

# Close Sustainable Bond Portfolio Fund

## Monthly fund manager update

AUGUST 2022

### FUND PERFORMANCE

The Close Sustainable Bond Fund returned -3.2% in August, bringing the year-to-date return to -13.6%. In comparison, the Investment Association (IA) Sterling Corporate Bond sector returned -4.7% in August, has declined -14.2% YTD.

The Fund is focused on risk-adjusted returns and has historically operated with lower duration than the corporate bond sector. As a result, it has historically outperformed the sector c. 83% of the time in 'down' markets, and c. 83% of the time when the sector is down by -25bps or more (since February 2014).

### MACRO BACKDROP

Newsflow in August was dominated by macro data and geopolitical events - with markets volatile on the outlook for gas and electricity markets in Q4 2022 - and the potential impact power prices will have on inflation and global GDP growth. Against the backdrop of volatile data, central banks remained active in their bid to tame inflation:

**The Bank of England** raised rates to 1.75% (from 1.25%) and clearly signalled a further rate hike in September 2022. Additionally, it was announced that Quantitative Tightening would begin from September 2022, while macro forecasts were updated - indicating inflation would reach 13.3% and the UK would enter a c. 15 month recession.

**The Federal Reserve** (Fed) did not meet in August but continued to increase the level of Quantitative Tightening (unwinding the USD 9trn of debt on the Fed's balance sheet).

**The European Central Bank** did not meet in August either, but language remains geared towards further rate hikes following their July decision to raise rates for first time in 11 years – taking the Depo Rate to 0.0% (from -0.50%), and the Ref Rate to 0.5% (from 0.0%).

In the UK, Composite Purchasing Managers' Index (PMI) data declined slightly – but remained in positive territory at 50.9 (July's reading was 52.1). Consensus 2022 GDP growth forecasts increased to +3.5% (from +3.4% in July), albeit they are significantly lower than March (+4.0%) and January (+4.5%). Inflation forecasts remain elevated, and end of year 2022 Consumer Prices Index (CPI) inflation is now forecast to reach +12% (likely peaking in October 2022). Unemployment data remained strong at just 3.8%.

In the US, Composite PMI data weakened to 45.0 (July = 47.7), while 2022 consensus GDP growth forecasts declined to +1.7% (July = +2.0%). US inflation forecasts for the end of 2022 remained stable at +7.3%, while unemployment strengthened further to just 3.5%.

In the Eurozone, Composite PMI data weakened to 49.2 (July = 49.9), while consensus 2022 GDP growth forecasts increased to +2.8% (July = 2.7%). End of year 2022 inflation expectations increased significantly to 8.6% (July = 7.9%; March = 5.1%) given ongoing concerns over Russian gas supplies. Unemployment remained stable at 6.6%.

### PORTFOLIO CHARACTERISTICS

The average credit rating on the portfolio remained strong at 'BBB+' and 35% of fund holdings are in AAA to A- rated bonds. The Fund offers a yield of 6.3% and duration of 4.7 years. We believe the very strong credit quality of the fund may de-risk it from future volatility.

### OUTLOOK AND STRATEGY

Fixed Income sub-asset classes:

- **Sovereign bond yields** are volatile and reactive to macro data – but remain rich across the UK, US and Eurozone
- **Sterling Investment Grade** bonds are cheap versus all historical timeframes, with sterling 'BBB' credit spreads at 243bps, versus their 5yr average of 175bps; 10yr average of 190bps; and 20yr average of 215bps
- **Sterling High Yield** spreads are cheap versus history, with 'BB' spreads at 491bps (5yr average = 333bps; 10yr average = 345bps; 20yr 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 sustainable investment grade sectors. We maintain our focus on stock selection reinforced by in-depth credit research.

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**IMPORTANT INFORMATION**

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