VT Tyndall Real Income Fund

Monthly Commentary | June 2023

TYNDALL

Review

June was a relatively steady month in equity markets, certainly compared to May. The UK market was more subdued than many other international markets, but the iShares UK Equity Index tracker still managed a gain of +0.81% for the month.

In the US, the 'debt ceiling' agreement was indeed reached and a potential default on US government debt was thus avoided. Meanwhile, the Federal Reserve, in the wake of an encouraging fall in inflation, decided to 'pause' its interest rate hiking campaign and await further data. Optimists hope this will mark the end of the aggressive increase in interest rates seen over the last 12 months or so, although Chairman Powell was at great pains to stress it may not be the case.

Elsewhere, economic data, particularly in the manufacturing sector, continued to weaken considerably, most notably in China and the Eurozone. In the case of China, the authorities do indeed seem to be adding incremental stimulus measures now and it remains to be seen how far they go and what the impact on growth will ultimately be. In contrast, central bankers at the ECB continue to talk tough on inflation and the potential for further interest rate increases, despite the signs of economic weakness.

Finally, here in the UK, considering higher than expected inflation rates, a seemingly resilient labour market and still strong wage gains, the Bank of England opted to surprise markets by raising interest rates 0.5% to 5.0%, the highest rate since 2008. We confess to being puzzled by many of the Bank's forecasts and actions over recent years and we cannot help but be concerned by this latest announcement, smacking as it does of panic. Interest rates were just 1.25% only 12 months ago and the lagged effects of the significant increases since then are unlikely to have had a full impact on the economy yet. Patience is an extremely valuable commodity in the investing world, and perhaps it ought to be for central banking too.

Unsurprisingly, UK government bond yields have risen sharply following the latest interest rate increase and mortgage costs are also rising rapidly. Whilst the UK consumer has remained resilient thus far, this will likely present yet another, in a seemingly endless list, of challenges going forwards.

Fund performance / Activity

Given the cyclical and mid-market bias to our portfolio, our fund declined modestly during June by -0.66% (share class A GBP Net Accumulation). Whilst this lagged the iShares UK Equity Index tracker gain of +0.81% it did, marginally, outperform the peer group average fall of -0.71%.

There were several positive relative contributors to performance in June, including holdings such as Games Workshop, Ashtead, MoneySuperMarket, Hill & Smith and Prudential. Not owning index heavyweight AstraZeneca also proved beneficial as their share price underperformed. Detractors to performance came from a variety of holdings such as DS Smith, PageGroup, Vistry, Ashmore and DFS Furniture. Not owning HSBC and Shell also proved detrimental as their share prices performed well.

June was another relatively quiet month in terms of portfolio activity, making no complete disposals and introducing one new holding to the fund, Polar Capital. We added modestly to Weir, Entain, PageGroup, Ashmore and Vistry, and took profits in Ashtead, Hill & Smith, Melrose, and Rolls Royce.

Market Outlook

As we enter the, typically quieter, summer months, markets remain caught in multiple cross currents with respect to the outlook for inflation, growth, interest rates and corporate profitability.

In general, the UK notwithstanding, there are good reasons to be hopeful that inflation rates have peaked and are coming down to more manageable levels. Whilst these may not be in the 0 – 2% range we have been accustomed to in recent times, it should still come as a welcome relief from the dizzy heights of 8 – 10% plus we have recently experienced.

That being the case, we ought also to be relatively close to the peak in the interest rate cycle, even if there are still a small handful of rate increases in our immediate future. The debate will then naturally move on to how long rates stay 'higher for longer,' and perhaps also to whether 2% is still the appropriate inflation target in a world that seems to have significantly changed with respect to deglobalizing supply chains, heightened geopolitical uncertainty and so on.

Whilst economic and corporate data has held up much better than many feared over the last 12 months or so, there are clearly signs of weakness emerging, and it remains to be seen how much further the data might deteriorate as the lagged effect of aggressive monetary policy tightening works its way through the various economies.

As we have written numerous times recently, our default position has been, in the face of some of the most extreme pessimism we have experienced, to err on the side of a more optimistic take on prevailing economic and market conditions and we continue to hold that view today. Additionally, we observe market pricing in many of the areas where investors are most concerned to already be reflective of a scale of weakness we feel highly unlikely to materialise in all but the most extreme scenarios. It is in these areas, such as mid-cap domestic cyclical companies, where we are finding the most compelling opportunities for the medium term.

We continue to expect a degree of volatility in markets in the near term, as investors wait for greater clarity regarding the outlook. Notwithstanding this uncertainty, we remain extremely enthusiastic for the upside potential for the portfolio, and we remain happy to purchase more shares, at attractive prices, in any further bouts of market weakness.

Simon Murphy, Fund Manager, VT Tyndall Real Income Fund, July 4th 2023
Data source (unless otherwise stated): Bloomberg, FE Analytics

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AAA Rated Fund Manager

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