DYNAMIC FUND

Fund Commentary

The first quarter of 2023 saw the Credo Dynamic Fund ("Dynamic" or "the Fund") return 0.4% over the period[1]. The Fund lagged the benchmark and sector (the IA Mixed Assets 40-85% Shares Sector), which returned 2.2%[2] over the period. The Fund has outperformed its benchmark by 14.6% since inception.

2023 started on a more positive note as four key factors came together: the US economy seemed to be weathering the rise in interest rates; the Federal Reserve Bank Chair began to refer to 'disinflation' on numerous occasions leading the market to believe the end of steep interest rate rises was close by; Europe battled through a winter of no Russian supplied gas without any notable interference; and finally, the quick Chinese reopening post COVID-19 buoyed the global economy.

A combination of the stocks that fell the most in 2022 bouncing in early 2023, and a reduction in the headwind of interest rate expectations, led to Growth stocks (particularly US technology stocks) leading the market in the period. Additionally, the ChatGPT release refocused investors on the power of artificial intelligence and its wide-reaching implications. The Nasdaq was up 18% in the period. In Dynamic, we utilised the bounce to reduce some of the exposure to Growthier stocks held and we also exited our long-term holding in Google.

The latter part of the quarter saw the market's focus shift to the biggest failures of US banks since the Global Financial Crisis (GFC) of 2008. Silicon Valley Bank's (SVB) failure was caused principally by investing in high-quality long-dated bonds, the value of which fell due to rising interest rates, combined with SVB's focus on niche markets. These factors led to a classic bank run reminding all that the banking relationship is implicitly built on the trust that one can access cash savings. Consequently, Europe's weakest globally systemic bank, Credit Suisse, which has been marred by years of problems resulting in financial losses, fell on its sword as UBS rescued it with the helping hand of the Swiss regulator.

The Credit Suisse / UBS takeover was controversial and sent ripples across the subordinated bond market as the most junior tier of bonds (Additional Tier 1 (AT1)) was written off while shareholders received some UBS shares. This was controversial and contravened the logic of the capital stack, while technically a possibility, the Swiss government changed the law to make it happen. European and UK regulators distanced themselves from the decision and outcome.

In Dynamic, since the significant uncertainty from the equities market emerged in 2022, the portfolio has been focused on equity-like returns from corporate bonds. This portion of the portfolio has a bias towards financials, which are high yielding yet better regulated, better capitalised and more profitable than at any time since the GFC. Our focus tends to be on the subordinated bonds (as opposed to junior subordinated / AT1) bonds, which in the Credit Suisse example were simply replaced by UBS bonds with no impairment to capital.

The Fund holds approximately 2.5% of assets in AT1 bonds and a further 2.5% across other junior subordinated bonds and preference shares across six issuers in total and these positions felt a ripple effect of the Credit Suisse write-down.

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(1) Source: Bloomberg, FE Analytics.
(2) Performance of the Credo Dynamic Fund Class A Retail Shares over the period 30/12/2022 to 31/03/2023.

The bonds were weaker over the quarter but have shown strength in recent sessions. The Fund intends to ride out any volatility, especially as there is no exposure to US regional banks where we see the greatest risk going forward, and note that none of the holdings are showing any individual signs of weakness at a business level.

Positioning

Overall, the Fund allocations remained stable, liquid, and poised to manoeuvre, and there have not been significant changes to the asset allocation. As at the end of the period, the asset allocation was 43% in equities, 41% in fixed income and 16% in alternatives.

We believe this is a very different asset allocation to our peers. We have allocated our higher returning bucket away from equities into higher-yielding bonds, which have ended the period with a prospective future return of 8.6%. Therefore, the Fund may experience periods of diverging performance in the short term, but we have strong conviction in delivering long-term returns to investors.

Contribution and Attrition

The Fund's holdings of third-party funds and ETFs tend to have larger weightings than single stocks or bonds, as the underlying is diversified, and some of these holdings saw a reversal of fortunes compared to 2022. The strongest performing asset, by some margin, was Polar Capital Technology Trust buoyed by the Nasdaq return. Conversely, one of the weakest assets was the AQR Managed Futures Fund as the trends of 2022 broke down, interest rate expectations whipped sawed on comments from Jerome Powell, and the impact from the fallout from the banking collapse.

In assessing the individual holdings, the standout performer was an overseas stock, Rheinmetall AG, which is a German automotive and arms manufacturer headquartered in Düsseldorf, Germany. The investment thesis is centred around the changing focus of European governments to restock and modernise their defence capabilities given their noisy and aggressive eastern neighbour in Russia. This process is impeded by legislative European bureaucracy, but as governments get the green light this should be a further catalyst for the company and its share price.

The largest attrition came from a UK midcap position, FRP Advisory Group plc (FRP), a professional services firm with a key focus on insolvency and restructuring. This stock is held to provide some hedge from an economic downturn especially as many companies took on extra debt to see them through the pandemic. Corporate insolvencies jumped by almost one-fifth in England and Wales in the year to February 2023 as businesses struggled with rising costs and a slowing economy. However, FRP recently notes there may be some timing issues of revenues depending on certain corporate finance transactions. This uncertainty caused some material weakness in the share price; we have been adding on weakness and see upside from current levels whatever the macroeconomic back drop, although clearly a weaker economy will be preferable for shareholders.

Looking Forward

In the current market environment, everything is very fluid and with social media and ease of access to information the market moves exceptionally quickly. For example, in the period under review, two-year US Treasury bonds were more volatile than seen in the last thirty-five years as interest rate expectations swung on bank collapses.

For the moment we believe positioning within the Fund should remain balanced and somewhat cautious. Exposure to equities is near its lows with a focus on larger companies and strong balance sheets. Our key area of focus remains in high yielding bonds which we believe provide the best risk-adjusted prospective total returns compared to other asset classes.

We look to remain agile and flexible to adapt and benefit from changing market conditions.

Please find further details on the current positioning below.

Benjamin Newton, Portfolio Manager

UK Equities	%
Gresham House plc	2.9
FRP Advisory Group Limited	2.4
Entain plc	1.8
Ecora Resources plc	1.3
TP ICAP plc	0.8
Total UK Equities	**11.8**

Equity Funds	%
DBX S&P 500 Equal Weighted UCITS ETF	8.1
Robecco Global Conservative Equities UCITS	5.4
Polar Capital Technology Trust	3.4
Jupiter European Opportunities Trust plc	2.1
iShares S&P 500 Hedged ETF	1.9
Total Equity Funds	**30.3**

Overseas Equity	%
Rheinmetall AG	0.7
Amazon.com	0.5
Total Overseas Equity	**1.2**

Alternatives	%
Hipgnosis Songs Fund Limited	2.3
AQR Managed Futures UCITS	2.2
BH Macro Ltd	2.1
Taylor Maritime Investments Limited	1.8
Gresham House Energy Storage Fund plc	1.6
Total Alternatives	**15.6**

Fixed Income	%
IG Group plc 3.125% 18/11/2028	2.7
BP plc Perpetual	2.6
Investec plc 06/03/2033	1.7
Co-operative Group 08/07/2026	1.7
Burford Capital plc 6.125% 26/10/2024	1.7
Total Fixed Income	**41.0**

Cash	%
GBP	0.2
Total Cash	**0.2**

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