Q3 2025 Commentary

EdenTree Global Sustainable Government Bond Fund

Performance and Yields

Note: As this Fund was only launched in October 2024 there is insufficient data to provide a useful indication of past performance to investors. Past performance information will be shown when the Fund has been in existence for a complete calendar year.

Market review

With the exception of the US and Canada, global bond yields rose across most major economies over the quarter, as higher-than-expected inflation, notably in the UK, led market participants to pare back their expectations of interest rate cuts. In France, fiscal concerns kept longer-maturity bond yields higher and were also the main driver behind Fitch's downgrade of the country's sovereign credit to single-A in September.

During the quarter, the US Federal Reserve (Fed) cut its benchmark interest rate for the first time in 2025 to a target range of 4.00-4.25%, with Fed Chair Jerome Powell citing growing concerns over an already weakening labour market. The European Central Bank (ECB), having cut by a cumulative 100 basis points (bps) so far this year, held its main benchmark interest rate at 2.00%. Policymakers have since declared this as a neutral level, given balanced risks to both economic growth and inflation in the euro area. The Bank of England (BoE) cut its benchmark interest rate by 25 basis points (bps) to 4.00% in August, its third such action this year. The BoE maintained guidance of a "gradual and careful" pace of further rate reductions. The Reserve Bank of Australia cut its benchmark interest rate by 25 bps in August to 3.60%. The Bank of Canada also cut its benchmark rate by 25 bps to 2.50% in September. The Bank of Japan left its main policy rate unchanged over the quarter at 0.50%.

Performance and activity

US Treasuries and Canadian government debt rallied over the quarter, as a weakening labour market outlook led to expectations for further interest rate reductions in the near term. As such, there were positive contributions from the Fund's selection of US dollar bonds, with the overweight allocation to Canadian dollar bonds also proving beneficial. Japanese government bond yields continued to rise on growing fiscal concerns, particularly as investors awaited the result of the Liberal Democratic party leadership contest. Therefore, the Fund's underweight allocation to this region mitigated underperformance.

Significant cash subscriptions over the period were invested across a number of existing holdings. These included increasing our exposure to the International Finance Facility for Immunisation (IFFIm) 4.25% 2028 bond, Community of Madrid 2.487% 2030 green bond, the International Development Association 4% 2030 sustainable bond, Japanese Government 0.3% 2028 transition bond, Inter-American Development Bank 4.5% 2030 bond, Canada Government 2.25% 2029 green bond and US Treasury 4.375% 2043 bond. We also established a new holding in the World Bank 4.375% 2035 USD sustainable bond.

Over the period, we reduced the Fund's duration primarily by selling our exposure to longer-dated government bonds such as the France 1.75% 2039 green OAT, Germany 1.8% 2053 green bund and UK Treasury 1.5% 2053 green gilt.

Outlook

The global interest rate cycle appears to be de-coupling, with faster reductions by major central banks in geographies such as Europe and Canada met with limited monetary policy loosening from the Fed and the BoE. The latter institutions have cut less, with the BoE, in particular, placing greater emphasis on lingering inflation risks. Even though the most recent disruption to trade has not yet resulted in higher consumer prices, a heightened level of uncertainty remains, particularly around fiscal policy.

In an environment marked by concerns around large and growing government budget deficits and a slower pace of interest rate cuts, shorter and intermediate tenor bonds tend to perform better. The trend for steeper yield curves looks set to continue. Despite deteriorating labour markets, the global economy's resilience in the face of ongoing shocks, not least recent trade tariffs, is confounding expectations and may well see market participants persist in their renewed search for yield.

Higher budget deficits amongst major economies such as the US, UK and France are rightly garnering more attention from bond markets, particularly as attempts to curb spending are met with stiff political resistance. Fitch's downgrade of France's credit rating to single-A following France's failure to implement the required fiscal consolidation could serve as a precursor to national budget announcements elsewhere in the coming months. Interest rate risk at the long end, therefore, looks underpriced.

We have reduced the Fund's overweight allocation to European sovereign debt in favour of US-dollar-denominated assets, with policymakers at the ECB having declared monitory policy settings as 'neutral'. The scope for interest cuts appears higher for the US, UK and Australia. However, the challenging fiscal backdrop and potential risks to inflation in these countries means we believe shorter to intermediate tenors are better placed to benefit from forthcoming interest rate cuts; we, therefore, prefer these bonds at present.

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