Close Brothers Asset Management

For professional adviser use only.
Not for distribution to retail clients.

Close Sustainable Bond Portfolio Fund

Monthly fund manager update

NOVEMBER 2021

ERAN HASSON
Investment Director

FUND PERFORMANCE

The Close Sustainable Bond Fund returned +0.4% in November, bringing the Year to Date (YTD) return to -0.9%. In comparison, the Investment Association Sterling Corporate Bond sector returned +0.9% in November and has returned -1.1% YTD.

The Close Sustainable Bond Fund is focused on risk-adjusted returns and has historically operated with lower duration than the corporate bond sector. As a result, the Fund has outperformed the sector 86% of the time in 'down' markets, and 91% of the time when the sector is down by -25bps or more (since February 2014).

As of 30 November 2021, the Close Sustainable Bond Fund maintained an average credit rating of A-.

MACRO BACKDROP

Newsflow in November 2021 was initially dominated by expected Central Bank actions to tackle inflation. However, the emergence of Omicron as a COVID-19 'variant of concern' over the last week of November presented concerns over potential lockdowns and economic growth, which may mean monetary tightening is delayed – even if inflationary factors persist. On 30 November, Fed Chairman Jerome Powell acknowledged it had become time to stop referring to inflation as "transitory", even if Omicron poses risks to the Fed's employment and inflation forecasts.

In the UK, November Composite Purchasing Managers Index (PMI) remained broadly flat at 57.7 (October was 57.8) as Manufacturing data strengthened to 58.1 (+0.3 Month on Month [MoM]) and Services data weakened to 58.6 (-0.5 MoM). The 2022 GDP consensus forecast was downgraded from 5.3% to 5.0%, and the anticipated data regarding Omicron's characteristics might warrant further revisions in the future. Inflation is now forecasted to be 3.6% in 2022, markedly higher than the 2.6% print in October.

In the US, November Composite PMI dropped to 56.5 (-0.9 MoM), with Manufacturing data strengthening to 59.1 (+0.7 MoM) and Services data weakening significantly to 57 (-1.7 MoM). The 2022 GDP forecast was therefore revised from 4.1% down to 3.9%, and 2022 inflation expectations were revised up from 3.0% to 3.7%.

Data in the Eurozone was the most benign for rates and credit. November Composite PMI strengthened to 55.8 (+1.6 MoM), with Manufacturing data stable at 58.4 (+0.1 MoM) and Services data stronger at 56.6 (+2.0 MoM). GDP expectations for 2022 were not downgraded as much as in the UK and the US (down to 4.2% from 4.3%). 2022 inflation expectations strengthened to 2.3% from 1.7%, while forecasts for 2023 remain comfortably below the ECB's 2% target.

PORTFOLIO CHARACTERISTICS

The average credit rating on the portfolio remained strong at 'A-', with 52% of the fund's holdings in AAA to A- rated bonds.

The fund now offers a yield of 2.1% and duration of 6.4 years. We believe the very strong credit quality of the fund helps de-risk it against potential future volatility.

OUTLOOK AND STRATEGY

All Fixed Income sub-asset classes continue to appear rich:

- **Sovereign bond yields** remain low across the US, UK, and Eurozone.
- **Sterling Investment Grade** bonds are rich versus all historical timeframes, with sterling 'BBB' credit spreads at 141bps, versus their 5yr average of 172bps; 10yr average of 206bps; and 20yr average of 215bps.

- **Sterling High Yield** spreads are rich versus history, with 'BB' spreads at 304bps (compared with the 5yr average of 318bps; the 10yr average of 366bps and the 20yr average of 436bps).

In an effort to preserve capital 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. We maintain our focus on stock selection reinforced by in-depth credit research.