Appian
Asset Management

Monthly Monitor

March 2018

Bonds – Past the Inflection Point

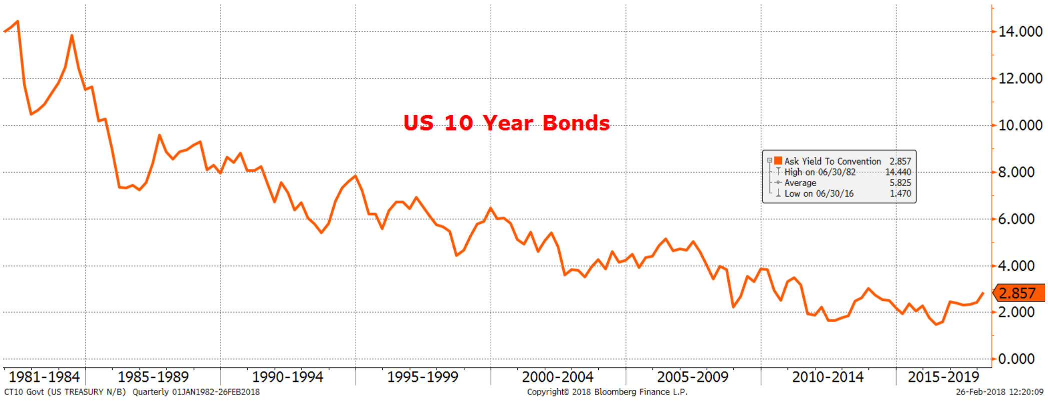
In January of this year, for our multi-asset funds such as the Appian Value Fund and the Appian Ethical Value Fund, we sold all of our holdings of government bonds. So for the Value Fund, for example, this meant going from a weighting of 14% at year end to 0% today.

We had been cautious of this asset class for some-time and within our bond portfolios were positioned quite defensively. However, to fully exit is clearly a significant move, but as we've noted on many occasions, we believe we should be truly dynamic when it comes to asset allocation decisions – as Appian have been in the past, making significant calls in key sectors such as property or Irish bank shares. We are neither constrained by benchmarks nor driven by peer groups. If we believe that a sector or asset class doesn't offer potential value for our investors there is little point in being merely underweight.

In our view, we see no potential return from holding government bonds in the medium term.

Why?

Firstly, we recognise no real value in bonds at these very low yield levels. At the time of writing, German 10-year bonds offer investors an income yield of 0.65%. We regard this as a very poor return, and given that the ECB has a target of 2% for inflation, a nominal return that will be eroded by price increases over time. In the US, we are already seeing signs of inflationary pressures building in labour and commodity markets. As we return to more normal levels of growth and inflation, we believe yields will rise which means that bond context for just how low bonds yields have gone in the US. So based on economic fundamentals such as growth and inflation we are cautious on bonds.



Source: Bloomberg.

Our other major concern in this asset class is that for the last few years there has been a new and unusual buyer in the market. Central Banks through their “Quantitative Easing” programmes have been buying up bonds, as they sought to pump liquidity into the financial system to spur the economy. This is now coming to an end. Central Banks are on a path to eliminate these bond purchases, and in any market when a large buyer exits, prices come under downward pressure. We don’t see a risk of Central Banks unloading their holdings precipitously into the market, but the mere fact that a price insensitive buyer is no longer present, is a negative for the asset, in our view.

Of course as yields move up, there will be a level where they become attractive again perhaps for pension funds who may look to match long term liabilities. So while we remain at zero in bonds, we also remain vigilant.

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Appian Unit Fund Prices

1 March 2018

Appian Value Fund	**141.41**
Appian Equity Fund	**183.49**
Appian SCOF	**206.21**
Appian Liquidity Fund	**105.63**
Appian Ethical Value Fund	**102.28**
Appian Burlington Property Fund	**103.85**

For more detailed information on each of our funds click **here**

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