TwentyFour
ASSET MANAGEMENT



TwentyFour

# Corporate Bond Fund

**This Commentary is a marketing communication for professional UK investors only**

## Market Commentary

October was a firmer month in risk assets, and with no obvious catalyst it could largely be described as a relief rally after a very weak September. The S&P 500 was up by 8% over the month and the Eurostoxx 50 returned 9%, while in credit, the iTraxx Crossover index tightened from 641bp to 555bp. Risk-off assets meanwhile drifted wider, with the exception of UK Gilts, which rallied after the news that Rishi Sunak was going to replace Liz Truss as UK prime minister.

Once again all eyes were on the US CPI inflation print, and once again it came in above expectations. The headline year-on-year and month-on-month numbers of 8.2% and 0.4% respectively were both higher than market consensus, but unlike previous periods this year when we'd seen similar beats, there was no sharp sell-off in risk assets and instead equities and credit rallied – perhaps a sign of just how much bad news was priced into markets. The US labour market offered mixed messages as the number of job openings fell by over 1m, but job creation remained strong with an increase of 288k in non-farm payrolls. The unemployment number also fell from 3.7% to 3.5%, helped by a decline in the participation rate, in more evidence that the labour market remains very tight.

The CPI print did lead to a cycle-high yield on the 10-year US Treasury of around 4.25%, aided by FOMC members pointing towards a 'raise and hold' policy. For example, Atlanta Fed President Raphael Bostic stated: "I am not advocating a quick turnaround toward accommodation. On the contrary." Treasury yields did come off their highs however as the Wall Street Journal's Nick Timiraos – a journalist considered well connected at the Fed – reported that officials would be debating a slowdown in hikes and a change in rhetoric after November's FOMC meeting.

European government bonds remained fairly flat across October, after an initial sell-off was reversed following the European Central Banks's October 27 policy meeting. The expected 75bp hike was followed by a dovish-leaning press conference from ECB president Christine Lagarde, where a reference to "several" more hikes was notably absent but the lagged effect of monetary policy and an increase in the probability of recession were both discussed.

UK Gilts outperformed in October after Liz Truss was replaced by Rishi Sunak as prime minister. Sunak and Jeremy Hunt, the new Chancellor, reversed almost all of Truss' mini-Budget policies which had destabilised the UK market. Furthermore, Sunak appears generally regarded as a safe pair of hands thanks to the markedly different economic policies on which he ran against Truss in the previous Conservative leadership campaign, which has reassured markets and saw 10-year Gilt yields tighten from 4.08% to 3.50% over the month.

Elsewhere in October there was some weakness in Chinese assets as President Xi Jinping began his third term by surrounding himself with loyalists, which made investors nervous about future shifts in domestic and foreign policy. In addition, OPEC+ decided to reduce output by 2m barrels per day to help prop up oil prices in the face of anticipated faltering global demand.

## Portfolio Commentary

The recovery in Gilts in October helped the Fund generate positive returns of 3.69% after fees. While this has been very welcome, Fund returns were behind benchmark returns of 4.63% for the month, with the benchmark helped by the significant Gilt rally at the long end of the curve. By contrast, the Fund, having been underweight the long end, struggled to match the returns of the benchmark such that year-to-date alpha remains positive but is not as large a margin as at the end of September.

YTD the Fund is now down -19.81% net of fees versus the benchmark return of -20.30%, outperformance of 49bp.

In contribution terms, the biggest driver of underperformance in October came from being underweight long dated senior telecoms, which returned 6.37% within the benchmark, contributing 38bp at the index total return level against 8bp at the portfolio level.

The second biggest driver of relative underperformance was being underweight the consumer sectors of discretionary and non-discretionary, which bounced strongly to return 4.68% and 5.34% respectively, contributing 21bp between them at the index level; that was versus no contribution from the portfolio as we have been very deliberately out of consumer-facing stocks for some time, given large headwinds.

In financials, our lower duration average positioning resulted in lower total returns than the benchmark, but our overweight to banks and insurers helped offset that to some degree, such that the total financials benchmark contribution was 132bp versus 126bp for the portfolio.

Utilities contributed 26bp to the benchmark, being up 5.48%, while the portfolio contribution was 19bp.

## Market Outlook and Strategy

Despite the rally in October, in both yield and spread terms, the Fund remains at attractive levels compared to recent years. The average yield is now 6.72% (versus 5.86% for the benchmark), with average spreads at 306bp versus the benchmark's 226bp and portfolio duration of -1yr versus the index. The managers continue to think that given the extreme moves higher in yields this year, it is prudent to keep relative duration at that -1yr level compared to -2yrs earlier in 2022. Clearly, risks to higher yields remain, but with a terminal rate in the UK now priced in at 4.75%, the managers believe we are getting closer to the top of the rate cycle before slowing GDP growth takes over the narrative from mostly inflation. The beta of the Fund overall is now very close to the benchmark, and at 0.97 is the closest we have been for some time.

In our view, the yield levels now available are pricing in not just a downturn but severe economic distress. The managers do not think this is warranted in a high quality portfolio such as this, which has for some time already been positioned away from deep cyclicals, high street retail and those sectors which have limited or no pricing power.

Ultimately this means we think the valuation argument should attract buyers. The uncertainty surrounding global inflation and policy responses means we cannot call the absolute bottom of the credit market just yet, but on any reasonable timeframe the yield opportunities now predict decent positive returns over the medium term.

| Rolling Performance | 29/10/2021 - 31/10/2022 | 30/10/2020 - 29/10/2021 | 31/10/2019 - 30/10/2020 | 31/10/2018 - 31/10/2019 | 31/10/2017 - 31/10/2018 |
|---|---|---|---|---|---|
| GBP I Accumulation | -19.76% | 1.65% | 4.34% | 8.43% | -0.04% |
| iBoxx GBP Corporate Bond Index | -20.38% | 0.55% | 4.66% | 10.34% | -0.14% |

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.

## 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.

## Fund Managers

Chris Bowie
Partner, Portfolio Management, industry experience since 1992.

Diana Chiu
Portfolio Management, industry experience since 2009.

Gordon Shannon
Partner, Portfolio Management, industry experience since 2007.

Graeme Anderson
Chairman, Portfolio Management, industry experience since 1986.

Jack Daley
Portfolio Management, industry experience since 2011.

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.


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


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