Fund Commentary

The third quarter saw the Credo Dynamic Fund (Dynamic) return -0.4% over the period[1]. Although a negative return, the Fund once again outperformed the peer group and benchmark (the IA Flexible Investment Sector), which returned -1.0% in the period[2]. The outperformance since inception now stands at 16.0%.

Contribution and Attrition

The UK did not cover itself in glory in the period. First with the ousting of Boris Johnson as Prime Minister, followed by the appointment of Liz Truss as his successor, and culminating in a 'mini-budget' where the UK's ability to balance the books was called into question by the markets.

A majority of positions were in the red, but the stocks in the positive territory had more notable moves. The Fund was assisted by its global holdings; Dynamic has notably reduced the UK bias within the portfolio, taking sterling holdings down from approximately 70% in 2021 to less than 60% currently. The devaluation in sterling led to our long-term global equity holdings delivering a positive return in sterling, albeit a negative return in their local currencies.

The moves in currency markets and the volatility in global capital markets assisted our holding in the UK mid-cap company, TP ICAP plc, which was our most significant contributor in the period with a gain of over 70% adding almost 1% to the Fund's performance. As an inter-dealer broker, the company benefits as trade volumes and respective revenues are expected to increase due to market volatility. The shares had appeared excessively cheap on many measures, and additionally, the company earns fees in US dollars whilst incurring costs predominately in sterling.

A large holding within the alternative allocation is the AQR Managed Futures Fund. This fund is a multi-asset momentum-driven trend-following strategy, which is expected to do well when markets are trending strongly in either a positive or negative direction. In the period, this holding delivered a positive return in its base currency of US dollars and the additional currency gain aided it to become the second largest returning asset, delivering a contribution of 0.5% to Dynamic's NAV.

As is typical in a negative trending market, many holdings produced a negative return due to a correlation with broader markets rather than anything stock specific. No individual position hampered performance by more than 0.25%, reflecting the Fund's diversity.

Equities

While in Dynamic we pride ourselves on flexibility, our equity allocation was notably quiet within this period. As managers, we aim to be on the front foot and move quickly. As such, midway through last year we reduced exposure to areas with higher risk and volatility. This included smaller companies, expensively rated companies, more leveraged companies, and general exposure to the UK. In the UK, due to the European

(1) Source: Bloomberg, FE Analytics.
(2) Performance of the Credo Dynamic Fund Class A Retail Shares over the period 30/06/2022 to 30/09/2022.

gas crisis, combined with higher and more persistent inflation, there is a heightened and potentially deeper recession risk. Equity exposure has been reduced from approximately two-thirds of the Fund last summer to currently approximately 45%, which is roughly flat over the period.

The key driver of markets at present is inflation and the effect this has on interest rates. Although equities have fallen from their highs seen last year, there is a limited temptation to increase this exposure until we see clear signs that inflation is under control or that equities show extreme value that is too cheap to ignore. As it stands, if the bear market were to end today, this would be the most expensively valued bear market in history. Thus, inactivity feels appropriate, even if uncomfortable.

Markets can move quickly and somewhat unpredictably. Therefore, we aim to retain our core long-term equity exposure.

Fixed Income

Whilst sitting on our hands in the equity allocation, the fixed income portion has proved somewhat different. Dynamic has been actively increasing exposure into market weakness.

Corporate bond prospective returns are composed of two constituents: the risk-free return (government bonds) and the additional return investors require for taking a company's credit risk (the spread) across the underlying maturities.

It has been well documented that the risk-free rate has significantly increased, albeit from a low level, to combat the threat of inflation. It is challenging for anyone to accurately predict the changes in interest rates, given it is very much dependent on the economic data and how quickly one can quell the spike in inflation. When interest rates rise, bond prices fall. However, it is essential to note that the bond market is forward-looking. Therefore, a change in rate expectations moves prices as opposed to the actual monthly changes made at the Bank of England monetary policy meetings. Partly due to the recent UK 'mini budget', UK rates are expected to accelerate past their US counterparts and peak out close to 6%.

In a similar vein to base rates, spreads in sterling have come from a low base of approximately 1% additional return for credit risk in 2021 to current spreads of 2.3%. This is attractive on a medium-term view and was only eclipsed in the last decade very briefly in the time of the market panic during COVID-19. However, this is still a long way from the financial crisis's credit spreads of severe distress. Although from a macroeconomic perspective, in a time of grave economic difficulty, one would expect rates to fall, implying a higher spread than stated.

Dynamic has been quicker to add bonds rather than equity as we see better relative value to history. We are paid to wait, and we ladder the portfolio including many short maturities. The short-dated bonds give the certainty (dependent on company solvency risk) that the capital and income return in the coming year will be reinvested at prevailing market opportunities.

The fixed income allocation troughed last summer below 20%; at the same time, the equity allocation peaked, and global bond yields bottomed. In the previous six months, yields have increased, so has the pace of our additions to fixed income, growing almost 7% per quarter to end the period at 37%. We would expect to see the allocation follow the trend of yields; if yields continue to rise so will our allocation.

Alternatives

Alternatives have been an important and profitable part of our strategy and performed exceptionally well over the last few quarters. The alternatives tend to be quite varied in nature. The common denominator is that we only invest in liquid assets and aim to have a low correlation to markets.

A popular aspect, particularly in a time of low interest rates, has been a broad number of income-generating investment trusts. Rewinding back to 2021, corporate debt was yielding 3 - 4% with limited potential for capital upside. Subsequently, Dynamic notably increased the allocation to the income generating alternatives universe, yielding 5 - 6% with additional capital upside potential. As this yield arbitrage has now reversed, so has the allocation to this type of asset, favouring an increase in allocation to fixed income. For example, Real Estate Investment Trusts (REITs) have been a key area for us in recent years especially as real assets are known to perform well in an inflationary environment. However, there are some concerns about the underlying value of the properties and the implication of the cost of debt given the increase in rates. As such, Dynamic has exited its long-term holdings in Supermarket Income REIT plc and Urban Logistics REIT plc at attractive levels. Additionally, the Fund had a significant holding in renewable energy investment trusts. It has been a profitable and rewarding journey for Dynamic, as these trusts benefit from increased power prices and inflation linkage while supporting the UK energy transition. Dynamic has reduced exposures in light of pressure on the UK government to tax energy providers. However, Dynamic retains exposure to a pan-European play with significant exposure in Gresham House Energy Storage Fund plc (GRID). GRID is a battery provider to the grid, helping to smooth the volatility of power supply and demand, which is ever-increasing with the penetration of renewables. Returns are generated from several means and benefits from intraday power price volatility and so appear less at risk of government legislation.

Alternative investments will always be a feature of this multi-asset fund to help smooth the volatility of returns. Dynamic finished the quarter with a 16% exposure to alternatives, down from 22% at the close of the prior quarter.

Looking Forward

There is no doubt in my mind that the future will bring new stock market highs, as it always does. Population and GDP will grow, and companies will continue to innovate. This will lead to higher company earnings, dividends, and a higher stock market. Valuations are reasonable once again, bonds, at long last have attractive yields, and even cash can generate a return. At some point, as history shows us, markets storm ahead, potentially without warning making us look back in astonishment at some of the bargains we could have achieved if a little braver or more fortunate. For this reason, there is no doubt in my mind those with long-term investment horizons should be investing.

DYNAMIC FUND

Nonetheless, taking a shorter-term perspective, it feels like markets are caught somewhere in no man's land. Whilst assets have fallen, this is relative to excessive pricing last year, fuelled by extreme amounts of stimulus and interest rate levels at all-time lows. As interest rates rise rapidly, the implication to the economy and company earnings has yet to be impacted. The conundrum of knowing things will get better in the long term, but worrying about short-term downside, can prove tricky and is a hard balance for all investors.

As a reminder, we assess Dynamic as a combination of two halves. Half of the Fund is invested for the long term (the core); accepting the price of long-term growth is volatility and recognising the many pitfalls of trying to time the market. The other half is more tactical (the satellite). The satellite is used to complement the core when we are constructive on the world or to reduce volatility, like at present, when we are concerned about the downside. Equity exposure in this satellite portion is low, and exposure to short-dated bonds and negatively correlated assets is high. As we are neither extremely risk averse nor fully embracing the pullback, we know we will not be the top or the bottom performing fund next quarter. That accolade will be taken by the manager who takes the most or the least risk, and I have no inkling as to which it will be. We do, however, believe the balanced and somewhat cautious approach will serve us well until we feel the time is right to embrace risk head on once again.

Please find further details on the current positioning below.

Rupert Silver, Lead Portfolio Manager

UK Equities	%
Gresham House plc	2.4
GSK plc	2.1
K3 Capital Group plc	1.7
North Atlantic Smaller Companies	1.6
TP ICAP plc	1.4
Total UK Equities	**16.3**

International Equity Funds	%
DBX S&P 500 Equal Weighted	6.6
Polar Capital Technology Trust	5.3
Robeco Global Conservative Equities Fund	2.7
Worldwide Healthcare Trust plc	2.4
iShares MSCI World Value ETF	2.0
Total International Equity Funds	**25.2**

Overseas Equity	%
Alphabet Inc	2.5
Amazon.Com	0.5
Total Overseas Equity	**3.0**

Alternatives	%
AQR Managed Futures UCITS Fund	3.4
Gresham House Energy Storage Fund plc	2.3
Hipgnosis Songs Fund Ltd	2.1
Literacy Capital plc	1.1
L&G Multi Strategy Enhanced Commodity ETF	1.0
Total Alternatives	**16.3**

Fixed Income	%
Burford Capital plc 6.125% 26/10/2024	2.5
UK Index Linked Gilt 0.125% 22/03/2024	1.9
USA Index Linked 0.75% 15/02/2045	1.8
Vodafone Group plc Var 03/10/2078	1.7
Ford Motor Credit Co LLC 2.748% 14/06/2024	1.2
Total Fixed Income	**37.1**

Cash	%
GBP	2.2
Total Cash	**2.2**

DYNAMIC FUND