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ADVISOR

# BONDS: A WINNING BET USING THE VALUE APPROACH

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IN BANOR CAPITAL'S VIEW, FIXED INCOME PRODUCTS HAVE SEEN DECADES OF EASY EARNINGS. BUT TODAY, WITHOUT A DEFENSIVE APPROACH, INVESTORS CAN GET THEIR FINGERS BURNT

Applying the value approach adopted for equity to the bond market That's one of the strong points that distinguishes the fund management style of Banor Capital, an independent UK-based boutique set up by a team of financial professionals who've been working together for over 17 years. Francesco Castelli, head of fixed income at the firm, illustrates how this approach can be both rewarding and successful, especially now that the bond market has become less remunerative.

"I think fixed income products have seen three decades of essentially easy returns, produced by the reduction in interest rates that began in far-off 1982 with the Federal Reserve's battle against inflation, which went on to conquer the world. Now this trend is at an end, with interest rates reaching a floor on 8 July 2016, the date of a change of direction that was epoch-making in its impact", observes Castelli. In his opinion, that date will enter the history books because it means that fixed income, as we have known and understood it, no longer exists. Today, while bonds could experience a rebound, reality tells us that this asset class is no longer providing returns. "Credit is an asset class that we managers have always used to gain an edge", explains Castelli, "but today the average spread for European corporates is below 100 basis points. If we add that to the Bund's yield we don't even reach 1%".

So what's to be done? Only invest in the equity market, going against all of the basic investment principles that advocate a proper degree of asset diversification? Definitely not. In Castelli's view the solution lies in high-yield corporate bonds. "Right now, high-rating securities aren't providing any major opportunities”, underscores the expert. “But high-yield products with a relatively short maturity could provide a refuge given that the index offers 260 bps in the short, low-duration part, which means low risk from interest rate rises. A defensive approach brings rewards: when you defend well, you’re in the best position to attack. And that could be a good solution at a time like this, when the outlook is still very difficult”, continues Castelli. The aim is to give clients the instruments they need to face the future and protect their capital. “Although in our view, there are still a lot of strategies out there that will lead clients to getting their fingers burnt”. To avoid getting hurt, then, it’s best to select products with a limited duration and an even lower sensitivity to rates, such as Banor SICAV’s Euro Bond Absolute Return. This fund adopts a bottom-up approach based on an in-depth fundamentals analysis. The Euro Bond fund only invests in sectors that managers know very well. The securities it invests in are financial (40%), with a component in the industrial sector too. In general, the preference is for products with a stable cash flow and a leading position, primarily in the European market.