Kames Absolute Return Bond Constrained Fund

August 2017 review

KAMES CAPITAL

For professional investors only

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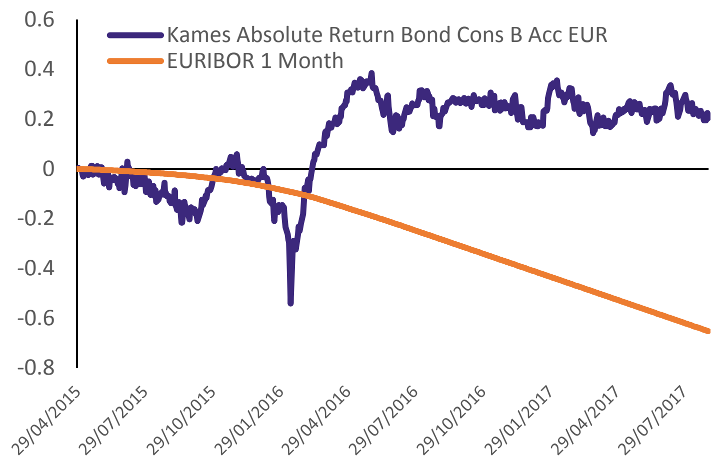
The Kames Absolute Return Bond Constrained Fund returned -0.09% in August, against the benchmark return of -0.03% from 1-month Euribor. The year-to-date return is 0.04%, outperforming the -0.25% return of 1-month Euribor.



Total since launch*

Fund total return	0.20%
Benchmark total return	-0.65%
Difference	0.86%
Best month	0.33%
Worst month	-0.22%
Up months	13
Down months	16
Maximum drawdown (daily)	-0.60%
Annualised volatility	0.39%
Sharpe ratio	0.83

*Source: Lipper as at 31 August 2017, net and noon prices. NAV to NAV total return with income reinvested. Local currency B (Acc) EUR class. Launch 29 April 2015. Since launch return is based on Cumulative Noon Lipper data. Benchmark is at close. Volatility and Sharpe ratio based on net annualised monthly returns since inception. Maximum Drawdown has been calculated as the largest peak-to-trough cumulative fall based on daily returns. Volatility is defined as the standard deviation of monthly returns.

The last month of the summer holidays is over and as the schools return for another year we hope that volatility will also return! Perhaps with such key events, such as the Fed and ECB meetings, to come in September the malaise in bond markets in August was warranted. The Fed are likely to start the balance sheet wind down in September and potentially signal whether a December hike will come. This will be clear tightening, unlike the ECB.

The ECB have a communication tightrope to walk. Eurozone inflation is not at target and is unlikely to be so over the medium-term. Also, they will have to stop buying so many bonds as they are reaching the maximum of 33% of German sovereigns per issue. As the current bond-buying programme ends in 2017 they will have to start the conversations to remove monetary stimulus in their September or October meetings. With inflation not at target and a desire to avoid the signalling of tightening (most likely due to effects on the Euro) – Draghi will have his work cut out.

Geopolitics is becoming more volatile. The North Korean situation is getting worse on an almost week-by-week basis but in general, risk and risk-free markets are not moving on the news. I suppose given the potential outcomes, markets may continue to ignore it as there is no middle ground – it's either catastrophically bad or it's not.

Rates

In the Rates module we took profits on our Australian 3-year versus 10-year curve steepening position in the early part of the month, the sell-off in late July saw 10-year assets underperform those further down the curve.

The Australian market proved to be more volatile than most over the month with a marked move wider in its bond yields versus other core markets. On the last day of the month we positioned for a reversal of this, adding a long position in 10-year Australian bond futures versus short 10-year US bond futures. The market is pricing in a similar degree of rate hikes in each market – we expect the Fed to tighten by more than the Reserve Bank of Australia allowing the Australian market to outperform.

We also opened a US 5-year versus 30-year curve steepening position. With a reduction in the size of the US Federal Reserve's balance sheet expected, we see that as being more negative for long-dated bonds. Add in the fact that, while US CPI continues to disappoint, the underlying growth of the economy is robust – this has the potential to support shorter-dated assets relative to longer-dated bonds. As of month-end the curve was broadly unchanged compared to our entry point. For this reason our 10-year long US inflation position slightly underperformed in the month. We expect a pickup in inflation over the coming months to help this position.

Credit

A relatively quiet month in the credit module, we selectively added to individual names on the month where we saw value.

Carry

The Carry module is a diversified range of investment grade assets with less than two years to maturity, which we expect to hold to maturity. We currently have close to 70 holdings in the Carry module; the majority are in US and UK markets and have an average maturity of close to 12 months.

James Lynch

*Source: Lipper as at 31 August 2017, noon prices, NAV to NAV returns; local currency B (Acc) EUR share class. Index based on closing prices.