JPMorgan Global Convertibles Income Fund

Balancing equity upside with downside protection

Investment companies

JPMorgan Global Convertibles Income Fund Limited (JGCI) targets income and capital growth through investment in a globally diversified portfolio of convertible securities. The fund's yield of over 4% is above the MSCI World and FTSE All-Share equity indices by close to two percentage points and one point respectively. A key attraction of convertibles is that they are seen to offer downside protection in a market downturn and a degree of participation in a stronger equity market, with lower volatility. As a closed-ended fund, JGCI is able to invest in more illiquid convertibles generally offering a higher return; this is likely to have helped the fund achieve a NAV total return performance at a similar level to equity markets since it was launched in June 2013.

Investment strategy

The fund focuses on high-yield, bond-like and balanced convertibles to provide an appropriate mix of income and growth potential. The fund has a relatively high exposure to small- and mid-cap companies reflecting both the nature of the convertibles market and the fund's income mandate. The managers have a strong emphasis on repeatable process, employing a customised screening tool before applying more detailed credit and equity analysis to investment candidates.

Rationale for convertible investment

Convertibles can offer a combination of equity and bond characteristics, providing yield and potential downside protection, but also participation in equity upside. Historically, over significant periods, they have delivered superior risk-adjusted returns versus bonds and equities (see page 6, Edison initiation note 13 June 2013). The relatively dynamic behaviour and complexity of some convertible securities and the scale of investment required to access new issues and build a global exposure argues for investment through a managed fund. As in the corporate bond market, many convertible issues can be relatively illiquid, and a closed-end fund is better positioned to access the liquidity premium on offer.

Outlook

Looking ahead, uncertainty exists over both fixed income and equity market outlooks, given increasing speculation over the timing and potential pace of interest rate rises and the expanded equity valuations following strong market performance. This suggests an environment in which convertible characteristics could appeal to many investors. A globally-diversified fund is well-placed to navigate a divergence in the interest rate outlook and convertible market issuance between Europe and the US as well as taking advantage of Asian market opportunities.

Valuation

Since inception (11 June 2013) the fund has delivered a total return of 10.7%, just ahead of the MSCI World Index. This and the attractive indicative yield of over 4% have contributed to a modest current share price premium to NAV of 2%.

1 August 2014

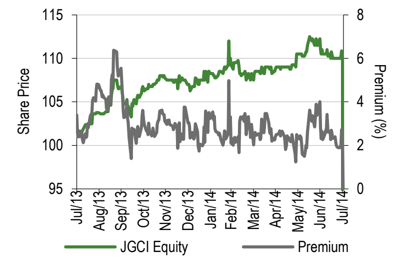
Price	**110.0p**
Market cap	**£177m**
AUM	**£176m**

NAV*	107.9p
Premium to NAV*	1.9%
Yield**	4.1%

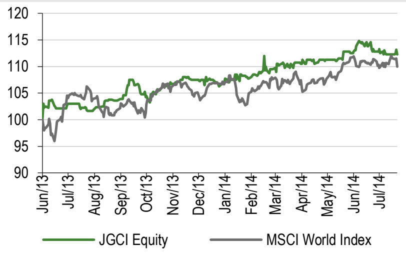
*Including income. **Prospective yield based on FY14 target 4.5p total dividend.

Ordinary shares in issue	161m
Code	JGCI
Primary exchange	LSE
AIC sector	Sector specialist: Debt

Share price/premium performance



Cumulative performance graph



52-week high/low	112.5p	101.6p
NAV* high/low	108.4p	98.6p

*Excluding income

Gearing

Gross	0.0%
Net cash	4.9%

Analysts

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Edison profile page

Exhibit 1: Fund at a glance

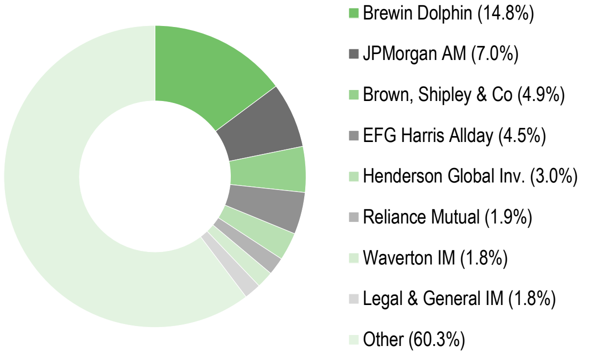
Investment objective and fund background	Recent developments
JPMorgan Global Convertibles Income Fund Limited (JGCI) seeks to generate dividend income combined with the potential for long-term capital growth by investing in a globally diversified portfolio of convertible securities and other suitable instruments exhibiting convertible or exchangeable characteristics. The dedicated convertibles team at JPMorgan Asset Management follows a well-developed process that combines equity and credit selection techniques. Currency exposures for capital and income are hedged.	27 February 2014: Interim results to 31 December 2013 +5.8% NAV total return since launch. 27 February 2014: 2.25p interim dividend declared. 20 September 2013: Prospectus published relating to a placing programme for up to 150m shares.

Forthcoming announcements		Capital structure and fees		Fund details	
AGM	November 2014	Ongoing charges	1.10%	Group	JPMorgan Asset Management
Preliminary results	September 2014	Net cash	4.9%	Manager	Team led by Antony Vallée
Year end	30 June	Annual mgmt fee	0.75% of net assets	Address	60 Victoria Embankment, London EC4Y 0JP
Dividends paid*	Quarterly	Performance fee	None		
Launch date	11 June 2013	Company life	Indefinite (cont. vote)	Phone	+44 (0)20 7742 9995
Continuation vote	AGM 2018 and 3-yearly	Loans, facilities	N/A	Website	www.jpmconvertiblesincome.co.uk

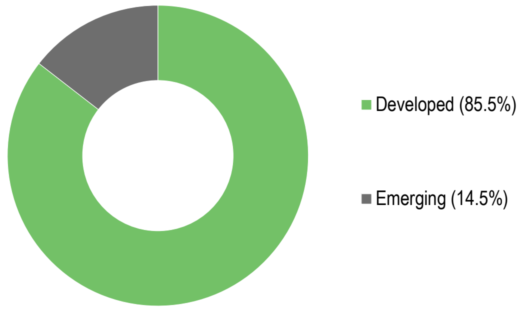
Dividend policy	Share buy-back policy
In the first year dividends are to be paid half-yearly with the intention to move to quarterly payments thereafter. The target is for a gross dividend yield of 4.5% on the issue price (100p) and the manager reports the fund is on track to deliver this. JGCI aims to smooth dividend payments over time.	JGCI may buy back up to 14.99% of the issued share capital. Subject, among other things, to directors' discretion, the company would expect to make purchases if the share price discount to net asset value exceeds 5% for any significant period of time.

Portfolio characteristics 30 June 2014		Portfolio allocation 30 June 2014 (%)	
Portfolio yield to best**	4.0%	**Sector**	
Delta (a measure of sensitivity to equity movements)	30.9%	Consumer Cyclicals	17.1
Duration (to put)	3.5 years	Other Financials	15.0
Number of securities	62	Real Estate	13.9
Available cash	4.9%	Energy	12.1
Bond quality		Basic Materials	9.8
Investment grade	14.9%	Industrial	8.7
Sub-investment grade	37.8%	Communications	8.6
Non rated	47.3%	Consumer Non-Cyclicals	5.7
	100.0%	Banks	5.2
		Technology	2.3
		Utilities	1.6
		Total	**100.0**

Shareholder analysis (as at 7 July 2014)



Regional portfolio analysis (as at 30 June 2014)



Source: JPMorgan Global Convertibles Income Fund. Note: *See dividend policy. **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. Yield to maturity is the internal rate of return of a bond for an investor holding it to maturity.

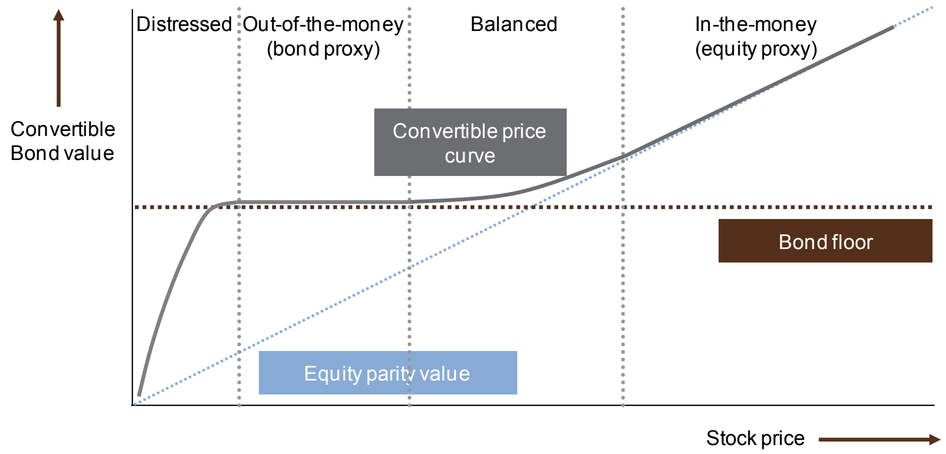
Convertible bonds in brief

- Convertible bonds combine characteristics of bonds and equities.
- They typically pay a fixed income (coupon) with the option of redemption at face value or conversion into the underlying equity at a predetermined rate at a particular date.
- They are issued as bonds, and the holder has the option to convert into the equity, normally at a premium to the share price at the time of issue.
- At the time of issue, the yield is usually below the level of an equivalent straight bond but above the equity yield of the issuer.
- Convertibles participate in the upside of the underlying equity.
- As bonds, there is a level of downside protection if the underlying equity price falls.
- The option to convert becomes more valuable if the equity volatility increases.
- The equity component reduces a bond's sensitivity to interest rate changes.
- Like corporate bonds they are exposed to default risk.
- As with corporate bonds, liquidity can be limited, adding the risk of exposure to crowded trades.

Bond and equity components interaction

Exhibit 2 illustrates how bond and equity components of a convertible bond might interact. At the right-hand side, where the stock price is above the conversion price, the convertible is in-the-money and its price moves closely with the equity price. Towards the left-hand side, in the out-of-the-money segment, the convertible is valued as a bond and does not respond significantly to marginal moves in the stock price; this is where the downside protection, or bond floor, of a convertible is evident. Between these segments, convertibles demonstrate a balance of characteristics, responding positively to equity upside while downside is limited as the bond floor price is approached. On the extreme left, were the company to become distressed, the bond is exposed to default risk: hence the price line trends to zero in this segment.

Exhibit 2: Illustration of interaction of bond and equity components of convertible bond

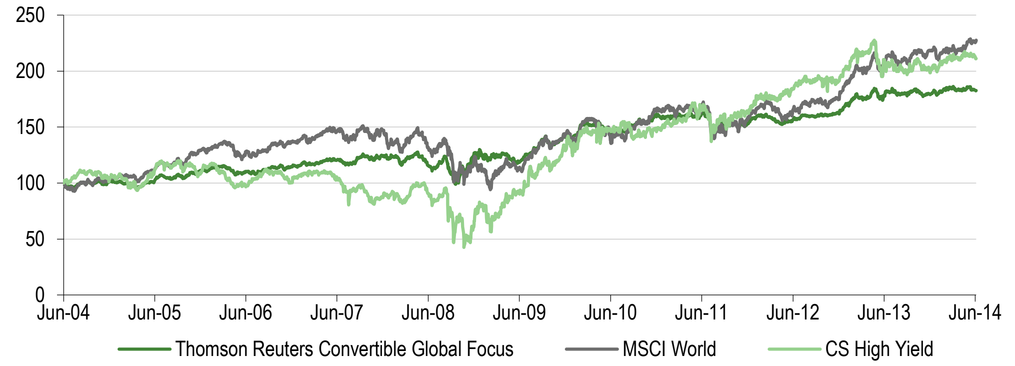


Source: JPMorgan Global Convertibles Income Fund

Outlook for the convertible market

To give a longer-term perspective on the convertible market, Exhibit 3 shows the performance of the Thomson Reuters (TR) Convertible Global Focus Index, the MSCI World Index and the Credit Suisse High Yield Bond Index over 10 years. This shows the relative resilience and lower volatility of convertibles during the global financial crisis and subsequent recovery. While equity and high-yield bond indices have outpaced convertibles from their low point during the financial crisis, it is worth noting that since launch, JGCI has been able to marginally outperform the world equity index.

Exhibit 3: Global convertible index versus world equity and high yield bond indices



Source: Thomson Datastream, Edison Investment Research. Note: Indices £-adjusted total return performance.

With many equity markets trading close to all-time high levels, an uncertain market outlook influenced by US quantitative easing drawing to an end and increasing speculation over the timing and potential pace of interest rate rises, the downside protection offered by convertibles may appeal to investors concerned about the risk of an equity market correction. Concern over the potential impact of rising interest rates could also make the equity exposure offered by convertibles more appealing to bond investors. Although convertibles would be expected to underperform a rising equity market, they should capture a significant part of the equity upside as well as providing a superior yield and may deliver better risk-adjusted returns. Exposure to small- and mid-cap companies and more cyclical sectors may provide greater sensitivity to equity performance.

Fund profile

Launched in June 2013, JPMorgan Global Convertibles Income Fund (JGCI) is an investment company, incorporated in Guernsey and listed on the main market of the London Stock Exchange. JGCI has an indefinite life, subject to continuation votes at the fifth AGM (2018) and three yearly thereafter. The fund aims to deliver income together with potential long-term growth through investment in global convertible bonds and other suitable instruments exhibiting convertible or exchangeable characteristics. The MSCI World is the reference index for the fund, but the portfolio is not benchmark-driven. The portfolio is managed by Antony Vallée, who has 16 years' experience in the convertibles market and heads the 10-strong JPMorgan Asset Management convertibles investment team, together with Natalia Bucci and Robin Dunmall.

The managers' view

Antony Vallée, Natalia Bucci and Robin Dunmall

Antony Vallée comments that with taper-talk having a negative impact on the market at the time of JGCI's launch the managers elected to slow the initial phase of investment and preferred short-dated high-yield bonds to longer-dated paper in this early stage. This allowed them to invest c 35% of the fund's assets at lower prices, which benefited early performance. Subsequently, fund performance was helped by the positive combination of credit spread tightening, equity market strengthening and declining government bond yields.

In 2014, global convertibles issuance has been strong, particularly from mid-cap companies, and the managers are seeing more attractive investment opportunities in the primary market, offering higher yields at lower premiums than secondary issues. JGCI participated in 27 new issues in the period from launch to 30 June 2014 (13 since 1 January 2014). While switching into these new primary issues increases portfolio turnover, this is not considered a detriment as the portfolio yield is improving as a result. A strong pickup in issuance this year is seen as a positive signal raising the prospect of a positive supply demand balance for the first time since 2010. Looking ahead, the key drivers of convertible issuance are judged to be strong equity markets and rising interest rates, increasing the attraction of issuing convertible rather than straight debt.

The team's screening process identifies mining as a sector currently offering a greater than average number of investment opportunities with attractive yields. However, the managers consider that risks in the sector remain above their threshold and they would like to see an improvement in the outlook before investing.

Asset allocation

Investment strategy and process

The managers invest predominantly in bond-like convertibles, where yield is the key attribute, and the balanced segment, where bonds start to capture equity upside. The portfolio includes high-coupon convertibles issued by small- and mid-cap companies where a liquidity premium helps to boost income and higher equity betas increase the equity sensitivity of the portfolio.

From a top-down perspective, the managers assess the prospects for yields and overall convertible market valuations to judge a strategic allocation between more defensive bond-like convertibles and more equity-sensitive securities. There are no formal constraints on geographical, sector or market capitalisation exposure. Bottom-up factors include individual company analysis, industry outlook and technical factors for the specific convertible. Antony Vallée places great emphasis on maintaining a consistent process and regards this as important in enabling repeatability and analysis of investment decisions.

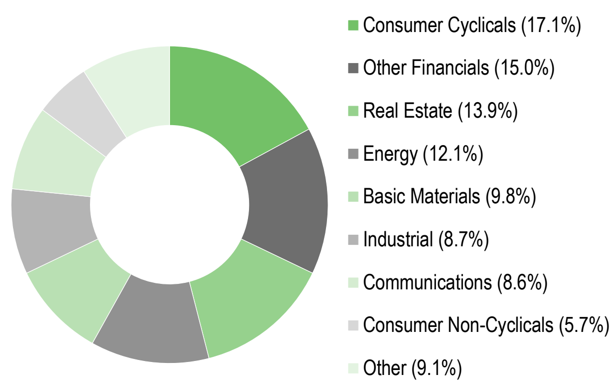
Investment restrictions set by the company include no exposure to a company greater than 10% of gross assets, no single counterparty exposure over 15%, unlisted holdings will not normally exceed 5%, no more than 10% of assets in investment funds at time of investment, and no more than 15% in other closed-end investment companies. In practice, individual holdings are unlikely to be above 5% of assets and the expected range of holdings is between 60 and 80 securities.

Current portfolio positioning

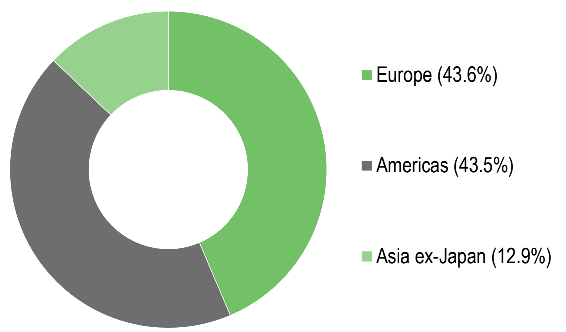
The portfolio currently comprises 62 holdings providing broad sector and geographic exposure.

Exhibit 4: Sectoral and geographic portfolio analysis as at 30 June 2014

Portfolio analysis by sector



Portfolio analysis by region



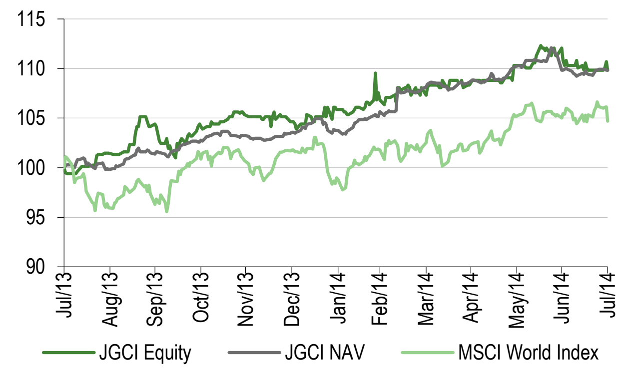
Source: JPMorgan Global Convertibles Income Fund, Edison Investment Research

As illustrated in Exhibit 4, as at 30 June 2014, the portfolio is predominantly exposed to Europe and the Americas (primarily the US: 39.7% exposure), with a much smaller exposure to Asia ex-Japan. Compared with 31 December 2013, Americas exposure increased from 41.4% to 43.5% at the end of June, offset by a reduction in Asia ex-Japan exposure from 14.5% to 12.9% and a small decline in exposure to Europe. This is reflected in an increase in developed market exposure from 82.7% to 85.5% (see Exhibit 1). At 30 June 2014, 17.1% consumer cyclicals was JGCI's largest sector exposure, similar to the 16.4% weighting at 31 December 2013. The most significant changes in exposure since December are 6.7 and 5.5 point reductions in industrials and basic materials.

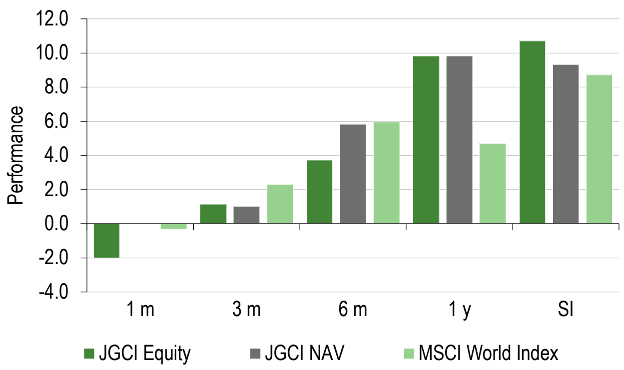
Performance: Outperformance since inception

Exhibit 5: Investment company performance

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



Price, NAV and index total return performance (%)*



Source: Thomson Datastream, Edison Investment Research. Note: Launched 11 June 2013. *Since inception (SI) figures are annualised compound returns.

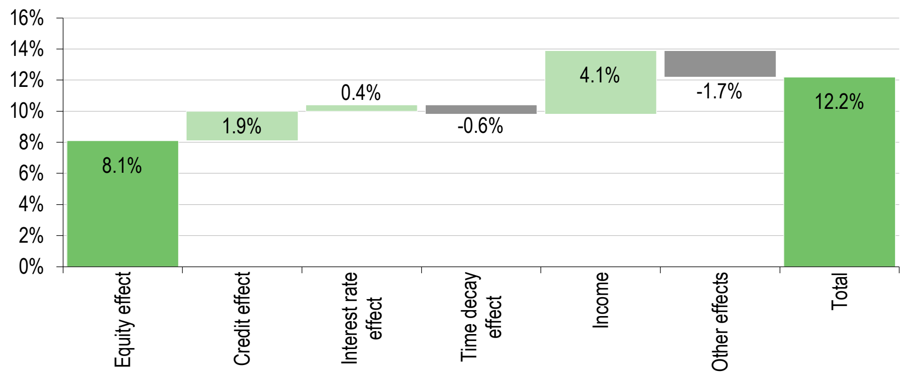
Exhibit 6: Share price and NAV total return performance vs. indices (percentage points)

	1 month	3 months	6 months	1 year	SI
Price versus MSCI World	(1.7)	(1.2)	(2.2)	5.1	2.3
NAV versus MSCI World	0.3	(1.3)	(0.1)	5.1	0.7
Price versus Credit Suisse HY	0.4	2.1	0.6	10.8	11.9
NAV versus Credit Suisse HY	2.4	1.9	2.7	10.8	10.3
Price versus TR Convertible Global Focus	(1.2)	1.9	3.0	11.1	10.2
NAV versus TR Convertible Global Focus	0.8	1.8	5.1	11.1	8.6

Source: Thomson Datastream, Edison Investment Research. Note: Data to end-July 2014. Indices £-adjusted.

JGCI's NAV total return has outperformed the TR Convertible Global Focus Index since inception in June 2013 and has performed just ahead of the MSCI World Index over the same period. Although JGCI's reported delta (sensitivity to equity movements) is 30.9% at 30 June 2014 suggesting that performance would lag a rising equity market, the fund's orientation towards higher-beta small- and mid-caps increases the leverage to equity market movements and may account, in part, for the small positive performance differential.

Exhibit 7: Share price performance attribution analysis – one year to 30 June 2014



Source: JPMorgan Global Convertibles Income Fund, Edison Investment Research. Note: Other effects include impact of volatility on convertibles valuation and contraction in share price premium to NAV.

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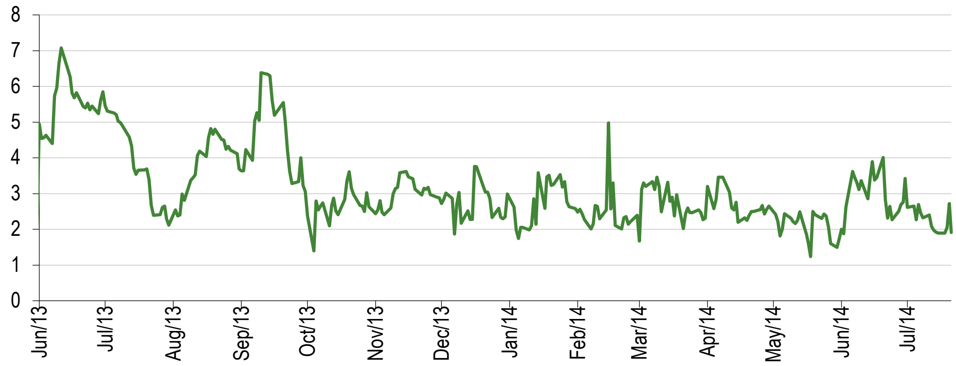
Exhibit 7 illustrates the components of JGCI's share price performance over one year to 30 June 2014, highlighting that the greatest contributor to performance over this period has been the capital gain attributed to the impact of the rising equity market, which substantially outweighed the reduction in option value through time decay and other effects.

Discount / premium

JGCI will seek annual shareholder approval for buy-backs up to 14.99%. Subject, among other things, to directors' discretion, the company would expect to make purchases if the share price discount to net asset value exceeds 5% for any significant period of time. The share issuance mentioned below has acted to moderate the premium the shares have traded on.

Exhibit 8: Share price premium to NAV (including income) since launch



Source: Thomson Datastream, Edison Investment Research.

Capital structure, fees and other items

At launch in June 2013, JGCI issued 136m ordinary shares and subsequent to the initial placing a further 25m shares have been issued, bringing the total to 161m. It has the authority to issue further shares on a non-dilutive basis and, in September 2013, issued a prospectus relating to a placing programme for up to 150m shares, providing the ability to respond to demand for the shares and enlarge the company, thereby spreading costs and improving liquidity in the shares. Gearing up to 20% of net assets is permitted, but the manager does not intend to deploy this in the near term.

JPMorgan Asset Management is paid a management fee of 0.75% pa of net assets and there is no performance fee. The management contract is terminable on six months' notice by either party, although notice cannot be served in the first two years of the fund's establishment. Ongoing charges are reported as 1.10% pa.

Dividend policy and tax treatment

For the first accounting period, JGCI is targeting a 4.5p gross dividend with a 2.25p interim dividend declared for the period to end December 2013 and a final dividend to be declared for the period to the end of June 2014. The intention is to move to quarterly payments in subsequent years.

The treatment of dividends paid by JGCI may be more favourable in the UK than for income from an open-ended fund, which may be counted as savings income and hence incur the investor's marginal tax rate. By dint of its Guernsey incorporation, JGCI may pay no tax itself on interest receipts and a UK investor may pay the lower marginal rate of tax that applies to dividends.

Peer group comparison

Exhibit 9 shows a comparison of JGCI with a closed-ended peer group investing in convertible securities. We have excluded two funds with exposure of 30% or less to convertible instruments to give greater comparability with JGCI. This leaves eight funds, all of which are US-based and predominantly invested in US securities and therefore differentiated from JGCI, with its UK listing and global diversification.

JGCI's NAV total return over one year is ahead of the relatively narrow peer group range by some margin, while it remains ungeared in comparison with a number of peers that have gearing in excess of 30% (debt/equity). The peer group average total return over three years is below the MSCI World Index, while over five years it is ahead. Peer group average Sharpe ratios at values of one or above, over one and three years, point to attractive risk-adjusted returns.

Exhibit 9: Closed-end funds investing in convertibles as at 30 July 2014

Fund name	Market cap £m	NAV TR 1 Year	NAV TR 3 Year	NAV TR 5 Year	Sharpe 1y (NAV)	Sharpe 3y (NAV)	Discount (ex par)	Ongoing charge	Perf fee	Net gearing	Dividend yield (%)
JPMorgan Global Convert Income	178.6	9.8					5.1	1.10	No	94	4.1
Advent Claymore Cnvt Secs&Inc	142.5	(1.5)	14.5	52.9	1.1	0.3	(7.8)	2.05	No	165	6.9
Advent Claymore Conv & Income	265.8	(1.0)	21.8	80.4	1.1	0.5	(4.4)	1.13	No	157	5.9
AGIC Convertible & Income	531.4	3.7	44.5	126.4	2.1	1.0	10.2	1.19	No	144	10.5
Bancroft Fund	62.9	2.3	28.2	73.2	2.0	0.8	(14.7)	1.10	No	97	2.4
Calamos Convertible & High	619.6	4.2	36.0	92.4	1.6	1.3	0.2	1.17	No	136	5.0
Calamos Convertible Opps & Inc	553.1	4.2	36.7	93.8	1.6	1.3	(0.2)	1.16	No	136	6.1
Ellsworth Fund	69.3	2.8	31.7	77.1	2.1	0.9	(15.1)	1.05	No	99	2.7
Putnam High Income Securities	82.3	1.3	26.6	81.1	2.3	1.0	(9.9)	0.85	No	99	3.7
Weighted average		**3.4**	**34.5**	**95.3**	**1.7**	**1.0**	**0.5**	**1.20**		**135**	**6.4**
MSCI World index		**6.7**	**40.5**	**86.7**							

Source: Morningstar, MSCI. Note: TR=total return. The Sharpe ratio is a measure of risk-adjusted return. The ratios we show are calculated by Morningstar for the past 12- and 36-month periods by dividing a fund's annualised excess returns over the risk-free rate by its annualised standard deviation. Net gearing is total assets less cash/cash equivalents as a percentage of shareholders' funds.

The board

The board comprises four directors all of whom are independent: Simon Miller (chairman and chairman of the remuneration and nomination committees), Philip Taylor FCA (chairman of the audit committee), Paul Meader, and Charlotte Valeur Adu.

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