Monthly Fund Commentary
Muzinich Global High Yield Fund
September 2018

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Fund

Muzinich Global High Yield Fund

Market Review

Risk-on was the sentiment of the month in September as global high yield, loans, and emerging markets (EM) outperformed Treasuries and investment grade corporates. High quality government bonds declined (yields increased) as global macro threats de-escalated (China trade tariffs at 10% not 25%, NAFTA agreement reached). September was a month of recovery within EM corporates following an eventful summer dominated by idiosyncratic geopolitical events. The countries that had made headlines earlier in the summer – Argentina and Turkey – were among the strongest performers in September as both countries made steps towards economic reforms. The European Central Bank reaffirmed its commitment to end its bond-buying program reducing its monthly purchases to €15bn from €30bn until the end of the year, although emphasized the continuation of loose monetary policy. Eurozone economic data prints continued to show a weakening of the economy, as the impact of the US/China trade war began to bite. The Italian budget dominated news flow towards the end of the month. While the final budget is not expected until later in October, the preliminary numbers emphasized a higher than expected deficit. This sent yields on Italian government debt higher amid fears of contagion into Italian financials and thus more broadly into the wider European financials landscape. In the US, the Federal Reserve (Fed) increased the Federal Funds rate as expected in September. The market (Bloomberg data) is assigning a 72% probability that the Fed will increase rates at its December meeting.

Fund Review

In this environment, the fund generated positive returns and outperformed the ICE BofA ML Global High Yield Constrained Index (HW0C) on a gross basis. The fund benefitted from strong performance across all asset classes with Emerging Markets in particular outperforming. EM generated 50% of the returns over the month, followed by the US. The fund has been increasing its EM exposure over the summer based on cheap valuations. At a regional level, the fund benefitted from an overweight in Latin America, which outperformed on both an absolute and relative basis. MEA countries underperformed on a relative basis due to the fund’s underweight in Turkey. The US led performance with 55% of the fund’s assets invested in the US, from a position low this year of 45%. Brazil and Argentina were also responsible for strong absolute and relative performance. Brazilian credit has been rallying on the improved polling of the market’s preferred candidate, Bolsonaro. On an absolute sector basis, energy and banking were the greatest contributors to performance, with energy benefitting from higher oil prices and tightening supply/demand dynamics as the market considers the prospect of Iranian oil being removed from global supply. Banking was driven by Turkish banks that rebounded in price aggressively as confidence returned with the Central bank hiking rates above expectation. By rating, the fund benefitted from an overweight of single B rated bonds, which outperformed BB and CCC rated bonds. On a duration basis, the fund remains underweight duration versus the index and underweight the long end of the curve.

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Outlook

US risk has significantly outperformed both its European and emerging markets (EM) counterparts. Is the outperformance a function of strong US economic data or a flight to quality into the perceived safety of the US? US economic data has been strong (jobs, PMI) and tax reform has added a further boost to corporate profitability. While corporate fundamentals in Europe remain strong, concerns about Brexit and the Italian budget have weighed on investors. In Emerging Markets, trade disputes with China and idiosyncratic crises in Brazil, Turkey and Argentina have led to risk-off sentiment. Are investors favoring the US as a safe haven? US valuations certainly reflect a strong technical bid while EM valuations are at their most attractive in years. The question remains, where can an investor find the best reward per unit of risk?

Important Information

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For Switzerland –

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For Singapore –

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