment Research. Note: *Performance data to 4 June 2018. TR = total return. **Open-ended funds: market cap refers to assets under management; discounts and gearing are not applicable to open-ended funds. Net gearing is total assets less cash and equivalents as a percentage of net assets (100 = ungeared).

The board

JGCI has five directors, all non-executive and independent of the manager. Four of them have served on the board since the fund's launch in 2013, including chairman Simon Miller, who is also the chairman of Brewin Dolphin Holdings and the North American Income Trust. Philip Taylor, Charlotte Valeur and Paul Meader (all of whom are resident in the Channel Islands, in line with the requirement for a majority of JGCI's directors to be based offshore) have also been in post since the fund's inception. Gailena Liew was appointed to the board in July 2017, following a period as a board apprentice. The directors have professional backgrounds in investment management, accountancy and business.

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