



Emerging Markets Overview

December did not play out quite the way we had hoped for as Euro-area debt and fiscal policy worries continued to weigh on market sentiment. On the one hand the ECB actually did deliver as the bank relaxed collateral rules and announced 3-year LTROs on top of lowering the refi-rate by 25bps to 1.00%. On the other hand the outcome of the December 9 EU summit proved somewhat disappointing as the fiscal brakes to be adopted in national constitutions and the monitoring of compliance still needs approval by national parliaments with the outcome being far from certain. Also, the funding of the EFSF's and the ESM, with the latter decided to be brought forward to July 2012, remained somewhat unenthusiastic and unclear. Consequently, the door to ECB all-in quantitative easing remained closed leaving Italian yield spreads and interbank risk metrics close to recent record highs.

With one of the pillars behind our early December call to scale up risk being seriously weakened (the other pillar being the history of solid risk asset performance in December) and with the euro in retreat we were forced to reconsider our investment strategy not least in our blended funds. Nevertheless, the damage was done as local currency debt benchmark GBI EM Global Diversified went from a MTD plus 1.40% to MTD negative 2.50% in a matter of days. GBI EM Global Diversified finished the month down 1.47% with Eastern Europe being the worst performing region, down 4.04%. GBI EM Global Diversified finished the full year down 1.75% (against the dollar). Hard currency debt markets fared better in December thanks to a rally in US treasury bonds leaving US 10yr yields 19 bps lower in 1.88% by the end of the month. Hard currency debt benchmark EMBI Global Diversified returned a monthly 1.13% taking the annual return to a decent 7.35%.

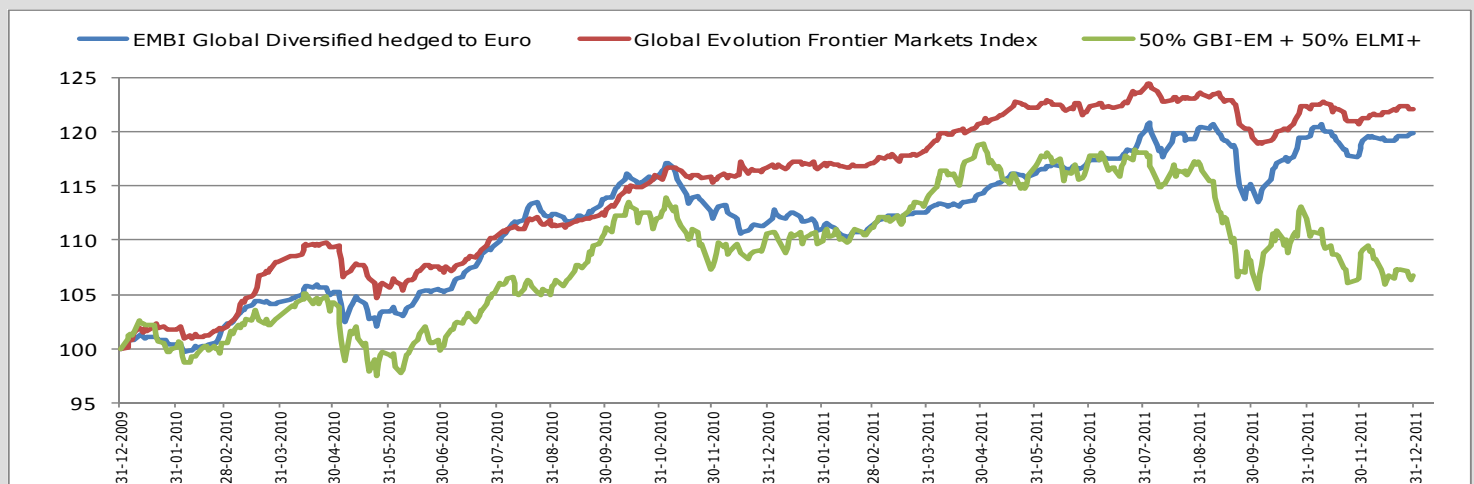
Elsewhere in risk markets, as the dollar gained strength gold lost its appeal leaving the glittering asset down 10.46% on the month. Germany's DAX stock index returned a monthly negative 3.13% whereas US S&P500 stock index gained a monthly 0.85% as US job market data as well as industrial/business data outperformed consensus expectations thereby fuelling expectations for better growth numbers in Q4 2011 and Q1 2012. WTI crude oil at some point during the month traded as low as USD 92.52 per barrel but managed a solid recovery to finish the month in USD 98.83 a barrel on the back of supply worries and Iranian rumblings in the strait of Hormuz.

In terms of portfolio flows the story in December was much the same as in November. Reflecting the dire outlook for global growth and not least the uncertain fate of the Euro-area, according to Emerging Portfolio Fund Research dedicated emerging markets fixed income funds suffered a monthly outflow of USD 611mn (0.5% of AUM) leaving YTD inflows at 5.6% of AUM. Local Currency funds saw monthly outflows worth 2.1% of AUM (up 11.1% YTD), whereas hard currency funds had a small monthly inflow representing 1.1% of AUM (up 2.6% YTD). Blended funds saw monthly outflows worth 0.5% of AUM (up 5.5% YTD).

Investment Outlook & Strategy

The Euro-area sovereign debt crisis is bound to dominate headlines and market sentiment in weeks to come starting with the Merkel-Sarkozy meeting on January 9 and to be followed by a minister of finance meeting on January 23 and a full EU27 summit by end January. With no doubt a status on the agreed incorporation of fiscal brakes in national constitutions will rank high on the EU27 summit agenda. Other issues likely to dominate risk sentiment in January are EMU sovereign financing needs and the raising of capital by European banks struggling to meet the 9% core Tier 1 ratio by end H1. Banks are expected to test investors risk appetite already in January whereas EMU sovereigns will test the demand among fixed income investors with an estimated financing need worth about 220bn in Q1. According to ECB statistics the money is there as deposits with the central bank rose to a record high EUR 446bn as of January 2nd. A lot of those money will have to be put to work, but to what extend will EMU sovereign coffers benefit? Medium term and longer term we strongly believe that Emerging Markets fixed income will see an increase in crossover flows from G3 institutional investors previously focusing on core markets fixed income. However, short term much will depend on overall risk sentiment, legal considerations and solvency issues. As for emerging markets hard currency debt despite the many uncertainties the technical picture looks good as investors remain structurally underweight and as sovereign net issuance in 2012 is expected to be about flat with more than 33% of coupon payments and amortizations to hit the market in Q1.

The fact that Chinese PMI surveys recently have risen to expansionary territories and that business and consumer confidence in the US and the EMU are diverging with the former beating consensus expectations are clearly positives supporting commodities and risk assets in general. However, due to short term headline risk and from a risk/reward perspective, while we see decent value in emerging markets hard currency debt we are inclined to reduce exposure to crowded local currency debt not least in Eastern Europe.



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Global Evolution Emerging Markets Local Currency Debt

Performance in December (I-Share Class)	
Portfolio	-1.46%
50% GBI-EM Global Diversified in dollar + 50% ELMi+ in dollar	-1.50%
Outperformance	0.04%
Performance YTD	
Portfolio	-3.30%
50% GBI-EM Global Diversified in dollar + 50% ELMi+ in dollar	-3.46%
Outperformance	0.16%

Fund Specification	
Name:	Global Evolution Emerging Markets Local Currency Debt
Domicile:	Luxembourg
Legal Structure:	Open-end – SICAV – UCITS
Share Classes:	Institutional: I, Retail: R
Registered Countries:	Germany, Austria, Luxembourg, Sweden, U.K. and Denmark
SRI Fund:	Yes
ISIN:	I: LU0616502372, R: LU0616502455
Bloomberg Code:	I: GEEMLCI LX, R: GEEMLCR LX
NAV:	I: 92.41
Fund Size:	€77mn
Benchmark:	50% GBI-EM Global Diversified in USD 50% ELMi+ in USD
Launch Date:	I: 21.06.2011
Min. Investment:	I: €1mn, R: €300
Base Currency:	EUR
Return Profile:	Accumulating (i.e. no dividends paid)
NAV Calculation:	Daily
Management Fee:	I: 0.85% p.a., R: 1.35% p.a.
Performance Fee:	5%
High Water Mark:	Yes
Reporting:	Monthly
Contact:	em@globalevolution.com

Investment Objective	
The objective of the emerging markets local currency strategy is to create attractive returns by utilizing a non-benchmark focused and diversified strategy within emerging markets focusing on sovereign local currency denominated debt and currency instruments	

Top-10 Country Distribution	
Mexico	12.10%
Turkey	9.45%
South Africa	9.20%
Poland	8.52%
Malaysia	7.15%
Brazil	7.10%
Uruguay	4.97%
South Korea	4.74%
Serbia	4.72%
Singapore	3.91%
Top-10 Total	71.86%

Fund Data	
Portfolio Yield:	7.28%
Portfolio Duration:	3.06
Number of Countries:	27
Average Portfolio Rating	BBB-
Volatility 1 year:	9.01%

Once again hopes were running high as we approached an EU summit and yet again we were disappointed. Consequently, the risk-on mode characterizing early December quickly disappeared thereby adding pressure on the euro and especially the euro sensitive Eastern European currencies. In other words, our bet that EU policy makers finally would deliver proved wrong. We started the month having a relatively high market exposure which we suffered from. However, we performed well on several off benchmark positions. During December we reduced exposure a bit primarily to some of the Eastern European countries since we still see this region as the most vulnerable.

Successful strategies

Our positioning in Africa once again proved beneficiary to overall performance as several African markets had very low correlation to the rest of Emerging Markets in December. Especially, our exposures to Uganda, Ghana, Zambia, Tanzania and Nigeria all gained relative to benchmark. In hindsight, several sub-Saharan markets performed poorly in the first 3 quarters of 2011 as inflation skyrocketed and with central banks proving behind the curve in most cases. However, during Q4 central banks have done a good job to get on top of the situation. With monetary policies now being much tighter foreign investors are back, lured by cheaper currencies and attractive carry. During the last couple of months we have raised exposure to several sub-Saharan countries at very attractive levels. Turning to Uruguay, a major off benchmark position performed very well during December as the government announced a debt swap at favorable prices. We switched from the 2018 inflation linkers into a new 2028 inflation linker at a pickup in real yields of almost 100 bps. We see Uruguay's inflation linkers as a very attractive carry play with real yields at 4.25% and expected annual inflation around 6-8% over the coming years (8.6% YoY in December). Finally, a small underweight in Eastern Europe contributed to outperformance.

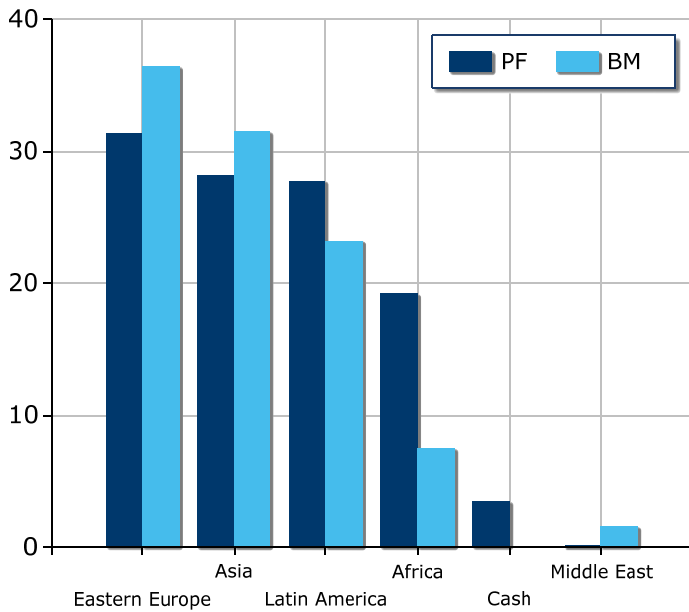
Less successful strategies

An underweight in Asia (which to a large degree comes from a zero weight and consequently large underweight in the pegged HKD) along with our composition of Asian country exposure proved a drag on performance during December. As an example, a very large underweight in Indonesia turned out the single largest contributor to underperformance as the Indonesian currency and local fixed income did very well thanks to continuous intervention from the central bank in both markets. We are very skeptical about the durability of central bank intervention especially so in the fixed income market. Therefore we stay underweight Indonesia for now. Turning to Latin America, overweight positions in Brazil and in Mexico performed poorly during December amid higher risk aversion. However, we remain of the opinion that Mexican peso and Mexican rates are extremely cheap in a scenario where we expect the US economy to muddle through. In Brazil, following the currency depreciation taking place since August 2011, we now find the real (BRL) fairly priced and at the same time well supported by a still attractive carry.

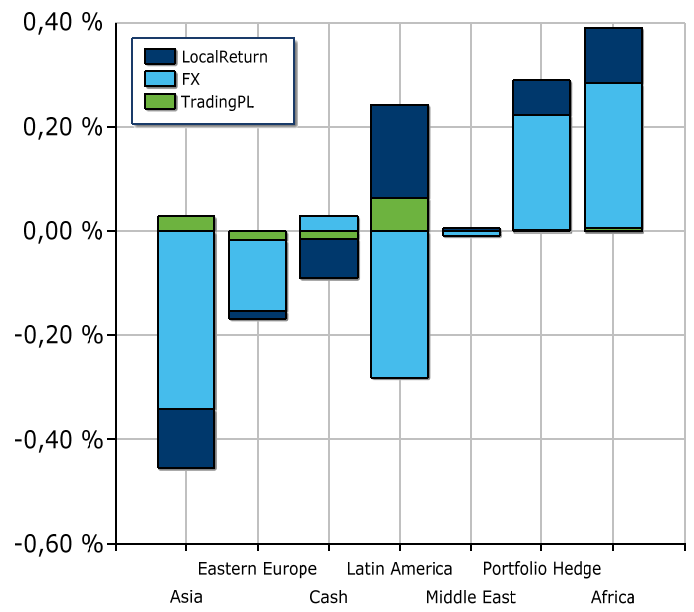


Global Evolution Emerging Markets Local Currency Debt

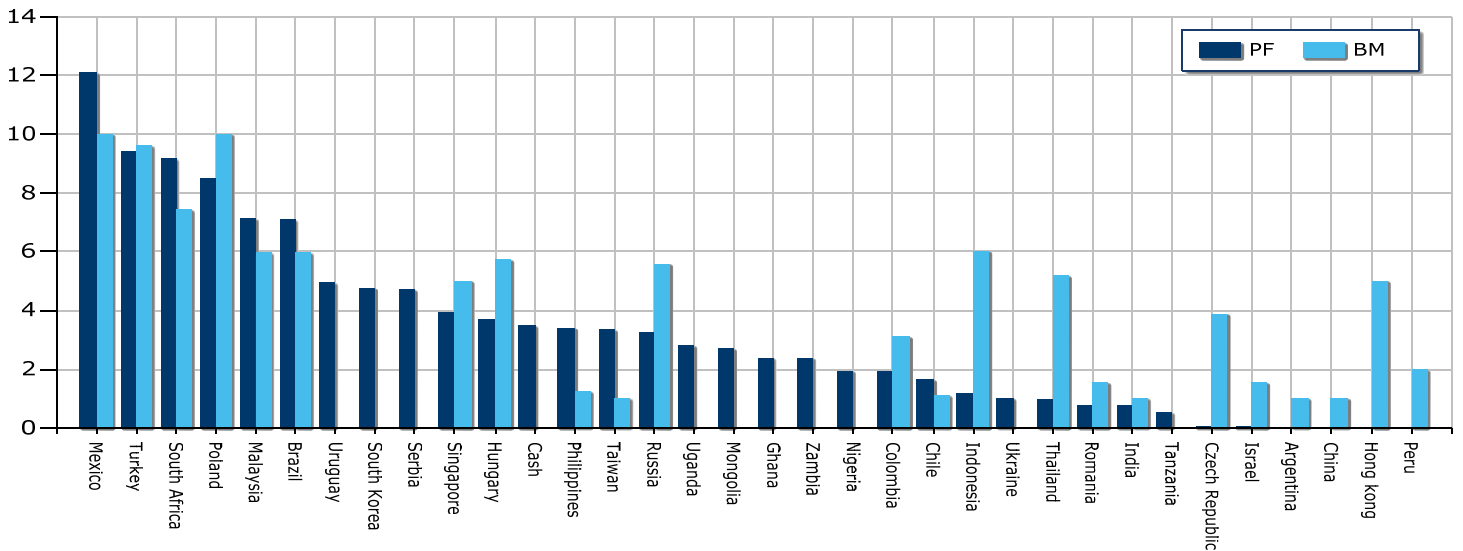
Regional Distribution



Regional Relative Performance



Portfolio Country Distribution



Portfolio and Benchmark Duration Contribution

