Vontobel Fund – TwentyFour Absolute Return Credit Fund

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Market Commentary

Ongoing volatility characterised risk and rates markets during May due to comments from central bankers, data prints and other market moving headlines. Ultimately, the S&P 500 finished just -0.55% lower for the month after falling ~8% intra-month. Meanwhile, the EuroStoxx 50 posted returns of 1.53%. In fixed income, the US 10 year Treasury yield tightened by 14bp, whilst both Gilts and Bund yields finished higher. Finally, the Xover widened by 15bp during the month. The Federal Open Market Committee met at the beginning of May and raised rates by 50bp. The members also signalled that the Fed would start reducing the size of its balance sheet in June. Fed chair Jerome Powell also stated Fed members were not considering 75bp rate hikes, which initially drove a rally in risk markets. However, as the market digested the number of upcoming hikes and the prospect of quantitative tightening, risk assets quickly sold off, accompanied by a sell-off in US Treasuries, with the 10-year yield touching 3.20% intraday. With the release of the US CPI report, which surprised to the upside by showing 8.3% year-on-year inflation against expectations of 8.1%, and headlines of Chinese lockdowns continuing, volatility remained during the beginning of the month.

As fears of a hard landing in the US grew, US Treasuries began to rally from intra-month wides, with investors speculating that the Fed would find it difficult to push through as many hikes as previously thought. Risk assets continued to underperform on growth concerns. The only bright spot for investors was the return of correlations, with US Treasuries finally behaving as a risk-off asset class. The release of the FOMC minutes reinforced the strength in rates, calming investors' fears over the hawkishness of the Fed. While the minutes confirmed the consensus of two 50bp hikes at the June and July meetings, they also indicated that a pause could follow later this year, helping to support the 10-year US Treasury yield, which rallied to 2.75%. Additionally, bullish comments from Brian Moynihan (Bank of America CEO) and Jamie Dimon (JP Morgan CEO) on the strength of the US consumer and the attractiveness of credit in general aided credit markets and resulted in a relief rally as month-end approached.

Elsewhere, the Bank of England (BoE) raised rates by 25bp as expected, but its forecast for a contraction in UK growth during 2023 caused Gilts to rally. However, this reversed towards the end of the month, coinciding with the UK Government's fiscal support package and a refocus on the high levels of UK inflation. There was no European Central Bank (ECB) meeting, but a strong consensus has now formed that net purchases from its Asset Purchase Programme will stop by July, and the ECB will begin their hiking cycle at the July meeting. As a result, the market has priced four 25bp hikes for the Eurozone during 2022.

Portfolio Commentary

ARC was down -0.27% after fees for the month, taking year to date returns to -2.92% net of fees, which compares with the ICE/BAML 1-5 Year Sterling Corporate Bond index, which was down -4.48%, outperformance of +156bp. The last nine months have seen significant pressure on the front end of global yield curves as markets deal with persistent inflation and the expectation of multiple rate hikes across developed markets.

The outperformance versus broader short-dated investment grade credit is the result of actions the portfolio managers took at the end of summer 2021, which included: reducing portfolio duration from 2.4 years to 1.7 years by the end of 2021; taking the portfolio's high yield weighting down; doubling our government bond exposure from 8% to 16%, and lastly increasing the exposure to bonds maturing within 0-12 months to more than one-third of the Fund. At the same time, the team sold the Fund's entire stock of two-year US Treasuries, buying two month and three month US Treasury Bills in their place and purchasing some one-year Gilts to reduce our US$ yield curve exposure. The managers also maximised the Fund's floating rate exposures to the ABS sector.

Nevertheless, the absolute losses in the Fund recently have been uncomfortable. So the only positive story here is the flip side of the capital moves: the portfolio yield, which has risen to 3.80% from 1.49% at the end of July last year – coincident with the duration reducing from 2.4 years to 1.7 years over that period, and the government bond weighting doubling. Moreover, that rise in yield of 2.3% means the total portfolio yield is now higher than on the day of launch in August 2015 – highlighting just how far bond yields have adjusted in 9 months.

Given the large volume of bonds maturing in the Fund throughout 2022, the portfolio managers expect to gain the ability to improve the portfolio yield further without taking any more credit risk by simply reinvesting the near term cashflows in a mix of one to three-year bonds and possibly three to five-year bonds if global yield curves have adjusted enough and become steep enough, to warrant taking the duration of the Fund up a little by the time of each maturity. Further, if the portfolio managers are happy to reduce the government bond weighting, they can improve the yield of the Fund more. The current higher yield of the Fund than previously, and the likely further improvement of the yield as we go through 2022, should set up a far better return environment for the portfolio.

In these times, liquidity is, of course, crucial. Therefore, the portfolio managers have temporarily decided to keep liquidity slightly higher than usual, with around 10% in our liquidity bucket.

In terms of attribution, the Fund's AT1 positions contributed most to performance with returns of 0.03%. Meanwhile, its Hybrids and ABS positions acted as the biggest detractors, with performance of -0.17% and -0.05% respectively.

Market Outlook and Strategy

The near term end of extremely cheap money and expanding central bank balance sheets, now coupled with geopolitical risk, has led to sharp moves in all risk assets so far in 2022 – and we expect volatility to continue to some extent throughout this year. However, at the front end of yield curves, a lot of bad news has been priced in already: multiple hikes remain priced for the US, and multiple hikes remain priced into the UK curve by the end of 2022, taking all short dated bonds with them.

Given the above, the markedly higher yield on the Fund and the prospect of yield-enhancing trades throughout 2022, the portfolio managers expect the Fund's return profile to improve from here. However, we are not necessarily calling the bottom of the market for short dated credit just yet. For now, we prefer to keep the Fund's beta lower than usual until we see more clarity on the expected tightening in financial conditions that will ultimately be the story of 2022.

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

Rolling Performance	31/05/2021 - 31/05/2022	29/05/2020 - 31/05/2021	31/05/2019 - 29/05/2020	31/05/2018 - 31/05/2019	31/05/2017 - 31/05/2018
Class G	-3.09%	4.15%	1.42%	2.02%	1.65%

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 28/08/2015.

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.
- The Fund can invest in structured credit products or asset-backed securities (ABS). The issuer of such products may not receive the full amounts owed to them by underlying borrowers, which would affect the value of the Fund. Credit and prepayment risks also vary by tranche which may affect the Fund's performance.
- The Fund has the ability to use derivatives, including but not limited to FX forwards, for hedging purposes only (EPM). This may magnify gains or losses.

Fund Managers

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

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Past performance is not a reliable indicator of current or future performance. Performance data does not take into account any commissions and costs charged when shares of the fund are issued and redeemed, if applicable. The return of the fund may go down as well as up due to changes in rates of exchange between currencies. The value of the money invested in the fund can increase or decrease and there is no guarantee that all or part of your invested capital can be redeemed.

For definitions of the investment terminology used within this document please see glossary at: https://twentyfouram.com/glossary

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