

PERFORMANCE

	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Fund Performance (B Class)	-1.5%	0.6%	-0.3%	19.2%	9.9%	58.6%
FTSE All Share TR GBP	-0.5%	2.6%	7.9%	33.2%	16.5%	78.0%
IA Mixed Investment 40-85% Shares	0.2%	2.4%	3.3%	12.6%	16.9%	68.2%
Sector Quartile	4	3	4	1	4	4

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

MARKET REVIEW

The ongoing interaction of inflation and interest rates was a dominant theme in the second quarter of 2023. This was felt across financial markets. Equities drifted sideways, with the notable exception of a cluster of US tech mega caps such as Nvidia, Apple and Microsoft. Sovereign bonds, for the most part, sold off at the short end as the prospect of higher-for-longer inflation and corresponding interest rate rises loomed.

The consequence of these moves was a number of skews in markets. The resurgence of the US tech giants was confined to just a handful of stocks, not the broader US market, which performed similarly to other developed markets. AI-mania played a part in this, with the launch of updated and more sophisticated chatbots. Nvidia roundly beat expectations in its quarterly results, pointing to huge demand for its chips that power AI uptake. But there was also a palpable sense that in highly uncertain times, the US tech giants were as safe a hiding place as any, even if the valuation distortion is as wide as it has ever been (bear in mind that Nvidia currently trades at an astonishing 25 times sales).

Also of note was the extent to which sovereign yield curves inverted further. This is typically defined as the difference in yield between two- and ten-year sovereign bonds. When shorter-dated bonds are at higher yields than longer dated ones for a reasonable length of time, this has historically always been a herald of recession and this is the situation we find ourselves in at the moment. Most inflation data in the US and in Europe suggested that inflation had started to drop, even if wage-related inflation was proving quite tenacious. The UK was an outlier in this, with inflation proving higher and stickier than elsewhere due to labour shortages and Brexit-related bottlenecks in the economy.

PERFORMANCE & ACTIVITY

The EdenTree Responsible & Sustainable Managed Income Fund fell in value over the quarter, by a margin slightly larger than its benchmark, the FTSE All Share. The bulk of this deficit was the consequence of the sharp rise in bond yields, which affected the Fund's fixed income holdings but also its exposure to infrastructure. In contrast, the equity portfolio performed solidly.

By the end of the quarter the portfolio consisted of about 20% in bonds, mostly corporates, with an average rating of investment grade and a yield-to-maturity of about 6.5%. While their performance was entirely in keeping with a sharp move higher in interest rates, the performance of the infrastructure portion of the portfolio was frustrating. This group of listed investment companies are mostly invested in areas such as renewable energy and have revenues that are inflation-linked and so should be more resilient in times of rising interest rates.

Among the equity holdings, German insurance group Talanx rose sharply and we used the opportunity to trim our position slightly. Also performing well was SPIE, a French technical services company, and Moneysupermarket.com, the UK price comparison website. Stocks with UK domestic exposure such as housebuilder Taylor Wimpey and Supermarket Income REIT were notably weak, alongside listed infrastructure.

As the new management team of the Fund, we continued the process of aligning the Fund's holdings with our investment process. This consisted primarily of increasing the bond weighting, in order to lock in the higher yields currently available and increasing the overall liquidity in the process. We considered this process more or less complete by the end of the quarter. Among new names included in the portfolio were Medtronic, the US maker of medical devices that has had a period of weak performance but nonetheless has raised its dividend every year for over 40 years and yields over 3.0%.

OUTLOOK

The great debate facing investors is when, or indeed if, recession kicks in, whether in Europe or the US. Bond markets are currently pricing in further interest rate rises and probably no cuts until well into 2024. But inverted yield curves also indicate recession. In this context, equities in many markets are not quite priced for this outcome, notably the US. European and UK equities continue to trade at more modest multiples, even if the growth outlook here is weaker than in the US. The starting point for any slowdown in economic activity is relatively robust, given very low unemployment and much lower levels of corporate and household debt (though not government debt), compared to the financial crisis of 2008. With these factors in mind, we remain defensively positioned with limited amounts of consumer and cyclical exposure with more emphasis on areas such as the ongoing energy transition and digitalisation, where funds are committed and relatively safe from a broader macroeconomic downturn.

For 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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