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TwentyFour
ASSET MANAGEMENT

Monthly Commentary | 29 October 2021

Market Commentary

October was a challenging month for credit, as volatility in rates weakened investor sentiment. Conversely, the S&P 500 index was up 6.9%, and the Eurostoxx 50 was up +5.0%, supported by primarily strong earnings releases. The iTraxx Xover index was wider by around 11bp, and key rates markets saw front-end yields move higher over the month.

Central bank rhetoric and the subsequent move in rate yields were the key focus, with the Bank of England and gilts market stealing the limelight as the market moved forward its expectations of a rate hike by the end of this year. The new Bank of England chief economist Huw Pill stated that inflation could rise higher than the central bank's 2% target and implied that the November committee meeting was "live" regarding a move in monetary policy. This followed comments from Governor Bailey that he expected inflation to last for longer, and the bank would have to act accordingly. In response, the market is now pricing in a rate hike at the BoE's next meeting on November 4th, followed by another hike February 2022 meeting. As a result, the five-year gilt yield widened by nearly 20bp over the month, finishing at 0.83%.

Inflation continued to be the key focus for fixed income participants as the evidence mounts that it may not be merely transitory as some central bankers maintain. Rising energy prices, supply chain disruptions, shortage of labour, infrastructure and transport problems and record lead times on raw materials are all compounding, leading to a continuation of high inflation prints from the summer, thereby fuelling a steady increase in average hourly earnings. In addition, US CPI beat expectations, coming in at +5.4% YoY and +0.4% MoM, which added weight to the discussion that the Fed would have to hike rates earlier than expected. Likewise, German CPI moved from 4.1% to 4.5%, with PPI in Germany now running at a staggering 14.2%.

Earnings season kicked off as usual with the US banks. Overall, earnings numbers were solid. However, there were some key misses; Apple, noticeably disappointed versus expectations, with the company citing "larger than expected supply constraints" as a factor, adding to the argument that supply chain disruptions will likely persist well into next year.

There were various other economic data releases over the month. China Q3 GDP was a small miss versus expectations at 4.9% (5.0% consensus), as was US Q3 GDP (2.0% vs consensus 2.6%). US non-farm payrolls also disappointed, coming in at 194k for September versus expectations of 500k whilst average hourly earnings ticked higher to +0.6% month-on-month and the unemployment rate was lower at 4.8% as the labour force participation rate declined.

Portfolio Commentary

In complete contrast to the aggressive steepening seen in September, October saw a reversal with the UK yield curve, in fact, flattening more than the steepening the month before, as the reality of likely base rate hikes in the UK became more priced in.

As such, the relative outperformance in September of +75bp was reversed, with the fund underperforming the index by -67bp for October, returning -0.47% (30th September to 1st November).

Year to date, CBF is now down -1.75% (after fees) versus the benchmark of -3.32%, outperformance of +1.57% or +157bp.

The portfolio's focus on the highest breakeven sectors, and then within that, the highest breakeven bonds, has helped ameliorate some of the worst capital losses seen in the most interest rate sensitive sectors year to date. As such, the Healthcare and Utility sectors have had the largest benchmark losses for the year, being down some -4.98% and -4.43%, respectively, given high average durations and low average yields. In contrast, our preference for shorter-dated hybrid (non-senior) Utilities meant losses in that sector were less than a fifth of the benchmark, at -0.77%. Similarly, other low yielding and high duration benchmark sectors such as Senior Telecoms bonds also had sizable losses, declining -3.59%.

The volatility in rates, and to a more limited extent in credit, has helped the headline portfolio yield, which is now 2.34%, versus 2.00% for the iBoxx benchmark – whilst we maintain an underweight duration stance versus that benchmark with also a continued expectation of slightly steeper sovereign yield curves to come – our beta remains under 1.0 at 0.86.

The broader fixed income market still appears expensive to us, especially for senior non-financials, and we continue to favour financials, hybrids and secured bonds instead. Further, we especially believe that stock selection will continue to be a primary source of finding additional value and income whilst maximising break even protection to keep capital preserved as much as possible.

Market Outlook and Strategy

With the large government aid programs likely needing many years of increased government bond issuance, the outlook for sovereigns will be challenging to say the least – again suggestive of credit outperformance over the longer term. On the face of it, we expect steeper government yield curves due to the twin pressures of increased government bond issuance, with the secondary pressures coming from the prospects of modestly higher inflation that increased fiscal policy may bring. These factors will likely lead to higher government bond yields than we see today, but this will be no straight-line move. More than ever, risk-off hedges in government bonds will be a crucial part of CBF's toolkit to protect capital and provide some welcome lower correlations to risk.

Ultimately this means we think markets are likely to exhibit further volatility for some time yet. By focusing on higher conviction, short and medium dated IG, and keeping positions restricted to our best ideas only (that is why we limit portfolio line items to a maximum of around 100 bonds), we believe we can continue to generate some of the best risk-adjusted returns in the corporate bond sector, whilst keeping capital preserved to a greater degree than others in periods of volatility.

Rolling Performance	30/10/2020 - 29/10/2021	31/10/2019 - 30/10/2020	31/10/2018 - 31/10/2019	31/10/2017 - 31/10/2018	31/10/2016 - 31/10/2017
GBP I Accumulation	1.65%	4.34%	8.43%	-0.04%	6.29%

The performance figures shown are in GBP on a mid-to-mid basis inclusive of net reinvested income and net of all fund expenses. Past performance is not a reliable indicator of future performance. Performance data does not take into account any commissions and costs charged when shares of the portfolio are issued and redeemed. *Inception date 15/01/2015.

The Team

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Jack Daley
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Johnathan Owen
Portfolio Management, industry experience since 2018.

COVID-19 Dealing Instructions

To better facilitate working environments during Covid-19, investors will additionally be able to subscribe into and redeem from the Corporate Bond Fund using email (**TwentyFourTAInstructions@ntrs.com**). Please note, only one instruction per email will be accepted. Please refer to our website at **www.twentyfouram.com** for further information.

Key Risks

- **All financial investment involves risk. The value of your investment isn't guaranteed, and its value and income will rise and fall. Investors may not get back the full amount invested.**
- Past performance is not a reliable indicator of future performance, and the Fund may not achieve its investment objective.
- Fixed income carries two main risks, interest rate risk and credit risk: (1) Where long term interest rates rise, there is a corresponding decline in the market value of bonds and vice versa; (2) Credit risk refers to the possibility that the issuer of the bond will not be able to repay the principal and make interest payments.
- Typically, sub-investment grade securities will have a higher risk of issuer default, and are generally considered to be more illiquid than investment grade securities.
- Overseas investment will be affected by movements in currency exchange rates.
- The Fund has the ability to use derivatives in order to meet its investment objectives. This may magnify gains or losses.

Further Information and Literature: TwentyFour Asset Management LLP

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Further information on fund charges and costs are included on our website at www.twentyfouram.com

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