

## Q&A: A global bond fund with an unconstrained approach and a cautious long-term philosophy

June 2019

For Professional Clients only. Not for distribution to or to be relied upon by Retail Clients.



Danny Fox

Geoff Hitchin

*"What we're aiming to do is produce steady returns through varying market conditions that will compound over time to produce attractive long-term performance."*

Geoff Hitchin

**Marlborough Global Bond Manager Geoff Hitchin and Assistant Manager Danny Fox explain the fund's unconstrained yet cautious approach and how they have acted to manage risk in the portfolio as the economic cycle matures.**

### What's the approach of the fund?

**GH:** "We are strong believers in investing for the long term and adding value through a conservative approach.

"The fund is unconstrained across both bonds and currencies and we make use of the freedom this offers, whilst also maintaining a cautious overall approach to risk. Our fund is highly diversified; both geographically and at the individual asset level. We invest in a portfolio of bonds from

companies and government bodies from around the world, with varying credit ratings and differing structures. We aim to add further incremental value by actively managing our foreign exchange exposures through a combination of specific currency positions and hedging.

"We have a well-established investment process, tried and tested over more than 30 years, and at the heart of this is a conservative and patient approach, with a strong focus on risk management. What we're aiming to do is produce steady returns through varying market conditions that will compound over time to produce attractive long-term performance.

"Diversification is a key strength and focus for us; we currently hold around 500 bonds from

approximately 350 issuers. Dealing in the credit markets can incur relatively high transaction costs so we focus on a core buy and hold strategy. This keeps turnover low and helps to preserve investors' capital over time. We also aim to hold bonds right through to maturity, which means that the fund generates its own stream of regular, natural liquidity."

### How is the fund positioned at the moment?

**DF:** "As you'd expect with our patient, long-term approach, the positioning of the fund tends to change only gradually over time. We have increased our average credit quality over recent months by reducing our sub-investment grade exposure to reinforce the fund's downside protection as the economic cycle matures.

Investor Support  
**+44 (0)1204 589 336**

Email  
**enquiries@marlboroughgroup.com**

---

"Currently over 80% of the fund is investment grade, or equivalent. The bulk of that, around 50%, is invested in BBB-rated bonds, where we have been reinvesting the proceeds from our reduction in high yield. Concerns have been voiced about the growth of the BBB category in recent years, with a reduction in the proportion of higher-rated bonds. Some were wary that we could see this direction of travel continue, with significant numbers of bonds slipping onto sub-investment grade ratings, with valuations to match. We believe that, in the main, these fears are overdone as most issuers have made the conscious decision to position themselves at the rating level that is most efficient for them rather than being forced there against their will. For this reason, we believe that BBBs offer the most favourable risk-return characteristics in the current environment.

"We also currently favour shorter-dated bonds and recently, through a strategy of focusing new investments at the shorter end of the curve, we've gradually been reducing duration, as yields hit historically low levels. Our aim in doing this is to reduce the impact on the portfolio when interest rates do eventually begin to push upwards again."

### **Are there any particular sectors you favour at the moment?**

**GH:** "We have some concerns about a weakening of global growth in the near-term and, as a consequence, we have a definite preference for some of the lower-risk sectors that should be better placed to weather recession. Just under 10% of the portfolio is in government-backed bonds and our corporate bond exposure is tilted towards the more defensive sectors. So, we've got nearly 11% in utilities and just over 40% in the industrials sector. We generally favour industrials over financials

anyway because the sector is so much more diversified.

"We're underweight financials, which are about 26% of the fund. Within financials, we favour insurance companies. Generally speaking, we think they have better prospects than banks, which are more directly exposed to the economic cycle.

"Geographically, our largest exposures are to North America and the UK, accounting for around 30% each. Despite the ongoing uncertainty over Brexit and US trade, we still have a general preference for UK and US businesses over those in continental Europe and the rest of the world."

### **How important are currency positions to your strategy?**

**DF:** "Currency positions are our preferred arena for tactical allocations that reflect our macroeconomic views. One of the reasons for this is that transaction costs are very low, so they don't wipe out the returns from positions based on these shorter-term views. Another benefit is that, because currencies trade against one another, there is the potential for taking positions with a lower correlation to other holdings in the portfolio. This is obviously attractive from a risk management perspective.

"We currently have a sizeable cash position in Japanese yen, which is a useful diversifier in an uncertain global environment.

"In terms of the fund's overall currency exposure, we're overweight the US dollar relative to our estimates of the positioning of our peers in the IA Global Bond sector. That's because we believe the US dollar can strengthen further against other currencies despite the recent calls for lower interest rates.

"Our overweight to the US dollar is mainly at the expense of the euro, where we've reduced our

exposure against the backdrop of a faltering economy. We're neutral on sterling, while we wait for some form of resolution on Brexit."

### **Can you give an example of a bond that fits with your investment process?**

**DF:** "We've been looking at InterContinental Hotels Group, which operates brands around the world, including the Holiday Inn and Crowne Plaza chains, and some more up-market hotels and spas.

"The growth of the middle class in many countries, particularly across Asia and most notably in China, combined with low-cost air travel, is resulting in increased spending on tourism.

"InterContinental is well positioned to reap the benefits of this trend and we think there's a strong investment case. The group has operations in over 100 countries, which mitigates country-specific risk, and its diverse range of hotel chains, from luxury to budget, should provide some protection through the economic cycle.

"InterContinental's bonds have been rated BBB since 2011 and there's protection for investors in the form of pay-outs should they fall below investment grade.

"We have recently begun to build a position in the 2022 sterling bond, as we have been favouring shorter-dated issues, but we would be equally happy to buy their longer-dated issues if we see any increase in the general level of yields pushing down the price."

### **How would you characterise the investment outlook?**

**GH:** "It's something of a mixed picture at present. Sentiment indicators and economic data for both developed and developing economies had been deteriorating since last autumn, which seemed to suggest that the momentum of global economic growth was fading.

"On the other hand, first quarter figures for the three largest economic blocs in the world - the EU, US and China - have been stronger than expected, suggesting that growth was stabilising, at least temporarily.

"We still have concerns though that the rebound in global economic growth will peter out, particularly with trade volumes falling and high levels of public and private debt.

"Inflation is lower than anticipated and that means the next move by central banks is more likely to be easing rather than tightening. A lowering of interest rates, even a modest one, is likely to be positive for bond prices and that's one factor encouraging us to believe the outlook is positive for global bonds overall."

## Risk Warnings

Capital is at risk. These are the investment manager's views at the time of writing and may be subject to change. These opinions should not be construed as investment advice. The Marlborough Global Bond Fund holds some or all of the bonds mentioned. The following is a summary only of some key items in the Prospectus. Investors in Protected Cell Company (PCC) must have the financial expertise and willingness to accept the risks inherent in this investment. Past performance is not a reliable indicator of current or future performance and should not be the sole factor considered when selecting funds. It should be appreciated that the value of Shares is not guaranteed and may go down as well as up and that investors may not receive, on redemption of their Shares, the amount that they originally invested. Investment in the Company should only be undertaken as part of a diversified investment portfolio. Investment in the Shares should be viewed as a medium to long term investment. Shares may not be redeemed otherwise than on any Dealing Day. There will not be any secondary market in the shares of the Company.

The Marlborough Global Bond Master Fund (The Master Fund) has significant exposure to bonds, the prices of which will be impacted by factors including; changes in interest rates, inflation expectations and perceived credit quality. When interest rates rise, bond values generally fall. This risk is generally greater for longer term bonds and for bonds with higher credit quality. The fund invests in other currencies. Changes in exchange rates will therefore affect the value of your investment. Bonds that produce a higher level of income carry greater risk that the issuer will not be able to pay the income or repay the capital at maturity. The fund may enter into various financial contracts (known as derivatives) in an attempt to protect the value of the fund's assets, to reduce the costs of investing or for investment purposes. There is however a risk that the desired result may not be achieved or may result in gains or losses greater than the amount originally invested.

## Regulatory Information

The Marlborough Global Bond Cell referred to is a cell of Marlborough International Fund PCC Limited (the 'Company'), a protected cell company incorporated in Guernsey and authorised as a Class B Collective Investment Scheme under the terms of the Protection of Investors (Bailiwick of Guernsey) law, 1987, as amended. Investment may only be made on the basis of the current Prospectus.

Marlborough International Management Limited is incorporated in Guernsey. Registration No. 27895.

Regulated by the Guernsey Financial Services Commission.

 **Marlborough International Management Limited, Town Mills South,  
La Rue du Pre, St Peter Port, Guernsey, GY1 3HZ, Channel Islands**

 **Investor Support: +44 (0)1204 589 336**

 **Email: [enquiries@marlboroughgroup.com](mailto:enquiries@marlboroughgroup.com)**

 **Website: [www.marlboroughinternational.gg](http://www.marlboroughinternational.gg)**

 **Administrator: (Postal applications) Louvre Fund Services Limited, First Floor,  
St Peter's House, Le Bordage, St Peter Port, Guernsey, GY1 1BR**

**Marlborough**  
International