Vanguard

Q4 2021

GLOBAL CREDIT BOND FUND

Quarterly update

LOW-COST ACTIVE FIXED INCOME

The Vanguard Global Credit Bond Fund is an actively managed fixed income solution investing primarily in a diversified portfolio of global investment-grade fixed income securities. The fund is managed by Vanguard's Fixed Income Group and aims to generate a diversified, consistent level of return and income over the long term.

Highlights

- Inflation and growth concerns drove heightened volatility in bond markets.
- Government bond yield curves flattened as shorter-maturity bond yields rose.
- Credit spreads finished the quarter broadly wider, led by emerging market high-yield bonds.
- The Vanguard Global Credit Bond Fund underperformed its index over the quarter.
- Volatility around central bank tightening could lead to additional credit dislocation.

Market overview

The fourth quarter began much as the third had ended, with heightened volatility in fixed income markets as commodities extended their run of strong performance and rising inflation concerns continued to add pressure to government bonds. This weighed on risk assets across the board, notably emerging market debt. Bond markets stabilised in November as central bank announcements around the gradual withdrawal of accommodative monetary policy were broadly in line with market expectations. However, the emergence of the Covid-19 Omicron variant late in the period led to fresh market concerns about growth, particularly around the impact on Covid-19 sensitive sectors.

During the quarter, the US Federal Reserve left the target range for its federal funds rate unchanged at 0% to 0.25%, and, as widely anticipated, announced that it would double the pace of the tapering of its bond-buying programme to $30 billion a month, which starts in January and is now expected to conclude by March 2022. In Europe, the European Central Bank (ECB) also announced a reduction in the pace of its Pandemic Emergency Purchase Programme (PEPP) in the first quarter of confirming that the PEPP would end in March 2022. In the UK, the Bank of England (BoE) became the first major central bank to tighten its policy, as it raised its Bank Rate to 0.25% at its December meeting.

In government bond markets, short- and medium-term US Treasury yields experienced a marked increase during the period, and the curve flattened as 20-year and 30-year US Treasury yields fell over the quarter. In Europe, the German Bund curve flattened as the yields on bonds with maturities between two and 10 years rose while 15-30-year bonds saw their yields fall. In contrast, other European government bonds, such as those of Italy and Spain, experienced yield rises across the curve. The UK gilt curve flattened significantly as bonds with maturities of between one and eight years saw yields increase while 15–50-year bonds experienced sharp falls in yields[1].

In the corporate bond markets, spreads moved tighter in October, then significantly widened in November before partially recovering in December, finishing the quarter broadly wider. Emerging market high-yield bonds were hit hardest, as spreads ended the quarter 45bps wider[2].

1 Vanguard and Bloomberg, as at 31 December 2021.
2 Source: J.P. Morgan EMBI Global Diversified Investment Grade and High Yield indices, as at 31 December 2021.

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Corporate earnings growth, despite moderating throughout the year, remained robust, particularly in cyclical sectors. Profit margins stayed relatively resilient in most sectors as inflationary headwinds were offset by cost cutting and price increases. Supply-chain bottlenecks remained an issue but have likely now peaked, although we continue to monitor developments around the Omicron variant, particularly in Asia. Meanwhile, consumer demand was strong as reopening continues to fuel economic activity.

In terms of technicals, supply of euro- and US dollar-denominated bonds in the fourth quarter was above the average for the same period in prior years, although issuance tailed off in December. Demand for new issues was robust throughout most of the period and appetite for "green" or "sustainable" assets remained very strong. However, flows overall remained lacklustre and are likely to remain sensitive to any further volatility in rates.

Fund performance and positioning

The Vanguard Global Credit Bond Fund returned -0.55% over the quarter. This compared with a return of -0.05% for its benchmark, the Bloomberg Global Aggregate Credit Index Hedged[2].

The fund's sector allocations to European corporate bonds detracted from performance during the period. Our sector allocations to emerging market bonds also weighed on performance.

The fund's sector bias to other sectors was a positive contributor to overall performance. Underweight positions in sovereign agency bonds also added value.

In terms of positioning, the fund's exposure to US investment-grade and emerging market debt was reduced during the quarter and we have continued to lower risk, our caution based on high valuations, slowing growth and the prospect of heightened volatility around rate hikes.

Amid the gradual removal of monetary easing by the Fed and other central banks, the fund maintains a larger liquidity position than usual, with enough "dry powder" to access opportunities should higher volatility arise.

Outlook

Looking ahead, the combination of rich valuations, stagnating growth and the potential for monetary tightening-induced volatility have led us to adopt a cautious and selective stance. The Fed's accelerated path of tapering makes the market more vulnerable, although we don't necessarily believe that this will cause the market to sell off. However, we do expect that additional credit dislocation will result.

We remain constructive on the credit asset class, although many of the highest-quality issuers are now priced too richly, in our view, while lower-quality issuers are vulnerable to a change in market sentiment. As a result, we have maintained our reduced credit exposure of the last several months and are now focused on investment in credits that have upside potential based on improving fundamentals. Relative to more than a year ago, overweight positions in specific sectors, business models or credit-quality buckets offer little value in today's market.

On a positive note, credit fundamentals have continued to be robust after a stronger-than-expected third-quarter corporate earnings season. Furthermore, some areas of credit, such as European investment-grade, high-yield and emerging market high-yield bonds, offer good value, although we remain cautious on US investment-grade debt, especially short-maturity bonds.

We remain focused on identifying security-selection and relative-value opportunities, which we believe will arise more frequently as market volatility increases.

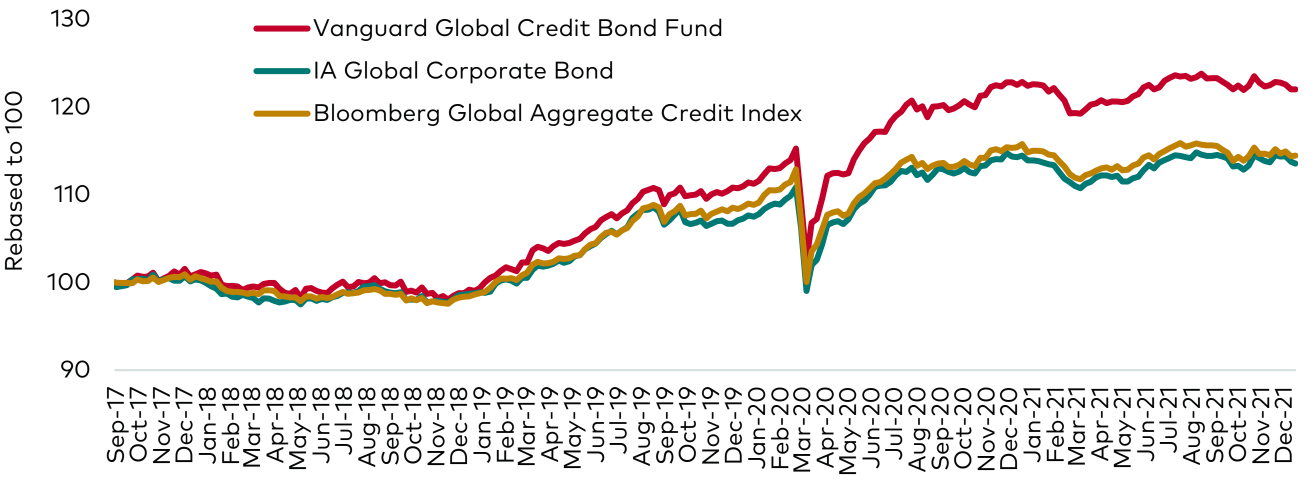
2 Source: Bloomberg, as at 31 December 2021.

Key fund facts (as at 31 December 2021)

Investment manager: Vanguard Group
Inception date: 14 September 2017
Domicile: Ireland
Benchmark: Bloomberg Global Aggregate Credit Index
Ongoing charges figure[1]: 0.35%
Fund AUM: GBP 488m

Number of holdings: 1,315
Average coupon: 2.5%
Average maturity: 8.3 years
Average quality: A-
Average duration: 7.3 years
ISIN: IE00BYV1RG46

Fund performance (as at 31 December 2021)



Cumulative (%)	YTD	3m	1 year	3 yr (ann.)	5 yr (ann.)	Since inception
Fund	-0.68	-0.55	-0.68	7.25	--	4.74
Peer Group	-3.28	-1.20	-3.28	3.57	2.42	2.29
Benchmark	-1.13	-0.05	-1.13	5.12	3.45	3.19

Year on year (%)	1 Jan 2017 - 31 Dec 2017	1 Jan 2018 - 31 Dec 2018	1 Jan 2019 - 31 Dec 2019	1 Jan 2020 - 31 Dec 2020	1 Jan 2021 - 31 Dec 2021
Fund	--	-2.01	11.50	11.41	-0.68
Peer Group	2.23	-0.29	6.65	7.89	-3.28
Benchmark	4.22	-2.13	9.97	6.83	-1.13

Past performance is not a reliable indicator of future results.
Source: Vanguard and Morningstar, as at 31 December 2021. Peer group is IA Global Corporate Bond. Performance figures include the reinvestment of all dividends and any capital gains distributions. The performance data does not take account of the commissions and costs incurred in the issue and redemption of shares. Basis of fund performance NAV to NAV. Basis of index performance is total return. All performance is calculated in GBP, net of fees, and the return may increase or decrease as a result of currency fluctuations.

[1]The Ongoing Charges Figure (OCF) covers the fund manager's costs of managing the fund. It does not include dealing costs or additional costs such as audit fees.

Fund breakdown (as at 31 December 2021)

Distribution by issuer (% of bonds)

	Fund %
Industrials	33.9
Financial institutions	24.6
Treasury/federal	17.7
Cash	12.9
Utilities	5.2
Sovereign	4.5
Agencies	1.3
Provincials/municipals	0.0
Asset-backed security	0.0
Commercial mortgage-backed security	0.0
Other	-0.1
Supranational	0.0
Local authority	0.0

The allocations are subject to circumstances such as timing differences between trade and settlement dates of underlying securities, that may result in negative weightings. The fund may also employ certain derivative instruments for cash management or risk management purposes that may also result in negative weightings. Allocations are subject to change. Cash includes physical cash on the account, cash like instruments (such as ultra-short term treasury bonds) and derivative instruments.

Distribution by credit quality (% of bonds)

AAA	17.2
AA	2.1
A	21.2
BBB	42.5
Less than BBB	4.2
NR	12.9

Credit quality ratings for each issue are obtained from Bloomberg using ratings derived from Moody's Investors Service, Fitch Ratings, and Standard & Poor's. When ratings from all three agencies are available, the median rating is used. When ratings are available from two of the agencies, the lower rating is used. When one rating is available, that rating is used.

Source: Vanguard, as at 31 December 2021.

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Investment risk information

The value of investments, and the income from them, may fall or rise and investors may get back less than they invested.

Past performance is not a reliable indicator of future results.

Some funds invest in emerging markets which can be more volatile than more established markets. As a result the value of your investment may rise or fall.

Investments in smaller companies may be more volatile than investments in well-established blue chip companies.

Reference in this document to specific securities should not be construed as a recommendation to buy or sell these securities, but is included for the purposes of illustration only.

Funds investing in fixed interest securities carry the risk of default on repayment and erosion of the capital value of your investment and the level of income may fluctuate. Movements in interest rates are likely to affect the capital value of fixed interest securities. Corporate bonds may provide higher yields but as such may carry greater credit risk increasing the risk of default on repayment and erosion of the capital value of your investment. The level of income may fluctuate and movements in interest rates are likely to affect the capital value of bonds.

The Vanguard Global Credit Bond Fund may use derivatives, including for investment purposes, in order to reduce risk or cost and/or generate extra income or growth. For all other funds they will be used to reduce risk or cost and/or generate extra income or growth. The use of derivatives could increase or reduce exposure to underlying assets and result in greater fluctuations of the Funds net asset value. A derivative is a financial contract whose value is based on the value of a financial asset (such as a share, bond, or currency) or a market index.

Some funds invest in securities which are denominated in different currencies. Movements in currency exchange rates can affect the return of investments.

For further information on risks please see the "Risk Factors" section of the prospectus on our website at https://global.vanguard.com.

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