COMMENTARY

Janus Henderson Absolute Return Income Opportunities Fund

December 2019

For promotional purposes
For professional investors only

Fund manager names: Nick Maroutsos and Jason England

Investment Environment

Global bond markets registered modest gains during the month with losses incurred from rising interest rates more than offset by narrowing spreads on corporate credit. Fuelling the optimism was a potential truce in the US-China trade war along with the possibility that global purchasing managers' indices (PMIs) have bottomed. With the US Federal Reserve (Fed) hinting that it would not raise rates until there was a noticeable acceleration in inflation, the yield curve on US Treasuries and other global sovereign bonds steepened during the period.

Performance Discussion

The fund underperformed its benchmark, the FTSE 3-month US Treasury Bill Index.

The fund's core holdings of cash-based corporate and securitised credit generated positive returns, with both the income generated from these securities and spread tightening contributing to performance. The duration component of these securities, especially on Australian holdings, moderately detracted from overall performance given the rise in interest rates over the period. Similarly, the fund's positions in government bonds also weighed on performance. Much of this exposure is aimed at hedging overall portfolio duration and thus it is expected that negative returns can be generated depending upon the behaviour of interest rates. On occasion we also attempt to generate excess returns in by capitalising on movements in foreign currency markets. For the month, positions in the euro detracted from results.

Outlook

We expect the fixed income environment in 2020 to be similar to what we experienced in 2019 in that the predominant trend will be one of growing policy accommodation by central banks. A notable exception is the uncertain trajectory of the Fed. While we expect it to ultimately resume lowering, it has hinted that after three rate cuts it is willing to pause until economic conditions merit action. In this sense, the Fed's normalisation program which commenced in 2015 paid dividends as it afforded the bank sufficient dry powder to react in an economic downturn. Other central banks are not so fortunate and will likely have to rely upon non-traditional measures to support their fragile economies.

We believe that inaction was likely the Fed's playbook for this past year, but the market forced its hand as concerns about weakening global growth festered. Some of these concerns have not left us. While inroads have been made in breaking the US-China trade impasse, a tenable resolution that could reignite the languishing manufacturing sector and soft trade flows is far from certain. Much of the optimism priced into riskier asset classes as we closed out 2019 reflected a "better-case" trade scenario. The high valuations of both corporate credits and equities could quickly reverse should the two countries retreat to a more protectionist stance.

In Europe, the Brexit saga continues to hang over markets as do questions about whether the European Central Bank (ECB)'s latest increase of asset purchases will move the needle for economic growth, especially if governments remain hesitant to implement fiscal stimulus. A new risk is the policy uncertainty thrust upon markets by the US election cycle. Sectors ranging from heath care and energy to technology and financials may all be impacted by proposals of leading presidential contenders.

Fed policy itself is a risk that merits close attention. We believe that lower nominal interest rates are a secular trend, and one from which the US is not exempt. Ultimately, we expect the Fed will reengage in rate cuts, but its timing represents a risk to markets. We don't foresee a "doom" scenario as we do not think a near-term recession is on the cards. In the wake of the Fed's "not-quite-dovish" October statement, futures markets have backed off their expectations for 2020 rate cuts, but they still price in more than what Fed officials estimate. Should the Fed stick to its guns and the yield curve steepen more than it already has, we could foresee repricing across a range of risk assets.

Despite our view that a strong US consumer and accommodative policy by central banks will likely stave off global recession, the lack of clarity on this cocktail of risks means that investors should expect higher levels of bond market volatility. One place where this volatility may manifest itself is the longer end of the US Treasuries curve. Tight spreads may mean that the upside of US corporate credits is limited as well. Other markets appear better positioned as their monetary authorities are firmly in the easing camp and their corporate sector may not be as richly priced as comparable US issuers.

Source: Janus Henderson Investors, as at 31 December 2019

Please note that with effect from 28 June 2019, Jason England also manages the fund. Effective 15th of February 2019, Bill Gross departed the portfolio. Please note that as of 15th February 2019, Nick Maroutsos now manages the fund. Effective 1 March 2019, the Janus Henderson Global Unconstrained Bond Fund has been renamed to the Janus Henderson Absolute Return Income Opportunities Fund.

Janus Henderson Absolute Return Income Opportunities Fund

For further information on the Janus Henderson fund range please contact your local sales office or visit our website: www.janushenderson.com

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