Candriam Bonds Total Return

Market Overview

2024 started with some pushback from central bankers on the aggressive cut pricing we saw develop in December which resulted in a partial retracement of December's sovereign bond rally. However this wasn't enough to impact the positive environment for risk assets which, in the main, continued to perform quite well. The fund was marginally negative over the month, down 17bps gross of fees.

After marginally reducing duration at the end of December, we reduced further our duration exposure via options by buying puts funded by selling calls to protect the portfolio somewhat against a rates sell off. At expiry of the options we elected to reduce overall duration to 1.75 ex options at an inopportune moment as rates rallied into month end (although have reversed that rally since). In terms of rates relative value positions, we took profit on longs in the UK and New Zealand while we also cut the Japanese rates short, preferring to express a view on relative policy expectations via the Japanese Yen instead. We also added a UK 5/30s flattening trade with monetary policy expectations exaggerated in our view as well as supply concerns overdone in the short term at least. While we added some investment grade credit in the early January supply, we decided to reduce risk at the end of the month on valuations, more positive investor sentiment and positioning and growing risks. We reduced European high yield via Xover as well as reducing our convertible bond exposure. In FX space we took profit on a short in Swedish Krone, initiated short in Swiss Franc, UK Pound and New Zealand Dollar as well as the aforementioned long in Japanese Yen.

Portfolio Highlitghts & Strategy Review

In terms of performance drivers, yield curve (-40bps) and FX (-9bps) detracted while spreads (+31bps) contributed and equity linked (+1bps) was almost flat.

Within yield curve, long positions in the US (-24bps), the UK (-11bps), Australia (-7bps) and New Zealand (-6bps) were negatives while positions in core European duration (+11bps) were additive.

In cash spreads European investment grade (+9bps) and European (+3bps) high yield compensated for losses in sovereign spreads (-8bps), where a short BTP position cost, and US high yield (-3bps). Carry added 30bps while credit derivatives contributions were flat.

In FX space, short US dollar positions (-5bps) cost as well as longs in Norwegian Krone (-3bps) and Australian Dollar (-3bps) while shorts in Swiss Franc (-3bps) and New Zealand Dollar (-3bps) were also marginal detractors. Longs in Japanese Yen (+4bps) and Swedish Krone (+5bps) helped to offset these.

Fund Outlook

The sharp reversal in global bond yields along with the decline in inflation suggests that we have now seen the peak in the cycle. The question now turns to when and by how much central banks will start cutting interest rates. The exception to the rule remains Japan, where the central bank still has to exit its negative interest rate policy. Regarding risky assets, we continue to prefer solid IG-names as well as financials in the Fund, as the carry versus government bonds remains interesting, especially in a soft landing scenario.