COMMENTARY

Janus Henderson Strategic Bond Fund

Q3 2020 **For promotional purposes**

Fund Managers Names

John Pattullo, Jenna Barnard, CFA

Macro backdrop

The third quarter was another strong quarter for corporate bonds as they continued the V-shaped recovery from the March sell-off. News flow during the quarter continued to substantiate and support our shift to corporate bonds. Firstly, default rate expectations in the high yield market fell precipitously with European high yield default rates now expected to be around 4% while the US market (which includes more energy/ commodity companies) fell as low as 6%. This compares to March estimates of 10-14%, which were in-line with previous recessionary peaks. Secondly, the investment grade corporate bond market in the US followed the Japanification/European-ification trend by recording an all-time low in yields (below 2%) and an all-time high in prices. This was our non-consensus expectation when the COVID-19-pandemic began to hit in early March and it has played out with remarkable speed.

Fund performance and activity

The fund returned 2.2% during the quarter, outperforming the IA Sterling Strategic Bond sector return of 1.9% as we continued to benefit from the major asset allocation shift towards corporate bonds during the COVID-19 crisis.

The aggregate credit beta or duration times spread (DTS) of the fund reduced through to the end of August as we sold down some longer-dated investment grade bonds following the strong rally in this asset class, and due to some concerns about sovereign bond yields being artificially low. It should be noted that following the rise in high yield bond spreads in September, we increased the DTS of the fund somewhat by allocating to this less-duration sensitive asset class. We remain structurally bullish on corporate credit markets and we think that the simple reality is that there is little credible alternative for income investors other than quality corporate bond exposure. We remain in an early cycle environment and, crucially, just past the peak of the default cycle. The distribution yield on the fund at end September was 3.4%.

The one area of the fixed income market that, in our view, looks mispriced relative to the news flow around the rate of change of the economic data, is sovereign bond yields. To be clear, we are not structurally bearish on government bonds and we think yields remain lower than in previous cycles, but from a tactical perspective they have clearly decoupled to the downside relative to the speed and scale of the recovery since April. This is highlighted clearly in our own proprietary rate of change model but could also be easily illustrated versus basic purchasing managers' index (PMI) levels too.

This downshift in yields may be permanently explained by the new guidance for central banks, which effectively sets an extremely high barrier to ever hiking rates. Or it may be a classic case of bonds lagging the recovery as we saw in 2012 and 2016. We lean somewhat towards the latter view and are aware that a Democratic sweep in the US election would increase the chances of a $2 trillion additional fiscal stimulus, which is equivalent to approximately 8.5% of US GDP growth. In August we reduced the duration on the fund both by selling investment grade corporate bonds and, latterly, using interest rate futures to further reduce the US duration contribution in particular.

Outlook/strategy

We remain structurally positive on our outlook for corporate credit and we have continued to increase the physical high yield corporate bond position of the portfolio during the quarter, having taken some profit on the high yield credit default swap (CDS) position in early June. We also took some profit on investment grade bonds.

Corporate bond markets have past the peak of the default cycle, spreads remain wide relative to government bond yields and in our view there are few alternatives to credit markets for solid, dependable income. Sovereign bond yields look tactically too low in yield, but we do not think this changes the structural outlook for credit markets more generally.

Source: Janus Henderson Investors, as at 30 September 2020

Janus Henderson Strategic Bond Fund

Fund information

Peer group benchmark	IA Sterling Strategic Bond
Peer group benchmark usage	Target,Comparator

The Investment Association (IA) groups funds with similar geographic and/or investment remit into sectors. The Fund's ranking within the sector (as calculated by a number of data providers) forms the basis of the Fund's performance target and can be a useful performance comparison against other funds with similar aims.

Objective	The Fund aims to provide a return, from a combination of income and capital growth over the long term.
Performance target	To outperform the IA Sterling Strategic Bond sector average, after the deduction of charges, over any 5 year period.

Performance in (GBP)

Performance %	I (Net)	Peer group	Quartile ranking
1 month	-0.5	0.0	4th
YTD	6.3	2.2	1st
1 year	5.7	3.1	1st
3 years (annualised)	5.0	3.3	1st
5 years (annualised)	5.1	4.2	2nd
10 years (annualised)	5.4	4.4	1st
Since inception 25 Nov 2003 (annualised)	6.0	4.4	-

Source: at 30 Sep 2020. , performance is with gross income reinvested. Performance/performance target related data will display only where relevant to the share class inception date and annualised target time period.

Discrete year performance %	I (Net)	Peer group
30 Sep 2019 to 30 Sep 2020	5.7	3.1
30 Sep 2018 to 30 Sep 2019	10.7	6.9
30 Sep 2017 to 30 Sep 2018	-1.2	-0.1
30 Sep 2016 to 30 Sep 2017	3.3	3.1
30 Sep 2015 to 30 Sep 2016	7.5	8.2

Source: at 30 Sep 2020. , performance is with gross income reinvested. Discrete performance data may change due to final dividend information being received after quarter end.

Source for target returns (where applicable) – Janus Henderson. Where quartiles are shown, 1st quartile means the share class is ranked in the top 25% of share classes in its sector.

Please note the performance target is to be achieved over a specific annualised time period. Refer to the performance target wording within the objective.

Since inception performance relates to the period from Nov 2003. Performance achieved prior to this date is not representative of the fund’s current strategy.

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Past performance is not a guide to future performance. The value of an investment and the income from it can fall as well as rise and you may not get back the amount originally invested.

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