

# Vontobel Fund - TwentyFour Sustainable Strategic Income Fund

This Commentary is a marketing communication for professional UK investors only

## Market Commentary

The month of March was dominated by key central bank meetings and market participants dissecting every economic data point to anticipate when central banks would start their easing cycles. The overall risk sentiment was supported by the market's view that the start of the easing cycle for the Federal Reserve (Fed) was only a few months away.

The European Central Bank (ECB) was the first of the major central banks to hold its meeting in March. While the main rate was left unchanged, officials struck a dovish tone and revised their inflation forecast downwards. Core inflation is now expected to be 2.6% this year, 2.1% in 2025 and 2.0% in 2026; therefore, ECB officials are pointing to core inflation rates being back at their target rate in the near future. The near-term growth forecast was also revised down to 0.6%. Overall, the market started to increase the probability that the ECB could be first of the key central banks to start its cutting cycle. Over the month, the market pricing of a cut for the ECB's June meeting increased.

In the US, March was a heavy month for data releases. First, the jobs report depicted a more nuanced environment; while the non-farm payroll report showed continued strength in the economy (275k versus 200k expected), the unemployment rate rose to 3.9% (its highest level since December 2021) and average hourly earnings slowed to +0.1% (versus +0.2% expected). Subsequently, the US Consumer Price Index (CPI) report indicated that inflation remained sticky: headline CPI came in at a six-month high of +0.44% month-on-month, and core CPI was at +0.36%, which also meant that annual core CPI was above expectations at +3.8% (versus +3.7% expected). This was further confirmed by the Producer Price Index (PPI) as headline numbers came in at +0.6% (versus +0.3% expected).

Despite the stronger readings for inflation, the Fed meeting still struck a slightly dovish tone. They made no changes to the base rate, and the revised dot plots showed that the median dot for 2024 was unchanged, with three cuts for the year expected. The Fed's economic projections were revised higher, with real GDP growth revised up from 1.4% to 2.1%, core Personal Consumption Expenditures (PCE) inflation up to 2.6%, and unemployment revised lower to 4.0%. February core PCE deflator which was published at the end of the month was more supportive however (+0.26% versus +0.3% expected); and although it remained somewhat elevated, it eased considerably after the +0.45% January print. In the face of the mixed data, market pricing for a Fed cut in June was lower over the month.

The Bank of Japan also held an important meeting where it lifted its key short-term interest rate from -0.1% to a range of 0% to 0.1%, its first hike since 2007. Despite a set of measures making monetary policy more restrictive, the tone remained dovish, which led to the yen making a 34-year low against the US dollar towards the end of the month.

The positive risk sentiment was broad based with equity indices making new highs and credit spreads tightening, with European and US high yield spreads down to their lowest since January 2022. In rates, price action was mixed over

the month but generally yields finished tighter; the 10-year German bund yield finished the month 11 basis points (bps) lower, the 10-year US Treasury yield declined by 5 bps, and the 10-year UK gilt yield was 19 bps lower.

## Portfolio Commentary

Markets remained busy with strong primary activity. Despite a month filled with central bank meetings, investment-grade (IG) issuance remained elevated ahead of Easter. The primary market was met with healthy demand from investors, often leaving limited premium in new deals. The European high yield market enjoyed a revival with a healthy pipeline building up for April. The portfolio managers (PMs) selectively participated in deals where they believed there was value but remained disciplined on price tightening. The secondary market was also active, and the team looked to trade some relative-value switches to optimise the portfolio.

With regards to the rate positioning of the Fund, the overall duration remained stable. The PMs made some minor changes to the composition of the government bonds allocation with a small switch-out of the 10-year US Treasury for 10-year bunds.

March enjoyed a broad base rally, with rates and credit indices posting positive returns. On the government bonds side, the UK gilt index outperformed, posting a return of 1.8%, followed by Euro rates (+1%) and US Treasuries (+0.6%), and the positive rates environment was naturally supportive for IG corporates; US IG was up by 1.2%, sterling IG was up by 1.9% and European IG index was up by 1.2%. Strong risk sentiment led to healthy returns for the iBoxx Contingent Convertible (CoCo) Index, which was up by 2.2% on the month. US and European high yield indices enjoyed returns of 1.2% and 0.4% respectively.

The Fund returned 1.7% over the month. For sector contributions, the biggest contributors for the month were Additional Tier 1s (AT1s), followed by insurance. The detractors were European high yield, followed by hedging.

## Market Outlook and Strategy

The market will remain focused on comments from central banks and economic data to assess the likely timing of upcoming rate cuts. The continuing strong economic data has increased the likelihood of cuts being delayed. Although the soft-landing narrative for the US may keep rates higher for longer, the PMs are happy to maintain a long-rates position which they feel offers attractive insurance against a negative shock and provides good flexibility within the portfolio. The market will turn its attention to the Q1 reporting season which will provide clues on the strength of the economy. In this context, the PMs will look to continue taking advantage of the current market conditions to do relative-value switches to try to enhance the portfolio.

## Key Risks

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- Limited participation in the potential of single securities
  - Investments in foreign currencies are subject to currency fluctuations
  - 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
  - Investment universe may involve investments in countries where the local capital markets may not yet qualify as recognised capital markets
  - Money market investments are associated with risks of a money market, such as interest rate fluctuations, inflation risk and economic instability
- The Sub-Fund's investments may be subject to sustainability risks. The sustainability risks that the Sub-Fund may be subject to are likely to have an immaterial impact on the value of the Sub-Funds' investments in the medium to long term due to the mitigating nature of the Sub-Fund's ESG approach
  - The Sub-Funds' 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 Sub-Fund may be obtained from [Vontobel.com/SFDR](http://Vontobel.com/SFDR)

## Fund Managers

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