SARASIN
STERLING BOND FUND

SARASIN & PARTNERS

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ECONOMIC AND FUND REVIEW

During the first quarter, sterling corporate bonds outperformed government bonds. This was mainly due to a pullback in government bonds after December's rally. Expectations that interest rates might be cut as early as April 2024 were frustrated by stronger economic data.

Inflation continued to fall, but is proving to be stickier than anticipated. Geopolitical uncertainty in the Middle East and resilient employment numbers held back the market. This caused uncertainty regarding the number of interest rate cuts.

FUND REVIEW

The fund outperformed its benchmark in the quarter as it benefited from holdings that have a greater degree of risk. As such, our corporate bond positions in subordinated financial debt and in insurance were the main contributors to positive performance. On the other hand, our longer-maturity bonds underperformed as they were hit by expectations that interest rates would remain higher for longer. However, these longer-dated positions are generally safer and difficult to source, so we maintain a strong conviction in them at this point in the economic cycle.

We maintained our overweight positions in the financials, utilities and asset-backed sectors. Financials performed well, with better-than-expected banking results and the continued prospect of a soft landing for the economy. The good performance of utilities was particularly due to our subordinated debt holdings. We also saw healthy returns from some asset-backed holdings, which generally lag corporate bond rallies. We do not hold Thames Water, which is experiencing financial difficulties. We feel our other water sector holdings will be unaffected by its challenges.

FUND TRANSACTIONS

We continue to favour having slightly more risk in the fund compared with its benchmark. We believe corporate bonds will remain attractive given pension fund demand, slow new issuance and flows into the asset class. That said, we reduced positions that have higher risks as valuations have become stretched, indicating that their returns might be lower going forward.

We took profits in several junior subordinated financial debt holdings as well as hybrid Électricité de France (EDF) bonds, all on stretched valuations. We also continued to add to several relatively lower-risk bond issues, including Porterbrook, Great Rolling Stock and Telefonica, as well as Tesco property-backed debt.

OUTLOOK

We think disinflationary momentum will continue to bring inflation close to central bank targets in 2024. We feel the interest-rate hiking cycle is over, barring an extraordinary inflationary shock. The question is when central banks will start to cut interest rates, and the timing of subsequent reductions. We expect a modest economic slowdown in the US and a cautious recovery in the UK and Europe. Economic activity in the UK is surprisingly resilient, with employment growth supporting real incomes.

We continue to believe that there is value in sterling bonds in the short to medium term. This applies to the credit spread over government bonds and all-in yields (the yield considering both the underlying government benchmark and the yield for credit risk). Stronger economic data surprises, including inflation or increasing bond risk premiums, could see near-term bond market weakness. However, we believe the fund is well-positioned to withstand possible weakness in credit markets and interest rate volatility.

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IMPORTANT INFORMATION

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There is no minimum investment period, though we would recommend that you view your investment as a medium to long term one (i.e. 5 to 10 years).

The Fund may invest in derivatives for efficient portfolio management purposes. This means Derivatives can only be used to manage the Fund more efficiently in an attempt to reduce the overall risk of its investments, reduce the costs of investing or generate additional capital or income, although this may not be achieved and may create losses greater than the cost of the derivative.

The Fund may invest in other collective investment schemes, including regulated and unregulated collective investment schemes. Investment in unregulated collective investment schemes carries additional risks as such schemes may, among other things, not be under the regulation of a competent regulatory authority, may use leverage and may carry increased liquidity risks.

This document does not explain all the risks involved in investing in the Fund and therefore you should ensure that you read the Prospectus and the Key Investor Information Document, which contain further information including the applicable risk warnings. The Prospectus, the Key Investor Information Document as well as the annual and semi-annual reports of the Fund are available free of charge from www.sarasinandpartners.com or from Sarasin & Partners LLP, Juxon House, 100 St Paul's Churchyard, London, EC4M 8BU, Telephone +44 (0)20 7038 7000 (telephone calls may be recorded).

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