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## Cautious optimism as asset values rebound

*Below, Ivy Asset Strategy Fund's investment team, led by Portfolio Managers Michael Avery and Ryan Caldwell, discuss the Fund's current positioning, the recent rebound in bond and equity markets and current fiscal and monetary policy initiatives. This commentary includes comments made by Ryan Caldwell during a June 9 Ivy Sound Solutions conference call with advisors.*

We think the Federal Reserve is having success restoring values across several asset classes, including bonds and commodities. This gives us a higher level of cautious optimism about credit and global equity markets than we've had in more than a year. However, Fed policies are also generating unintended effects, and the overall U.S. economy remains quite weak.

### Green shoots in the credit markets

There's been a lot of talk in Washington and on Wall Street about green shoots. We've been fairly skeptical because most recent economic data suggest merely a change in the rate of decline rather than actual growth. However, one area where we have seen real improvement is in the credit markets. Credit markets were the epicenter of the nation's financial crisis last year. We believe this is where a recovery was most needed, and in fact has occurred. To us, the credit recovery is visible in the following ways:

- Spreads, or the difference in market yields between Treasuries and a vast array of fixed-income products, have tightened substantially since the beginning of 2008.
- The credit default swap market has regained about 75 percent of its loss since the end of 2007.

**Past performance is not a guarantee of future results.** The opinions expressed are those of the Fund managers and are not meant as investment advice or to predict or project the future performance of any investment product. The opinions are current through June 9, 2009, and are subject to change due to market conditions or other factors. ● Investment return and principal value will fluctuate, and it is possible to lose money by investing. The Fund allocates from 0-100% of its assets primarily among stocks, bonds, and short-term instruments, across domestic and foreign securities. International investing involves additional risks, including currency fluctuations, political or economic conditions affecting the foreign country, and differences in accounting standards and foreign regulations. These risks are magnified in emerging markets. ● With regards to fixed income securities in which the fund may invest, these are subject to interest rate risk and, as such, the net asset value of the fund may fall as interest rates rise. ● Because the Fund may concentrate its investments, the Fund may experience greater volatility than an investment with greater diversification. ● The Fund may use short-selling or derivatives to hedge various instruments, for risk management purposes or to increase investment income or gain in the Fund. These techniques involve additional risk, as short selling involves the risk of potentially unlimited increase in the market value of the security sold short, which could result in potentially unlimited loss for the fund, and the value of investments in derivatives may not correlate perfectly with the overall securities markets or with the underlying asset from which the derivative's value is derived. ● Investing in physical commodities, such as gold, exposes the Fund to other risk considerations such as potentially severe price fluctuations over short periods of time and storage costs that exceed the custodial and/or brokerage costs associated with the Fund's other holdings. ● These and other risks are more fully described in the Fund's prospectus.

**Investors should consider the investment objectives, risks, charges and expenses of a fund carefully before investing. For a prospectus containing this and other information for the Ivy Funds, call your financial advisor or visit us online at [www.ivyfund.com](http://www.ivyfund.com). Please read the prospectus carefully before investing.**

# Ivy Asset Strategy Fund

Thinking Beyond Boundaries

## PORTFOLIO PERSPECTIVES | JUNE 2009

- Corporate bonds have gained almost 50 percent back from their cyclical lows, while equities (as measured by the S&P 500 Index) have only recovered about 40 percent.
- Corporate bonds and the credit default swap market have outperformed the U.S. equity market so far in 2009, a trend that became more pronounced during the past few weeks.

The reopening of U.S. and global credit markets and a renewed ability of companies to issue debt is helping business sustain capital spending and/or refinance existing obligations. Such issuance can be viewed as the proverbial fertilizer for economic growth.

As credit markets have opened up, investor risk appetite has increased, and we think this is a major reason why we have seen such a sharp spike in Treasury yields (and decline in long-term Treasury prices) in recent weeks. Yes, increased inflation concerns are an important part of the story, but the bond market is also seeing a rotation out of Treasuries into corporate credit. As the long end of Treasury market has backed up in yields, we've seen tightening across the board in spreads from municipals all the way down the quality spectrum to CCC-rated high yield corporate bonds.

*"In our opinion, equities based on free cash flow yield are much more attractive than investment grade bond issues at this point."*

### China's growing currency clout

Outside the U.S., we think one of the most important developments over the past month is China's effort to use its currency in trade negotiations and as an alternative denomination for global bonds. In our view, China has taken important steps toward creating a more convertible currency.

China has recently implemented currency swap agreements with Argentina, Brazil and Taiwan. This is important for Chinese manufacturers who have historically only been able to trade in U.S. dollars. With these new swap lines in place, Chinese manufacturers will be able to source business in their local currency, which we think is important for overall economic growth and flexibility. Meanwhile, leading Chinese bankers have been talking about floating Chinese-currency denominated debt in both the U.S. and Europe.

While the Chinese very publicly have said that they are supportive of the U.S. dollar and they are supportive of holding a large U.S. Treasury position, to us their actions this spring show that they are trying to do things to start to diversify away from the U.S. dollar.

### Equity exposure increased; cash down to 9 percent

Within Ivy Asset Strategy Fund's equity portfolio, we hope to capitalize on China's economic growth rebound and renewed long-term growth in Asia generally. Over the past several weeks, we have increased the Fund's overall net equity exposure to about 45 percent of the portfolio (as of May 31, 2009). This positioning includes S&P 500 Index put contracts (the right, but not the obligation, to sell the index at a specified price by a specific date in the future) amounting to about 20 percent of the portfolio. At the same time, we have sharply reduced cash to about 9 percent of the portfolio (as of May 31), from 32 percent as of March 31, 2009.

Compared to the U.S., Asian households not only generally have healthier balance sheets, but enjoy rising incomes, and we think are more likely than not to increase their use of financial leverage. Major Fund holdings continue to include Chinese financials and companies that provide better health care, better education, telecom services, property, plus a variety of consumer themes. Over the past month, we also removed a hedge on our China exposure by not renewing a futures contract on Hong Kong's Hang Seng Index.

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### Technology may fuel recovery

On a sector basis, one area where we have increased equity exposure relative to our historical positioning is information technology. Our global exposure as of May 31 was about as high as it has been since the end of the late 1990s. Our single largest holding is Qualcomm (2.9 percent of net assets as of March 31, 2009 and third largest equity holding). If you look across world markets, technology has been one of the best performing sectors on a year- to-date basis in our view. We believe the sector has the potential to help lead the world out of the global recession, particularly in China, where we are seeing things such as a build out of 3G telecom networks.

Among other asset classes, the Fund's gold bullion and overall bond position are slightly lower than two months ago (at approximately 16 percent and 11 percent of net assets as of May 31, respectively, compared to 17 percent and 13 percent as of March 31). We haven't sold many positions, but have been deploying new Fund cash flows into equities.

### Profit recovery potential favors equities

Given the amount of spread tightening we've seen in the investment grade bond market, we are considering reducing our bond exposure as 2009 progresses. As we think about stocks versus bonds, we see that many companies appear to enjoy a lot of opportunity to grow earnings. In fact, we believe there is as much potential operating leverage built in among S&P 500 companies as we've seen in history. So we feel any revenue growth uptick is going to be a fairly strong catalyst for earnings growth. Generally speaking, we think revenue growth is going to be slow for many companies. However, if we are wrong, you may see a very rapid profit recovery. It's one of the things we think about as far as the equity market's potential upside. On the downside we are very closely watching the credit market. In our opinion, equities based on free cash flow yield are much more attractive than investment grade bond issues at this point.

Despite a rise in gold prices to more than \$950 an ounce recently as the U.S. dollar has fallen and oil prices have rebounded, we expect to maintain our gold position. We still see gold as a beneficiary of two long-term trends:

- other currencies moving away from a U.S. dollar peg and
- inflationary U.S. monetary policy initiatives.

The majority of the Fund's fixed-income exposure (excluding cash) comes from investment grade U.S. credit. The credit quality of this portfolio (excluding cash) is very high with an average quality of A minus. We try to have exposure to many facets of the fixed income world without taking on too much interest rate risk. Hence, the effective duration of the fixed income portion (excluding cash) of the portfolio is 2.5 years. The yield on this portion of the portfolio is now just over 6 percent, which compares to about 8.5 percent a few months ago, a volatile time when the market seemed to view the whole bond market as toxic.

# Ivy Asset Strategy Fund

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## Why Ivy Funds?

Ivy Funds is an exceptional combination of investment managers that offers global reach and capabilities to advisors and their clients. Ivy seeks to enable its fund shareholders to remain comfortably committed to their long-term goals. We are:

**Proven:** We're part of an organization whose roots date to 1937, with an investment style emphasizing participation in positive markets and, especially, seeking to manage risk.

**Focused:** We do our own work, believe in our own research and act on our own ideas. Our steady approach is guided by a belief in fundamentals over fads.

**Constant:** We say what we mean, and do what we say. What we value most, and remember every day, is the trust that we have earned, and must continue to earn, from our shareholders.

The Ivy Funds are managed by Ivy Investment Management Company and distributed by its subsidiary, Ivy Funds Distributor, Inc.



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