TwentyFour
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Fund Commentary | 30 April 2024

TwentyFour Corporate Bond Fund

This Commentary is a marketing communication for professional UK investors only

Market Commentary

April was a more difficult month for markets, with the 'higher-for-longer' sentiment strengthening, as continued strong macroeconomic data, combined with stubbornly high inflation readings, pushed global yields higher. Treasury yields, which had been slowly moving higher so far this year, rose sharply in response to the strong data, with 10-year yields spiking from 4.2% at the start of the month, to finish just shy of 4.7%, with these moves echoed by UK and European government bonds. The outlook for rate cuts also changed significantly once again, with just one cut now expected from the Federal Reserve (Fed), when between two and three cuts were expected for the year at the start of the month, and almost six cuts were expected at the beginning of the year – this optimism has faded markedly. The higher rates also, finally, negatively impacted on equity markets, with most indices falling by between 3.5% and 4.5%, albeit from near record high levels.

The tone was set by the US at the start of the month, with ISM Manufacturing and Prices Paid Data coming in stronger than the consensus, followed by strong Job Openings and Labor Turnover Survey (JOLTS) and factory orders data. While ISM Services data was weaker than expected, it was followed by employment data pointing firmly to a strong economy, with a 303k non-farm payroll print, compared to an expectation of 214k, and average hourly earnings remaining unchanged at high levels. When inflation data came in hotter than expected, for both headline and core readings, the rates selloff gathered pace and most Treasury bulls seemed to throw in the towel on any significant cuts this year. In light of the strong data, and inflation that was proving to be stickier than expected, Fed officials also began to guide markets towards fewer cuts, with most emphasising the need to be patient "until inflation was moving sustainably towards 2%".

The data in Europe during the month was more mixed, with core inflation continuing to decline, and, although services PMIs continued to show strength, manufacturing PMIs remained in contractionary territory. Importantly, however, and although euro rates weakened in sympathy with US Treasuries, there seems to be consensus from European Central Bank (ECB) officials that data supports a rate cut in June, and markets still expect between two and three cuts by year-end. Similarly, in the UK, economic data was mixed but generally weak. However, inflation continued to fall, and Bank of England (BoE) officials, including governor Andrew Bailey, seemed confident that this trajectory will continue and support rate cuts later this year. However, despite hopes of cuts to come, gilts continued to give back some of the aggressive rally at the end of last year.

Although macroeconomic data in the US remained robust, there were signs of weakness in various segments, with small businesses reporting continued struggles due to high inflation and tight financial conditions. In addition, small businesses reported much lower hiring expectations, almost the lowest reading in a decade, highlighting that although the job market remained tight, higher rates are taking a toll. Subprime delinquencies and defaults for credit cards and auto loans also continued to increase, suggesting that excess savings have been extinguished, for less affluent segments at least.

April also saw an increase in idiosyncratic risks, especially in the high yield sector, as a number of businesses hired advisors to advise on their capital structures. Altice France reversed an announcement it made last year to use the proceeds of sales of non-core businesses to reduce their leverage, and instead tried to force bond holders to the negotiating table and to include them in the deleveraging process by haircutting the bonds. Although the companies in question were already trading at distressed levels, and these actions are not symptomatic of the market, it highlights the impact that higher yields are having on companies that over-levered on low yields during the post-Covid era of quantitative easing.

Portfolio Commentary

With pressure on government bond markets during the month, the Fund was down -1.73% for the month after fees, compared to the benchmark return of -1.83%, generating alpha of +10 basis points (bps). Year-to-date, this takes Fund returns to -0.14%, compared to the benchmark return of -1.64%, strong outperformance of +150bps.

Attribution for the month shows strong performance in relative terms from financials, especially banks. For example, banks held in the portfolio returned -0.72%, compared to a loss of -1.08% from the benchmark, generating +10bps of relative contribution. Similarly, the insurance sector also saw outperformance versus the benchmark, returning -1.45% versus -1.83%.

Utilities saw very strong outperformance, returning -0.24% at the portfolio level, compared to -2.20% from the benchmark, generating +9bps of contribution alpha, with the focus on shorter dated hybrid utilities protecting capital to a greater extent.

Underweight positions in sectors such as consumer discretionary, consumer staples, materials and healthcare also helped the Fund to outperform, with these benchmark sectors returning between -2.53% and -2.25% respectively, lower returns than the portfolio average.

Having de-risked the credit portfolio in early Q2 2023 due to concerns about the regional banking crisis in the US potentially spilling over into volatility in Europe (which are coming to the fore again in 2024), plus concerns about the lagged impact of significant rate hikes in 2022 leading to economic slowdowns and even ultimately contractions, our portfolio managers (PMs) kept a lower level of beta and credit spread duration than the benchmark throughout most of last year, and this has continued into early 2024. Interest rate duration, however, was significantly increased in 2023 compared to 2022, although a slight bias towards yield curve steepening was retained. In February, and further in March and April, duration was further increased to lock in some of the outperformance versus benchmark, given the rise in yields seen so far in 2024. As such, the portfolio's duration is the closest to benchmark in many years, reflecting the large-scale rise in yields seen globally in 2022, in the first three quarters of 2023 and at the start of 2024.

Market Outlook and Strategy

With the Fed, BoE and ECB now appearing to be at terminal rates, the large risks to capital from duration risk have ended – but the significant yield curve inversion in rates curves still makes very long-dated credit look especially expensive, even allowing for the potential for rate cuts later this year which may take yield curves back towards historic levels of steepness. As such, a modestly lower-than-average interest rate duration profile is still warranted. However, our PMs remain concerned that increasing unemployment rates across the US, UK and especially Germany signal worsening GDP data to come – and recession risks, in the views of our PMs, both remain significant and are not fully priced into non-financial spreads. Therefore, a lower beta credit stance is still warranted.

As such, we believe the combination of lower-than-benchmark duration (-0.25 years versus benchmark) and higher average yield, with high average credit quality, is the best way to address the likely volatility in the broader market we expect over the next few months while still producing a solid income. This stance is designed to maximise the breakeven yield as much as possible within the constraints of the Fund, meaning, with a yield of around 5.75% and a duration of 5.75 years, the breakeven yield is exactly +100bps, which provides more protection against rising yields than the benchmark.

In these markets, we appreciate having access to portfolio managers is more important than in 'normal' times. Therefore, we would encourage you to reach out to your sales contacts and set up meetings with our PMs to go through anything you would like in more detail.

					Annualised			
Cumulative Performance	1m	3m	6m	1y	3y	5y	10y	Since Inception*
GBP I Accumulation	-1.73%	-0.12%	7.82%	6.46%	-3.48%	-0.04%	N/A	1.77%
iBoxx GBP Corporate Bond Index	-1.84%	-0.78%	6.53%	5.15%	-4.01%	-0.40%	N/A	1.62%

Discrete Performance	YTD	2023	2022	2021	2020	2019	2018	2017	2016	2015	2014
GBP I Accumulation	-0.14%	9.09%	-17.70%	-1.55%	7.56%	9.73%	-2.26%	7.21%	8.48%	N/A	N/A
iBoxx GBP Corporate Bond Index	-1.64%	9.70%	-18.37%	-3.19%	8.63%	11.03%	-2.20%	5.01%	11.83%	N/A	N/A

Past performance is not a reliable indicator of future performance. The performance figures shown are in GBP on a mid-to-mid basis inclusive of net reinvested income and net of all fund expenses. Performance data does not take into account any commissions and costs charged when shares of the fund are issued and redeemed. The value of an investment and the income from it can fall as well as rise as a result of market and currency fluctuations and you may not get back the amount originally invested. *Inception date 15/01/2015.

Key Risks

- Limited participation in the potential of single securities
- Success of single security analysis and active management cannot be guaranteed
- It cannot be guaranteed that the investor will recover the capital invested
- Derivatives entail risks relating to liquidity, leverage and credit fluctuations, illiquidity and volatility
- Interest rates may vary, bonds suffer price declines on rising interest rates
- High-yield bonds (non-investment-grade bonds/junk bonds) may be subject to greater market fluctuations, risk of default or loss of income and principal than higher-rated bonds
- The Fund's investments may be subject to sustainability risks. The sustainability risks that the Fund may be subject to are likely to have an immaterial impact on the value of the Fund's investments in the medium to long term due to the mitigating nature of the Fund's ESG approach
- The Fund's performance may be positively or negatively affected by its sustainability strategy.
- The ability to meet social or environmental objectives might be affected by incomplete or inaccurate data from third-party providers
- Information on how environmental and social objectives are achieved and how sustainability risks are managed in this Fund may be obtained from **www.twentyfouram.com/responsible-investment**

Fund Managers

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Further information on fund charges, costs and other important information pertaining to the fund can be found in English and free of charge on the fund pages of our website and/or in the relevant offering documents available at www.twentyfouram.com/document-library