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Amity Sterling Bond Fund – Q1 2019 Commentary

Quarter to end March 2019

Performance

	3 months	6 Months	1 Year	3 Years	5 Years
Fund Performance (B class)	3.01%	2.07%	1.81%	14.79%	22.13%
FTSE Gilts All Stocks TR GBP	3.38%	5.37%	3.71%	11.09%	30.66%
IA £ Strategic Bond	3.65%	2.31%	2.07%	12.23%	17.92%
Sector Quartile	3	3	3	2	2

Source: Morningstar. Figures compared on a Bid to Bid basis with Net Income Reinvested

Yields

	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19
Distribution	3.30%	3.50%	4.21%	4.20%	4.22%	4.23%
Underlying	3.30%	3.50%	4.21%	4.20%	4.22%	4.23%

Review

Gilts registered another strong quarter on the back of safe-haven demand as geopolitics and trade uncertainty weighed on the prospects for global growth. Earlier hopes that a parliamentary consensus could be reached on the terms of the UK's withdrawal from the European Union (EU), which had lifted bond yields in February, were dashed as the quarter drew to a close. Similarly, the US-China trade dispute remained unresolved. The 10-year gilt yield fell from 1.28% to a low of 0.99% in March, having touched a high of 1.35% in January, before ending the period at 1.00%.

Following its strategy of exercising patience in its assessment of further rate hikes in January, the US Federal Reserve revised down its interest rate outlook for the year ahead. Given the recent slowdown in global economic growth, the bank's dovish pivot elicited a strong reaction from debt markets. The European Central Bank (ECB) also announced another round of monetary support for Eurozone banks, to stimulate lending within the region, whilst also cutting its growth forecasts for the year ahead.

Apart from a small decline in sentiment towards the end of the quarter, risky assets more than recouped the losses incurred as 2018 drew to a close, with risk premiums declining significantly. Even though corporate bonds have relatively shorter duration, the narrowing in credit spreads more than offset an adverse interest rate impact as longer-dated maturity gilts rallied in March. This led corporates to outperform gilts over the period under review.

Performance & Activity

The return on the Amity Sterling Bond Fund was lower compared to that of its FT All Stock Gilt Index benchmark and the IA Strategic Bond Sector over the period under review. Despite benefitting from an overweight allocation to corporate bonds as risky assets rallied, there was an adverse impact from our short duration position as prices on longer-dated maturities surged towards the end of the quarter.

Our niche holdings in PIBS and preference shares bounced in tandem with the rally in risky assets and recovered the bulk of their relative underperformance registered in the previous quarter as global central banks adopted a more supportive monetary policy stance.

Cash inflows were largely deployed by adding to existing holdings, with some new positions established as well. New holdings in Fidelity 6.75% 2020, International Bank for Reconstruction & Development (World Bank) 0.75% 2021 and Coventry Building Society 6.875% perp (2024 call) were initiated whilst we also added to positions in Legal & General 5.375% 2045 (2025 call), Prudential

5.625% 2051 (2031 call), Co-Operative Group 11% 2025, Sainsbury's plc 6.5% perp (2020 call), RSA Insurance plc 5.125% 2045 (2025 call) and Greensleeves Homes Trust 4.25% 2026.

Outlook

The sharp decline in bond yields as the quarter drew to a close serves as a timely reminder of how precarious market sentiment is with regards to geopolitical risks, with global trade uncertainty beginning to impinge on economic growth. The UK's withdrawal from the EU is yet to be agreed, with the Bank of England inclined to support the economy via looser monetary policy on the basis of heightened uncertainty, albeit with respect to a stated level of tolerance for inflation. Whether a cross-party consensus to forge a way through the current impasse can be reached in time for the EU to consider remains to be seen. In the meantime, the global central banks' newly adopted dovish positioning is likely to exert downward pressure on yields or keep them range-bound at the very least. It is worth highlighting that a successful resolution to either the US-China trade dispute or the current Brexit negotiations would be catalysts for a bond market correction.

We remain of the view that the market's late-cycle characteristics, notwithstanding greater political uncertainty, support the case for higher interest rates with the risk that the market reprices lower as political headwinds dissipate. In that context, our favoured approach also continues to focus on higher quality credit with the risk-reward trade-off appearing less favourable on lower-rated debt after last quarter's rally in risky assets. A large weighting towards short-duration gilts has been maintained to enhance portfolio liquidity. This has bolstered our short duration bias and should avail more flexibility to seize opportunities to pick up good quality credits at valuations that we deem attractive.

Yields

The Distribution Yield reflects the amounts that may be expected to be distributed over the next 12 months as a percentage of the mid-market share price of the fund as at the date shown. The Underlying Yield reflects the annualised income net of expenses of the fund (calculated in accordance with relevant accounting standards) as a percentage of the midmarket share price of the fund as at the date shown. Both Yields are based on a snapshot of the portfolio on that day. The yields do not include any preliminary charge and investors may be subject to tax on distributions. The Distribution Yield is higher than the Underlying Yield because the fund's expenses are charged to capital. This has the effect of increasing the distributions for the year and constraining the fund's capital performance to an equivalent extent.

Further Information

To obtain further information please speak to your normal EdenTree representative, visit www.edentreeim.com or call our support team on 0800 011 3821.

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