EdenTree R&S Sterling Bond Fund

Q2 2024 Commentary

PERFORMANCE

	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Fund (B Class)	0.4%	1.5%	11.8%	-6.0%	3.6%	26.3%
R&S Sterling Bond Benchmark*	-0.1%	-0.1%	9.7%	-11.3%	-4.0%	25.8%
IA £ Strategic Bond	0.5%	1.5%	8.8%	-3.1%	6.6%	26.2%
Sector Quartile	2	2	1	3	3	3

Source: Morningstar. Figures compared on a Bid to Bid basis with Net Income Reinvested

YIELDS**

Distribution	*4.52%*
Underlying	*3.97%*
Historic	*4.36%*

Source: EdenTree.

MARKET REVIEW

Global bond yields rose as market participants pared back expectations of interest rate cuts amidst higher-than-expected core inflation. Whilst further declines on headline consumer prices were welcomed, central bankers remained cautious in guiding towards loosening monetary policy in 2024. The Bank of England held its benchmark interest rate at 5.25%, albeit with some committee members voting for a cut in June. The 10-year yield began the quarter at 3.93% and rose to 4.40% in May before ending the quarter at 4.17%.

Similarly, the US Federal Reserve also maintained its benchmark interest rate at 5.5%, unchanged since last July. Officials remain data-dependent and see less urgency to cut interest rates with economic growth proving robust and services inflation more persistent. The European Central Bank's Governing Council cut its benchmark interest rate by 0.25% but was less certain about further reductions until policymakers were more confident on the inflation outlook vis-à-vis its 2% target.

Credit risk premia ticked up briefly in June largely in response to the announcement of the snap parliamentary elections in France, whilst the asset class remained supported by improved risk sentiment. Lower quality investment grade debt underperformed as credit spreads widened with the carry component of total returns proving crucial, notably for high yield. Corporate debt outperformed sovereign debt despite lagging as the quarter drew to a close.

PERFORMANCE & ACTIVITY

The Sterling Bond Fund's total return outperformed its iBoxx Sterling Non-Gilts index benchmark and marginally lagged the IA Strategic Bond sector of the period. The Fund's credit selection more than offset the adverse contribution from its greater interest rate sensitivity as underlying gilt yields rose.

Sovereign debt yields were the main driver of returns for the period under review, aided by favourable credit selection in niche holdings including the successful tenders of positions Leeds Building Society PIBs and its WM Morrisons Supermarkets debt securities at significant premia. Whereas some flight to quality occurred as the quarter ended, which boosted the Fund's longer-dated gilt holdings, more meaningful weakness in risky assets has proved elusive.

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Over the quarter, the Fund initiated holdings in Co-Operative Bank 11.75% 2034, UK Treasury 0.625% 2050, Royal London 10.125% perp (2033 call) and also purchased the newly-issued Motability 5.75% 2051. It also added to Bupa 4.125% 2035, John Lewis 4.25% 2034, UK Treasury 4.25% 2049 and UK Treasury 0.875% 2033. The Fund exited holdings in A2 Dominion 3.5% 2028, Mobico 4.25% perp (2026 call) and reduced positions in Hiscox 6.125% 2045 (2025 call), Assura 1.625% 2030 whilst successfully tendering Phoenix 6.625% 2025, WM Morrison 3.5% 2026, WM Morrison 4.75% 2029 and Leeds Building Society 13.375% PIB at premia.

OUTLOOK

The decline of global interest rates from cyclical peaks is apparently underway, with major central banks including the European Central Bank and the Bank of Canada having enacted initial benchmark rate cuts. Despite an increasing focus on core price movements, the progress on deceleration in headline inflation somewhat justifies a looser monetary policy stance particularly as labour market indicators suggest a softer employment outlook. Thus far, robust economic growth has accorded policymakers time to assess the restrictiveness of financial conditions.

Services sector growth has continued to confound expectations, with companies' profitability thus far better able to weather cost and wage increases. Services price inflation has therefore proved 'sticky', with associated upside risks warranting caution in context of forward-looking price stability. In the run up to key leadership contests, fiscal discipline also merits close attention for incoming governments around the world. The higher for longer interest rate environment arguably raises the significance of debt sustainability and deficit reduction proposals. Slower execution of such plans will at best be given short shrift if not penalised with sovereign rating downgrades. Both outcomes are precursors for higher risk premia and could further cascade into lower credit ratings for related sectors including banks. Whilst a benign outlook for corporate debt defaults prevails, more highly-indebted and often speculated grade issuers are resorting to debt restructurings to refinance. We therefore continue to maintain a bias towards high quality credits offering attractive risk-adjusted yields.

We remain vigilant in seeking out opportunities to add to high quality credits, scrutinising the robustness of business models and cash flows to ensure adequate compensation for risk. With the interest rate hike cycle pivoting, we have incrementally added to interest rate sensitivity and are positioned for moderately longer relative duration. Having reduced cash, we continue to rely on higher credit quality to enhance overall portfolio liquidity whilst preserving capital.

PERFORMANCE DISCRETE	12 Months to 30/06/2020	12 Months to 30/06/2021	12 Months to 30/06/2022	12 Months to 30/06/2023	12 Months to 30/06/2024
Fund (B Class)	3.5%	6.5%	-11.7%	-4.8%	11.8%
R&S Sterling Bond Benchmark*	6.4%	1.7%	-13.1%	-6.9%	9.7%
IA £ Strategic Bond	3.1%	6.7%	-10.8%	-0.2%	8.8%
Sector Quartile	3	2	3	4	1

Source: Morningstar. Figures compared on a Bid to Bid basis with Net Income Reinvested.

Past performance is not necessarily a guide to future returns.

*As the Fund has greater exposure to corporate bonds over gilts we compare the Fund's performance to the iBoxx Sterling Non-Gilt Overall Total Return Index, however the portfolio manager is not bound or influenced by the index when making investment decisions

**The Distribution Yield reflects the amounts that may be expected to be distributed over the next 12 months as a percentage of the mid-market share price of the fund as at the date shown. The Underlying Yield reflects the annualised income net of expenses of the fund (calculated in accordance with relevant accounting standards) as a percentage of the midmarket share price of the fund as at the date shown. Both Yields are based on a snapshot of the portfolio on that day. The yields do not include any preliminary charge and investors may be subject to tax on distributions. The Distribution Yield is higher than the Underlying Yield because the fund's expenses are charged to capital. This has the effect of increasing the distributions for the year and constraining the fund's capital performance to an equivalent extent. The Historic Yield reflects distributions declared over the past twelve months as a percentage of the share price.

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