

Candriam Sustainable Bond Global

Market Overview

At the start of 2024, global bond yields rebounded slightly following the significant move lower seen during the last two months of 2023. Expectations regarding central bank easing were probably a bit exaggerated, as the growth continued to be more resilient than expected, especially in the US.

Indeed, Q4 GDP growth in the US once again beat expectations with an annualized growth figure of 3.3% following already a stellar Q3 GDP growth figure of 4.9%. Although inflation has been coming down quite significantly, these strong growth figures along with a tight labor market suggest a continued cautious approach from central banks regarding the start of the easing cycle. Indeed, during the first meeting of the US Federal Reserve, president Powell poured some cold water on market expectations regarding a first rate cut in March.

On the other side of the Atlantic, the ECB also welcomed the declining trend in inflation, and signaled that they are awaiting more information on the wage negotiations typically taking place at the start of the year, before taking a decision on the start of the easing cycle. During the Davos meeting, president Lagarde suggested that a potential first rate cut would only come during the summer.

Over the month, US and German 10-year yields moved slightly higher, as the yield curve continued to re-steepen. This was also the case in the UK and Japan, where the central bank is still discussing the end of its Negative Interest Rate Policy (NIRP) and is also awaiting the outcome of the Spring wage negotiations (Shunto) in this regard. The only outlier is still China where the growth outlook continues to disappoint and deflationary forces are still reigning. Chinese 10-year yields as a result continued their downtrend falling below the COVID-levels below 2.5%.

From a credit point of view, the market digested very well the massive amount of supply with credit spreads overall tightening, except in the US High Yield segment. Renewed concerns about exposure towards the US Commercial Real Estate (CRE) market did not (yet) affect overall market sentiment with equity markets in general continuing to rally higher. Once again with China being the big exception.

On the FX market, the USD rebounded strongly, while the JPY was one of the weakest currencies in a reversal move of what happened during the month of December. The INR benefited from the strength in the USD and gained almost 2% versus the EUR. The IDR on the other hand failed to keep up pace, as concerns about the upcoming elections kept investors sidelined. The NOKSEK cross stabilized following the strong outperformance of the NOK in December.

Portfolio Highlights & Strategy Review

Regarding the funds' positioning in January. On the duration front, we have taken profit on our long duration positions in the UK and Norway, while maintaining our long positions in the US, New Zealand and Mexico. Overall, the fund still has a short duration due to its short positions in Japan and China, although we slightly reduced our short in China following our investment in a 5-year green bond from IBRD denominated in CNY. We also held on to our spread trade at the short end of the curve between US and German 2-year yields, as we find the yield differential exaggerated.

Curve-wise, we maintained our steepeners at the long end of the curve in both the US and Germany between 10- and 30-year yields.

On the FX side, we took partly profit on our NOK exposure and started to gradually phase in again a long JPY position after we sold the JPY mid-December following the strong rally versus the USD. On the EM side, we maintained our long INR and IDR bonds for the high carry.

On credit side, the fund has continued to increase its corporate exposure mainly by participating in a number of primary issues. As such, the fund is overweight to European Investment Grade bonds with a preference for financials given the more attractive valuation versus non-financials. The fund continues to have a marked active exposure to Green, Social and

Sustainability Bonds, which is now above the 20% level.

In January, the fund outperformed its benchmark by around 10 basis points.

The main contributors to the fund's performance during the month were:

- The short duration in Japan
- The steepening of the US yield curve
- The long INR exposure
- The credit overweight

The main detractors to the fund's performance during the month were:

- The long duration in the UK, Norway and New Zealand

* net of fees in EUR terms

Fund Outlook

After the strong rates rally at the end of last year, we have reverted to a more neutral duration positioning. Whilst from a fair value perspective we still see potential for rates to come down further, in the short term high supply and some pushback from central banks against the aggressive easing cycle priced by markets is likely to put upward pressure on rates. We will use this move higher to re-install long duration positions later in the year. In Japan, we still expect the central bank to exit its negative interest rate policy during the spring. The fund is well positioned to benefit from the divergence in monetary policy given its short duration bias in Japan and its long JPY positioning. 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.

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