Sparinvest

FEAR OF POLICY MISTAKE

Losses across markets

Markets. Looking at market returns without currency risk, global stocks (MXWOHEUR) fell -4.90% in euro hedged terms. Contrary to previous quarters, we now see growth companies outperform Value companies. Initially due to expectations of peaking inflation and falling rates. When more hawkish expectations followed, growth companies held their ground and kept the outperformance.

Interest rates rose while credit spreads stayed flat leaving Global High Yield (HW00) with a -1.67% loss, Global Investment Grade (G0BC) fell -5.11%, while Emerging Market Bonds (JPM EMBI) fell -5.31%.

Patience

The Portfolio returned -4.08% and -4.45%, gross and net of fees, in the third quarter. The benchmark and Morningstar category of comparable global convertible funds returned -2.42% and -2.47%, respectively.

After seven consecutive quarters of outperformance, we have had a quarter of underperformance, mainly due to two things: Growth companies outperformed Value companies, and our current slightly defensive positioning. We see extraordinarily good opportunities in the low delta papers right now. Therefore, our portfolio reacts more slowly and we did not participate in the market rebound in July and August. On the other hand, we give better protection when the market drops.

We have a long term and patient approach in our portfolio construction. It is always difficult to be in the middle of a crisis, but we try to find the right balance between downside protection and participation when the market turns positive.

Our implied spread is 500 bps with an average credit rating of BBB-. In comparison, the straight credit market has a spread of roughly 200 bps for a BBB rating.

EDF, the French nuclear energy company, was bought by the French state, which contributed 0.6%-points to the convertible benchmark this quarter. We were not invested.

We have seen more activity in the primary market the last couple of months, in contrast to the first half of the year that has been surprisingly quiet. We have participated in some of the new issues, among others the new Lenovo convertible bond, which seems very attractive in our view.

2022 has been a frustrating year with almost all asset classes dropping significantly. On the positive side for the convertible portfolio, we have managed to get through somewhat better than a balanced portfolio with similar risk, as we would expect. Return YTD for the convertible portfolio is -17.01 and -17.94, gross and net of fees. Return YTD for global indices euro hedged:

IG index (BAML G0BC): -18.09%
HY Index (BAML HW00): -17.19%
EM Bonds index (JPM EMBI Diversified): -25.43%
Equity index (MSCI World): -23.10%
Balanced (50 equity/50 credit): -20.37%

If we turn to 3-year returns and risk adjusted returns, the convertible portfolio is a top performer, which confirms the strategic qualities of the asset class. In spite of several crisis, we have delivered an annual return of 4.1% gross the last three years.

See performance and fund data Click here >

Strategy

Sparinvest Global Convertible Bonds is a well-diversified global fund of convertible corporate bonds. Convertible corporate bonds are an asset class in the intersection between stocks and bonds that give some exposure to the stock market with a significantly lower risk than direct investment in the stock market. The strategy utilizes long-term factor premiums such as value, low debt and small cap. These are investment styles that, with certain fluctuations along the way, have historically delivered a long-term excess return compared to investments in the entire market.