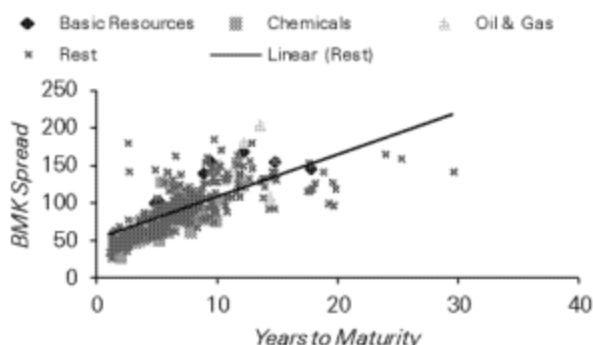




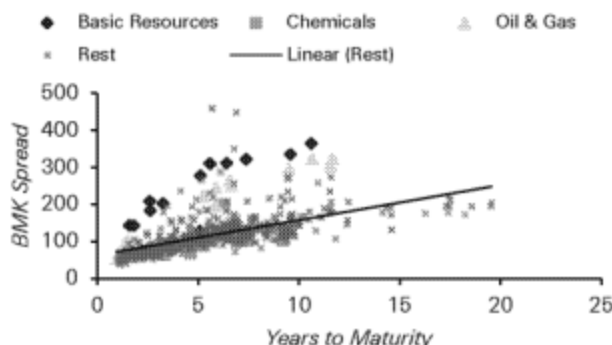
current state of ratings and the lessons from the past commodity sell-off in 2008-2009 suggests this is wrong.

Figure 28: Non-Financial single-A's BMK spreads vs maturity by sector excluding bottom rated bonds



Source: Deutsche Bank, Mark-it Global

Figure 29: Non-Financial BBB's BMK spreads vs maturity by sector excluding bottom rated bonds



Source: Deutsche Bank, Mark-it Global

Something will give – either these bonds will be downgraded or they will outperform. At the moment it seems unlikely they will be downgraded and therefore we think there is a good chance that they outperform, especially if we see any semblance of stability in global commodity markets. Given that the commodity market remains very volatile what gives us some comfort in this view is that a number of these bonds are already trading as if they have been downgraded giving us some rating slack.

To pull out which bonds in the sector we think might offer the best value we have 4 core criteria:

- Basic Material or Oil and Gas Bond
- Single-A or BBB
- Not A-/BBB- on negative watch
- Potential Price Return >4% if move to trade in-line with broader market

In Figure 30 we list the bonds which meet these criteria and estimate potential spread tightening and price returns if these bonds move to trading in-line with the rest of the single-A/BBB market. Results are ranked by potential percentage price return under the above criteria (highest to lowest, by sector).

There are two clear risks to this list. First is the obvious risk that commodity prices take another leg lower. What gives us some comfort here is the risk return profile with the rating slack we've discussed and the potential upside in a number of these bonds. The second is that this list of single-A and BBB EUR IG commodity bonds is relatively concentrated in a just a handful of names. Clearly any investment would require deeper analysis therefore of the actual companies listed. However we feel that as (a) these bonds recent performance has been driven largely by macro rather than company specific factors and look set to continue to perform along these lines for some time yet and (b) our analysis of how a number of these bonds are trading as if already downgraded gives us some comfort that company-specific factors shouldn't necessarily dominate near term performance.