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investing ON THE go

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[INTRODUCTION]

Staci West (SW): Welcome back to the Investing on the go podcast brought to you by FundCalibre. Although markets may be volatile, opportunities are still emerging for bond investors willing to look beyond the headlines. In this episode, we explore how high yield bonds are holding up amid geopolitical uncertainty and more.

Chris Salih (CS): I'm Chris Salih, and today we are joined by Rhys Davies, manager of the Elite Rated Invesco Bond Income Plus Investment Trust. Rhys, once again, thank you very much for joining us today.

Rhys Davies (RD): Morning thank you very much for having me.

[INTERVIEW]

CS: No problem at all. Unfortunately, there is only one place to start that is geopolitics and everything that's going wrong in the world again. [**RD:** Yep.] So I read your Q1 update a couple of weeks back, and you sort of mentioned that high yield's actually been quite resilient to the end of March, and we should say that now because it's six weeks ago almost. But have things started to change in the past six weeks? Are things starting to bite? Are you having to sort of be a bit more active? Active is probably not the right word. So are you starting to have to change your approach basically with things starting to look like they're gonna last a bit longer between the US and Iran?

RD: Sure. Yeah. Well, thank you for having me today. So you are referring to an update to the end of March and I would've said that bond markets have been resilient during April even more resilient to put it in a Trump way. They have been very resilient. They did react, of course to the start of events in the Middle East and in broad brush terms we saw the high higher index yields move maybe 1% higher at the start of March. But then much like equity markets, they changed direction very quickly again.

So in Europe, the yield to maturity on the European hide index, it's around 6.2% today, compare that to around 5.8% at the start of the year. So not a huge move higher, hence that kind of resilient point. I would say the price action that we've seen since the end of February and through April is very reminiscent to what we saw a year earlier when markets were dealing with all of the tariff headlines. This spike higher in yields then a rapid turnaround.

But you raised an important point about inflationary concerns because of higher oil prices. That is a key difference to a year ago. And I think so far, risk markets including higher bond markets are much more inclined to see that as a one-off impact that doesn't lead to inflation setting in. And also there's a lot of focus on a resolution and we can all see this with equity markets. High bond markets are harder for most people to observe.

But with equity markets, we've all see in it, we're recording this at the start of May and really equity markets are looking through to a resolution where oil and goods start flowing again. So when we see that kind of optimism in the market, I think it is important to just pause, reflect, make sure that we are thinking about whether risks are being priced appropriately. And that's a concern right now that risks are not being priced appropriately.

So with that in mind, the portfolio is, I would say, more cautiously positioned and just treading carefully. So choosing bonds that we feel pay us enough yield for the various risks that are out there.

CS: We'll come back to some of those points quickly, but I just wanted to quick follow up on that. So it's almost a case of like, if you're not sure, just sit tight because Trump comes out with headlines and they change, move market and then the opposite thing happens to what he says and then two days later he comes out headlines and the move markets. Is it a case of like, just sit tight with what we have unless something really stellar stands out?

RD: I think so. I mean the portfolio that we put together all the way back, you know, going back into late 2024, so if you remember 2022, we had the big move in bond markets, some great opportunities coming out of that to put some yield back into the portfolio, 2023 good year for that 2024 similar. And then towards the tail end of 2024 into 2025, it was start to think about is are we getting enough yield now for an uncertain outlook you know, relatively weak growth outlook, et cetera. So the portfolio's been in a good position for these types of events for a while.

Certainly when you have sell offs, that's an opportunity to not just kind of sit tight, but to actually be buying more so last year than this year's sell off. And that's because we're coming at it from a slightly different starting point in terms of the, you know, web bonds yields had got to and where they moved to it wasn't as attractive this year as it was a year ago.

But yeah, I think we've got the portfolio that we like with the potential for, you know, a variety of different risks to come through the system and yeah, sitting type makes sense. And the great thing about credit so by that I mean bonds that are issued by companies is that we are getting paid an income, we're getting paid a coupon. So we are earning that income whilst we're sitting there waiting for the next positive tweet or the next negative tweet. Those companies are still every day accruing a coupon that they must pay us every quarter or a half year. And so we've got lots of those.

The idea, we've got lots and lots of those in the portfolio and they're all doing their thing. And we can sit here and yes, of course, be looking at the risks out there and how the picture is evolving, but certainly, and

especially in these markets where they are just so volatile and event headline driven, it makes sense to sit tight.

CS: And just quickly, when we look at sort of higher bonds in general, I mean the average investor might just sort of look at them and go, well, they're the riskiest type of bond in the market, but the market has changed a lot in the last sort of 20 years. I mean the BBs, which are sort of seen as the more secure end of the high yield bond market, are they sort of account for around 6% of the index and it was about 40% after the global financial crisis. So I guess the question is do you still feel that perhaps people judge it on standards 20 years ago? And I guess the other thing is we are also seeing many higher yield bonds looking to improve corporate balance sheets in recent years as well, which is part of that, is there still a challenge with that in trying to communicate that to investors?

RD: Yeah, I mean, it's a fair point. You know, we used to call high bonds junk bonds. We stopped calling them that many years ago, mainly because it doesn't sound great. But also I would say it's not very fair because you can have higher bonds that have some very, that have issued by very good quality companies that are rated as high yield where the chances of them actually defaulting are still relatively low.

Your point about the quality of the index, and especially in Europe or the universe, the higher universe in Europe is accurate. So we now have much more BB rated issuance, and that's at the very high the highest quality end of the hired market.

And that has changed a lot in the last 20 years. And my career spans a little bit beyond that and I've seen those changes. So yes, we do have a you know, on the whole a better quality universe to be picking from. And then more recently, yeah, we've also seen companies go through a lot of changes. You know, we've all been through this journey, this big shift in borrowing costs. Whether it's an individual with a mortgage governments, anyone with debt is now paying more interest on that debt for high bond markets that peaked in 2023. And it's been improving since.

That in itself takes some pressure off those companies because interest rates are a little lower today than they were at the peak in 2023. But also as companies have got more used to the idea of having to pay more interest after, you know, have decades of paying very low rates of interest, then we've seen a lot of refinancing activity over the past couple years as companies issuing new bonds to repay those bonds sooner rather than later.

So just prudent balance sheet management. I'm not really concerned about the quality of the higher bond market as a whole. I think it's a better place than today, than it has been for many, many years. But there is always going to be pockets of risks, individual companies that are that are facing their own issues. And so we really need to just make sure that the yield we're earning from high bonds is sufficient for the risks as we see them, especially in an environment like this.

CS: You mentioned, we talked about the resiliency right at the top of the podcast. What have spreads actually been like in high yield bonds space? Maybe just explain for listeners as well what the importance of that too possible.

RD: Yeah, sure. So spreads or credit spreads, that's the extra yield that you can earn over a government bond. And they've, you know, also been very resilient over this period. They've moved in a similar way to bond yield, so they don't always move in the same, quite the same way because Government bond yields can do one thing and spreads can do something a little different. But they've been the description there is is probably

more resilient than than yields at the government bond yields. So that means we are back again today at historically very low levels. So that extra yield compensation is historic on a historic basis, is very low, very tight, as we call it, in bond speak. And that's something to be thinking about when I'm putting the portfolio together. When spreads are low tight, it's investors taking it positive view on the outlook. And before Iran conflict began there were some good reasons for that positive view inflation was generally heading in the right direction. That's good news for bonds. Economic growth was not strong, but it was still positive. That's good news for bonds and for credit. So there is a risk that high bond spreads today are not factoring in the potential for an economic growth shock because of the conflict.

That, you know, there's definitely something coming down the line for the period of time that we've had so far with this disruption to oil and goods flowing through the strait of Hormuz. So again, it leads us to just trade carefully. So choosing those bonds that we feel are paying us enough for those enough spread for the credit risks, or we can also be favouring companies that are just in this environment, less exposed to those growth risks. So not banking everything on this very optimistic outlook.

A good example recently there would be a company that makes capsules that go around medication. So buying their bond deal a couple of weeks ago felt like a good kind of a cyclical investment we make. And they should be very indifferent to any economic growth list.

CS: Okay. You mentioned something's coming down the line. I'm sure you wouldn't be the first manager who hears the word inflation a little shiver down their spine, hearing that word. We talked about Trump saying we kind of almost have to not ignore him, but kind of take the step back and if in doubt do nothing, inflation sounds like it's coming, we dunno how badly or it will be, but there's talks of rate rises, et cetera. Can you slash are you trying to mitigate that in the portfolio yet as a risk or are you waiting?

RD: Yeah, I mean, during March we saw how the Iran conflict started to raise concerns over inflation. And then as you point out, central bank policy. So in the UK we've seen expectations go from interest rate cuts to now to back then talk about rate hikes. I think we're now back to kind of a more neutral outlook. You know, maybe neither.

Personally I think it would be premature if the Bank of England to shift towards interest rate increases, particularly given the labor market conditions. Wage pressures were not especially strong before the conflict began. But having said that, as I mentioned earlier, before the conflict began, inflation was generally looking under control, reduced bond markets, interest rates were supposed to be coming down a little further. The trajectory of both of those is now being questioned.

We still see very strong demand for bonds in our markets and that's apparent in those credit spreads. So I think that overall, the best way for us to mitigate those risks is keep the rate sensitivity of the portfolio relatively low. So if there is a resurgence of inflation and that results in fresher on yields, then the rate sensitivity can be kept relatively low by focusing on owning bonds with maturities inside of five years or even four years. You know, that's a prudent way to do it, especially when spreads are also at these very low or tight levels.

CS: Okay. I feel like we've started the sort of first half of the podcast are quite a lot of the negative back foot stuff, so there are some good things going on. So let's start with that. I mean you've sort of got gross gearing in the portfolio. I think it's around 12% we said, we mentioned recently. I mean, sort of in the normal area, I think it's normally 10 to 15%, but you've also sort of been in quite a fortunate position of having sort of cash coming in from share issuance. So you know, those two things together. Tell me that maybe you are actually

finding opportunities in the market. Maybe just talk us through where you see the opportunities in a couple of examples maybe.

RD: Sure. Well the normal gearing range for BIPS is around 10%. So sometimes little above, sometimes below. If we see lots of opportunities in the market perhaps all of a sudden because markets have sold off, then it is very useful to be able to quickly deploy gearing to buy bonds at cheaper levels. And it's what we did during the market sell off in April 2025 when we had that tariff induced sell off. Less so as I mentioned this year because we did come from a less attractive starting point and the moves were not quite as much as we would've liked to see.

As you point out as well, BIPS has been in this very fortunate position of been able to issue more shares on a fairly consistent basis for some time now, including a larger 25 million placing earlier this year. And then about the same again, just in regular issuance. So we've got some, the trust has got some really good support from investors, some nice momentum behind the trust at the moment.

In terms of the opportunities again, it's that point about credit spreads being relatively tight going into the around conflict. And so the sell off that we saw there just didn't provide as many opportunities as it did a year ago, but there were some bonds that we added to the portfolio cheaper levels. But having said that, my job as a fund manager for BIPS is to really open up the index to be looking inside that universe and to find those opportunities. And we're still doing that.

CS: Okay. Are there any specific examples you're able to talk about?

RD: Yeah, sure. So more recently then, since the conflict has began, I can give a couple of examples and I would say the appeal of both of these, especially the first one is around the less cyclical nature of their business in this more uncertain environment.

So the first example that I'll point to from a recent new issue would be a European satellite operator called SES, which you could define as Europe's national champion in satellite infrastructure. So their bond pays a coupon on for almost 7.5%. So fairly attractive looking coupon. A company like that will have these long-term contracts, good stability about earnings, which as a bond investor you really like to see. But they've been on this very interesting journey over the past few years. A few, you know, starting to face this real threat from Starlink in the US which uses a very different type of satellite technology. But then what we've seen is as governments have suddenly become a lot more concerned about their reliance on the US and even a company like Starlink, SES is seen as this safe, strategically important partner. It's based in Luxembourg for European government and defense spending. So that kind of brings us back to thinking that this is quite an attractive company to be investing in. It's the reason we're very happy to buy this bond for BIPS, having never invested in them before.

The second example that I would point to again from just a couple of weeks ago during the conflict is a junior bond from the insurer of Liverpool Victoria in the UK. So you know, a very different kind of business because of the timing of that issue, because it's not a particularly big company. It’s a smaller bond, 150 million pounds in size which is relatively small in bond terms. That meant that the company did pay a premium on their coupon. I think because it's smaller also because of the timing. So that coupon came at just under 7.7%. So again, very attractive to put into the portfolio. So for BIPS, which is a closed ended investment trust and can really think about owning bonds like this that might be smaller, may trade less frequently, I'm very happy to put a bond like that into the portfolio. So that's another quite different example to SES, but again, something very, very comfortable to put into the portfolio.

CS: Okay. And I just wanted to finish with sort of how you sort of give investors sort of peace of mind with the portfolio. So you know how your bonds are often sort of seen as a middle ground investment, they're higher returns than investment grade bonds but with more volatility, but on the other side, sort of, people often sort of view them as behaving a bit more like equities. How do you sort of manage that in terms of trying to give investors these returns whilst managing that perceived volatility around investments in this sort of area of the market?

RD: Yeah, yeah. I mean, well the first point I would make is ultimately a high yield bond is still a bond, and a bond is a loan. It must be repaid by the company who issued it if and BIPS is mainly investing in corporate bonds. So yes, they can be price volatility, but the beauty of a bond is that we know what the end result will be. It's contractual obligation. So a bond that may trade at a price of 90 today, we know we'll still get repaid at 100 at maturity, provided the company doesn't fail on that obligation. So price volatility, even in higher bond markets should generally be less than with equities for that very reason, that contractual obligation reason. And that certainty of what we're gonna get at the end even.

So how do we try to manage that within the BIPS portfolio because we do see volatility and a couple of very important tools that we use. So one is good credit analysis. So understanding the credit risks of every company whose bonds going within the portfolio. And the other is diversification. So investing in a wide, a very broad range of bonds. So typically anywhere from a 100 to 150 different companies whose bonds have within the portfolio. They're the two very important main tools that we have.

There are some other tools that we can use when we start to worry that maybe markets are not pricing risks as well as they should be, which I think is where we are right now actually. So we can use derivatives to protect portfolio like a credit default swap. They rose to fame during the financial, you know, The Big Short film, et cetera. That's what it was all about. Sometimes government bonds can act as a risk off hedge. Sometimes the US dollar can be used as a risk off hedge, but I would caveat that by saying the relationship between both of those and volatility and risk markets has really broken down in recent years. So there's possibly moments when they work, but we can no longer rely on those as offering us the same kind of risk off hedge.

So product default swaps quite an interesting one because it's a volatility product. So if you see volatility increase, then the value of that hedging rises. We can sell it, take a profit, reinvest that into the portfolio…

CS: And you've also got the attractive dividend. We should mention that before we get to the end of the podcast as well.

RD: Yeah, yeah. The dividend, absolutely. I mean the, I think to finish on the last point, ultimately keeping that portfolio diversified, understanding the credit risk companies whose bonds own, that's the key tools we have. And then that allows me to put together a portfolio with a clear dividend target in mind, and that's how the trust is run. And that today, that is £12.25p per share per annum paid quarterly, and that equates to a dividend yield on today's share price of around 7%.

CS: Okay. On that note, Rhys, thank you very much for joining us today.

RD: Thank you, Chris. Thanks.

TRANSCRIPT: EPISODE 395

SW: The Invesco Bond Income Plus investment trust, or BIPS, aims to provide capital growth and a high income by investing predominantly in high-yielding fixed income securities. Rhys and his team have demonstrated their ability to manage risk through diversification, while also paying a consistent level of dividend for a number of years. To learn more about Invesco Bond Income Plus investment trust please visit fundcalibre.com and don't forget to subscribe to the Investing on the go podcast, available wherever you get your podcasts.