Marketing Communication

Nedgroup Investments Global Strategic Bond Fund

Core, Nimble, Proven

In my youth, I used to love a good rollercoaster, although the attraction has diminished with age. These days, I am more focused on the ups and downs of the bond market. After above-normal returns in recent months, October brought bonds back down to earth with a bump. I'm not sure I will go back to Alton Towers any time soon, but I am looking forward to further bond market gyrations.

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Performance and markets

October was the worst month for global bonds since early 2022 - most of the drawdown came from the rates markets. Credit, like most risk assets. cared little about elections or value it seemed. An increase in term premium in the treasury market – the amount investors require to own government bonds above economic factors – rose as Trump election odds increased. The fund entered the period with less duration than the market, adding incrementally into the sell- off. We bought too soon. However, a near 70 basis point rise in core ten-year US yields moved the market from expensive to cheap and should stand the fund in good stead to make progress once election dust settles.

Returns to (%, US$)	Fund[1]	Index[2]
October 24	-1.71%	-1.35%
Since Inception	4.54%	3.67%

Past performance is not indicative of future performance and does not predict future return.

Key performance drivers

Over the month, the fund returned -1.7%, and the index -1.4. The majority of returns came from falling capital values as yields rose in response to central bank action. Underperformance largely came from a reversal of previous positive trades such as steepening government curves and outperformance of western markets. An unprecedented collapse in European swap spreads helped drive excess returns within credit.

The excess return has been attributed roughly as follows using a top-down methodology:

Total excess return for the month: -36bps		
Contribution		**Positioning comments**
Duration	**0bps**	• Started around 4.75 years, added incrementally toward 6 years. • Initial gains offset as yields moved to top end of range.
Curve	**-20bps**	• Approx. 1-year long between 0-10 years, curve flattened around 20bp. • Curve reversed sharply following US September jobs data. • "Trump trade" pushed curve too flat, costing performance.
Geography	**-26bps**	• Approx. 1 year "long" US versus other markets. • The short Canada position made money in absolute terms but was offset by the US. • Asian markets (zero fund exposure) outperformed.
Asset allocation	**10 bps**	• Allocation to credit generated excess returns with higher beta credits outperforming. • European credit performed well as swap spreads collapsed.
Credit sector/ security selection:	**0bps**	• Our sector allocation performed, with financials and non-cyclicals driving returns. .

Positioning recap and outlook

Total portfolio: Yield = 5.1% (% exc. futures), Duration = 5.7 years, ESG rating: A

Rates (weight = 25.6% (60.2% inc. futures), yield = 4.3%, duration = 3.4 years)

Positioning in sovereign bonds	Fund	Expected fund range	Index
	25.6%	**30 - 40%**	**53%**
Investment perspectives	**Valuations[3]** Huge rise in bond yields moves from rich to cheap, especially with gentle downtrend in G7 CPI.	**Fundamentals** Data has been mixed, but not supportive of G7 recession. Attention pre US election remains on labour market.	**Technicals** Investors moved from long to short, positive to negative, hence technicals are now supportive.

- Rates markets gave up all recent gains given data was better than many expected.
- Around half the G7 bond sell-off was down to previously overbought markets and decent data.
- The rest was related to market concern on fiscal stimulus with the focus on US and UK (Trump and Reeves).

Credit (IG: weight = 54.4%, yield= 5.2%, duration = 5.1 years)
(HY: weight = 15.8%, yield= 7.0%, duration = 3.0 years)

Positioning in credit	Fund	Expected fund range	Index
	Investment grade: 54.4%	**20-60%**	**19%***
	High yield: 15.8%	**20-30%**	**0%**
Investment perspectives	**Valuations** After a brief wobble, valuations remain expensive, with A/BBB spread back to its tightest in 10 years. Some cyclical premia has begun to be priced in.	**Fundamentals** Solid fundamentals remain but European cyclicals are suffering from margin compression with one of the longest manufacturing recessions in living memory.	**Technicals** Technicals remain strong, However, demand has operated on a 4-6 week lag. Lower all in yields may potentially dampen demand at a time that supply picks up.

*"Pure" IG credit. Add in Structured, Agency and EM and the index has 47%

- European swap spreads collapsed as significant high quality investment grade issuance in previous months coupled with a rates' sell off created the perfect backdrop for tightening spreads.
- Volatility within rates yet again failed to impact credit spreads. If anything, higher all in yields attracted inflows into the asset class.
- Autos continue to generate profit warnings with surprisingly little knock-on effect to other manufacturing sectors performance.

Portfolio changes and where next

We incrementally added duration into the sell off favouring US, Germany and more recently, Australia. We continue to avoid peripheral Europe and most of Asia. UK yields rose significantly and with gilts paying around 20bp more than US again, we were happy to remove our index underweight. Within credit, we continued to trade up in quality as stretched valuations meant we gave up very little in terms of spread. Overall, bond yields look too cheap for prevailing fundamentals and should provide a solid base for positive total return, over the coming 12 months.

What to watch out for next month

Rates: It's all about the US elections. G7 data is not strong enough to warrant current yield levels. The market is rightly concerned at expansionary fiscal policy and the potential that has to curb rate cuts. We would use any material bounce and curve flattening to tactically reduce existing positions.	**Credit:** With spreads trading at multi-year tights, we will continue to look for opportunities to trade up in quality. Political uncertainty may give us an opportunity to change tact if credit markets finally react.

Contribution and positioning information as at 30 September 2024. Yield shown is yield to worst and indicative. Source: Nedgroup Investments

1 Fund returns are in US$ based on Class D Accumulation. Source: Morningstar

2 Index returns in US$ based on Bloomberg Global Aggregate Total Return Index (hedged to US$). Source: Morningstar

3 Valuations are based on a medium-term outlook. For government bonds, this is determined by market returns (beta) relative to inflation/inflation expectations and real growth. For corporates, this is determined by adjusting expected excess returns for risk (default and volatility). Valuation based strategic positioning may be adjusted for shorter term technical or fundamental economic factors.

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