Since 1903

Investment Opportunity in the European Sovereign Bond Market

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Brief Background

- ULJK Group is now in its 5th family generation of serving the financial services community.
- Based out of the Bombay Stock Exchange towers, we take pride in our 113 years old history of independent advice and efficient execution.
- Mr Laldas Vora, late partner was the President of Bombay Stock Exchange for 9 years and was instrumental in overseeing the construction of the BSE Tower.
- We constantly strive to anticipate the rapidly changing environment and develop services to enable our clients to adapt and capitalize.
- ULJK Group has expanded its services to European market and has tied up with a leading Serbian based investment and brokerage firm for Portfolio/Fund Management Services.

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Why Serbia and Croatia?

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Serbia and Croatia, like most sovereigns in the region issue bonds in a number of denominations

- The US$ denominated bonds are traded OTC and settled via Euroclear.
- The most liquid bonds have the tightest bid/ask spreads
- They are also the most volatile

- The EUR(€) denominated bonds are traded and cleared locally via the Central Securities Depositary and Clearing house in Belgrade (CRHoV) and (SKDD) in Croatia
- They are less liquid and more costly to trade actively but much less volatile

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- The RSD (Serbian Dinar) and HRK (Croatian Kuna) denominated bonds are traded and cleared locally via central Securities Depositary and the Clearing house in Belgrade (CRHoV) and (SKDD) in Croatia
- They are fairly liquid due to high percentage of local participants (banks and insurance companies) and recent uptick of foreign interest
- These local currency bonds have FX risk but can be offset via FX swaps

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Macro overview of Croatia and Serbia (Stable Economy)

- Croatia entered the European Union (EU) in 2013. After the global financial crisis of 2008-09, a return to GDP growth of more than 1% is expected in 2016. The highest contribution to this growth comes from exports of goods and services and tourism. GDP growth is expected to accelerate to 2-3% in 2017 on stronger domestic (investment) demand.
- For Serbia, we see 1.75% GDP growth this year and expect further GDP growth of 3-5% in the following years. More recently, there has been greater fiscal responsibility and a reengagement on critical issues such as state owned enterprise reform, public administration reform, and public sector efficiency.
- We expect a significant reform agenda in the new cabinets of both Croatia and Serbia, which will provide a sustainable future for both countries in the coming years.

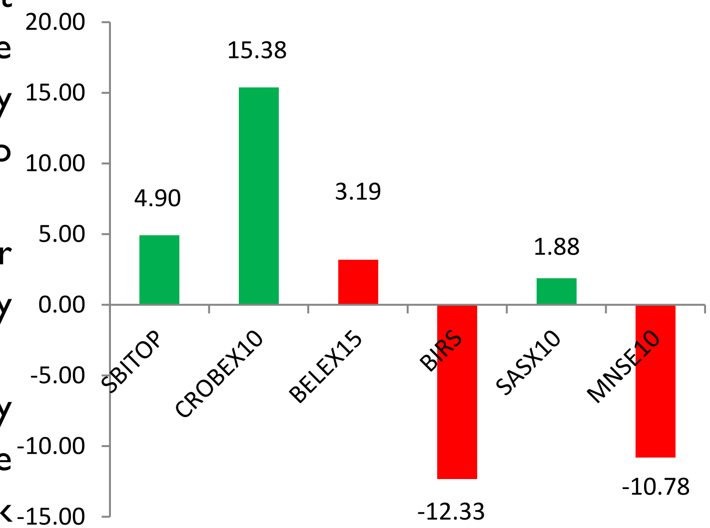
	Croatia					Serbia				
	2013	**2014**	**2015**	**2016F**	**2017F**	**2013**	**2014**	**2015**	**2016F**	**2017F**
Nominal GDP (EUR bn)	43.5	43	43.3	43.6	44.4	34.3	33.3	33	33.3	34.5
GDP per Capita (EUR)	10,225	10,114	10,186	10,280	10,468	4,783	4,666	4,615	4,666	4,840
Unemployment rate %	17.3	17.3	16.7	16.8	16	22.1	19.3	17.9	18.2	17.6
CPI %	2.2	-0.2	-0.3	1.1	1.4	7.8	2	1.4	1.8	3.1
Public Debt (% of GDP)	80.6	85	90.2	94.4	99.1	58.8	68.3	76.5	80.9	83.3
FDI (% of GDP)	2	3	4.2	4.1	4.3	3.8	3.7	5.5	5.8	5.9
Export (EUR)	18.80	19.90	21.27	21.97	22.69	13.94	14.45	15.62	16.27	16.85
Import (EUR)	18.60	19.00	19.76	20.16	21.34	17.78	18.10	18.90	19.44	19.68

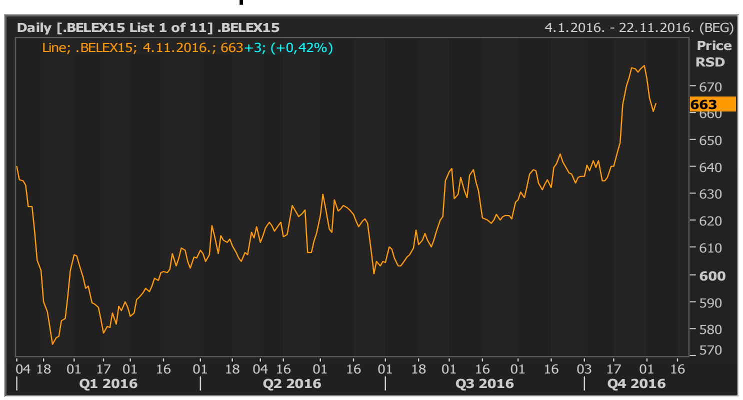
Source - Government statistical offices and Reuters Eikon

Why Serbia and Croatia?

- In contrast to the negative performance of SEE (South East Europe) equities in which almost no index was positive from last December, we must highlight that CROBEX rose singnificantly this year, but we don't expect that trend to continue.
- Clearly the fixed income market is a better investment alternative to any of the SEE equity indexes in long run.
- All SRB an CRO issues offer substantially higher yields relative to other sovereigns in the region, but with marginally increased risk providing a much better risk-return relationship.

SEE Equities Indexes in 2016 (YTD)





Source - Government statistical offices and Reuters Eikon

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Country comparison of the investment region

	Selected Economic Forecasts						Ratings		
		2013	2014	2015	2016	2017F	S&P	Moody's	Fitch
Slovenia	Nominal GDP(EURbn)	35.9	37.3	38.5	39.1	40.3	A	Ba3	BBB+
	GDP per capita (EUR)	17,431	18,091	18,665	18,892	19,439			
	Unemployment Rate (%)	10.1	9.7	9.1	8.8	8.4			
	FDI (%of GDP)	0.1	16	2.3	2.1	2.2			
	CPI Inflation(average %YOY)	1.8	0.2	-0.5	-0.5	1.2			
Croatia	Nominal GDP(EURbn)	43.5	43	43.3	43.6	44.4	BB	Ba2	BB
	GDP per capita (EUR)	10,225	10,114	10,186	10,280	10,468			
	Unemployment Rate (%)	17.3	17.3	16.7	16.8	16			
	FDI (%of GDP)	2	3	4.2	4.1	4.3			
	CPI Inflation(average %YOY)	2.2	-0.2	-0.3	1.1	1.4			
Serbia	Nominal GDP(EURbn)	34.3	33.3	33	33.3	34.5	BB-	B1	BB-
	GDP per capita (EUR)	4,783	4,666	4,615	4,666	4,840			
	Unemployment Rate (%)	22.1	19.3	17.9	18.2	17.6			
	FDI (%of GDP)	3.8	3.7	5.5	5.8	5.9			
	CPI Inflation(average %YOY)	7.8	2	1.4	1.8	3.1			
Bosnia	Nominal GDP(EURbn)	26.3	26.8	27.1	28.3	29.7	B	BB	NA
	GDP per capita (EUR)	3,507	3,564	3,613	3,764	3,948			
	Unemployment Rate (%)	27.4	27.5	27.2	26.7	26.1			
	FDI (%of GDP)	1.7	3.1	2.5	3.5	2.6			
	CPI Inflation(average %YOY)	0.1	-0.9	-1	1.1	1.8			
Monteregro	Nominal GDP(EURbn)	3.3	3.4	3.6	3.8	4	B+	B1	NA
	GDP per capita (EUR)	5,359	5,460	5,743	6,095	6,456			
	Unemployment Rate (%)	19.5	18	17.5	17.1	16.8			
	FDI (%of GDP)	9.7	10.4	17.3	19.6	15			
	CPI Inflation(average %YOY)	1.8	-0.5	1.4	1.8	2.1			

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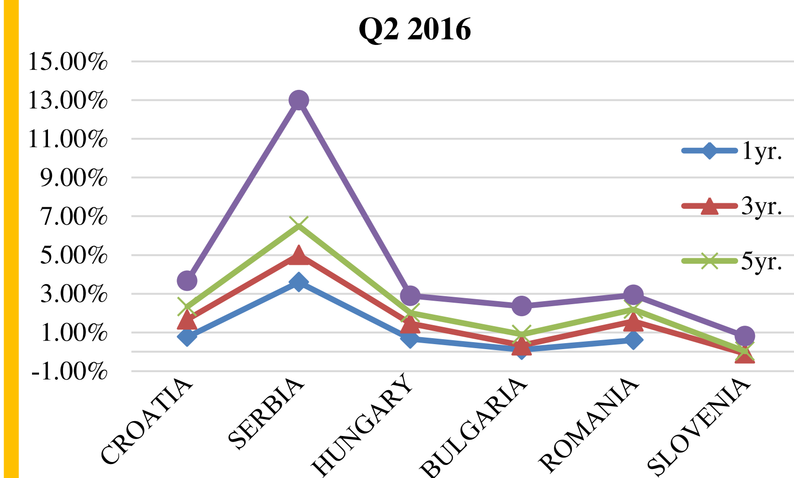
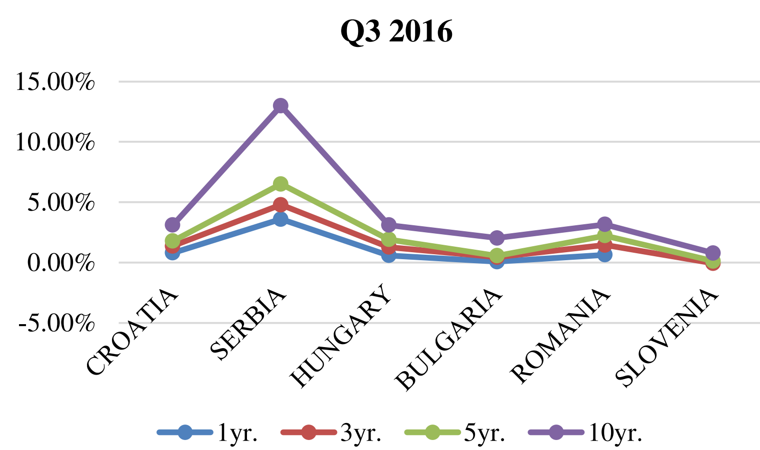


	1yr.	3yr.	5yr.	10yr.
CROATIA	0.77%	1.67%	2.33%	3.66%
SERBIA	3.59%	5.00%	6.50%	12.99%
HUNGARY	0.67%	1.46%	2.01%	2.89%
BULGARIA	0.10%	0.33%	0.89%	2.35%
ROMANIA	0.60%	1.57%	2.19%	2.93%
SLOVENIA		-0.09%	0.02%	0.80%

Serbia and Croatia offer higher yields compared to the countries in the region, especially Serbia, which makes them an a compelling investment opportunity



	1yr.	3yr.	5yr.	10yr.
CROATIA	0.80%	1.36%	1.78%	3.10%
SERBIA	3.59%	4.79%	6.50%	12.99%
HUNGARY	0.58%	1.27%	1.91%	3.10%
BULGARIA	0.07%	0.44%	0.56%	2.03%
ROMANIA	0.64%	1.45%	2.23%	3.15%
SLOVENIA		-0.07%	0.12%	0.78%

Comparing to Q2, we see a slight decline in the yields, it should be noted that Slovenia is already experiencing negative yields. And we see continued yield contraction for Serbia and Croatia going forward.

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Inexpensive capital

- The ECB interest rate fundamentally sets the price that banks pay to borrow funds from the European Central Bank
- Since March 16th 2016, the ECB interest rate is 0%
- Key policymakers feel that European markets have weathered the uncertainty experienced in the days after the Brexit referendum with encouraging resilience and believe that the current monetary policy measures have helped keep market stress contained

Banking sector in the region

SRB

30 banks operating

Total assets	Top 10	Top 10 (foreign)
24,573	18,435	15,510
	75%	63%

CRO

28 banks operating

Total assets	Top 10	Top 10 (foreign)
52,800	49,093	46,898
	93%	89%

- The region is dominated by Austrian, Italian and Greek banks.
- The top 10 banks in Croatia have 93% of all asset, which is significantly higher then any country in the region, where this percentage averages around 75%.
- Largest banks:
  - Serbia (Intesa, Komercijalna, UniCredit)
  - Slovenia (NLB, KBM, Addiko)
  - Croatia (ZABA. PBZ, Erste)
  - Bosnia (UniCredit, Raiffeisen, Addiko)

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Why Serbia and Croatia?

Serbia have attracted lucrative investments from the Middle East and Far East Countries

Key recent reference investments for Serbia have been:
- **Hesteel group from China (Steel)**
- **Belgrade WaterFront from the UAE (Real estate development)**

Future investments are under discussion:
- **Railroad infrastructure (China)**
- **Investment in IT park by Mubadala Development group(UAE).**

There is significant investment from Russia in acquiring the National petrol company NIS.

Serbia's main exports are automobiles and other products from the automotive sector. Automotive exports have become one of the most important sectors as a result of significant investments from the Italian carmaker FIAT.

Croatia, on the other hand, has made significant improvements to their tourism market, where growth of 15-20% is anticipated in the coming years. The recent tourist season broke previous records in terms of number of guests. Also, due to Croatia's membership in the EU, they are able to refinance EU funds to develop their economy in rapid fashion.

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Investment Opportunity

Economic fundamentals of Croatia and Serbia are solid, which illustrates that they will be able to meet their obligations, further we expect further positive developments of the economies of these two countries.

High yields: Some of the countries in the region already have negative yields, which makes Croatia and Serbia great investment opportunities.

Inexpensive capital – the ECB rate of 0% is providing low cost capital enabling our fund to refinance up at very advantageous rates.

Croatia is a member of the EU and Serbia has initiated membership talks with the EU, which provides important clarity about their economic futures.

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Liberalized Remittance Scheme (LRS)

- LRS is a window provided by the government of India to remit money across the border, without seeking specific approval.

- One can freely remit an amount within the LRS limit every financial year for a permissible set of current or capital account transactions. The current LRS limit is $250,000 per person.

- The scheme is available to all resident individuals, including minors.

- The person under LRS would be taxed as per Rule 37BB of Income Tax Act 1962.

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Investment Procedure

1 **LRS**

Investment

USD *$250K per person* every year

2

Account

***Wire transfer* to the PMS account**

3

Investment in Bonds

Sovereign Bonds* backed by *government guarantee

4

Returns

- ***13 % ++ returns annually in USD/EUR* if hold to maturity**
- ***Additional Capital Gains* if increase in value**

Investment Procedure

- Our investment strategy is based on taking advantage of the credit spreads of emerging market high yield bonds and current global refinancing rates i.e. the spreads between the currently low interest rates in the Euro zone and US markets used to finance the portfolio versus current YTM yields available on selected emerging markets (EM) sovereign bonds.

- The investment model is based on building a portfolio of EM high yield bonds with high coupon rates, preferably with semi-annual pay outs, generating strong cash flow and which are accepted as collateral in order to refinance the portfolio at historically low money market rates.

- Applying the appropriate refinance ratios (depending on the risk profile) allows us to augment the yields of these bonds and achieve substantially higher returns on capital invested.

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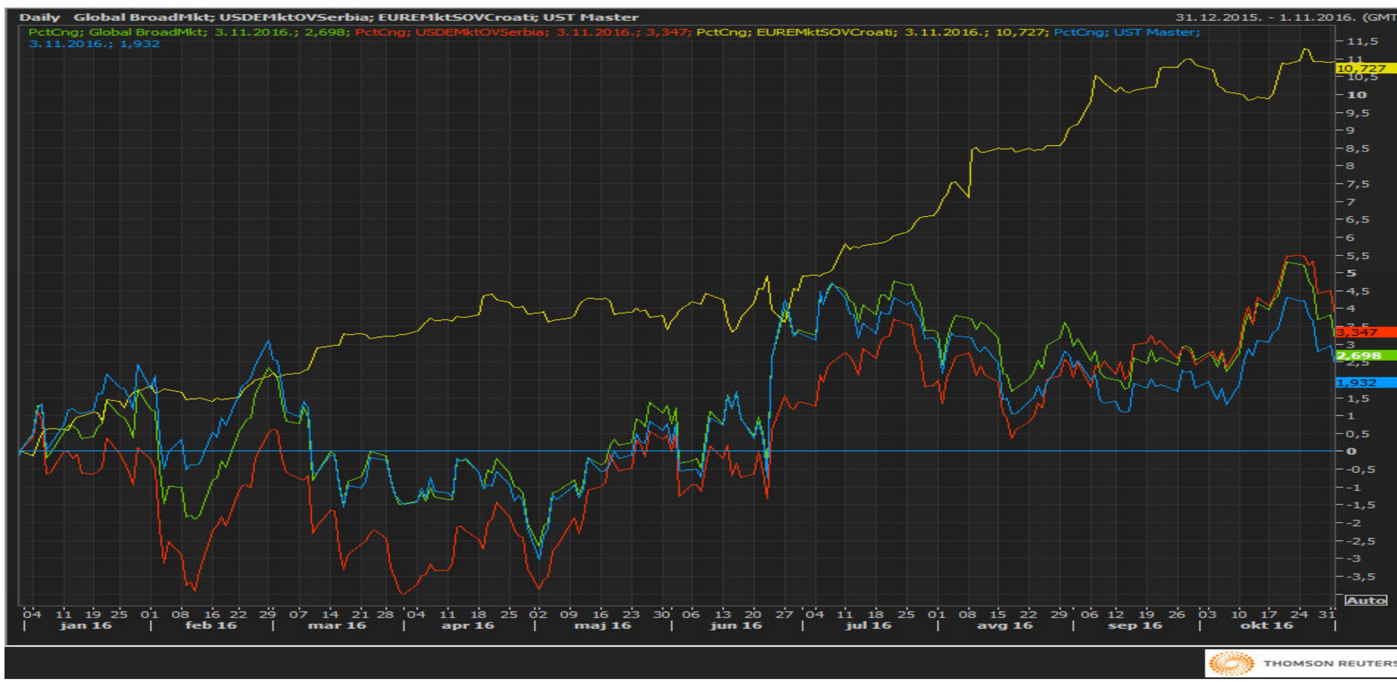
Proven performance: Overall our investment model has been able to generate double digit returns in each of the last four years.

				Return on Invested Capital on Current Portfolio				
Share Class	Type	Mat	CRY	Start Date	1 month	3 months	6 Months	To date
SERBIA	GOV	2018	$	31-Dec-14	3.33%	8.73%	17.45%	63.43%
SERBIA	GOV	2021	$	28-May-16	2.78%	8.08%	NA	14.80%
CROATIA	GOV	2020	$	28-Jan-16	3.38%	8.68%	16.85%	25.28%
CROATIA	GOV	2025	€	9-Jul-16	2.33%	7.00%	NA	7.00%
CROATIA	CORP	2017	€	10-Feb-16	5.36%	16.07%	32.14%	48.21%
CROATIA	CORP	2022	€	5-Feb-16	3.19%	8.49%	16.61%	24.92%



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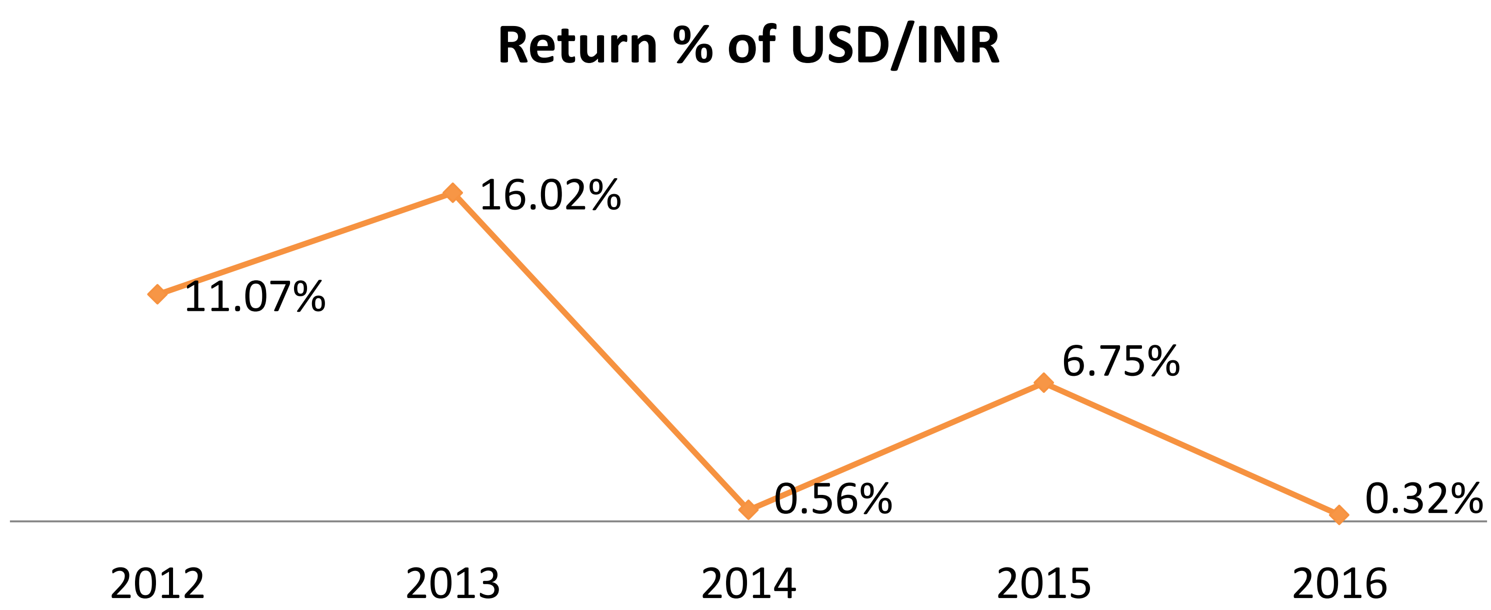

As shown in the figure, investing in USD in the past could have been lucrative and same is the situation now with the falling rupee. For instance, if invested in USD four years back, you could have earned approx 35% returns due to currency fluctuation in addition to 13 % returns on the bond. Hence the average annual expected returns would be 20% (13% returns on bonds+7 % returns on currency fluctuation)

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Capitalizing on the opportunity

- Most investors have a buy and hold strategy which produces a solid return for very conservative pension funds or insurance companies.
- The buy and hold model allows investors to benefit from a single variable - price.
- But this is not sufficient for active investors looking to maximize their ROIC at acceptable risk levels.
- In order to take advantage of all the variables previously mentioned we have developed a proven model (three years running) allowing investors to achieve substantially higher ROIC (in the double digits) without substantially increasing the risk profile of their investment.
- The model involves capturing value based on the combination of arbitrage of yield/interest rate spreads, capital appreciation by riding certain parts of the yield curve and swapping denominations.

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Expected Rate of Return

Bond Value- $1,13,000
Lot Size - 1000

Refinance Multiple	Total Investment (In USD)	Total Investment (In INR)	Indicative annual return net before tax	Expected IRR
5	$ 45,200	Rs 3,164,000.00	11.00%	22%
6	**$ 56,500**	**Rs 3,955,000.00**	**13.34%**	**27%**
7	$ 48,429	Rs 3,390,000.00	15.44%	31%
8	$ 56,500	Rs 3,955,000.00	17.60%	35%
9	$ 50,222	Rs 3,515,555.56	20.00%	40%
10	$ 45,200	Rs 3,164,000.00	22.00%	44%

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Opportunity and Takeaway

- Serbian and Croatian sovereign bonds have had a strong bull market over the last few years with significant yield contractions as they converge to comparable rates seen in the neighboring markets.
- Despite this, the yield spreads are still substantial and still provide ample investment opportunities.
- Our view is that this is the result of the perceived risk of Serbian sovereign debt is out of alignment with the actual risk, but this is slowly changing as rating agencies are improving their view of Serbian risk.
- Currently the most compelling opportunities are in the US$ and RSD yield curves.
- Serbian and Croatian sovereigns offer the opportunity of compounding the yield/interest rate differentials and capital gains to achieve compelling ROIC at acceptable risk profiles.

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1. What will be expected indicative returns annually?

The expected indicative return is 13% upwards in EUR/USD.

2. What is the Minimum ticket size in USD/EUR?

The minimum ticket size would be USD $60,000.

3. Why should I invest in this investment model?

- Because our proven investment model allows investors to make attractive returns on EM Sovereign Bonds without substantially increasing the risk profile.
- Offering high yields in a negative yield environment, etc. as explained in our investor presentation.

4. What is the lock in period?

The lock in period is 13 months.

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FAQ's

5. **How long can I redeem the portfolio and get the money back if I need it?**

   The process takes around 10-15 working days from receipt of redemption notice.

6. **Is it exchange based trading? How do I exit?**

   Mostly OTC and settlement via Euro clear / Clear stream. A client can exit with a redemption notice according to the lock-up protocol.

7. **What is the penalty if I break my lock in period?**

   If within the first 13 months 2.5% of invested amount after that no penalty.

8. **What are the tax implications on the income?**

   Under current Laws there is no capital gains tax on Serbian sovereign bonds.

   Tax issues are regulated by double Taxation Avoidance Treaty signed by India and Serbia in 2006.

   You will taxed as per your regular income tax policy.

   http://www.incometaxindia.gov.in/DTAA/Comprehensive%20Agreements/108690000000000076.htm

FAQ's

9. How quickly will you invest my funds in the bonds after you receive the transfer?

Funds will be invested as soon as satisfactory market price is achieved, usually up to 5 working days after funds received. Bonds can be replaced depending on maturities or market conditions.

10. How will often will I receive my coupon? Annually / semiannually.

This depends on the bonds itself. In general USD denominated bonds usually have semiannual coupon payouts while Euro and locally denominated bonds usually have annual coupon payouts.

11. Will the coupon be deposited in my bank account? If not, then where will my coupon be held?

All coupons are paid to global custody account and then credited to respective client accounts and reinvested and paid out at the end of the investment unless otherwise agreed to.

FAQ's

12. Whose name do I write the Cheque to?

Usually we do not work with cheque because they are slow, costly and take time to clear. Wire transfer is to be effected to C1 an account as stipulated by Portfolio Management Agreement.

13. Who is the custodian?

Any one of the prime banks or with whom we have repo and transaction lines (**Raiffeisen Bank , Erste Bank, UniCredit Bank Austria, Hypo Alpe Adria Bank** etc.). It also depends on whether the bonds are cleared locally or via Euro Clear/Clear stream. All the above institution are extremely well reputed banks that in business for decades.

14. What is the Investment Class?

Fixed Income – Sovereign Bonds.

Thank You

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