Rathbone Ethical Bond Fund Bryn Jones – Lead Fund Manager

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An Ethical Bond fan said A phenomenal year this year.

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We've had some great returns.

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We've performed extremely well through some of the credit selection that we've had.

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One example is Virgin Money where we had a huge overweight this year and and we saw a significant upside in that name when Nationwide took it over.

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We've also got some strong legacy debt in there which continues to be bought out by insurance companies and you know, that's been an addition to the performance of the fund.

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Also, we've traded duration really well.

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You know, interest rate expectations have not moved in a straight line.

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And you know, the start of this year when interest rates looked like they weren't going to be cut as aggressively as people priced in, we had an underweight duration.

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And you know, we timed it quite well.

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And we, we increased the duration of the ethical bond funds into the summer.

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And that's been a great 'cause we've started to see interest rates fork and expectations of interest rates fall.

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When interest rate expectations are rising, we've been underweight duration.

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We use a lot of technical analysis like Fibonacci and relative strength indicators to give us an indication technically when we can enter or exit the gilt market and in particular green gilts, which is what we use for the ethical bond fund.

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And we've been able to use those technicals quite well.

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But also tying them into the fundamental analysis about macroeconomic research, inflation, growth expectations and all those things put together have meant that we've been able to trade duration quite well in the fund this year.

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So the ethical bond funds has got a bit of a kind of barbell at the moment.

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So the long duration assets that we hold in the fund of all very high quality.

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So these would be like green gilts and supranationals.

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And as you come down the curve, you sort of move into sort of AA and then into single A.

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And as you get down to the front end of the curve, we're in some really good quality triple B credits with loads of risk adjusted return.

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So kind of what we tried to do with portfolio is and I think you know, many updates to to our clients over the year, we've been talking about this, we've been saying we've been trying to create a bond portfolio that's going to perform in most scenarios.

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If there's no landing, we're going to perform really well because we've got a lot of credit down the front end and that gives you loads of yields.

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In a soft landing, we're going to get some protection from our duration assets.

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And of course in a harder landing, having good break even duration at the front end means that you're protected from interest rate and spread widening.

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And that's that's important.

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What we tried to achieve this year.

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And I think you know, what we've been able to do is, is an example of putting that those stretches in place.

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The path for UK interest rates is not certain.

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If we look at sort of G7 economies, most economies have been cut in rates.

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The Federer are about to cut rates, ECB income rates, Switzerland, Canada as many countries being current rates.

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UK you know has not been that aggressive in kind rates, you know, we still got a reasonable growth rate.

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Our unemployment rates are very low and inflation if it comes into check is also been you know, fairly stable as well.

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So I don't think the Bank of England are going to be as aggressive as perhaps some other central bankers.

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So the path for interest rates whilst is downwards, we might not see as aggressive rate cuts in the UK as we do in other economies.

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Well, in particular, credit markets have been very liquid.

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So I mean, you know, you quite often hear that there's liquidity in corporate bonds and that's not necessarily been the case.

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You know, we see new issues come to the market and there's been a huge amount of demand for those.

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And secretary markets have been quite robust and the volume of deals going through market makers and brokers still remains quite high.

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And so, so credit markets have been quite liquid.

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As to of government bond markets, you know we haven't seen a major liquidity premium.

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I suspect maybe in Manic Monday when we saw the reversal of the N carry trade, there was a bit of a liquidity, but that was kind of a microcosm in one day.

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Generally through the year, liquidity has been pretty robust.

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Credit spreads have been a little bit choppy this year, but the general direction has been downwards.

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Credit spreads have been sort of tied into a Fed policy.

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Every time we have a Fed meeting and they expect interest rate cuts, then you know, credit spreads are going to come tighten.

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And when the Fed didn't deliver through the summer and the early part of of the autumn, credit spreads started to rise.

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And you know, each time we come to a Fed policy meeting, there's an expectation of cuts.

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You know, cuts going to be good for credit, it's going to be good for equity and say we see a rally what we're looking for in the in the markets, it spreads actually to tighten a bit further after the first Fed policy cuts.

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And that will probably give us a little bit of opportunity to start de risking some of the portfolio in the old sort of adage of sort of being fearful when everyone's being greedy.

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You know, recession is a is a probability.

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Recession is also a higher probability when you've had interest rate hikes, you know, you go back through history, 198019771994 many periods after interest rate policy hikes from the Fed.

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At some point you get a recession.

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But, you know, going back through looking from when the first Fed hike was to when we get recession, we're kind of now entering the danger.

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And so recession could be a probability.

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But it's all kind of based on a few things.

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You know, you need to see unemployment rise.

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You need to see wage inflation disappear, and you also need to see excess savings disappear.

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You know, sometimes people say, well, we can borrow out of this, but you know, householders and corporates can't.

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Interest rates are higher and credit card rates are all time high.

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So it really is based around employment at the moment.

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And when you look at a lot of the data and you know, the markets reacting to employment data quite significantly because it is that kind of last sort of pillar that's holding up the economy.

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If employment was to crack, then you know, it becomes a self fulfilling prophecy that we would like to get a recession.

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You know, yeah, perhaps we we will get a soft landing or, or a shallow recession.

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But remember to get to a hard recession or a hard landing, you have to go through a shallow one first.

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So there is a probability of a recession in the US at some point, but not necessarily this year in Europe.

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Again, in the UK there again, there is a potential, but in the UK we're, we're seeing less of a probability of recession right now.

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You know, and there is a kind of slight ironic joke about the 9th of December that I've got made quite a bit.

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You know, it's Taylor Swift's last tour day and you know, there's been a huge amount of growth in economies around the world where she's been to visit.

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And you know, arguably, is there going to be a global recession on the 9th of December after her ERAS tool?