Manager
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Capital is at risk. Please read full risk warning at the end of this document.

Monthly Commentary: October 2024

High Yield Fixed Interest

- Invests in sterling-denominated high yield bonds issued by companies in the UK and overseas
- Large and experienced team identify strongest risk-adjusted opportunities across industries, sectors and geographies
- Robust risk management underpins all stages of the investment process

Market News

The European High Yield market, represented by ICE BofA European Currency High Yield Constrained Index (GBP), returned +1.2% in September – the 5th consecutive month of positive returns for the asset class that has taken year-to-date performance to +7.9%.

Risk assets were buoyed mid-month by central bank easing as we move firmly into a cutting cycle. The ECB cut their deposit facility rate by a further 25bp to 3.75% as Eurozone inflation dissipates and attention turns to addressing weak growth prospects for the region. The US Federal Reserve cut by 50bp to 4.75-5%, slightly catching a market split between a 25bp or 50bp cut off guard. Initial concerns that this signalled a deteriorating labour market, having followed a weak nonfarm payroll print for August and over 800k of negative revisions to prior months' numbers, were somewhat assuaged by Chairman Powell's comments that the cut represented a 'recalibration' and he pushed back against the idea of additional 50bp cuts. Risk assets nonetheless rallied into month-end, helped by a wide-ranging set of monetary easing measures announced by the Chinese government. In the UK, the Bank of England held rates at 5% having cut 25bp in August with UK Consumer Price Inflation (CPI) still expected to rise modestly into year-end and both services CPI (+5.6%) and private sector wage growth (+4.9%) remaining elevated. Governor Bailey did latterly suggest in an interview that the BofE could become 'a bit more aggressive' if inflation cooled.

The Real Estate sector again drove performance and returned over 6% in the month as the market has grown increasingly comfortable with the sector's ability to withstand higher interest rates and worst-case insolvencies are likely to be avoided. Many of the Real Estate names in the index began the year at very depressed levels and balance sheet restructurings felt inevitable, so the rebound has been astonishing. The Automotive sector underperformed in September (it was the only sector with a negative return contribution) after a raft of profit warnings towards the end of the month. We heard bellwether OEMs VW, BMW, Mercedes and Stellantis (owner of Fiat Chrysler and Peugeot Citroen) all warn on earnings citing weak demand, from China and for EVs in particular. We saw further warnings from the automotive suppliers Forvia, ZF Friedrichshafen and Standard Profil in the month.

Investment Outlook

Whilst we are mindful that European High Yield spreads have tightened a long way from the mid-2022 peak of 600+, we see scope for spreads to tighten further towards 300 in the medium-term as inflation concerns continue to ease and central banks steadily cut rates. We do think that near term risks to growth have increased as a result of central banks having held rates at elevated levels, as evidenced by weakness in the Automotive sector, and therefore have a cautious short-term outlook, but ultimately think that any material macro weakness would be met with more

Data source: Abrdn and Morningstar

aggressive rate cuts which would then be positive for High Yield spreads. Rate cuts will have obvious tailwinds for the market as corporate issuers will face lower interest and refinancing costs, and as such we would expect the default rate to remain contained. The asset class has benefitted from a positive technical backdrop for some time with steady inflows into a shrinking market and we expect inflows to continue with rate cuts as money exits short-term products to reach for a higher yield.

Risk Warnings

Capital is at risk. The value and income from investments can go down as well as up and are not guaranteed. An investor may get back significantly less than they invest. Past performance is not a reliable indicator of current or future performance and should not be the sole factor considered when selecting funds. Our funds invest for the long-term and may not be appropriate for investors who plan to take money out within five years. The fund has exposure to bonds, the prices of which will be impacted by factors including; changes in interest rates, inflation expectations and perceived credit quality. When interest rates rise, bond values generally fall. This risk is generally greater for longer term bonds and for bonds with perceived lower credit quality. The Fund invests in other currencies. Changes in exchange rates will therefore affect the value of your investment. Bonds that produce a higher level of income carry greater risk that the issuer will not be able to pay the income or repay the capital at maturity. In certain market conditions some assets may be less predictable than usual. This may make it harder to sell at a desired price and/or in a timely manner. In extreme market conditions redemptions In the underlying funds or the Fund itself may be deferred or suspended. The insolvency of any institution providing services, such as safekeeping of assets or holding investments with returns linked to financial contracts (known as derivatives), may expose the Fund to financial loss. The Fund may enter into various financial contracts (known as derivatives) in an attempt to protect the value of the Fund's assets or to reduce the costs of investing, although this may not be achieved. All or part of the fees and expenses may be charged to the capital of the Fund rather than being deducted from income. Future capital growth may be constrained as a result of this.

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