Fund report, October 2021
Global Ethical High Yield
Fixed Income

Sparinvest

CONTINUED DARKNESS IN CHINA

Declining order intake and rising prices

Markets. Credit spreads widened by 11 bps in the High Yield (HY) market in October. The benchmark index gave a return of -0.76%, which brought the year-to-date return down to 1.98%.

The latest set of leading growth-related indicators still paints a picture of declining momentum. Figures from U.S. and Europe show, for example, that the ratio between order intake and inventories has fallen further. This probably means that industrial production will have to continue to adapt to lower activity in the coming period. Despite the prospect of lower growth momentum in the manufacturing industry, the latest indicators point to, even higher, end prices. End prices continue to act as a buffer despite signs of lower activity. This merely indicates extraordinarily large imbalances in the global manufacturing industry. Part of that development is due to broken supply chains and built-up bottlenecks in the wake of Corona-related restrictions. The remaining part can be attributed to a generally strong demand. At present, there is no sign that the existing imbalance between supply and demand is showing material improvement.

Developments in China in particular have worsened since the summer. China is currently experiencing electricity and energy supply problems that exceed previous periods of bottlenecks. This comes on top of the debt problems in the Chinese real estate sector that have been going on for several months. Data from September and October indicate somewhat lower activity in the housing market in China and a negative spillover on prices. This sector alone accounted for approx. 60% of the negative index return for the month.

Negative return, ahead of benchmark

The Portfolio had a negative return of 0.21% in October, which was 0.55 percentage points ahead of the benchmark. Year-to-date the return is 5.29%, which is 3.31 percentage points ahead of the benchmark.

Materials and Communications were the two sectors that generated the largest positive contribution to the portfolio relative to the benchmark, while IT as the only sector contributed slightly negative relative to the benchmark. The positive contribution from materials was based broadly on a number of the fund's positions, which continue to benefit from the generally high commodity prices. In Communication, the positive contribution was also spread across several positions, while a number of positions in the benchmark index had a very hard month. The small negative contribution from IT came from a Nordic provider of automated messages to corporate customers. The company's recent acquisition ended up being canceled, as the parties could not agree on the price. The news of its cancellation had a negative impact on the bonds, as the acquisition would have been financed with new equity, effectively reducing leverage for the combined entity.

In October, one bond was called and three sold as they had reached their expected return potential. The proceeds were invested in six new issues, one new name and in increasing the weight in several existing positions. The changes resulted in a decrease in the underweight in the U.S. and increased the fund's overall credit spread, while the portfolio duration maintained the same level, still below that of the benchmark.

See performance and fund data Click here >

Strategy
Ethical High Yield Value Bonds invests in global corporate bonds, cf. the fund's prospectus. Bond selection is based on the value approach, meaning that the team focuses on bonds issued by companies with healthy long-term earnings power and strong balance sheets as well as an expected ability to service outstanding debt. The portfolio is diversified across sectors, regions and credit ratings. At least 2/3 of the portfolio are invested in High Yield bonds. Up to 15% may be invested in corporate bonds issued by companies operating in Emerging Markets.