

Fixed Income Quarterly Strategy

JULY 23

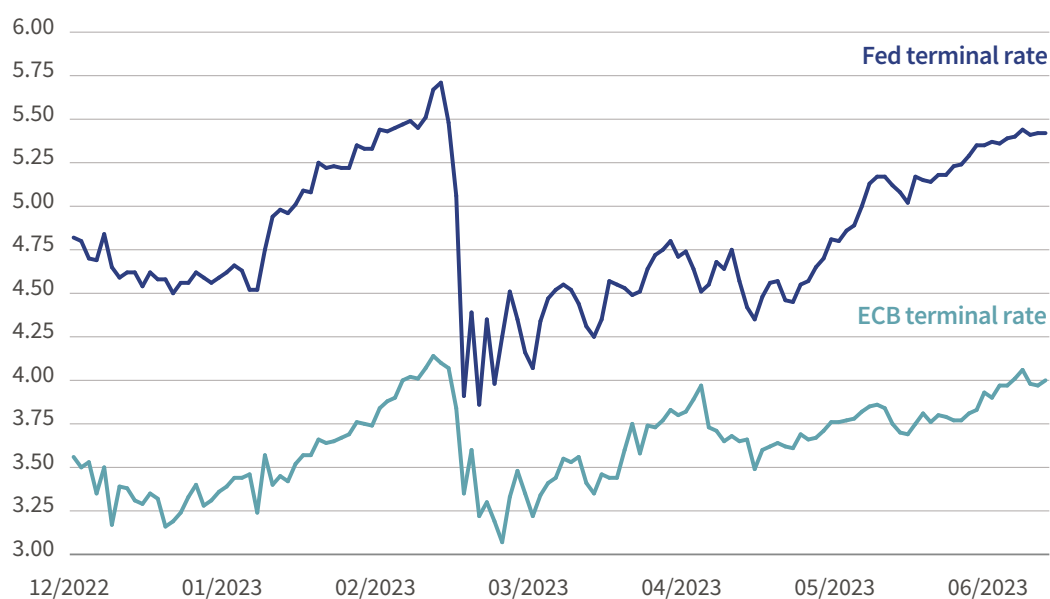
→ In the first quarter of this year, investors were wondering whether central banks would be able to rein in inflation. The last three months have shown that the danger now lies in potential over-optimism.

The glass half-full

It has been quiet sailing on the markets in very uncertain waters. A split has, in fact, emerged between the signals emitted by the fixed Income market and the assessment of risky markets. Risky markets seem very confident that central banks will be able to control inflation without significantly undermining the economy or triggering a recession. We don't believe in this scenario, but it does seem to be the currently predominant. As an example, fears surrounding the banking sector have faded rapidly, and key rate forecasts have returned almost to levels that prevailed prior to the collapse of Silicon Valley Bank and Credit Suisse. This event is now considered an epiphenomenon.

Evolution in key rate forecasts to end 2023

%

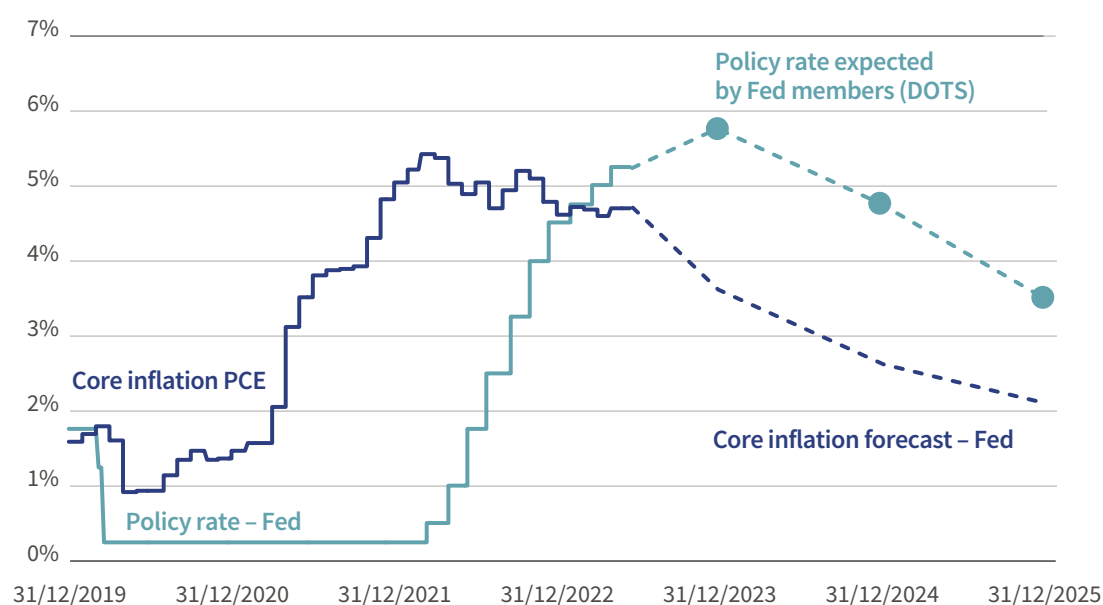


Sources: Bloomberg, Rothschild & Co Asset Management, 30/06/2023.

In general, we are seeing relative complacency regarding the current uncertain environment. This is showing up in risk premiums, which remain rather narrow, and in low levels of volatility. Even so, the yield curve has become even more inverted than it was in the first quarter, and to a degree not seen since the Volcker period. The long section is stuck in place, suggesting that inflation expectations are still anchored (10-year forecasts are currently at 2.25%⁽¹⁾). This situation illustrates how much confidence the markets have the central banks.

(1) Source: Fed, Bloomberg, Rothschild & Co Asset Management
26/06/2023

Core⁽¹⁾ PCE inflation and forecasts – USA %

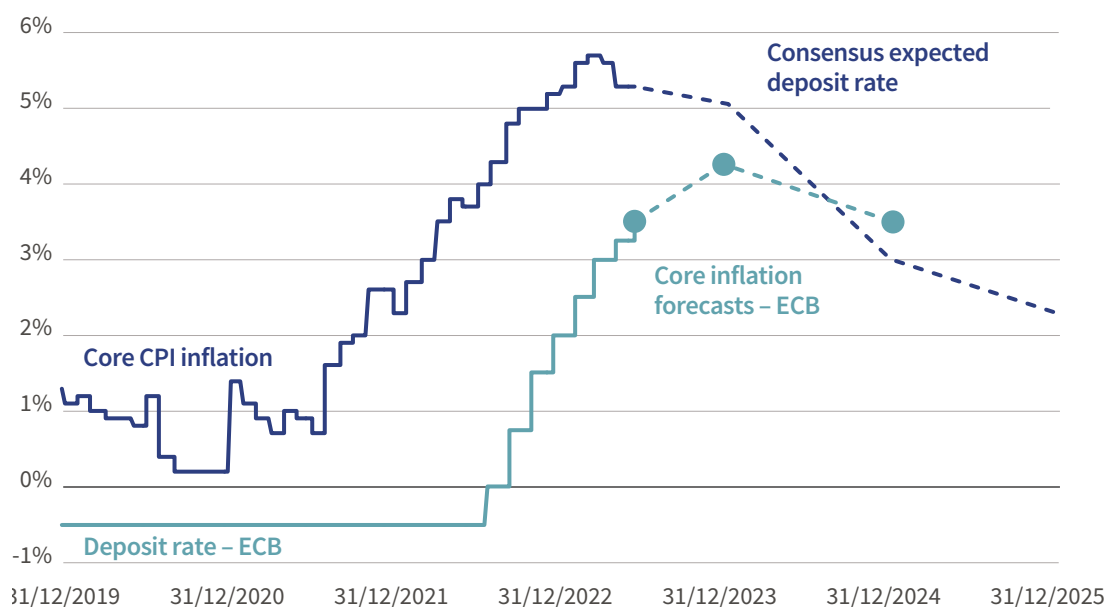


Sources: Bloomberg, Rothschild & Co Asset Management, 30/06/2023.

(1) Excluding food and energy.

Core CPI⁽¹⁾ inflation and forecasts – Eurozone

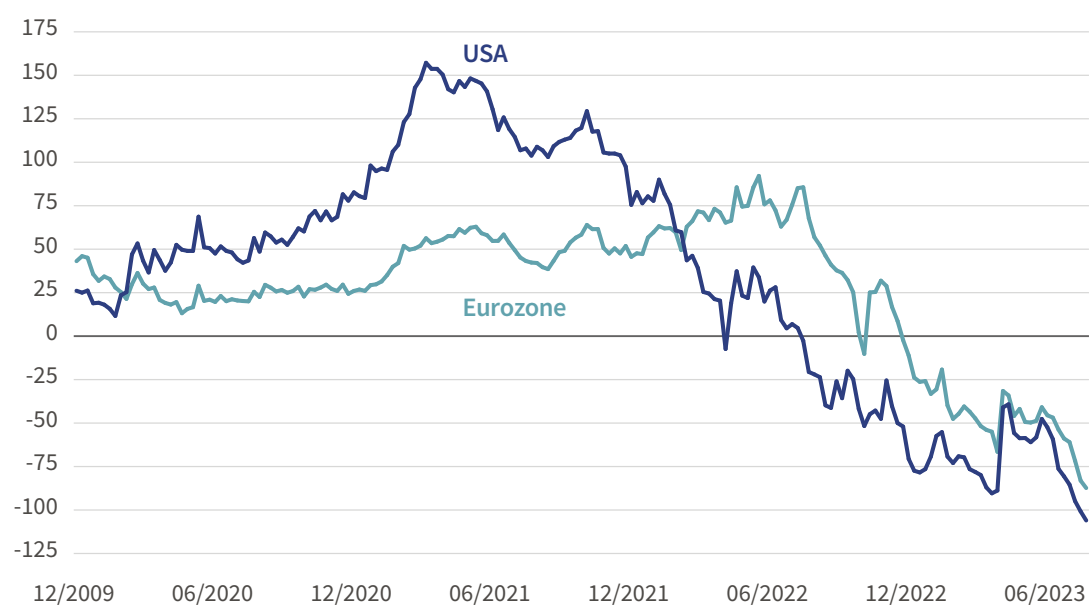
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Sources: Bloomberg, Rothschild & Co Asset Management, 30/06/2023.

(1) Consumer Price Index

Yield curve - Slope 2 years - 10 years in bp



Sources: FMI, Bloomberg, Rothschild & Co Asset Management, 15/06/2023.

Too much confidence?

Central banks now face a new task – to avoid euphoria spreading through the markets. Aware of the risks inherent in excessive optimism, they are hammering away at a message of hawkishness, with their paramount goal being to get inflation back to their 2% target. But yet, the Fed has opted for the status quo in its tightening cycle – In March the central banks of Canada and Australia had done likewise before resuming their rate hikes. The mystery is even greater as the language is more hawkish than during the months preceding this decision.

Moreover, the Fed is still projecting two consecutive hikes, while the markets are now pricing in just one. There is always a lag between the implementation of a monetary policy and when its effects show up. We are entering a phase in which we will be assessing, month-by-month, the impact of the latest decisions, especially as a disinflationary trend seems to be beginning. Indeed, this could suggest that the situation will gradually “normalise” without the steep rise of previous months having had a major impact on the economy.

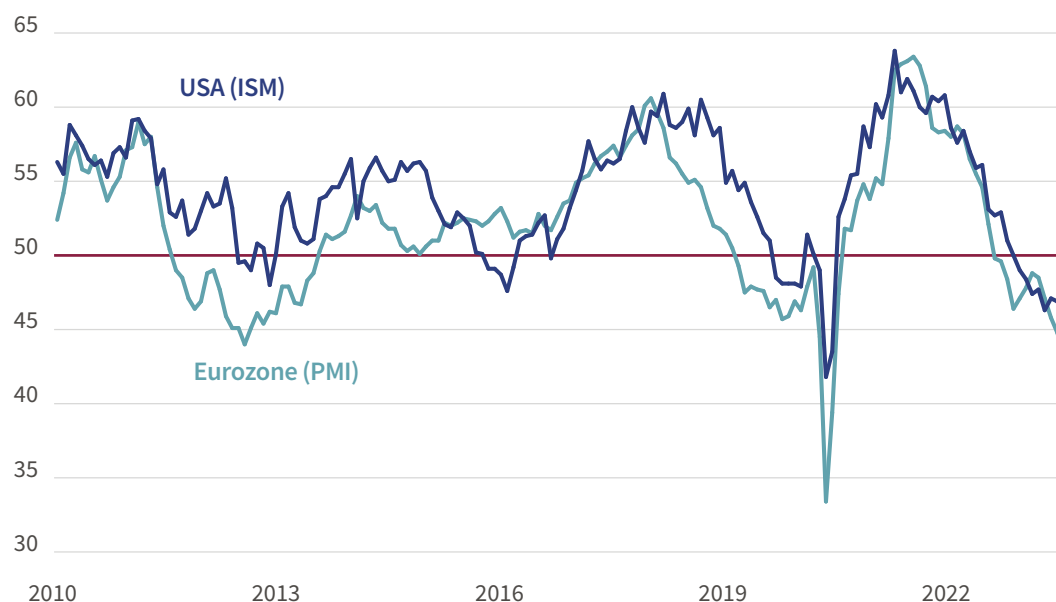
Hard to get a true read

In the US, economic activity is holding up, inflation is receding slightly, and the labour market is still robust. And yet, the spectre of recession continues to hover. All leading macroeconomic and market indicators are pointing in that direction, and things have worsened again since late March. The consequences of the rate hikes cannot be overlooked, especially as financing conditions remain clearly restrictive. Meanwhile, PMI⁽²⁾ services indices are trending downward but for the moment are holding above 50. PMI manufacturing indices, however, are under this threshold. Historically, the services indices tend to track behind the manufacturing indices, and on both sides of the Atlantic.

Even so, inflation is receding far more slowly in Europe than in the US. So, the context is more challenging for the ECB and offers investors less visibility on the “landing point” of its

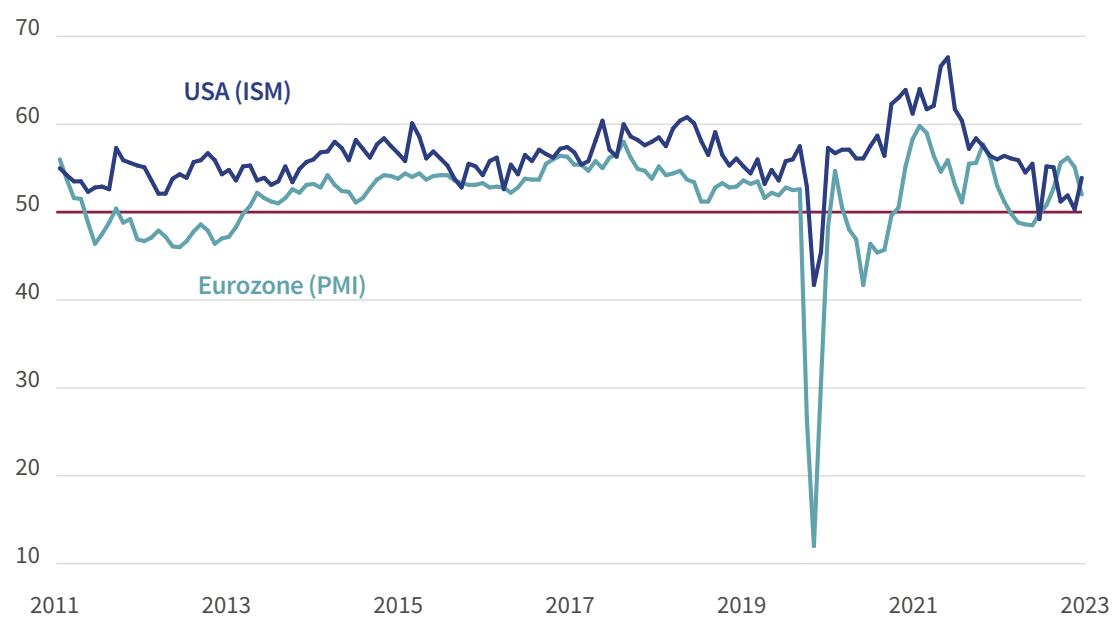
(2) Purchasing Managers' Index, indicator reflecting the confidence of purchasing confidence in an industry sector. Above 50, it indicates an expansion in activity; below 50, a contraction.

US & Eurozone – Business confidence Index (Manufacturing)



Sources: Macrobond, Rothschild & Co Asset Management, 30/06/2023.

US & Eurozone – Business confidence Index (Services)



Sources: Macrobond, Rothschild & Co Asset Management, 12/05/2023.

monetary policy. This lack of clarity is being maintained by the cyclical lag between Europe and the US. In raising its rates higher and faster, the Fed has managed to achieve results that are now tangible. In Europe, the situation is more nuanced. However, if the US slips into a recession, European long-term rates yields will track US long-term rates yields downward, although the ECB says it will continue to hike.

A prudent and selective strategy

Against this backdrop, we have raised the portfolios' interest-rate sensitivity to quasi-neutrality vs. the market. However, we are avoiding overweighting interest-rate sensitivity, as Europe is still in a negative real-rate environment and it is impossible to know how ECB monetary policy will "land". We have also reduced the portfolios' tracking error⁽³⁾ in general, lessening their exposure to risky assets by selling high-beta bonds. Hence, after having overweighting very-long-dated sovereign bonds in order to hedge risk at attractive absolute levels, we have shifted our allocation to five-year paper, as the yield curve has inverted even more, and have taken this opportunity to raise portfolio sensitivity slightly. This positioning seems to fit a potential shift in monetary policies.

Meanwhile, we are overweighting sectors such as banks that are able to use the latest interest-rate movements to generate considerable profits and that enjoy solid fundamentals. Similarly, we are opportunistically investing in bonds with attractive yields. We are invested in all Investment Grade⁽⁴⁾ ratings but the more we descend the scale, the more we try to identify positive credit trajectories and a potential for improvement in fundamentals to provide some resiliency to the portfolios. For the most flexible funds, we prefer to retain some leeway for positioning ourselves on riskier investments when during surges of volatility.

(3) Standard deviation of a fund's volatility to its benchmark index.

(4) Debt securities issued by companies or governments rated between AAA and BBB- by Standard & Poor's.

Our fund selection

R-co Conviction Credit Euro

SRI risk :



EURO-DENOMINATED INVESTMENT GRADE BONDS

Inception date: 08/11/2019 | Recommended investment period: 3 years | Article 8 SFDR

The flagship fund in our bond range, R-co Conviction Credit Euro offers active and opportunistic management of the euro-denominated bond market. Its core portfolio consists of securities, complemented by satellite strategies and a careful selection of high yield and non-rated bonds. The investment strategy aims at a constant optimisation between yield and maturity as well as a careful monitoring of the portfolio's sensitivity.

Performance and risk indicator

	Year to date	2022	2021	2020	2019	2018	1 year volatility
R-co Conviction Credit Euro C EUR	3.44%	-13.17%	1.00%	2.72%	5.17%	-3.58%	5.03%
R-co Conviction Credit Euro IC EUR	3.62%	-12.86%	1.37%	3.09%	5.55%	-3.23%	5.03%
Markit iBoxx™ € Corporates	2.16%	-14.17%	-1.08%	2.73%	6.29%	-1.29%	5.80%

Source: Rothschild & Co Asset Management, 30/06/2023.

R-co Target 2028 IG

SRI risk :



MATURITY FUNDS | EURO-DENOMINATED INVESTMENT GRADE BONDS

Inception date: 09/09/2022 | Recommended investment period: until 31/12/2028 | Article 8 SFDR

A credit fund based on a bond-carrying strategy until maturity, R-co Target 2028 IG invests in Investment Grade bonds from all geographical areas. This strategy is based on a selection of securities with an average maturity between January and December 2028 while benefiting from active management allowing for arbitrage in order to control the portfolio's risk level or seize market opportunities. The marketing period runs until 31 December 2023.

Yield to maturity: 4.9 %⁽¹⁾

(1) Source: Rothschild & Co Asset Management, 30/06/2023.

R-co Thematic Target 2026 HY

SRI risk :



MATURITY FUND | EURO-DENOMINATED HIGH YIELD BONDS

Inception date: 28/02/2020 | Recommended investment period: until 31/12/2026 | Article 8 SFDR

R-co Thematic Target 2026 HY is a high-yield bond maturity fund that invests in euro-denominated bonds from all geographical areas. The selected securities have an average maturity between January and December 2026. The investment approach includes active, agile and disciplined management, making it possible to seize opportunities, arbitrage and even sell if the risk of default becomes too great. The marketing period runs until 1 September 2023.

Yield to maturity: 7.9 %

Performance and risk indicator

	Year to date	2022	2021	Since inception	1 year volatility
R-co Thematic Target 2026 HY C EUR	6.85%	-11.63%	5.29%	15.85%	6.72%
R-co Thematic Target 2026 HY IC EUR	7.12%	-11.17%	5.82%	16.28%	6.72%

Source: Rothschild & Co Asset Management, 30/06/2023.

R-co Valor Bond Opportunities

SRI risk :



GLOBAL BONDS | CARTE BLANCHE

Inception date: 28/08/2019 | Recommended investment period: over 3 years | Article 8 SFDR

R-co Valor Bond Opportunities is an global bond fund with a «carte blanche» approach means that it can be invested in all segments of the bond market, across ratings, maturities and in geographical areas. Thanks to its flexibility and based on the analysis of growth, inflation and monetary policy outlooks, this investment solution aims to take advantage of the diversification of fixed income products by combining satellite strategies around a core credit portfolio.

Performance and risk indicator

	Year to date	2022	2021	2020	Since inception	1 year volatility
R-co Valor Bond Opportunities C EUR	4.10%	-9.71%	3.66%	6.74%	5.35%	6.06%
ESTER Capitalisé + 2.585%	2.61%	2.90%	2.50%	2.51%	11.88%	0.18%
R-co Valor Bond Opportunities I EUR	4.34%	-9.31%	4.14%	7.01%	7.%	6.07%
ESTER Capitalisé + 3.035%	2.83%	3.34%	2.95%	2.96%	13.%	0.18%

Source: Rothschild & Co Asset Management, 30/06/2023.

R-co Conviction Credit Euro

We have classified this product as risk class 2 out of 7, which is a low risk class and mainly reflects its positioning on private debt products while having a sensitivity between 0 and +8. In other words, the potential losses associated with the future performance of the product are at a low level and, should market conditions deteriorate, it is very unlikely that our ability to pay you would be affected. The risk indicator assumes that you hold the product for 3 years, otherwise the actual risk may be very different and you may get less in return.

Main risks: Discretionary management risk, interest rate risk, credit risk, counterparty risk, performance risk, risk of capital loss, risk related to the use of derivatives, risk related to temporary acquisitions and sales of securities, specific risk related to the use of complex subordinated bonds (bonds with a maturity of less than one year) of securities, specific risk related to the use of complex subordinated bonds (contingent convertible bonds, so-called «CoCs»).

R-co Thematic Target 2026 HY

We have classified this product as risk class 3 out of 7, which is a low risk class and mainly reflects its positioning on credit risk and interest rate products with a residual maturity of 1 year or less on 31 December 2026. In other words, the potential losses related to the future performance of the product are at a low level and, if the situation were to deteriorate in the markets, it is very unlikely that our ability to pay you would be affected. The risk indicator assumes that you hold the product until 31 December 2026, otherwise the actual risk may be very different and you may get less in return.

Main risks: Discretionary management risk, interest rate risk, credit risk, credit risk («speculative» or «high yield»), liquidity risk, counterparty risk, performance risk, risk of loss of capital, risk linked to the use of derivatives, exchange rate risk, equity risk, risk linked to exposure to non-OECD countries (including emerging countries)

R-co Target 2028 IG

We have classified this product as risk class 2 out of 7, which is a low risk class and mainly reflects its positioning on credit risk and interest rate products with a residual maturity of 1 year or less on 31 December 2028. In other words, the potential losses related to the future performance of the product are at a low level and, if the situation were to deteriorate in the markets, it is very unlikely that our ability to pay you would be affected. The risk indicator assumes that you hold the product until 31 December 2028, otherwise the actual risk may be very different and you may get less in return.

Main risks: Discretionary management risk, interest rate risk, credit risk, counterparty risk, performance risk, risk of capital loss, risk related to the use of derivatives, extra-financial criteria (ESG) risk, sustainability risk.

R-co Valor Bond Opportunities

We have classified this product in risk class 2 out of 7, which is a low risk class and mainly reflects a discretionary management policy that exposes the portfolio in a diversified way to the interest rate markets over the medium term. In other words, the potential losses related to the future performance of the product are low and, if the situation were to deteriorate in the markets, it is very unlikely that our ability to pay you would be affected. The risk indicator assumes that you hold the product for 3 years, otherwise the actual risk may be very different and you may get less in return.

Main risks: Discretionary management risk, interest rate risk, credit risk, credit risk («speculative» or «high yield»), counterparty risk, performance risk, risk of loss of capital, risk linked to the use of derivatives, specific risk linked to the use of complex subordinated bonds (convertible contingent bonds known as «CoCos»), exchange rate risk, equity risk, risk linked to exposure to non-OECD countries (including emerging countries).

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Our development is focused on a range of open-ended funds, marketed under five strong brands: Conviction, Valor, Thematic, 4Change and OPAL, leveraging our long-term expertise in active management with conviction as well as in delegated management. Based in Paris and established in 9 European countries, we manage more than 27 billion euros and employ nearly 160 people.

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