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Aegon Absolute Return Bond Fund

Q1 2025

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Market summary

The opening three months of the year have proved to be roller coaster ride for fixed income markets. The interplay between politics, economics and financials markets succeeded in delivering one of the most uncertain periods for investors since the Covid pandemic - and one which appears to have no near-term end in sight.

Much of the market volatility came from the new White House administration. Since the election in November last year, the prevailing market narrative was around upside risks for the US economy, equity markets and Treasury yields - this spilled into the start of this year with 10yr US Treasuries touching 4.80%, its highest level since Q4 2023.

After the inauguration, President Trump's more aggressive stance on trade tariffs (and frequent backtracking on policies), caused uncertainty to rise and sentiment to fall within businesses and consumers. This increased the downside risks to US GDP. This theme has dominated since mid-February, causing the S&P to fall sharply and 10yr US Treasury yields to fall 60bps from their year-to-date peak. Credit spreads spent much of the period unmoved by the volatility before moving wider through March – US investment grade and high yield spreads widened 20bp and 70bps respectively from their February lows.

Arguably the biggest event in Q1 took place in Germany, as a massive fiscal package was agreed and passed. Totalling over EUR500bln, the mix of defence and infrastructure spending is far in excess of any increased spending plans that had been expected. This announcement saw 10yr Bund yields surge 50bps higher, turbocharged European equity markets and added further support to European credit markets. Near term growth challenges still need to be overcome - impact of trade tariffs etc – but the longer-term outlook for the European economy looks more positive.

The UK market found itself caught between the influence of offshore markets (US and Europe) and its own domestic fundamentals. The upcoming changes to National Insurance payments and concerns over the level of fiscal headroom saw UK Gilts trade poorly in early January and then fail to keep up with the fall in US Treasury yields through the remainder of the period.

The Government's Spring Statement looks to have bought the Chancellor some time, but the medium-term challenges of sluggish economic growth but with rising debt interest costs has not gone away. The Bank of England cut rates to 4.50% in February and will likely do so again in the coming months unless the stickiness in inflation proves to be too much.

Fund review

The Aegon Absolute Return Bond Fund returned 1.66% over Q1 vs 1.14% for its cash benchmark.*

The fund seeks to add value through investments in primary short-dated bonds, with active management of market risk and additional returns via relative positions. In the first three months of the year, we saw gains across each of these areas.

The market backdrop through January and February was supportive for credit risk. Robust corporate fundamentals and attractive yield levels saw strong and steady demand for corporate bonds, with short-dated bonds being a beneficiary of this dynamic. The flatness of both yield curves and credit curves increased the attraction for short-dated corporate bonds which helped push both yields and spreads initially lower.

As a result, the fund was well placed to take advantage of these moves, which drove the positive performance in the first 2 months of the year. The level of market risk or beta was managed through a combination of iTraxx Xover and iTraxx Sub-Financial contracts. Due to the supportive market backdrop, we favoured a moderate level of credit protection to allow us to take advantage of the continued spread compression. Alongside this, the uncertain and volatile macro backdrop argued against hedging any duration risk – rates market views were instead expressed through relative value positioning (see below).

In March, market sentiment became more negative with fears over growth headwinds emanating from US policy uncertainty. This caused a risk-off tone to develop: this started in US equities before spreading into corporate bonds, pushing spreads wider. To counteract these moves, we reduced the level of market risk in the fund by increasing our credit hedge via iTraxx Xover. This larger level of credit hedge was retained at month end given the uncertainty surrounding the upcoming announcements on US tariffs due in the first week of April.

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Bottom-up security selection was key over the quarter, generating an important source of alpha across a wide range of holdings. Our exposure to financial institutions was advantageous with names such as Metro Bank, Generali and Rothesay Life all adding value alongside positions in RAC, AA and Close Brothers. Our preference for European over US credit benefitted from the improved sentiment following the German fiscal announcement.

Government bonds were at the centre of the volatility within fixed income markets. They were reacting to the changing macro outlook in the US (more downside risks), in Europe (longer term upside risks) and the UK (weak growth but with fiscal headaches). The result was a varied performance across the different rates markets over the period that we looked to take advantage of.

Our rates market relative value positions performed well over Q1. After a quiet start to the year, with a short 10yr US vs long 10yr UK+ 10yr Germany adding value, our core, high conviction positions performed well from mid-February through to the end of March. Firstly, our curve steepening positions worked well. We held long 5yr vs short 30yr positions in both the US and Germany that generated alpha for the fund – the US position benefitted from the growing “stagflation” risks and in Germany from their fiscal spending plans and the debt issuance required to fund it. These positions have been retained with further upside likely over the medium term.

The fund also benefitted from a short in 10yr German Bund futures vs a long in 10yr Australian futures. The upcoming German election had the potential to usher in a period of higher fiscal spending, while in Australia, we expected the RBA to finally kick-off its rate cutting cycle. In the end, the German fiscal spending plan was much larger than anyone expected, and the RBA cut rates in February. This caused a meaningful outperformance of Australian bonds vs German bonds allowing us to take profits by mid-March.

*Source: Lipper as at 31 March 2025, B (Acc) GBP class. NAV to NAV, noon prices, income reinvested, net of ongoing charges, excluding entry or exit charges.. The benchmark is SONIA GBP 3 Month. The benchmark changed from LIBOR to SONIA on or around 9th of December 2021.

Calendar year performance (%)

	2024	2023	2022	2021	2020
Fund B Acc GBP	6.03	6.19	-0.62	0.53	2.79
Benchmark	5.16	4.34	1.03	0.09	0.29
	2019	**2018**	**2017**	**2016**	**2015**
Fund B Acc GBP	1.71	-0.14	0.81	1.44	0.71
Benchmark	0.81	0.73	0.36	0.50	0.57

Source: Lipper as at 31 December 2024, B (Acc) GBP class. NAV to NAV, noon prices, income reinvested, net of ongoing charges, excluding entry or exit charges. Launch 30 September 2011. The benchmark is SONIA GBP 3 Month. The benchmark changed from LIBOR to SONIA on or around 9th of December 2021. Since launch return is based on Cumulative Noon Lipper data. Benchmark is at close.

Important information

Investment policy

The Aegon Absolute Return Bond Fund investment policy: invests worldwide in:

- Investment grade (lower risk) and high yield (higher risk) bonds issued by companies and governments;
- Derivatives (financial contracts whose value is linked to an underlying asset);
- Cash, deposits and money market instruments (a form of debt security); and
- Up to 20% in a combination of investments in emerging markets (those economies that are still developing) and high yield (higher risk) bonds.

The Fund is actively managed.

The Fund has discretion in its choice of investments and is not restricted by market sector. It may also hold a limited range of other investments and it is not constrained by any benchmark or index.

The Fund may use derivatives for investment purposes, to benefit from changes in the price of an underlying asset without actually owning it.

The Fund may use investment techniques to manage risks and costs. These techniques include 'hedging' (using derivatives and other financial contracts to reduce the risk associated with: (i) making investments in other currencies; or (ii) interest rates changing). Up to 5% of the Fund may not be 'hedged' i.e. the Fund is exposed to the risks of investing in another currency for this portion.

The Fund may hold substantial amounts of cash to implement investment techniques or meet its objective.

Risks

The following risks are relevant to the Fund:

Credit: An issuer of bonds may be unable to make payments due to the Fund (known as a default).

Liquidity: The Fund's value may fall if bonds become more difficult to trade or value due to market conditions or a lack of supply and demand.

For more details on the risks for this fund please see the KIID or Prospectus.

Important information

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