COVERING NOVEMBER 2020

FUND COMMENTARY
THREADNEEDLE (LUX) GLOBAL INVESTMENT GRADE CREDIT OPPORTUNITIES FUND

Alasdair Ross
Fund Manager

Ryan Staszewski
Fund Manager

Summary

- The investment-grade (IG) credit market advanced as credit spreads tightened amid optimism about Covid vaccines and the US election result.
- Gross of fees, the fund posted a positive return. Our modest long position in credit risk was favourable as credit spreads narrowed overall.
- We are optimistic on the outlook, given the vaccine news, the credit-friendly policy backdrop, and the deleveraging potential enjoyed by many IG issuers.

Market Background

November was a positive month for credit and other risk assets, as investors welcomed a market-friendly outcome in the US election and landmark results in coronavirus vaccine trials. Despite some large swings, core government bond yields were little changed overall, but credit spreads tightened across the board. The 10-year Treasury yield fell 3 basis points (bps), while the German and UK equivalents rose 6 bps and 4 bps respectively. Global IG credit spreads narrowed by around 21 bps.

Apparently unfazed by President Trump's attempts to overturn the election result, investors seemed to welcome not only a clear Biden victory, which removed not only the threat of any serious legal challenge to the outcome, but also the likelihood of a split Congress. If the Republicans retain the Senate in January as expected, it will be harder for the Democrats to raise corporate taxes and increase regulation; on the flip side, any fiscal support package that does emerge will probably be smaller than the market would like. Lower expectations for fiscal stimulus helped Treasuries outperform other core bonds over the month.

While Moderna and AstraZeneca/Oxford later reported similar successes, the big vaccine breakthrough came on 9 November, when Pfizer and BioNTech said that their candidate achieved over 90% efficacy. Core bond yields spiked, and credit spreads tightened significantly – particularly in those areas that have been most affected by the pandemic, such as travel- and leisure-related sectors.

Later, core yields fell back as record global coronavirus rates and related curbs on activity refocused investors on the short-term outlook. In recognition of the hard months ahead, the European Central Bank hinted that it would expand its stimulus in December, which also provided support for European government bonds. Credit spreads, however, did not retrace their earlier rally and indeed continued to grind tighter over the remainder of November.

Performance and Activity

In this environment, the fund delivered a positive return of 0.69% for the month (gross of fees). The moderate long credit-risk position helped performance as spreads over government bonds narrowed.

The directional strategy accounted for around half of the positive return, making a contribution of 33 bps. Top contributors included holdings in AbbVie (biopharmaceuticals), ING Groep (financial services), Southern Water Services and General Electric. The capital structure arbitrage strategy added 14 bps, with strong performance from positions in Lloyds Bank and HSBC more than offsetting negative contributions from positions in Barclays and Deutsche Bank. The event book added 12 bps, most of which was attributable to KBC (banking/insurance) and GKN (vechicle components), while the relative value book added 8 bps, with the holding in Rabobank contributing most. The carry strategy made a small positive contribution of 3 bps.

The primary market was quieter than is usual for November, though we did take part in six new issues. Four of these – from OP Bank, Thames Water, Deutsche Bank and Engie – were added to the IG directional book. The other two, from NatWest and HSBC, were added to the capital structure arbitrage book; here we also increased the existing holding of Lloyds, as well as swapping out of our dollar exposure to NatWest into the bank's aforementioned new (sterling) issue.

On the disposals side, we exited a number of issuers including Bupa (health insurance), Bharti Airtel (telecoms), Vodafone, and Upjohn (pharmaceuticals), while reducing holdings such as GKN, Digital Realty (data centres) and APT Pipelines, among others.

Outlook

The valuation case has clearly become less compelling in recent months, given the market's powerful recovery since the March sell-off. Global IG spreads finished November inside their 20-year average, roughly where they were at the start of this year.

More positively, while some difficult months remain before vaccines can turn the tide, a return to something approaching economic normality is surely now in sight. In the meantime, the support measures introduced by governments and central banks will help to mitigate the ongoing interruption to economic output and employment. Furthermore, much of the policy response to the crisis has been targeted specifically at keeping the credit channel open.

While there might be some default or downgrade risks as these monetary and fiscal support schemes wind down, the makeup of the market means this should not be a major concern. Banks, for example, represent IG's biggest single sector, and one which is underpinned by an economic policy to manage losses. Here, we would expect weaker players to merge with stronger ones and overall credit quality to remain little changed. Meanwhile, the outlook for some sectors, such as technology and food & beverages, is as good – if not better – than before the pandemic.

Even for negatively affected sectors, many IG-rated companies have significant levers they can pull in order to react, including cost-cutting, capex phasing, and working capital management, as well as inorganic activity such as asset sales, dividend cuts or equity raisings.

The policy backdrop, combined with the fact that this asset class can and will deleverage, makes us reasonably optimistic for the future – more so, in fact, than we were coming into 2020.

Important information
For internal use and for Professional and/or Qualified Investors only (not to be used with or passed on to retail clients)

Past performance is not a guide to future performance. The value of investments and any income is not guaranteed and can go down as well as up and may be affected by exchange rate fluctuations. This means that an investor may not get back the amount invested. Performance attribution source FactSet, calculated using a daily time-weighted methodology based on gross returns as at global close on the last working day of the month.

Threadneedle (Lux) is an investment company with variable capital (Société d'investissement à capital variable, or "SICAV") formed under the laws of the Grand Duchy of Luxembourg. The SICAV issues, redeems and exchanges shares of different classes, The management company of the SICAV is Threadneedle Management Luxembourg S.A, who is advised by Threadneedle Asset Management Ltd. and/or selected sub-advisors.

Certain sub-funds of the SICAV are registered in Austria, Belgium, France, Finland, Germany, Ireland, Hong Kong, Italy, Luxembourg, Macau, the Netherlands, Portugal, Singapore, Spain, Sweden, Switzerland, Taiwan and the UK; however, this is subject to applicable jurisdictions and some sub-funds and/or share classes may not be available in all jurisdictions. Shares in the Funds may not be offered to the public in any other country and this document must not be issued, circulated or distributed other than in circumstances which do not constitute an offer to the public and are in accordance with applicable local legislation.

Threadneedle (Lux) is authorised in Spain by the Comisión Nacional del Mercado de Valores (CNMV) and registered with the relevant CNMV's Registered with number 177.

Het compartiment is op grond van artikel 1:107 van de Wet op het financieel toezicht opgenomen in het register dat wordt gehouden door de Autoriteit Financiële Markten. / Pursuant to article 1:107 of the Act of Financial Supervision, the subfund is included in the register that is kept by the AFM.

Shares in the Funds may not be offered, sold or delivered directly or indirectly in the United States or to or for the account or benefit of any "U.S. Person", as defined in Regulation S under the 1933 Act.

Please read the Prospectus before investing.

This material is for information only and does not constitute an offer or solicitation of an order to buy or sell any securities or other financial instruments, or to provide investment advice or services. Information obtained from external sources is believed to be reliable but its accuracy or completeness cannot be guaranteed. All source information used in the preparation of this document is available on request. This document should be read in conjunction with the appropriate fund factsheet for the same fund. The mention of any specific shares or bonds should not be taken as a recommendation to deal.

Subscriptions to a Fund may only be made on the basis of the current Prospectus and the Key Investor Information Document, as well as the latest annual or interim reports and the applicable terms & conditions. Please refer to the 'Risk Factors' section of the Prospectus for all risks applicable to investing in any fund and specifically this Fund. The above documents are available in English, French, German, Portuguese, Italian, Spanish and Dutch (no Dutch Prospectus) and can be obtained free of charge on request by writing to the SICAV's registered office at 31, Z.A. Bourmicht, L-8070 Bertrange, Grand Duchy of Luxembourg and/or from in Austria: Erste Bank, Graben 21 A-1010 Wien; in France from CACEIS Bank, 1/3 Place Valhubert, 75013 Paris;; in Germany from JP Morgan AG, Junghofstr. 14, 60311 Frankfurt, in the UK from JPMorgan Worldwide Securities Services, 60 Victoria Embankment, London EC4Y 0JP; in Sweden from Skandinaviska Enskilda Banken AB (publ), Sergels Torg 2, 106 40 Stockholm.

The mention of any specific shares or bonds should not be taken as a recommendation to deal.

This document is a marketing communication. The analysis included in this document have not been prepared in accordance with the legal requirements designed to promote its independence and have been produced by Columbia Threadneedle Investments for its own investment management activities, may have been acted upon prior to publication and is made available here incidentally. Any opinions expressed are made as at the date of publication but are subject to change without notice and should not be seen as investment advice. Information obtained from external sources is believed to be reliable but its accuracy or completeness cannot be guaranteed. All source information used in the preparation of this document is available on request. This document should be read in conjunction with the appropriate fund factsheet for the same fund. The mention of any specific shares or bonds should not be taken as a recommendation to deal.

Threadneedle Management Luxembourg S.A. Registered with the Registre de Commerce et des Societes (Luxembourg), Registered No. B 110242

44, rue de la Vallée, L-2661 Luxembourg, Grand Duchy of Luxembourg.

In the UK issued by Threadneedle Asset Management Limited. Registered in England and Wales, Registered No. 573204, 78 Cannon Street, London EC4N 6AG, United Kingdom. Authorised and regulated in the UK by the Financial Conduct Authority.

Columbia Threadneedle Investments is the global brand name of the Columbia and Threadneedle group of companies.

columbiathreadneedle.com