Close Sustainable Select Fixed Income Fund

Monthly fund manager update

April 2024

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FUND PERFORMANCE

The Close Sustainable Select Fixed Income Fund returned -1.1% in April, and +0.3% year-to-date (YTD). In comparison, the Investment Association (IA) Sterling Strategic Bond sector returned -1.2% in April, and -0.2% YTD.

The Close Sustainable Select Fixed Income Fund has therefore outperformed the IA sector by +0.6% YTD. It is a 2nd Quartile fund YTD, and a 1st Quartile fund on a 1 year, 3 year and 5 year basis (versus the IA sector).

For readers who missed the March commentary, the Close Sustainable Select Fixed Income fund was also named as, "*the most consistent UK strategic bond fund over the past decade*", and, *"one of the most consistent UK bond funds of the decade across all sectors*" by Trustnet. Close Sustainable Select Fixed Income is the only strategic bond fund to outperform the IA sector in 9 of the last 10 years. More details in the link: **The most consistent UK bond funds of the decade | Trustnet**

MACRO BACKDROP

Newsflow in April was focused on inflation data and Central Bank rhetoric. In brief, inflation expectations rose in the US - but not in the UK or Eurozone - which generally saw expectations of Central Bank rate cuts in the US and UK being pushed into Q3 and Q4 2024 (from Q2 2024).

The Bank of England did not meet in April. However, the BoE held the policy rate at 5.25% on 21 March, and maintained the Quantitative Tightening programme ("QT") at GBP 100bn / year. Futures markets expect 2 rate cuts in the next 12 months, with the first cut to emerge in Q3 2024.

In a sign that rate cuts are edging closer in the UK:

- One member of the MPC voted for a rate cut (after also voting for a rate cut in the February 2024 meeting). This was the first vote for a rate cut since March 2020;
- No members voted for a rate hike. This is the first time no members have voted for a rate hike since September 2021.

The US Federal Reserve did not meet in April. However, the Fed held the policy rate at 5.50% on 20 March, and maintained the QT programme at USD 95bn / month. Futures markets expect 1-2 rate cuts in over the next 12 months, with the first cut to merge in Q4 2024 (a significant push back from expectations of a Q2 20204 rate cut in March).

The European Central Bank held rates on 11 April, and maintained the QT programme at EUR 25bn / month. The Depo Rate was maintained at 4.00% and the Refi Rate was maintained at 4.50%. Futures markets expect up to 3 rate cuts in the next 12 months, with the first cut to merge in Q2 2024.

In the UK, the Composite Purchasing Managers Index (PMI) data improved to 54.0 (Mar-24 = 52.8), while consensus 2024 GDP growth forecasts remained stable at +0.3% (Mar-24 = +0.3%). CPI inflation declined to +3.2% (Feb-24

= 3.4%), while core inflation (i.e. excluding volatile energy and food prices) also declined to +4.2% (Feb-24 = +4.5%). Forecasts indicate inflation will continue to decline to c. +1.8% in Q2 2024. Unemployment increased slightly to 4.2% (Jan-24 = 4.0%.

In the US, Composite PMI data weakened to 50.9 (Mar-24 = 52.1), while consensus 2024 GDP growth forecasts improved to +2.4% (Mar-24 = +2.2%). US CPI inflation increased to +3.5% (Feb-24 = 3.2%) – and forecasts indicate inflation will decline to c. +2.9% in Q4 2024. Unemployment decreased slightly to 3.8% (Feb-24 = 3.9%).

In the Eurozone, Composite PMI data improved to 49.9 (Feb-24 = 49.2), while consensus 2024 GDP growth forecasts remained stable at +0.5%.Eurozone inflation declined to +2.6% (Jan-24 = +2.8%), and forecasts indicate it will continue to decline to c. +2.1% by Q3 2024, albeit forecasts are volatile given ongoing concerns over Russian gas supplies. Unemployment was stable at 6.4%.

PORTFOLIO ACTIVITY

Close Sustainable Select Fixed Income is an active and nimble fund. In February and March, the team sold c. 27% of fund holdings (all longer-dated corporate bonds) at very rich valuations, and rotated proceeds into a combination of shorter-dated 'best ideas' credit, Government bonds and cash.

As a result of the busy trading period in February and March – coupled with very rich valuations in credit markets - April was a very quiet month for the fund. Indeed, the team:

- Maintained cash levels at 15% (earning an attractive rate of 4.5% on cash);
- Bought a 2.5% position in the Hikma 2025 bond (rated BBB-) at an attractive yield of 6.7%;
- Increased Government bond holdings by 2% (to 33% of the fund) in order to maintain fund duration at 4.9 years.

On the portfolio construction side, the yield-to-call is 6.0%; duration is 4.9 years; the average rating of the fund is A+; cash levels are 15%; and the unrated portion of the fund is 4%.

OUTLOOK AND STRATEGY

Fixed Income sub-asset classes:

- **Sovereign bond yields** offer fair value in the UK and US and Eurozone.
- **Sterling Investment Grade** bonds are Rich versus all historical timeframes, with sterling 'BBB' credit spreads at 144bps, versus their 5 year average of 186bps; 10 year average of 185bps; and 20 year average of 218bps.
- **Sterling High Yield** bonds are Rich versus all historical timeframes, with 'BB' spreads at 266bps (5 year average = 372bps; 10 year average = 348bps; 20 year average = 430bps).

In an effort to preserve capital and deliver a good level of monthly income, we continue to seek out the best risk / reward ideas across investment grade, high yield and unrated sectors. We maintain our focus on stock selection reinforced by in-depth credit research.

IMPORTANT INFORMATION

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