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Close Bond Income Portfolio Fund

Monthly fund manager update

June 2019

Performance

The Close Bond Income Fund returned +1.03% in June 2019, and 5.25% YTD. In comparison, the IA Sterling Corporate Bond sector returned +1.34% in June and 6.32% YTD. We remain very conservatively positioned versus the sector (i.e. higher credit quality and lower duration).

Macro backdrop

On the UK macro side, data remained volatile and politics continued to be the main driver of fixed income markets. The two contenders to be the next UK Prime Minister emerged (Boris Johnson and Jeremy Hunt) – with both raising the risk of the UK leaving the EU in October 2019 with ‘no-deal’. Regarding data, GDP growth (for April) fell by -0.4% month-on-month following a busy month of stockpiling ahead of the potential ‘no deal’ Brexit in March 2019. Unemployment remained stable at 3.8%; inflation fell slightly to 2.0% (from 2.1%, which itself was boosted by Easter-related spending); while PMI data was stable month-on-month at 50.9 – with manufacturing continuing to weaken as a result of global trade tensions, while consumer spending kept the services component in positive territory.

In the US, macro data remained relatively strong. The Q1 2019 Annualised GDP growth was revised down slightly to +3.1% (though still a significant improvement on the Q4 2018 reading of +2.2%); inflation decreased slightly to +1.8% (from +2.0). Unemployment remained stable at a very strong 3.6% and average employee earnings fell slightly to a still strong +3.1%. PMI survey data was the weakest for about 4 years, reflecting ongoing concerns around President Trump’s increasingly aggressive trade

policies, which are causing manufacturing weakness across the world

In the Eurozone, data improved on the previous month, but remains weak. GDP growth for 12-months ending in Q1 2019 was confirmed at 1.2%; inflation fell to 1.2% and unemployment improved to 7.6%. PMI survey data also staged a small improvement, with manufacturing remaining very weak, but more than offset by a stronger Services sector. Given ongoing trade tensions and political volatility in the UK (Brexit) and US (Iran, China, immigration rhetoric), the Eurozone now has the strongest PMI survey data of our three core markets.

Portfolio activity

The average rating on the portfolio was maintained at ‘A’, and 50% of fund holdings are in AAA to A- rated bonds. The fund now offers a yield of 2.7% and duration of 5.6 years (2.8 years of which is attributed to our 7.5% holding in long duration UK Gilts). We believe the very strong credit quality of the fund further de-risks the fund from any future volatility.

Outlook and strategy

The first half of 2019 saw bond markets deliver the strongest 6-monthly return since the financial crisis in 2008, and returns were paradoxically strong across all segments, with both long-dated gilts (the ultimate ‘risk-off’ instrument) and High Yield (a ‘risk-on’ instrument) both delivering returns of c. 8%. We do not expect this ‘Goldilocks’ environment to continue. Indeed, sovereign bond yields are trading at, or near, historic lows, and we also believe that spreads are trading slightly rich to fair

value (sterling BBB credit spreads are now 184bps, versus a 5yr average of 184bps; 10yr average of 232bps; and 20yr average of 217bps). In order to ensure capital preservation and deliver a high level of monthly income, we continue to seek out the best risk:reward ideas

across investment grade, unrated and high yield bond sectors while always maintaining our minimum of 80% Investment Grade risk. We continue our focus on stock selection reinforced by in-depth credit research, and continue to favour shorter duration corporate bonds.

Close Bond Income Portfolio Fund discrete performance as at 30 June 2019

	YTD	2018	2017	2016	2015	2014
Close Bond Income Portfolio Fund	5.3%	-2.7%	7.6%	7.2%	1.0%	7.6%
IA £ Corporate Bond	6.3%	-2.2%	5.1%	9.0%	-0.3%	9.8%
IA £ Strategic Bond	6.3%	-2.5%	5.3%	7.3%	-0.2%	6.1%
IA £ High Yield	7.5%	-3.2%	6.1%	10.1%	-0.7%	1.3%

Source: FE Analytics 05.07.2019; all are X Acc share classes; performance is total returns, net of fees with dividends reinvested.

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