Close Diversified Income Portfolio Fund

Monthly fund manager update

April 2024

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PERFORMANCE

The Close Diversified Income Fund returned -0.1% in April. This compared favourably to a return of -0.7% for the Investment Association (IA) 20-60% Shares Sector. For the second month in a row the Fund recorded a new intra-month all-time high.

The 13 year 3 month (manager tenure) track record is +78.3%, versus +69.2% for the IA 20-60% Shares Sector. Over this long-term period Diversified Income is first decile on risk-adjusted returns.

In March US equities fell -4.2% (-3.2% in sterling terms). European equities slid -3.2% (-3.3% in sterling terms), while UK large-cap stocks advanced +2.4% and the UK mid-cap index added +0.4%. Being overweight the UK helped this month in terms of performance.

The 10-year gilt yield rose to 4.35% from 3.93% as the market narrative switched to a greater focus on sticky inflation prints and factored in a further delay to interest rate cuts. This was despite, in the UK, the Consumer Prices Index (CPI) measure of inflation falling further to +3.2% from +3.4% and the Retail Prices Index (RPI) measure falling to +4.3% from +4.5%. If one just looks at the last eleven months' data rather than twelve months', then the CPI rate is just 2% and for RPI it is just 2.7%. We continue to believe that the release of May's inflation print will see another step down in the annual rate, and it will be interesting to see if this changes the narrative once again.

BBB corporate bond spreads were stable in April at 1.43% (remaining below the 2.1% long-term average). Duration on the bond portfolio remains fairly low at 3.5 years (the same as last month), so the bond portion of the fund generally outperformed as the gilt market has a longer duration (all things being equal, longer duration bonds fall more for a given interest rate rise). With an average yield of 8% the corporate bonds we hold are offering equity-like returns on a hold-to-maturity basis. Their low duration will reduce the volatility in the bond exposure.

In the alternatives space, gold continued to rise, +3% (+4% in sterling terms), with commentators pointing to central bank buying and demand from Chinese private investors (looking for an alternative after losing money on housing / stock markets) as reasons why.

We have been actively pushing the boards of our investment trust holdings to take action on attempting to reduce their discounts. In the month it was positive to see GCP Infrastructure announce the first in an expected series of disposals, selling a stake in Blackcraig Wind Farm at a 6.4% premium to its Net Asset Value (NAV). The shares reacted positively, rising 6% over the course of the month.

ON ENVRIONMENTAL, SOCIAL AND GOVERNANCE (ESG)

Whilst the Close Diversified Income Fund is not an ESG-labelled fund, we do consider and monitor ESG factors as part of our research. Unilever and Nestlé are stocks we sold some time ago, and have in our opinion significant ESG risks ahead of them, relating to their sugary & ultra-processed food offerings. These risks have been clearly laid out in recent books, such as “Metabolical” by Dr Robert Lustig and “Ultra-Processed People” by Dr Chris van Tulleken, which has been shortlisted at this month’s British Book Awards 2024 (a.k.a. The Nibbies). These books show how wider reading can be both interesting and useful for a generalist fund manager.

It is interesting to see that these perceived high quality and highly valued stocks (Nestlé trades on 17x and Unilever on 16.6x earnings) are now being compared to tobacco stocks, which are excluded from many people’s portfolios, without hesitation, for ESG reasons and trade on much reduced ratings these days (Imperial Tobacco on 5.6x and British American Tobacco on 6x earnings).

It has been no surprise to us to see negative headlines hitting the wires. What is also interesting about the problem facing these companies is that to make their products healthier, they need to be less processed and less sugary / fatty which could also make them less appealing (and therefore lead to a decline in sales). Is that why shareholders voted against making Nestlé a healthier company in April? (We note that one of Nestlé’s recent innovations is KitKat cereal, which is 25% sugar).

Shareholders in such cases may have chosen the short-term easy option of not doing anything, but the risk remains that people become more informed about their health, or that governments take action on the back of research from doctors, to deter purchases of sugary / processed foods in order to subsidise / encourage the purchase of natural / fresh food alternatives.

It was also interesting to see that “AAA-ESG--rated” poster child Unilever has decided that sustainability does not pay with reports that ESG targets will be diluted to focus more on profit.

PORTFOLIO ACTIVITY

There were no trades of note in the month.

YIELD

Diversified Income’s yield (based on end of month prices) rose to +6.8% from +6.7%. At this level, the Fund is still generating c.0.55% of income a month, which will help to offset any future downward volatility.

OUTLOOK

We remain underweight equities for valuation reasons and especially given the number of fixed income ideas we have been able to find offering equity-like returns. Volatile markets increase the likelihood of finding more investments at valuations we consider good risk / reward and which will aid forward-looking returns.