Capital Gearing Trust/ CG Absolute Return Fund / Capital Gearing Portfolio

- 2.2% return in the quarter compared to MSCI UK All Cap of 4.7%, annually the returns were 11.1% against 17.5% in the MSCI UK All Cap
- Risk assets (c.46% of the portfolio) returned 3.6% in the quarter (20.2% for the year) against 4.2% MSCI UK All Share and 3.7% for the investment trust index
- Both UK and European equities contributed to performance, with Investor AB gaining 16.4% in the period
- The property holdings (c.19% of the portfolio) delivered 4.1% (17.8% for the year) driven by strong performances in UK residential, including PRS REIT increasing 11%, and Tritax Big Box up 14% over Q4
- After a strong period of property gains through the year, we continued the rotation into infrastructure (now 5.3% of the portfolio) with key holdings including Greencoat UK Wind, Bluefield Solar and Digital 9 Infrastructure. A strong power price environment supported a 6% gain in the infrastructure assets over the quarter (14.3% annually), despite this we believe they continue to offer good value
- Index-linked bonds (30% of the portfolio) returned 1.3% in the quarter (4% for the year) as high recent CPI prints globally resulted in large inflation accrual gains
- With the LSE Group 4.75% and National Grid 1.25% maturing, the credit portfolio is reducing in size naturally, albeit at a slower rate this quarter as we increased our ZDP activity, including a cornerstone investment in the EPE Special Opportunities 27s
- The portfolio remains defensive overall with an objective of capital preservation and inflation protection

Real Return Fund

- Returns of 1.5% in the quarter (4.2% in 2021) compared to 1.3% (4.1% annually) for the Global Index linked ex UK index in the quarter
- In March a new GBP hedged share class of the Real Return fund was launched and has returned 2.5% this quarter
- The US, Canada and Australia all contributed positively, although sterling strength towards the end of the quarter softened performance
- Ongoing relatively small additions were made in the short end of in US, German and Swedish Index-linked
- Relative was performance also helped by the short duration of the Canadian holdings and the overweight to US Tips
- US CPI printed 6.8% YOY in November with one year forward breakevens at expanding 50bps to 3.5% over the next 12 months
- The transitory narrative is fading away as inflation underlying elements are appear much more persistent and broadly based, with the market expecting a rate increase as early as march
- Responding to the strong TIPS gains, portfolio duration was shortened via disposals of long bonds and reinvestment into the belly of the curve
- The federal reserve continues to view the current inflationary impulse as transitory and the modest breakevens (and nominal bond yields) suggest this view is largely accepted in the market
- We are concerned inflation could prove more sticky given evidence of wage acceleration, rising housing costs and sustained commodity price increases
- The inflationary indicators in most other markets point to future cost of living increases, although currently the US is experiencing by far the highest current inflation rate

Dollar Fund

- Weighted average duration at 8.8 years, slightly longer than the index (8.1)
- Unhedged share class returned 2% for the quarter (6% annual) compared to the index which returned 2.1% (7% annual)
- Hedged share class returned 2.5% (5.2% for the year) in the quarter compared to the index which returned 2.4% for the period (5.8% annual)
- US CPI printed 6.8% YOY in November with one year forward breakevens expanding 50bps to 3.5% over the next 12 months
- The 5Y5Y forward inflation swap rose from 2.4% to 2.5% over the quarter
- Real yields hit their low of the year at -1.2% offering a good opportunity to shorten duration
- The shortening of duration was achieved by selling long bonds and reinvesting proceeds into the belly of the curve
- Since the summer the nominal bond yield has backed up to c.1.5% which has been associated with a back up in real yields to -0.9%
- Energy price rises will also cause inflation to remain sticky in the short term with 1 year breakevens hitting 3%
- The federal reserve continues to view the current inflationary impulse as transitory and the modest breakevens (and nominal bond yields) suggest this view is largely accepted in the market
- We are concerned inflation could prove more sticky given evidence of wage acceleration, rising housing costs and commodity price increases
- Given the back up in real yields and low breakevens we have considered lengthening duration but have not done so yet