



# Global Fixed Income

March 2024 review

## Liontrust GF Strategic Bond Fund



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The Liontrust GF Strategic Bond Fund returned 1.9%\* in US dollar terms in March. The average return from the EAA Fund Global Flexible Bond (Morningstar) sector, the Fund's reference sector, was 1.1%.

### Market backdrop

March was a big month for central bankers. The Bank of Japan finally ended its negative interest rate policy and yield curve control, but this is unlikely to be the start of a rate hiking cycle. In line with expectations, both the Federal Reserve and Bank of England held rates steady – there are nuances for both entities which I expand upon below. Economic activity data has been robust; inflation data, whilst heading in the right direction, still has further to go particularly with respect to sticky services inflation. This has led the bond market to push out the timing and reduce the quantity of rate cuts expected. The Bank of England may well join the European Central Bank by cutting in June but the Fed is more evenly poised; the risk bias is towards waiting until later meetings.

In a seven-two vote, the Bank of Japan finally ended its negative interest rate policy after eight years. Rates were hiked for the first time in 17 years, to a policy rate range of 0.0% to 0.1%. The recent strong wage data has given Governor Ueda the excuse he needs to exit the most unconventional policies. On that front, yield curve control has been terminated; the policy had not been relevant for the last six months anyway. Unless economic activity significantly picks up in Japan, this is unlikely to be the start of a series of rate hikes. This does not preclude a little more tightening as monetary policy would still be loose, but I view the most likely motivation behind this month's move as Ueda getting rid of unconventional policy rather than beginning a rate hiking cycle.

The Bank of England's Monetary Policy Committee (MPC) voted by a majority of eight to one to maintain rates at 5.25%. Haskel and Mann both dropped their hawkish dissent, whilst Dhingra continued to vote for a cut. Even with the hawkish dissenters now voting in line, there clearly remains a range of opinions on the MPC with some requiring greater evidence that inflation's persistence has been beaten before committing to a shift in monetary policy stance. The MPC has included a new sentence that it will "...continue to consider the degree of restrictiveness of policy at each meeting". Putting aside the blatant truism, I take this as a signal that cuts will be seriously considered at each meeting. Unless there is some new shocking economic data, it is highly unlikely

enough MPC members will change their votes by the May meeting. Further evidence of slowing wage growth and reducing services inflation is required to make the majority vote for a cut. Greater data availability, especially around April's wage rises and indexlinked price increases, makes June my central case for when the first cut occurs, with a reasonable tail risk this slips to the August meeting.

The Federal Open Market Committee (FOMC) held Fed funds rates steady in the 5.25% to 5.50% range. The statement was close to a carbon copy of the prior month. The most important sentence in the statement is still "...the Committee does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent". The main focus was on the Summary of Economic Projections (SEP) and Powell's press conference. The SEP has the core PCE inflation forecast for 2024 revised up from 2.4% to 2.6% which is a marking-to-market of the inflationary data already seen year-to-date, with the outlook for the rest of the year forecast to be in line with prior projections. Marrying this with the jump in the 2024 real GDP forecast from 1.4% to 2.1% implies some supply side improvement assumptions must have been made. These could be productivity related, as well as due to immigration easing labour market pressures. Importantly, core inflation forecasts for the time horizon beyond 2024 were left unchanged.

The dot plot of FOMC participants' estimates for interest rates was also revised. For 2024 there are still three rate cuts anticipated by the Fed – the dots hung on to the 75bps of easing but it would only take one or two members to change their stance to take this down to 50bps. 2025 and 2026 projections show less easing than prior forecasts is now anticipated. For the Fed members to gain the "greater confidence" they need that inflation is sustainably falling, further progress will need to be seen on services inflation; explicitly I believe there will be greater focus on supercore inflation measures with a little less emphasis on shelter inflation. There is unlikely to be enough improvement in the data by early May, so my best estimate is that the Fed cuts rates for the first time in this cycle in June; there remains the risk that this is pushed out until the late July FOMC meeting.

As a reminder, whilst it is interesting to work out when rates are going to be cut, it matters far more to bond investors that the conditions are in place for policy loosening and how much rates will eventually be cut by than the exact start date of the easing cycle. As restrictive monetary policy continues to work through the economies, the Fed and Bank of England can head back towards neutral base rates: somewhere in the 2-3% region. I believe it is therefore a good time to be locking in attractive bond yields.

## Fund positioning and activity

### Rates

There were only minor adjustments made to rates positioning during March. The Fund has just over 7.5 years of duration exposure. This is split between 3.5 years in the US, -0.6 years in Canada, 1.0 years in New Zealand, 2.3 years in the Eurozone, and 1.4 years in the UK. We continue to prefer short-dated and medium-dated bonds; the net duration exposure in the 15+ year maturity bucket is zero.

### Allocation

Whilst the total yield on corporate bonds is attractive, credit spreads are expensive. The Fund has just under 40% exposure to investment grade credit, 41.2% in bonds and minus 2.5% in a risk reducing overlay using a liquid credit default swap index; this is below our 50% neutral level. Similarly, high yield exposure is below our 20% neutral at 16%; the weighting in bonds is 25.1% and there is an 8.8% risk reducing overlay.

This aggregate underweight position in credit gives the Fund a lot of risk budget to buy once credit spreads widen. We are targeting adding exposure to corporate bonds during a period of volatility as opposed to anticipating a lurch higher in defaults and the permanent destruction of capital.

### Selection

Some of last year's laggards continued to rebound from oversold levels. A strong rally was seen in Heimstaden Bostad and CPI Property's bonds. We continue to carefully manage the position sizing given the volatility in the bonds; we did trim a little and reinvested the proceeds into Aroundtown's debt. The latter announced an exchange and tender for some of its bonds, including the one we purchased, just after the end of March so our purchase timing was very fortuitous.

Due to expensive valuations, euro denominated long-dated Becton Dickinson bonds were sold. Staying within investment grade, we switched out of some Lloyds lower tier 2 debt in US dollars into a sterling denominated senior bond.

In high yield, the Fund participated in one high quality new issue from Pinewood, a leading independent provider of infrastructure required to produce film and TV content. We liked the fact the credit is supported by rents that are mostly long-term and inflation linked. It has recently expanded out their sites and have pre-let most of the expansion before completion, indicating the level of demand for space, alongside the positive demand for online streaming provides a good tailwind for the credit.

#### Discrete years' performance (%) to previous quarter-end\*\*:

	Mar-24	Mar-23	Mar-22	Mar-21	Mar-20
Liontrust GF Strategic Bond B5 Acc	7.7%	-3.9%	-4.0%	13.2%	-0.4%
EAA Fund Global Flexible Bond - USD Hedged	7.4%	-3.2%	-3.1%	12.7%	-1.9%

\*\*Source Financial Express, as at 31.03.24, total return, B5 share class. Discrete data is not available for ten full 12-month periods due to the launch date of the portfolio (13.04.18). \*Source: Financial Express, as at 31.03.24, B5 share class.

For a comprehensive list of common financial words and terms, see our glossary at: <https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms>

#### Key Features of the Liontrust GF Strategic Bond Fund

Investment objective & policy <sup>1</sup>	The investment objective of the Fund is to maximise total returns over the long term through a combination of income and capital. The Fund will seek to achieve its objective by investing in bond and credit
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	<p>markets worldwide. The Fund invests in a wide range of bonds issued by corporates and governments, from investment grade through to high yield. The Fund invests in developed and emerging markets, with a maximum of 40% of its net assets invested in emerging markets. Investments may be made in "hard" currencies, such as US Dollar, Euro and Sterling, and up to 25% of the net assets of the Fund may be invested in soft currencies, such as those of emerging markets. Where the Fund invests in non-US Dollar assets, the currency exposure of these investments will generally be hedged back to US Dollar. Up to 10% of the Fund's currency exposure may not be hedged, i.e. the Fund may be exposed to the risks of investing in another currency for up to 10% of its assets. The Fund may invest both directly, and through the use of derivatives. The use of derivatives may generate market leverage (i.e. where the Fund takes market exposure in excess of the value of its assets). In addition, the Fund may invest in cash or cash equivalents, such as deposits and Money Market Instruments, for cash management purposes. Within the limits stated above, there are no geographical or economic sector restrictions on the Fund's investments. The Fund has both Hedged and Unhedged share classes available. The Hedged share classes use forward foreign exchange contracts to protect returns in the base currency of the Fund. The fund manager considers environmental, social and governance ("ESG") characteristics of issuers when selecting investments for the Fund.</p>
Recommended investment horizon	5 years or more
Risk profile (SRI) <sup>2</sup>	3
Active/passive investment style	Active
Benchmark	The Fund is actively managed without reference to any benchmark meaning that the Investment Adviser has full discretion over the composition of the Fund's portfolio, subject to the stated investment objectives and policies.
Sustainability profile	The Fund is a financial product subject to Article 8 of the Sustainable Finance Disclosure Regulation (SFDR).

Notes: 1. As specified in the PRIIP KID of the fund; 2. SRI = Summary Risk Indicator. Please refer to the PRIIP KID for further detail on how this is calculated.

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## Key Risks

**Past performance does not predict future returns. You may get back less than you originally invested. We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.**

The fund manager considers environmental, social and governance ("ESG") characteristics of issuers when selecting investments for the Fund.

Bonds are affected by changes in interest rates and their value and the income they generate can rise or fall as a result;

The creditworthiness of a bond issuer may also affect that bond's value. Bonds that produce a higher level of income usually also carry greater risk as such bond issuers may have difficulty in paying their debts. The value of a bond would be significantly affected if the issuer either refused to pay or was unable to pay.

Overseas investments may carry a higher currency risk. They are valued by reference to their local currency which may move up or down when compared to the currency of the Fund.

The Fund can invest in derivatives. Derivatives are used to protect against currency, credit or interest rate moves or for investment purposes. There is a risk that losses could be made on derivative positions or that the counterparties could fail to complete on transactions.

The Fund uses derivative instruments that may result in higher cash levels. Cash may be deposited with several credit counterparties (e.g. international banks) or in short dated bonds. A credit risk arises should one or more of these counterparties be unable to return the deposited cash.

The Fund invests in emerging markets which carries a higher risk than investment in more developed countries. This may result in higher volatility and larger drops in the value of the fund over the short term.

The Fund may encounter liquidity constraints from time to time. Participation rates on advertised volumes could fall reflecting the less liquid nature of the current market conditions.

Counterparty Risk: any derivative contract, including FX hedging, may be at risk if the counterparty fails.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

## Disclaimer

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