PICTET
Asset Management

Pictet - EUR Short Term Corporate Bonds - I

Risk and reward profile

Don't take unnecessary risks. Read the Key Investor Information Document.

Lower Risk						Higher Risk
1	**2**	3	4	5	6	7

Typically lower rewards — Typically higher rewards

Market review

Russia's invasion of Ukraine overshadowed what had already been an eventful month. It began with growing noises that central banks would be forced to embark upon a much more aggressive tightening cycle than anticipated. The month ended with a massive risk-off move prompted by warnings and then the reality of Russia's invasion of Ukraine, which in turn triggered severe sanctions on Russia that have had a severe market impact across asset classes. The negative tone from geopolitics and central banks weighted on risky asset performance. In fixed income, the prospect of higher inflation and hawkish central bank action hurt sovereign bonds although there was some relief towards the end of the month in the risk-off move. Regardless, treasuries (-0.7%), bunds (-1.2%) and gilts (-1.6%) all lost ground while periphery spreads widened and underperformed. As a result, government curves bear flattened. The 1-3 & 3-5Y maturity segments repriced tremendously. Elsewhere in fixed income, major DM credit indices fell, with losses shared among IG and HY, across EUR, GBP and USD. It was the worst start of the year for the DM IG since 1980. DM HY underperformed DM IG and European credit (-2.6% for IG) underperofmed US credit (-2.2%). Nevertheless, the short-term EUR IG market held up relatively well, delivering -0.91%. EDF was downgraded from Baa3 to Baa1 and Sparbank from A2 to A3 by Moody's.

Performance analysis

The fund performance was negative in absolute and relative terms. Both duration and credit spreads contributed negatively to the monthly P&L. Our overweight 3-5Y duration compared to the 1-3Y benchmark duration range explained the bulk of the underperformance as the 3-5Y segment repriced sharply on the back of more hawkish central banks. Within credit, both our financial and non-financial exposures contributed negatively. We were negatively impacted by the subordinated decompression, especially on our long corporate hybrids exposure compared to the benchmark. Futures hedges contributed positively but were not enough to compensate the losses. At the single name level among our top contributors, we can mention our zero weight in Raiffeisen, Aroundtown, BMW, and HSBC, which have some indirect exposure to Russia. On the negative side, we can mention our overweight to EP infrastructure, Enel and BP. These issuers have business activities related to oil & gas and therefore were directly impacted by the Ukraine/Russia situation. We exited EP but maintained our exposure to BP and Enel as those issuers have a strong and solid balance sheet. Otherwise, we don't have any direct Russian, Ukrainian or Chinese exposure in the fund.

Portfolio activity - overweightings & underweightings

Trading activity using cash bonds remained subdued in February amid the market sell-off and mounting uncertainties. We moved from underweight to overweight duration to take advantage of the likely more dovish stance from the European central bank. We might be neutral again in the coming weeks. We added a few quality names with good ESG credentials. We reduced our cross currency trades, focusing on EUR as value is emerging in EUR. EUR credit has underperformed USD GBP credit; it is therefore interesting to buy euro again in the short term. We initiated a short OAT to hedge the portfolio while going into the French election. Finally, we reduced our exposure to names with a tight spread to give us the ability to redeploy capital in more attractive bonds. The current market environment is starting to create dislocations and we stand ready to capture opportunities when they will arise. We maintain a healthy 5-10% cash buffer. Yield is attractive at 1.1% (especially compared to the 2Y Bund closing at -0.54%) and our short duration approach comes as an hedge in this inflationary environment.

Market outlook

At a macro level, the three main risks we are monitoring for 2022 are the geopolitical risks and associated sanctions on Russia, a China slowdown bleeding into global growth and the ongoing fallout of a higher inflationary backdrop. Russia's invasion is clearly at the forefront of investors' minds. While we don't have any Russian or Ukrainian exposure, we are monitoring the impact of the sanctions and what they can bring to the financial system in terms of counterparty risks; these are so far underappreciated by the market. If these risks escalated, they would undoubtedly lead to dovish central banks. However, at present they are trapped in a corner, with inflation remaining elevated but with growth at risk of slowing even before they start hiking. The ECB might have to find ways to dial down its recent hawkishness with war and sanctions on its doorstep. We still note many underlying credit market fragility in weaker names such as questionable fundamentals, elevated corporate leverage and the overall deterioration of credit quality, particularly in terms of IG indices. Differentiation between stronger and weaker ESG names is set to continue as the number of funds migrating to SFDR Article 8 and 9 is increasing.

Portfolio strategy

Parts of IG are beginning to look more attractive in terms of the spread levels, and we will selectively look to add here, particularly if the situation shows signs of improvement. Therefore, we are keeping a positive cash balance to put capital at risk and take advantage of new opportunities when they arise. We will also look into the primary market to source new opportunities with attractive premiums. Following the sharp repricing of government curves in February, we tactically shifted the portfolio duration from underweight to overweight to take advantage of the flight to quality. Specifically, we maintained our overweight in the 3-5Y but reduced our underweight 1-3Y segment. We might go back to underweight or neutral duration depending on the future rate moves. In addition, we turned our attention toward EUR credit as value is emerging in EUR compared to USD or GBP. EUR has indeed unperformed USD and GBP credit in this market sell-off, creating opportunities for EUR credit. Overall, we maintain a long bias toward more defensive sectors and quality (Senior vs Sub). That being said, we are analysing and gathering investment ideas, especially looking at subordinated debts (both corporate and hybrid) and longer-dated bonds in which we can deploy capital quickly enough to benefit from the rally should the situation improve

General information

Legal form	Sub-fund of a SICAV
Regulatory status	UCITS
Domicile	Luxembourg
Inception date	25.11.2013
Launch date	25.11.2013
Share class currency	EUR
Compartment currency	EUR
ISIN	LU0954602677
Reference index	BLOOMBERG INDICES EURO-AGGREGATE CORPORATE 1-3 YRS A-BBB BOND INDEX
Min. investment horizon (year(s))	1

Fees

Ongoing charges (OCR)	0.46%
Performance fee (excluded from OCR)	-
Management fee (included in OCR)	0.25%
Max. conversion fee	2.00%
Max. subscription fee	5.00%
Max. redemption fee	1.00%

Management team

Jon Mawby
Mathieu Magnin
Charles-Antoine Bory

Source: Pictet Asset Management

Further information can be found in the prospectus.

Pictet Asset Management

For further information, please visit our website assetmanagement.pictet