Baillie Gifford™

Investment Grade Bond Q2 investment update

July 2025

Investment manager Nektarios Chatzilefteris Michalas gives an update on the Investment Grade Bond Strategy covering Q2 2025.

Your capital is at risk. Past performance is not a guide to future returns.

Nektarios Chatzilefteris: Welcome to the Q2 2025 update for the Baillie Gifford Investment Grade Bond Strategy. My name is Nektarios Chatzilefteris, and I'm a co-manager of the strategy.

In April, in the wake of 'Liberation Day,' markets were highly volatile, and the potential for a major shift in the global trade regime resulted in a broad-based selloff. Markets went on to steady and recover over the rest of the quarter, following the announcement of a "90-day pause", and the subsequent progress on trade deals. Investment-grade bonds behaved in a similar pattern, but exhibited significantly lower volatility than equity markets, as you would expect.

Despite this challenging backdrop, I am happy to report that during the period, the strategy outperformed its index, excluding the impact of swing pricing, continuing the positive trend from Q1. This was achieved by focusing on our strengths rather than reacting to every headline.

Bond selection was the key driver of relative outperformance. Strong contributors included event-driven idiosyncratic positions, which played out as expected. For example, **CK Hutchison** offered to buy back the strategy's bonds at a premium following the sale of an asset, an event we call a tender. **Weir Group** also tendered bonds we held at a premium, while looking to increase its US dollar financing.

In terms of portfolio positioning, the challenge is to balance caution and optimism in the context of current market conditions. When we form our market view, we think carefully about key elements of the macroeconomic backdrop, such as growth and inflation, in conjunction with valuations and company fundamentals. So, what is the key factor driving current positioning?

What really gives us reason to be cautious is relatively high valuations in investment-grade markets and, within this context, the high potential for future volatility. Risks include higher-than-expected inflation, rising geopolitical instability, and the potential eruption of trade wars.

As a result, we continue to position the portfolio relatively defensively, with plenty of dry powder to take advantage of opportunities should they arise. In addition, we have reduced exposure to bonds with greater subordination risk, which yield more but are more volatile in a selloff.

Despite taking action to reduce portfolio risk, the strategy is still risk-facing overall. You would ask me, why? While policy uncertainty remains front of mind, there is still cause for optimism, as growth is supportive in Western economies, and company fundamentals in the investment-grade market are robust.

Within this context, we have positioned the portfolio to outyield the index. This is primarily achieved in two ways:

- First, by expressing a significant overweight to BBB-rated investment grade bonds, and
- Second, by maintaining an overweight in bonds at the front end of the yield curve. In other words, corporate bonds that are due to mature relatively soon, whose prices should be less volatile in a selloff. We like these bonds because, despite their lower risk profile, they continue to offer attractive yields.

Overall, investment-grade yields remain very attractive, with our high-quality portfolio providing a 5 per cent yield, which is significantly higher than the average of the last 15 years. We are also excited about the return potential on offer from individual bonds, where we continue to identify new sources of added value for clients.

Volatility during the quarter presented opportunities to top up positions in favoured names at attractive valuations. For example, **Public Property Invest**, a social infrastructure Real Estate company in the Nordics, which we believe has long-term potential.

We also found opportunities when companies came to the market to raise new capital. Investments sought to take advantage of both short-term price dislocations; for example, in **Barclays** subordinated debt that was offered at an attractive discount and which we sold shortly after once the market corrected, but also to invest for the longer term, for example, in **James Hardie**, a leading building materials supplier in the US that sought to refinance a recent acquisition, with a concrete plan to reduce debt, making bonds attractive.

So, in summary, there are three key takeaways this quarter. The strategy continued its positive trajectory of outperformance from Q1. The portfolio is cautiously positioned but continues to outyield the index. Finally, the portfolio is full of potential. I have talked about Public Property Invest and James Hardie. These are just individual positions in the portfolio that hold the potential to add value through bond selection.

Thank you for your time, and if you do have any follow-up questions, please get in touch with your Baillie Gifford contact.

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Investment Grade Bond

Annual past performance to 30 June each year (%)

	2021	2022	2023	2024	2025
Investment Grad Bond Composite (gross)	7.5	-14.7	-1.2	12.0	8.3
Investment Grade Bond Composite (net)	3.2	-13.4	-6.9	10.7	6.8
Investment Grade Bond Benchmark*	1.8	-12.9	-7.1	9.7	5.4

Annualised returns to 30 June 2025 (%)

	1 year	5 years	10 years
Investment Grade Bond Composite (gross)	8.3	-0.3	2.6
Investment Grade Bond Composite (net)	6.5	-0.6	2.2
ICE BofA Sterling Non-Gilt Index	6.8	1.0	3.1

Source: Revolution, ICE. sterling. Returns have been calculated by reducing the gross return by the highest annual management fee for the composite. 1 year figures are not annualised.

Past performance is not a guide to future returns.

Risk factors

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