

IN FOCUS

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March 2012

Nordea 1 – European Low CDS Government Bond Fund

The “safest” sovereign debt haven in Europe

In a nutshell:

- New fund concept with the aim of being the most secure UCITS European Government Bond Fund based on a “real” market view of credit risk
- Given the increased level of uncertainty in the market, the need and the demand for safe haven investments are great
- The fund will be actively managed using the usual strategies available to bond investing

securities backed by low quality loans. The European sovereign debt crisis, only two years later, once again disillusioned investors. They were alarmed to find out the heightened credit risk that existed in safe “AAA” sovereign debt and the subsequent number and speed of downgrades.

Eventually, the debt crisis that started in Greece, Portugal and Ireland before engulfing Spain and Italy ratcheted up pressure on the wealthier members of the Eurozone. This is the first time that we see the spectrum of a large contagion effect all across Europe. This situation is not over and has fomented speculation and uncertainty, forcing market participants to consider new sources of risk. While investors sought safety from declining sovereign credit quality, the number of “AAA” European countries decreased and the supply of “AAA” investments has been shrinking ever since.

Why did we launch this new fund? The need for Safe Haven

On the 23rd of February 2012, Nordea launched a new fund concept with the aim of being the most secure UCITS European Government Bond Fund. The fund is based on a “real” market view of credit risk as given by the credit default swap spread (or “CDS”) and offers a true alternative to the dominant rating agency based investing system.

We launched this new fund for two main reasons. The first being, like many investors, we have experienced the increased level of uncertainty in the market. The need and the demand for safe haven investments during these volatile times are great. Put simply, investors are looking for safety and liquidity. The second reason is the difficulty faced by the rating agency system to provide reliable and consistent reflections of credit quality that has, in turn, repeatedly failed investors. The speed and number of downgrades has seemed chaotic and often came too late. That is why we felt we needed to offer an investment alternative using a market driven measure of credit risk.

Before the subprime and the sovereign debt crisis, it was much easier to find the “safest” debts as investors needed only to look at one of the few rating agencies and select the highest rating possible (i.e. AAA). During the subprime crisis in 2008, investors became disenchanted for the first time when they discovered that AAA bonds were in fact “unsafe” mortgage

The fund has a simple and straightforward investment process. It invests in the “safest” European government bonds based on a 3 months moving average of 5 yrs CDS spreads quoted by CMA (Credit Market Analysis).

The 5yrs CDS spread is the premium paid (i.e. the cost) to insure against the risk of a default in the next five years. It stands to reason, then, that the lower the cost, the lower the credit risk. The CDS market has the advantage of being liquid on a daily basis and CMA gives market prices in real time. The 5yr CDS contract for a credit tends to be the most liquid compared to shorter or longer term contracts. Furthermore, investors don’t need to decide which rating agency to trust and avoid having to reconcile conflicting ratings across agencies.

The five countries with the lowest CDS spreads are selected in the portfolio at all times and we invest only in government bonds with the most liquid CDS in Europe. The fund will be actively managed using the usual strategies available to bond investing. The fund manager’s active management style means that he can use his expertise to pick the bonds that offer the best risk/reward from the five countries with the lowest CDS spreads. In addition, he is unconstrained in terms

* investing for their own account - according to MiFID definition

of portfolio duration and can take full advantage of the yield curve development. Finally, currency risk is hedged in principle, and although there is no official benchmark, we aim to beat the typical Eurozone Sovereign AAA index.

Currently there are less than twenty countries selected, which include seven countries outside of the Euro zone. Thus, in case of a renewed severe Euro zone crisis and if the CDS market indicates that the fund should be invested outside of the Euro zone countries, we will do so.

Country	Moody's	S&P	5 Year CDS
Denmark	Aaa	AAA	118
Finland	Aaa	AAA	66
France	Aaa	AA+	184
Germany	Aaa	AAA	81
Ireland	Ba1	BBB+	629
Netherlands	Aaa	AAA	99
Norway	Aaa	AAA	30
Portugal	Ba3	BB	1,222
Spain	A3	A	407
Sweden	Aaa	AAA	53
Switzerland	Aaa	AAA	42
United Kingdom	Aaa	AAA	68

Source: Bloomberg. Date: 06.03.2012

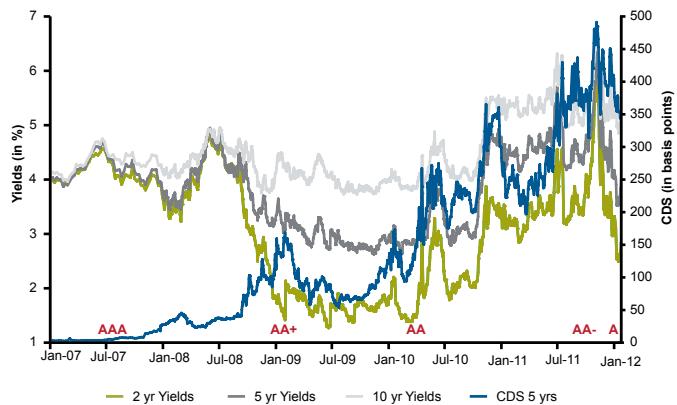
The idea of using CDS spreads instead of agency ratings in an active portfolio comes from solid market observations and research.

To reinforce our point, let's take the example of Norway which is rated by Moody's as a "Aaa" credit, the same as Germany and France. Now, if we look at S&P only Germany and Norway have the same level of credit risk, not France. On the other hand, if we look at the 5yrs CDS we would clearly have to pay 2.7x more for Germany (81 bps) and 6.1x more for France (184 bps) than for Norway (30 bps). From an investor point of view, Norway is the least risky as it costs much less to be hedged against a potential credit default.

From an active management standpoint, one of the big criticisms of the rating agency system is that it tends to lag the market and movement in yields, making virtually each change in investment allocation reactive and usually too late. By choosing the CDS spread, we know that there is an anticipation of rating announcements or changes by the credit default market. Clearly, we see an advantage for an active manager to avoid big losses from downgrades or anticipate gains from an upgrade as bond yields are closely related to CDS spreads.

In the Spain example below, we can clearly see this relationship between the CDS spread and bond yields, as well as the anticipation by the CDS spread on the effective rating changes.

Spanish Example



Source: Bloomberg. Date: 10.02.2012

Why choose Nordea for this new Product?

The **Nordea 1 – European Low CDS Government Bond Fund** has been back-tested using the principles described above except the active management. The backtest displays a relative out-performance compared to the IBOXX Euro Sovereign Eurozone AAA of more than 6%* over the last three years.

The fund is managed by Martti Forsberg from the Nordea International Fixed Income Team. Martti is also our portfolio manager for European bond products. He joined Nordea Investment Management in 2000 and has conducted research on all major asset classes including corporate bonds, high yield and emerging market bonds. He has successfully managed both Emerging Market fixed income portfolios and Euro bonds.

For those investors seeking a higher yield and willing to take more risk, we also offer a wide range of credit funds ranging from Investment grades to High Yields in Europe, Global and US.

Nordea 1 – European Low CDS Government Bond Fund

Retail	BP - EUR	LU0634509953
Institutional**	BI - EUR	LU0637308585
Hedged (to SEK) retail	HB - SEK	LU0733664022
Hedged (to NOK) retail	HB - NOK	LU0733663727

* Sources: Bloomberg and Datastream. Period under consideration: 07.08.2009 - 27.01.2012. The back test of the CDS based index was done by applying 20% weight for each country and the 20bps buffer rule before excluding any country (the 20bps buffer rule is defined so that a country is dropped from the portfolio when the difference to the new entrant has exceeded 20bps). 3 months' moving average on CDS spreads is also used. The performance represented is back-tested. Back tested performance is not a reliable indicator of future results and investors may not recover the full amount invested. The value of shares can greatly fluctuate as a result of the sub-fund's investment policy and is not guaranteed. If the base currency of the respective sub-fund differs from the currency of the country where the investor resides the represented performance might vary due to currency fluctuations. Performance calculated gross of fees. The back test start date (07.08.2009) is defined by data availability. This goes back to as far as Bloomberg has CDS quotes for each of the eligible countries.

** BI-EUR share classes: only for distribution towards institutional clients. Minimum investment amount: EUR 75,000 (or the equivalent).

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Our distributor in Portugal is BEST - Banco Electrónico de Serviço Total, S.A., duly incorporated under the laws of Portugal and registered with the CMVM as a financial intermediary. **Additional information for investors in Italy:** Fund documentation as listed above is also available in Italy from the distributors and on the website www.nordea.it. The updated list of distribution agents in Italy, grouped by homogenous category, is available from the distributors themselves, at State Street Bank S.p.A. branches (located in the main towns of each region), BNP Paribas Securities Services, Banca Sella Holding S.p.A., Allfunds Bank S.A., Societe Generale Securities Services Sp.A. and on the website www.nordea.it. 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Valdemara St. 62, Riga, LV-1013. **Additional information for investors in Estonia:** The Representative and Paying Agent in Estonia is Nordea Bank Finland Plc, Estonia Branch, Hobujaama 4, 15068 Tallinn. **Additional information for investors in Lithuania:** The Representative and Paying Agent in Lithuania is Nordea Bank Finland Plc, Lithuania Branch, Didžioji str. 18/2, LT-01128 Vilnius. Shareholders must evaluate possible investment risks and take this into consideration when making investment decisions. **Additional information for investors in Brazil:** Nordea 1, SICAV have not been, and will not be, registered with the CVM and may not be offered or sold in Brazil except in circumstances which do not constitute a public offering or distribution under Brazilian laws and regulations. Investors within Brazil should consult with their own counsel as to the applicability of these laws and regulations or any exemption there from. 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