Global Strategic Bonds strategy

UK bond market implosion adds to uncertainty

- The new UK government's "mini budget" was met with a very negative market reaction
- UK gilt yields spiralled sharply higher and the Bank of England was forced to step in
- The strategy was well protected from a duration perspective in another volatile month

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Strategy in focus – representative account (30/09/22)		
Assets under management		$1,052m
Duration		0.90 yrs
Yield[1]		6.13%
Running yield[1]		4.19%
Spread to government[2]		264
Number of holdings		292
Launch date		11/05/2012
Net performance – representative account (USD)[3]		
	Cumulative	Annualised
One month	-2.07%	
One year	-13.43%	
Three years	-6.64%	-2.26%
Five years	+2.98%	+0.59%
Ten years	+21.95%	+2.00%

Source: AXA IM as at 30/09/2022. The data is based on a representative account that follows the Global Strategic Bonds strategy and is not intended to represent actual past or simulated past performance of the strategy. **Past performance is not a reliable indicator of future results.** Performance calculations are net of fees, based on the reinvestment of dividends.

What's happening?

- Rate hikes, hawkish central bank narrative and continued sticky inflation data continues to drive markets as total returns were once again deeply negative for global fixed income during the month.
- Markets were hit with a new dynamic in September as the new UK Prime Minister and Chancellor announced a very generous fiscal package with no transparent funding plan accompanying it and hence sent UK bonds into a tailspin.
- The implosion of UK fixed income markets led to an unwind of leverage within the large pension fund industry and subsequently exacerbated the issue and led to large selling of credit and other assets. Once again in 2022, this sharp increase in volatility led markets lower.
- US 10-year bond yields moved nearly 65bps higher although ended off their 2022 peaks. UK 10-year gilt yields touched 4.5% having started the month below 3%. Investment grade credit spreads moved to their wides of the year, while developed market high yield markets moved lower in line with equities, although not yet at their cheapest levels year-to-date.

Portfolio positioning and performance

- Defensive (35%): whilst our government bond exposure went up to 35%, we subsequently brought the strategy's duration sensitivity down to its lowest level since launch in 2012, using government bond futures to reduce exposure to barely above zero, our allowable limit. Within that, we mitigated all GBP duration risk on a view that yields would head higher, given the complex and fragile political and economic situation in the UK. Towards month-end we added back some duration from its extreme low, but still not quite at 1 year of exposure by the end of the reporting period.
- Intermediate (31%): the market fall meant that our credit exposure sank to its lowest point this year, albeit some of that was hedged by our government bond duration exposure. Looking ahead, global investment grade potentially offers a very attractive risk-reward opportunity, with significantly higher yields than we have seen for a long while. The sweet spot to us appears to be BBBs and sterling-related assets, which sit at the more attractive end of the asset class.
- Aggressive (34%): high yield and emerging market exposure remains at around 34%, with a preference still for developed market high yield. We continue to favour US high yield with single name opportunities, particularly in shorter maturities and at the lower end of the rating spectrum, offering potentially attractive future return profiles. As a partial hedge to the cash bonds, we added a -5% hedge using CDS indices.

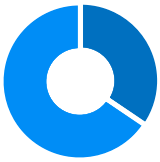
Outlook

- 2022 keeps providing shock after shock for global markets, particularly for fixed income and government bonds – the highest quality from a credit risk perspective – although all markets are suffering. The fact that the foundations of capital markets are struggling to find an anchor, together with high inflation and hawkish central banks, means it's difficult to be too positive on the short-term direction of markets given the serious destabilising knock-on effects.
- One theme that is coming increasingly to the fore is the attractive valuations on offer across global fixed income and the potential return opportunity is interesting many prospective buyers of global bonds.
- While the short term is uncertain, the medium-term prospects for the asset class look attractive, which in theory could set the asset in good shape for potential future returns, but as ever, to expect the market to move in a straight line would be foolhardy.

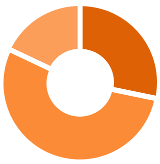
Portfolio breakdowns

Strategy breakdown	
Defensive	34.9%
Intermediate	30.6%
Aggressive	34.4%
Total	100.0%

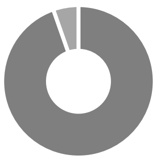
Defensive breakdown	34.9%
US Government Bonds	15.4%
Core Europe Government Bonds	7.6%
Rest of World Governments	0.0%
Inflation-Linked Bonds	6.3%
Cash	5.7%



Intermediate breakdown	30.6%
US IG Credit	10.6%
Euro & Sterling IG Credit	20.1%
Periphery Governments	0.0%



Aggressive breakdown	34.4%
Emerging Markets (HC 9.7%/LC 0%/FX 0%)	9.7%
US High Yield	18.5%
European High Yield	6.2%



Derivatives breakdown	-73.3%
Bond Futures	-90.6%
Credit Default Swaps	-5.1%

Credit rating breakdown

Category	Rating	Total
Defensive	Cash	5.7%
	AAA	7.3%
	AA	22.0%
	Total	34.9%
Intermediate	AA	1.0%
	A	5.5%
	BBB	24.1%
	Total	30.6%
Aggressive	AA	0.3%
	A	0.1%
	BBB	3.1%
	BB	11.6%
	B	12.6%
	CCC & Below	6.2%
	Not rated	0.7%
	Total	34.5%
Total		100.0%

(1) Yield figures quoted will vary in the future and are not guaranteed. Yield calculated to maturity, assuming next call date, using local currency yields.

(2) Average credit spread relative to government bonds.

(3) Representative account has been selected based on objective, non-performance-based criteria, including, but not limited to the size and the overall duration of the management of the account, the type of investment strategies and the asset selection procedures in place. Therefore, the results portrayed relate only to such accounts and are not indicative of the future performance of such accounts or other accounts, strategies and/or services described herein. In addition, these results may be similar to the applicable GIPS composite results, but they are not identical and are not being presented as such. Account performance will vary based upon the inception date of the account, restrictions on the account, along with other factors, and may not equal the performance of the representative accounts presented herein. The performance results for representative accounts are net of all fees and reflect the reinvestment of dividends or other earnings.

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