Strategic Bond Opportunities Fund

July 2019 Fund Commentary

MARKET DEVELOPMENT

In July, the US Treasury bond curve experienced a soft bear flattening move on better economic figures and a reluctant Fed first rate cut.

In Europe, German yields reached fresh new lows on the back of weakening economic data and a slower growth outlook. The credit bond market gained support from improved employment and consumption figures in the US, and by expectations of the ECB's new QE programme to be implemented before year end. During the month, both the ECB and the Fed moved towards a looser monetary policy. The ECB policy remained unchanged but opened the door to a rate cut and the potential for additional measures to be announced during its next meeting on September 12th. Interestingly, Mr Draghi noted that the ECB cannot understand why the transmission belt between wage pressures and inflation does not work in Europe and in Germany in particular, and also mentioned that the outlook for the Eurozone economy is "getting worse and worse". At the end of July, the US Fed chairman, Jerome Powell, cut the Fed funds rate by 25bps (from 2.50% to 2.25%) for the first time since 2008. Although the move was widely expected, the FOMC provided a welcome surprise by putting an immediate end to its policy of reducing the size of its balance sheet (quantitative tightening) two months in advance. This said, the market was somewhat disappointed by Mr Powell's explanation that the first rate cut didn't mark the beginning of an easing cycle in the US. As a result, this month was characterized by opposite performances in asset classes represented by: Bloomberg-Barclays US Treasury total return, the Bloomberg-Barclays Global Aggregate and the S&P 500 TR delivering -0.12%, -0.28% and +1.44%, respectively.

PORTFOLIO STRATEGY

During the month, the Investment Adviser slightly decreased the portfolio's duration by taking some profit on the long end of the US Treasury curve.

MARKET OUTLOOK

The Investment Adviser's outlook is tied to two major topics, inflation and Central Banks' behavior. Inflation risk remains subdued in US and substantially below the ECB's target in the Eurozone. Yield curves may continue to flatten and the US curve to invert as a result of increasing fears of a significant global growth slowdown spreading into the domestic economy.

In the US market, the Investment adviser believes that long term US Treasuries are still attractive and may increase duration on escalating global trade tensions and recession fears. The Investment Adviser will consider building positions in US protection inflation securities if inflation expectations reach depressed levels. A further inverted US curve slope can still not be ruled out in the coming months with markets concerned that the Fed may

Eric Vanraes
PORTFOLIO MANAGER

INVESTMENT APPROACH

The Fund is a diversified bond fund, investing in bonds predominantly denominated in USD, including Sovereigns, Supranationals and Agencies (together SSAs), corporate bonds across all sectors and financials. A strong conviction portfolio of 30-60 issuers, seeking exposure to all continents (including developed as well as emerging markets), all types of ratings from AAA/Aaa to BB/Ba2 (Standard & Poor's/Moody's) and non-rated bonds (10% maximum), senior or subordinated debt (hybrid corporates and Tier II bank debt) with either fixed or floating coupon rates.

INVESTMENT OBJECTIVE

To achieve a total return through a combination of capital growth and income by investing in a globally diversified portfolio of fixed income securities.

A sub-fund of E.I. Sturdza plc. Registered in Ireland.

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already be behind the curve. The Investment Adviser believes that the best strategy today is to keep investing in a timely manner, in a selection of short term high quality corporate bonds and investment grade emerging markets bonds, combined with a barbell strategy on the US Treasury yield curve and an overweight of 1-2y combined with long dated US Treasuries. The Fed has delivered its first rate cut since the financial crisis and may be forced to implement additional cuts should global growth continue to weaken and trade tensions remain. In this context, the Investment adviser believes that the Fed will continue to ease monetary policy before year end, or even implement a QE4 at some point.

In Europe, the Investment Adviser is of the opinion that current macro conditions and Brexit uncertainties will support new easing measures from the ECB. An easing package is likely to be delivered in September with a cut in the depo rate and a new QE programme.

In the Emerging Markets, the Investment Adviser continues to monitor the spread patterns (both governments and corporates) closely and EM countries ability to absorb trade shocks in the context of a weak FX and a broad commodity market under pressure.

In conclusion, the Investment Adviser still believes that the best performing asset class is a mix of high quality short term Investment Grade corporates combined with long term US Treasuries. Emerging Markets still offer an attractive opportunity to stay invested selectively in very high-quality EM issuers. Bonds denominated in euro and hedged in US dollar also offer an attractive carry. However, in the current environment, due to a global spread widening risk, the Investment Adviser may continue to increase the weight of US Treasuries to the detriment of the three other pillars (corporate spreads in dollars, emerging markets in dollars and corporate spreads in euro). A mix of High Grade corporate carry and US Treasuries will represent an opportunity to deliver a robust performance in the coming months despite a very low yield environment and an outstanding performance since inception of the Fund.

IMPORTANT INFORMATION

The views and statements contained herein are those of the Eric Sturdza Group in their capacity as Investment Advisers to the Funds as of 16/08/2019 and are based on internal research and modelling.

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