R&S Short Dated Bond Fund

Q4 2023 Commentary

Performance with principles®

PERFORMANCE

	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Fund Performance (B Class)	3.7%	6.6%	5.9%	-1.0%	4.2%	-
iBoxx Non-Gilts ex BBB 1-5 TR GBP	3.8%	7.1%	5.9%	-2.5%	2.7%	-
IA £ Corporate Bond	7.8%	10.0%	9.3%	-10.4%	5.9%	-
Sector Quartile	4	4	4	1	3	-

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

YIELDS

Distribution	*3.12%*
Underlying	*3.12%*
Historic	*2.40%*

MARKET REVIEW

Shorter-dated bonds rallied sharply over the quarter as market participants not only priced in peak interest rates but also expected looser policy in the months ahead. While some central banks maintained higher for longer forward guidance, further declines in headline inflation were acknowledged with the Bank of England holding its benchmark interest rate unchanged over the period at 5.25%. The FTSE UK Gilts under 5-year yield began the period at 4.53% and briefly rose to a high of 4.72% in October before falling to a low of 3.57% in December and ending the quarter at 3.59%.

The US Federal Reserve also maintained its benchmark interest rate at 5.5%, the level it had last raised it to in July. With economic data including growth and unemployment appearing robust, policymakers began to anticipate interest rate cuts over the forecast horizon in a notable shift. While the European Central Bank's Governing Council also kept monetary policy settings unchanged, a hawkish stance prevailed on lingering concerns around elevated levels of inflation relative to target. Reinvestments under the Pandemic Emergency Purchase Programme are to be discontinued at the end of 2024.

Credit spreads declined steadily over the quarter, in a similar manner to the previous months, with lower-rated debt gaining considerably more than higher-quality securities as risky assets rallied. Shorter-maturity corporate debt outperformed sovereign debt over the quarter.

PERFORMANCE & ACTIVITY

The Short-Dated Bond Fund's total return of 3.73% was virtually in line with that of its iBoxx Non-Gilts 1-5 years ex BBB Index benchmark (3.77%) over the period under review. While its shorter relative duration held back performance, this was offset by favourable credit selection.

The Fund's increased exposure to quasi-government debt with greater interest rate sensitivity proved beneficial as underlying gilt yields fell, as did the reductions in its holdings of floating rate notes. Higher beta credit such, as subordinated financials, continued to gain from credit spread tightening as sentiment towards risky assets improved.

Over the quarter, the Fund initiated holdings in Asia 5.125% 2028, KFW 4.875% 2028, International Finance Corp 4.5% 2028, Coventry Building Society 7% 2027 and Inter-American Development Bank 4.75% 2029. It added to positions in European Investment Bank 3.875% 2028, Society of Lloyds 4.75% 2024, Phoenix 5.867% 2029 and Inter-American Development Bank 2.5% 2027 while reducing floating rate note (FRN) exposure through sales of Royal Bank of Canada July 2026 covered FRN alongside maturities of Coventry Building Society November 2023 and Yorkshire Building Society November 2023 FRNs. There were also early redemptions of Pension Insurance Corp 8% 2026, Places for People Homes 5.09% 2024, with Phoenix 5.625% 2025 also being partially tendered in December.

OUTLOOK

The reluctance to tighten monetary policy further, with some central bankers even beginning to signal policy cuts, implies a 'peak interest rate' scenario following the latest global rate hike campaign. Whereas upside risk to the prices of goods and services remains, with tight labour markets also warranting the need to retain optionality, continued inflation declines from post-pandemic highs are noteworthy. Therefore, the market's focus has decidedly shifted to the timing with which policymakers ease financial conditions from present more restrictive levels.

Global economic growth has, thus far, held up better than expected. Near-term price increases above desired longer-term targets may serve to limit the urgency with which interest rate cuts are implemented as well as their magnitude. This points towards the latter half of 2024 as a preferable commencement period for any such changes, which also allows more time to assess the cumulative effects of the policy actions delivered thus far. Ongoing quantitative tightening at a time of reduced fiscal headroom justifies caution vis-à-vis term premia. Policymakers are nonetheless keen on softening the economic impact of higher interest rates as growth is re-prioritised ahead of key leadership contests. This policy pivot, in what has so far been a benign environment for corporate defaults, creates a favourable backdrop for bonds particularly relative to money markets. Corporate default potential appears under-priced. We also consider a cautious stance towards lower-rated and 'higher-beta' assets as crucial, along with a bias towards higher-quality debt, based on a deteriorating outlook.

We remain vigilant in seeking out opportunities to add to high-quality credits, scrutinising the robustness of business models and cash flows to ensure adequate compensation for risk. Our investment approach continues to focus on good quality short-dated credits with attractive yields.

PERFORMANCE DISCRETE ROLING 12 MONTHS	12 Months to 31/12/2019	12 Months to 31/12/2020	12 Months to 31/12/2021	12 Months to 31/12/2022	12 Months to 31/12/2023
Fund Performance (B Class)	2.9%	2.3%	-1.4%	-5.2%	5.9%
iBoxx Non-Gilts ex BBB 1-5 TR GBP	2.6%	2.7%	-1.5%	-6.6%	5.9%
IA £ Corporate Bond	9.5%	7.9%	-1.9%	-16.4%	9.3%
Sector Quartile	4	4	2	1	4

Past performance is not necessarily a guide to future returns.

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 the 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.