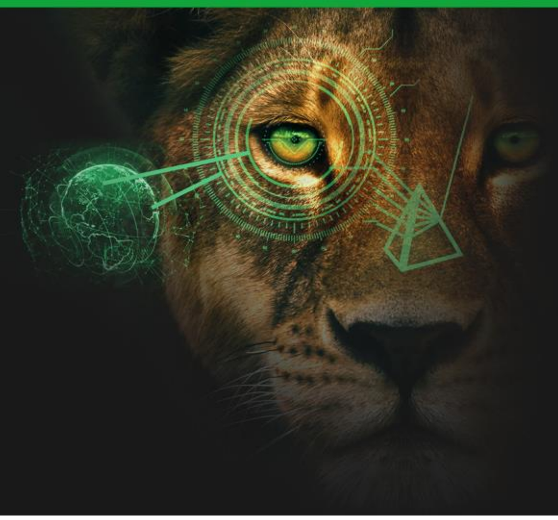

Global Fixed Income

Q1 2024 review

Liontrust GF Absolute Return Fund

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The Liontrust GF Absolute Return Bond Fund (C5 share class) returned 1.1%* in sterling terms in Q1 2024 and the IA Targeted Absolute Return, the Fund's reference sector, returned 2.5%. The Fund's primary US dollar share class (B5) returned 1.1%.

The yield carry on the Fund produced the largest positive impact during the quarter. From the bond market perspective, a rise in government bond yields was only partly mitigated by tightening in credit spreads. Stock selection and cross market rates positions added value in the first quarter.

Market backdrop

The first quarter of 2024 witnessed economic activity levels coming in higher than consensus expectations. Inflation did continue to fall, including core inflationary measures, however the pace was slower than markets and central bankers would have hoped for. The common theme across most developed economies is sticky services inflation. We note that in the US, shelter inflation is a large constituent part of the consumer price inflation basket. Services inflation that excludes housing, a measure referred to as "supercore" services, has been running at higher levels than anticipated. This stronger economic data has led the bond market to push out the timing and reduce the quantity of rate cuts expected. The Bank of England may well join the European Central Bank by cutting in June, the Fed is more evenly poised; the risk bias is towards waiting until later meetings.

At their most recent meeting, the Bank of England's Monetary Policy Committee (MPC) voted by a majority of eight to one to maintain rates at 5.25%. Haskel and Mann both dropped their hawkish dissent, while Dhingra continued to vote for a cut. Even with the hawkish dissenters now voting in line, there clearly remains a range of opinions on the MPC with some requiring greater evidence that inflation's persistence has been beaten before committing to a shift in monetary policy stance. The MPC has included a new sentence that it will "*…continue to consider the degree of restrictiveness of policy at each meeting*". Putting aside the blatant truism, I take this as a signal that cuts will be seriously considered at each meeting. Unless there is some new shocking economic data, it is highly unlikely enough MPC members will change their votes by the May meeting. Further evidence of slowing wage growth and reducing services inflation is required to make the majority vote for a cut. Greater data availability, especially around April's wage rises and index-linked price increases, makes June my central case for when the first cut occurs, with a reasonable tail risk this slips to the August meeting.

The Federal Open Market Committee (FOMC) held Fed funds rates steady in the 5.25% to 5.50% range. The statement was close to a carbon copy of the prior month. The most important sentence in the statement is still "*…the Committee does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent*". The main focus was on the Summary of Economic Projections (SEP) and Powell's press conference. The SEP has the core PCE inflation forecast for 2024 revised up from 2.4% to 2.6% which is a marking-to-market of the inflationary data already seen year-to-date, with the outlook for the rest of the year forecast to be in line with prior projections. Marrying this with the jump in the 2024 real GDP forecast from 1.4% to 2.1% implies some supply side improvement assumptions must have been made. These could be productivity related, as well as due to immigration easing labour market pressures. Importantly, core inflation forecasts for the time horizon beyond 2024 were left unchanged.

The dot plot of FOMC participants' estimates for interest rates was also revised. For 2024 there are still three rate cuts anticipated by the Fed – the dots hung on to the 75bps of easing but it would only take one or two members to change their stance to take this down to 50bps. 2025 and 2026 projections show less easing than prior forecasts is now anticipated. For the Fed members to gain the "*greater confidence*" they need that inflation is sustainably falling, further progress will need to be seen on services inflation; explicitly I believe there will be greater focus on supercore inflation measures with a little less emphasis on shelter inflation. There is unlikely to be enough improvement in the data by early May, so my best estimate is that the Fed cuts rates for the first time in this cycle in June; there remains the risk that this is pushed out until the late July FOMC meeting.

As a reminder, whilst it is interesting to work out when rates are going to be cut, it matters far more to bond investors that the conditions are in place for policy loosening and how much rates will eventually be cut by than the exact start date of the easing cycle. As restrictive monetary policy continues to work through the economies, the Fed and Bank of England can head back towards neutral base rates: somewhere in the 2-3% region. I believe it is therefore a good time to be locking in attractive bond yields.

Fund performance

We split the Fund into the Carry Component and three Alpha Sources for clarity in reporting, but it is worth emphasising we manage the Fund's positioning and risk in its entirety. As a reminder, the Carry Component invests in investment grade bonds with <5 years to maturity, within this there is a strong preference for investing in the more defensive sectors of the economy.

The yield carry on the Fund produced the largest positive impact during the quarter. From the bond market perspective, a rise in government bond yields was only partly mitigated by tightening in credit spreads. Stock selection and cross market rates positions added value in the first quarter.

Alpha sources

Rates

The Fund spent most of the quarter with duration a little under 2.0 years in the 1.8–1.9 year range. As a reminder, the Fund's permitted range is 0-3 years with a neutral level of 1.5 years. The split at the end of March was 0.85 years in the US, minus 0.5 years in Canada, 0.5 years in New Zealand, 0.8 years in Europe, and 0.2 years in the UK.

Regarding cross market rates positions, the short Canadian duration relative to the US was flat during the quarter. A new position was established by buying New Zealand government bonds and selling the duration equivalent amount of US bond futures. The Reserve Bank of New Zealand (RBNZ) was early to raise rates and the associated slowing in economic activity is flowing through. The RBNZ is unlikely to start cutting rates until the second half of the year, in the meantime one is still being paid a decent spread premium for owning Kiwi bonds relative to other developed market sovereigns. The position has been profitable since implementation, we anticipate further relative outperformance by New Zealand's sovereign debt.

Allocation

The weighting in the Carry Component has been in the mid 80's percentage area throughout the quarter, due to the compelling yield on short dated defensive investment grade. As credit spreads have become expensive we have further reduced exposure to other credit in Selection, as well as selling a couple of the relatively higher risk positions within the Carry Component.

Selection

Stock selection was additive to performance during the quarter. Within Selection, the best performance emanated from Castellum's bonds, the position was trimmed with a smaller holding size retained. Zurich Insurance, AIA, and 3i Group added 2-3 basis points of performance each. Zurich's bonds were sold, the AIA position maintained, and 3i Group's bonds will become short enough maturity to qualify for the Carry Component in June.

Within the Carry Component, the performance from credit spread tightening or widening at the individual bond level was very muted, with just three small exceptions. An incremental positive arose from Santander retiring a bond one year ahead of maturity. Heimstaden Bostad added 4 basis points, the position was sold due to residual risk of a ratings downgrade. Aroundtown's bonds added 3 basis points, this position was maintained. Along with bonds maturing, the Fund also sold out of Bayer as the overhang from litigation continues to weigh on the credit. New purchases for the Carry Component included Credit Agricole, Aon, and a new Toyota bond issue which offered more compelling value than the existing holding the Fund had.

Key Features of the Liontrust GF Absolute Return Bond Fund

Investment objective & policy[1]	The investment objective of the Fund is to generate positive absolute returns over a rolling 12 month period, irrespective of market conditions. There is no guarantee the investment objective will be achieved over this or any other time period. The Fund aims to achieve its investment objective through investment in corporate and government fixed income markets worldwide, including developed and emerging markets. In achieving its objective, the Fund also aims to minimise volatility and reduce the possibility of a significant drawdown

	(i.e. a period where the Fund is worth less than the initial investment at the start of a 12 month period). The Fund invests in a wide range of bonds issued by companies and governments, from investment grade through to high yield. The Fund invests in developed and emerging markets, with a maximum of 20% of its net assets invested in emerging markets. Investments are made in US Dollar denominated assets or non-US Dollar denominated assets that are predominately hedged back into US Dollar. Up to 10% of the Fund's currency exposure may not be hedged (i.e. the Fund may be exposed to the risks of investing in another currency for up to 10% of its assets). The Fund may invest both directly, and through the use of derivatives. The use of derivatives may generate market leverage (i.e. where the Fund takes market exposure in excess of the value of its assets). The Fund has both Hedged and Unhedged share classes available. The Hedged share classes use forward foreign exchange contracts to protect returns in the base currency of the Fund. The fund manager considers environmental, social and governance ("ESG") characteristics of issuers when selecting investments for the Fund.
Recommended investment horizon	5 years or more
Risk profile (SRI)[2]	2
Active/passive investment style	Active
Benchmark	The Fund is actively managed without reference to any benchmark meaning that the Investment Adviser has full discretion over the composition of the Fund's portfolio, subject to the stated investment objectives and policies.
Sustainability profile	The Fund is a financial product subject to Article 8 of the Sustainable Finance Disclosure Regulation (SFDR).

Notes: 1. As specified in the PRIIP KID of the fund; 2. SRI = Summary Risk Indicator. Please refer to the PRIIP KID for further detail on how this is calculated.

Discrete years' performance (%) to previous quarter-end:

	Mar-24	Mar-23	Mar-22	Mar-21	Mar-20
Liontrust GF Absolute Return Bond C5 Acc GBP	6.2%	-1.5%	-1.9%	6.4%	-2.5%
IA Targeted Absolute Return	6.3%	0.3%	2.5%	10.1%	-3.3%

*Source: Financial Express, as at 31.03.24, total return (net of fees and interest reinvested), C5 class. Discrete data is not available for ten full 12-month periods due to the launch date of the portfolio

For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance does not predict future returns. You may get back less than you originally invested. We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.

The fund manager considers environmental, social and governance ("ESG") characteristics of issuers when selecting investments for the Fund.

Overseas investments may carry a higher currency risk. They are valued by reference to their local currency which may move up or down when compared to the currency of the Fund.

Bonds are affected by changes in interest rates and their value and the income they generate can rise or fall as a result;

The creditworthiness of a bond issuer may also affect that bond's value. Bonds that produce a higher level of income usually also carry greater risk as such bond issuers may have difficulty in paying their debts. The value of a bond would be significantly affected if the issuer either refused to pay or was unable to pay.

The Fund can invest in derivatives. Derivatives are used to protect against currency, credit or interest rate moves or for investment purposes. There is a risk that losses could be made on derivative positions or that the counterparties could fail to complete on transactions.

The Fund uses derivative instruments that may result in higher cash levels. Cash may be deposited with several credit counterparties (e.g. international banks) or in short dated bonds. A credit risk arises should one or more of these counterparties be unable to return the deposited cash.

The Fund invests in emerging markets which carries a higher risk than investment in more developed countries. This may result in higher volatility and larger drops in the value of the fund over the short term.

The Fund may encounter liquidity constraints from time to time. Participation rates on advertised volumes could fall reflecting the less liquid nature of the current market conditions.

Counterparty Risk: any derivative contract, including FX hedging, may be at risk if the counterparty fails.

There is no guarantee that an absolute return will be generated over a rolling 12 month period or any other time period

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

Disclaimer