RATHBONES

# RATHBONE HIGH QUALITY BOND FUND

QUARTERLY UPDATE JUNE 2026

**Government bonds had a volatile ride over the quarter as the war in the Middle East kept energy prices high and inflation fears very much alive. Corporate bonds proved more resilient, even as the AI giants unleashed fresh waves of supply.**

The quarter began with the huge energy supply shock triggered by the war still working its way through the system. The Strait of Hormuz, through which around a fifth of the world's oil and liquefied natural gas (LNG) usually flows, remained largely closed, bottling up a big chunk of global supply. The price of a barrel of Brent crude oil, which had started the year at around $60 a barrel, spiked to a quarterly peak of above $115. More expensive oil stoked fears of a big spike in inflation, driving bond yields higher (meaning their prices fell). High inflation is bad news for bonds since it increases the chances that the world's big central banks raise interest rates (or hold them higher for longer) to try to keep prices in check, while also eroding the value of bonds' fixed interest payments.

But the mood had shifted by mid-May. As hopes of a durable truce between the US and Iran grew, the price of Brent crude fell to just over $90 and government bonds rallied. In mid-June, it looked like a war-ending deal might finally be sealed when the US and Iran signed a memorandum of understanding that paved the way for a 60-day ceasefire. But optimism about that deal proved short-lived. In early July, fighting between the two sides broke out again and President Donald Trump says the memorandum of understanding is effectively over. The market reaction has been swift: Brent crude is back above $80 per barrel and most government bond yields have spiked higher.

## OIL PRICE RETRACES... AND RISES AGAIN

Source: FactSet, Brent crude oil global spot price ($/bbl) as at 14 July 2026

The world's big central banks are in a tight spot. They can't do much to tame inflation when it's energy-driven. But they risk losing control of long-term inflation expectations if they sit on their hands and steeper energy costs start feeding through into wages and broader consumer prices. Both the US Federal Reserve (Fed) and Bank of England (BoE) left rates unchanged over the quarter, while warning about the risks of a lasting upturn in inflation. The European Central Bank (ECB) raised rates by 0.25% at its June rate-setting meeting. Investors expect both the Fed and the BoE to lift rates by at least the same amount this year.

We still think the BoE is pretty unlikely to hike this year. Tightening into an energy shock would do little to address the source of the inflation and would only sharpen the drag on economic growth from more expensive energy costs.

### Gilts in the firing line

Meanwhile, the gilts market has proved particularly vulnerable to warflation worries. That's because it's a government bond market that tends to swing more sharply than its US and European peers, it's grappling with stretched public finances, it's harder to trade in and out of than its bigger cousins, and inflation can quickly feed through to the UK's wider economy. The 10-year gilt yield began the quarter at 4.88% and hit 5.10% on 13 May (its highest level since 2008). It then rallied back to around 4.80% by quarter-end, but was back above 4.90% in the first half of July. The 10-year US Treasury yield was steadier, starting the quarter at 4.31% and drifting up to 4.42% by its end, though it spiked to nearly 4.60% as fighting resumed after quarter-end.

While the energy shock kept most government bond markets on edge over the quarter, gilt market volatility got a further kicker from the uncertainty over whether Prime Minister Keir Starmer would be replaced by someone less wedded to fiscal discipline. Much of the noise centred on clear frontrunner Andy Burnham, widely viewed as more of a borrower and spender than Starmer and his Chancellor, Rachel Reeves. Burnham has been at pains to stress he'll stick to Labour's existing fiscal rules once he becomes Prime Minister. That messaging helped calm nerves in the immediate aftermath of Starmer's resignation, but the political risk premium weighing on gilts is unlikely to disappear over the summer.

### Performance review

| | 3 months | 6 months | 1 year | 3 years | 5 years |
|---|---|---|---|---|---|
| **Rathbone High Quality Bond Fund** | 2.14% | 1.36% | 3.92% | 19.26% | 22.35% |
| Bank of England Base Rate + 0.5% | 1.08% | 2.16% | 4.54% | 16.82% | 8.17% |

| | 30 Jun 25-30 Jun 26 | 30 Jun 24-30 Jun 25 | 30 Jun 23-30 Jun 24 | 30 Jun 22-30 Jun 23 | 30 Jun 21-30 Jun 22 |
|---|---|---|---|---|---|
| **Rathbone High Quality Bond Fund** | 3.92% | 5.86% | 8.40% | -1.60% | -7.82% |
| Bank of England Base Rate + 0.5% | 4.54% | 5.43% | 5.99% | 3.79% | 0.91% |

Source: Morningstar; data to 30 June, I-class, mid price to mid price.

**These figures refer to past performance, which isn't a reliable indicator of future returns.**

It's important to remember that while surging gilt yields are unsettling and dent gilt prices, this environment does create opportunities for us to capture very attractive income streams or 'carry' from shorter-dated credit. When gilts rallied from mid-May into June, we decided to lock in some of these gains by trimming back our **UK Government 4.375% 2030s**. In late May, we sold some of our **European Investment Bank (EIB) 0% 2028s**. The EIB is a supranational, an institution established by the governments of two or more countries to pursue specific policy goals (this government backing earns it the highest possible credit rating). But sterling supranational paper has rallied so hard that bonds like the **EIB 2028s** are now trading extremely tight to gilts, meaning investors are getting paid very little extra to hold supra credit over UK government debt.

### Credit holds its nerve

Notwithstanding all the big-picture turbulence, corporate bond markets held up remarkably well over the quarter. Credit spreads (the extra yield corporates offer over government debt to compensate investors for default risks) continued to tighten. As a result, credit spreads as measured by the ICE Bank of America Sterling Corporate Bond Index narrowed from 92 basis points (bps) to 80bps over the quarter. That resilience held even as bond markets digested a record wave of new supply from the AI giants. But with their issuance through the roof, it's hard to see how much longer credit can stay quite so bulletproof.

As we've explained before, the AI hyperscalers (the largest being Amazon, Google parent Alphabet, Meta and Oracle) are borrowing huge amounts to pay for the computing power, servers and infrastructure they need to train and deploy AI at scale. All this borrowing is reshaping the composition of many investment-grade corporate bond benchmarks.

The hyperscalers' headline issuance numbers, and the bigger weightings they now command, tell only part of the story. The AI giants tend to favour jumbo deals with very long maturities (meaning the debt won't be repaid for many years). Longer-maturity debt is more sensitive to changes in credit spreads, meaning any spread tightening or widening has a larger monetary impact on its value than on shorter-maturity debt.

At the moment, most of the hyperscalers remain exceptionally strong credits. But we fear the risks are skewed towards more and more AI-related issuance. We fear that the sheer volume of long-term AI borrowing could saturate bond markets, driving AI hyperscaler credit spreads wider, and thereby eroding the value of this debt. There are already signs that investors are starting to feel a tad overwhelmed: Amazon launched a $25 billion eight-part investment grade bond deal in early July and found it attracted a lot less investor demand than its previous offerings.

Meanwhile, the glut of new issuance from the AI giants means that passive investors chasing index-eligible bonds have been forced to load up on some pretty pricey bonds that, in our view, don't always offer much real value. We've stayed highly selective about what we buy in primary markets, while our focus on shorter-duration bonds should help insulate us from any spikes in credit spreads.

Over the quarter, we snapped up several newly issued bonds we felt were attractively priced, including some new **Morgan Stanley 5.432% 2032s**, Canadian **Bank of Nova Scotia 4.943% 2030s** and Norwegian bank **DNB 5% 2032s**. We also bought some more **Telereal Securitised Property 1.3657% 2031s**. Telereal manages a large-scale commercial property portfolio that's mainly leased to BT. The bonds, which offer a very attractive spread, are backed by the rental cash flows the firm earns from its long-term leases. We regard Telereal as a very high quality issuer: its bonds are very rarely available to buy as they're often held to maturity.

When you invest, you could lose some or all of your investment.

**Two risks to watch**

The resumption of fighting in the Middle East has made the inflation-versus-growth balancing act facing central banks a whole lot harder. If the Strait of Hormuz fully shuts again, the inflation impulse that ebbed through May and June will return with force, leaving bondholders warier about the rates outlook.

Meanwhile, AI's biggest names are quickly becoming some of the largest and longest-dated issuers in investment grade credit markets. In our view, that's raising concentration risks that make active credit selection more important than ever.

**STUART CHILVERS**
Fund Manager

For more info on our fund, including factsheets, performance and fund manager views, please click here.

If you require further clarification on this commentary, then please contact your adviser or Rathbones at the contact details below.

Any views and opinions are those of the investment manager, and coverage of any assets held must be taken in context of the constitution of the fund and in no way reflect an investment recommendation. Past performance should not be seen as an indication of future performance. When you invest, you could lose some or all of your investment.

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