

31 August 2021

Market review

Spreads for global investment grade bonds were largely stable over the month. However, the total return was still negative at -0.27% (hedged to Australian dollars), owing to a rise in Treasury yields. In the case of 10-year Treasuries, the yield rose by 8 basis point to 1.31% by the end of the month.

The global economic recovery continued in August, with vaccine rollouts making steady progress and restrictions on activity being eased further in several countries. The fast spread of the more contagious Delta variant of coronavirus remained a concern for both consumers and investors. However, sentiment was helped by vaccination rates exceeding 70% of the population in many developed countries and hospitalisation rates staying much lower than in previous virus waves.

Portfolio review

The Fund comfortably outperformed the benchmark in August, owing mainly to good security selection.

In terms of individual holdings, after the severe sell-off of the previous month, when China's domestic regulatory crackdown had a negative impact, many of the worst performers bounced back strongly in August. Examples of this included the property companies Sunac, Country Garden, Zhenro Properties and Shimao Group. On the negative side, a number of the Fund's longer-dated holdings detracted, including those of ratings agency Moody's, US energy provider Exelon and the US wireless telecoms company T-Mobile.

In the primary markets, we bought the attractively priced 2025, 2028 and 2051 euro bonds of the German residential real estate company Vonovia. We like the property sector generally for its high degree of earnings visibility. Similarly, we bought the new issue 2051 sterling bonds of the UK's largest housing association, Clarion. We also bought the 2028 euro bonds of National Grid, which benefits from reliable earnings, helped by the UK's transparent, stable and predictable regulatory regime. In US dollars,

purchases included the attractively priced 2041 bonds Westlake Chemical.

In the secondary market, we bought the 2031 bonds of Citigroup. On the sell side, in the light of ongoing regulatory developments in China, we reduced associated risk and took profits in Alibaba Group. We also reduced exposure to American Tower, by selling its 2029 euro bonds, which had significantly outperformed the US dollar bonds of the same issuer.

Outlook & strategy

Globally, we have reached peak growth, peak inflation (mostly through base effects) and peak central bank liquidity, with credit valuations no longer being cheap. However, we expect the favourable carry environment in global credit markets to persist over the near term as the reduction in central bank liquidity will be very gradual if inflation proves to be mostly transitory. The European Central Bank's (ECB) new symmetric inflation target and adjusted forward guidance

- that quantitative easing will continue just before the first rate hike
- sets the ECB on a more dovish course than other global central banks. The market currently does not expect the ECB to reach its medium-term symmetric inflation target of 2% and hence does not price in any rate hikes at all over the next two years. With the US Federal Reserve, our base case is a reduction in quantitative easing by the end of this year, despite some moderation in growth during the summer. Meanwhile, flows into US credit from foreign buyers and pension and insurance investors remain a technical tailwind and supportive of valuations.

In the meantime, the favourable economic backdrop allows credit profiles to improve further. Yields at the short end will remain low for longer, which will keep the search for yield alive. It is not inconceivable that as in the 2004-2006 period, we could see low volatility and minimal spread movements for an extended time. But this would be unlikely to last forever. Over the near term, we think spreads are likely

Investment strategy

The Fund is actively managed and may invest in a wide range of bonds (e.g. corporate bonds including high yield bonds, government backed securities, overseas bonds, index-linked bonds, floating rate notes ('FRNs') and asset backed securities ('ABSs') and/or money market instruments) in order to take advantage of opportunities identified.

Investment objective

The Fund aims to provide long term growth and outperform the Benchmark over rolling 3 year periods (before deduction of fees, costs and taxation) by investing predominantly in global investment grade bonds.

to remain largely range bound. However, some spread compression should still be possible in areas with potential for positive rating migration, which the Fund will look to exploit.

Fund performance is available on the relevant factsheet.

The opinions expressed are those of Aberdeen Standard Investments as of the date of publication and are subject to change at any time due to changes in market or economic conditions.

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