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CQS New City High Yield (NCYF)

NCYF is set to become the only bond fund to be an AIC Dividend Hero.

Thomas McMahon thomas.m@keplerpartners.com

Overview

Investment objective

To provide investors with a high gross dividend yield and the potential for capital growth by mainly investing in high yielding fixed interest securities.

Source: Morningstar

As at: 09/10/2026	Latest Market Capitalisation £369,659,240
Trust Name CQS New City High Yield	Latest Net Gearing (Cum Fair) 12%
Ticker NCYF	Latest Ongoing Charge Ex Perf Fee 1.11%
Management Company Manulife CQS	Shares Outstanding 730,551,858
Manager Name Ian Francis; Darren Toner;	(Discount)/ Premium (Cum Fair) 7.5%
Association of Investment Companies (AIC) Sector Debt - Loans & Bonds	Daily Closing Price 50.6p
Dividend Yield 8.9%	
Dividend Distribution Frequency Quarterly	

CQS New City High Yield Fund (NCYF) delivers an exceptionally high yield, 8.9% at the time of writing, having grown its dividend for 19 consecutive years. One more year will qualify it for AIC Dividend Hero status.

Managers Darren Toner and Ian 'Franco' Francis invest in the smaller, more complex and less liquid issues in the high yield bond market to generate this income. NCYF uses the closed-ended structure to the full, taking advantage of its ability to handle illiquidity, gearing up the portfolio and managing a revenue reserve which supports payments in times of volatility. The appeal to income investors is obvious, and the trust has mostly traded on a premium for a number of years, regularly issuing shares to grow.

Current expectations are for interest rates to rise in the coming quarters in the key jurisdictions of the UK, US and EU, and this would play into the managers' hands. Higher rates are likely to feed through into higher absolute yields on offer, and make it easier for the managers to reinvest maturing bonds into those paying higher coupons. The portfolio has a low duration, having a high yield and short average time to maturity, and so the impact on portfolio values should be small.

Darren and Franco continue to find plenty of opportunities in the market. They note any stress from volatility in energy markets, from higher rates and from the impact of AI should lead to differentiation in company performance and outlook and therefore opportunities for active investors.

Franco is set to retire next May, but has worked with Darren, head of the global high yield and financials teams at CQS, for 16 years and the specialist team of analysts remains in place, so there will be no change to the approach.

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Analyst's View

NCYF employs a relatively straightforward strategy to generate an exceptionally high yield. Darren, Franco and their team specialise in a naturally inefficient part of the market which is too small for most investors and which often lacks external credit ratings or analyst coverage. They can do this thanks to the closed-ended structure, which means they can own relatively illiquid securities and hold them to maturity. The ability to gear up structurally and set aside income in a revenue reserve are other key factors behind the trust's success in growing the income year on year from such a high base.

Franco has managed the trust successfully for almost 20 years, but we are confident that there shouldn't be any disruption from his retirement. Darren has led the team which generates the analysis and stock-picking ideas Franco has employed, and spoken daily with Franco for 16 years, implementing the team's ideas in different mandates. The bedrock of the approach is devoting the resources to an inefficient part of the market many investors don't cover, with an experienced analyst team.

We think NCYF is an outstanding option for investors who want a high yield and have a long-term time horizon. Capital growth is unlikely to be a significant part of the investment case given the income-first mandate and could be negative for periods, while the premium rating increases the importance of having a longer-term time horizon.

Bull

- Exceptional income offering, both yield and dividend growth
- Highly experienced and specialist managers working poorly-covered niches
- Healthy revenue reserves

Bear

- Significant premium could deliver losses to newer shareholders if it deflates
- Issue and issuer specific risks have to be borne in mind with a concentrated and illiquid portfolio
- Continued growth would hamper ability to invest in the same way, albeit this is not likely for some years

Portfolio

CQS New City High Yield Fund (NCYF) aims to exploit inefficiencies in the bond market to generate an exceptionally high yield and grow the dividend year on year. The managers are Darren Toner and Ian 'Franco' Francis, with Franco set to retire next May, and they look for opportunities in the smaller and less liquid issues. These are uninvestable for managers running much larger funds or those running open-ended funds, but the closed-ended NCYF can take meaningful positions and benefit from higher yields as a result. The smaller issues are often unrated by credit ratings agencies and not covered by research analysts, both factors which mean some larger or institutional investors steer clear and which mean there is greater opportunity for a specialist team able to devote the resources to research to add alpha and pick up higher yields. The strategy is to find stock-specific opportunities in over-sold debt, or issuers the market feels are facing serious or structural difficulties, and as such volatility boosts the opportunity set. This means that a number of sources of uncertainty in the economy could be increasing the opportunity for the trust, including the disruptive effects of AI, volatility in energy markets and global trade, and rising interest rates.

High yield credit ratings start at BB at the top end. NCYF's income target means it tends to lean towards the lower credit ratings, with the managers relying on credit analysis to ensure they are investing in issuers less likely to default than the market thinks. Additionally, the strategy is very low turnover, Franco and Darren expecting to hold many of their bonds to maturity in order to receive the high coupons. This means that any volatility in the pricing and credit spreads of these bonds is only a mark-to-market phenomenon, as bonds

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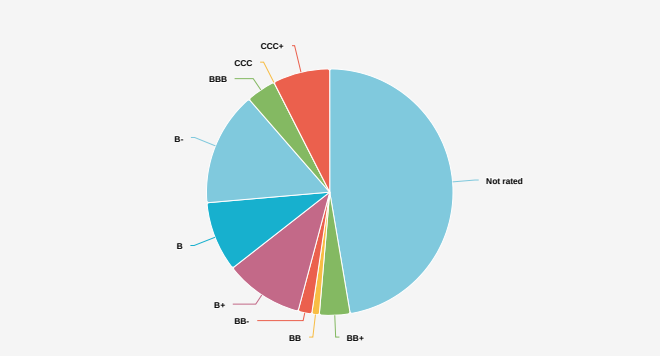
repay the full principal on maturity if they don't default. The chart below shows that the credit rating of the portfolio as of 30/06/2026, with essentially half invested in bonds without a rating and a bias towards those with a lower credit rating even within high yield.

CREDIT RATING

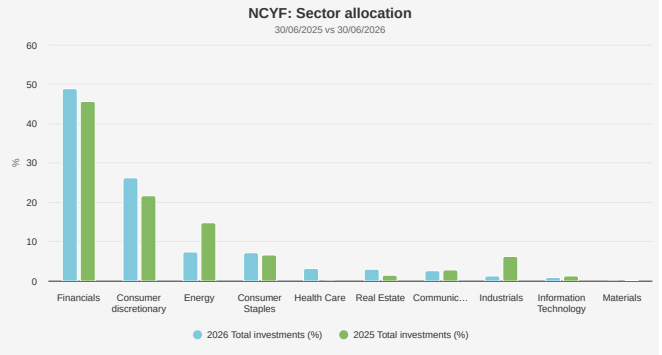


Source: NCYF

Past performance is not a reliable indicator of future results.

Financials have long been an area of focus for the team. Banks and insurers tend to have complicated capital structures and issue lots of debt on a frequent basis to manage their ever-changing funding needs. This is a prime example of where smaller, more complex deals can provide a higher yield for specialists. Darren heads a team of high yield analysts including a devoted financials analyst, which allows the manager to access this part of the market. Many years of experience in these segments for both managers and analysts underpins their confidence in participating in this market.

SECTOR EXPOSURE



Source: NCYF

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In general, sector and stock positioning is led by yield and the managers being comfortable with the risks rather than any macro positioning or intent to trade price gains. That said, AI is a factor which will clearly lead to huge disruption, and Darren and Franco think it is prudent to remain on the sidelines given the unknowns, and as such they prefer sectors such as financials and commodities where disruption is harder due to regulation or business models. One area they have had success in is the consumer discretionary space as this is where the managers note the UK consumer has maintained its spending despite inflationary pressures. Here the portfolio has benefitted from a number of recovery stories in their top ten positions delivering price appreciation as well as yield. This includes debt issued by Travelodge, Stonegate pubs and Asda. All have been under pressure from rising employment costs and business rates, but have outperformed market expectations. Meanwhile, in the same sector, bonds issued by Pizza Express have benefitted from the announcement of a potential sale of the business.

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TOP TEN HOLDINGS, AS AT 31/07/2026

NAME	% OF NAV
SHAWBROOK GROUP 22-08/06/2171 FRN	4.41
TVL FINANCE 10.25% 23-28/04/2028 (Travelodge)	4.28
STONEGATE PUB 10.75% 24-31/07/2029	4.27
RL FINANCE NO6 23-25/11/2171 FRN (Royal London)	3.73
SHERWOOD FINAN 9.625% 24-15/12/2029 (Arrow)	3.67
CIDRON AIDA FINC 9.125% 25-27/10/2031 (Advanz Pharma)	3.44
BELLIS ACQUISITI 8.125% 24-14/05/2030 (Asda)	3.23
WHEEL BIDCO 9.875% 21-15/09/2029 (Pizza Express)	3.22
BARCLAYS PLC 22-15/12/2170 FRN	2.86
ASTON MARTIN 10.375% 24-31/03/2029	2.76
Top Ten Holdings Represent	35.87

Source: CQS

Franco and Darren tend to hold onto positions to maturity unless they can find more attractive yield options, but will trade positions if the investment case changes. For example, they recently sold bonds issued by Aston Martin paying a 10.375% coupon following a new financing transaction which changed the asset backing supporting the existing senior debt. They used the cash to add to bonds issued by Virgin Media. While the coupon is lower at 7.875%, the bonds were trading below par, meaning the yield is higher than this and there is the potential for capital growth if they are held to par. The top ten is relatively concentrated for a bond fund, with 36% in the largest ten issues, but Darren and Franco view the next ten or twenty positions as their pipeline, adding to their highest conviction positions when the cash is available.

Poor sentiment towards UK consumer-exposed names has been one source of volatility in bond markets. Another is the prospect of higher interest rates. The managers are finding opportunities in the real estate sector as valuations come under pressure. They note that in 2022 there was a huge repricing down in property values, equity and debt. Since then, companies have improved their balance sheets and business fundamentals markedly. This means that there is a misalignment between sentiment and technicals and the fundamentals of the underlying businesses, which is bringing opportunities to lock in high yields by buying into falling prices.

The disruption to energy and trade markets from the war in Iran is another source of opportunity. The managers have bought into the bonds of some energy companies this year, and benefitted from buying a position in the equity of Frontline plc, a tanker shipping company. It yielded close to 5% when bought, so well below target, but Franco saw the chances of the dividend doubling given the effect of the war on shipping rates. In fact, the dividend declared in August for Q2 was itself more than the total dividends paid for 2025, at $2.61 including a $0.8 special versus $1.76.

This is a good example of how the managers use equity in the portfolio. It can be a good source of yield and dividend growth, which is particularly useful when rates are lower in the debt market and can help protect the capital from inflation. The team have strong links to the shipping sector, and so have dabbled in the equity in this space, while insurance is another sector they know well and which currently features highly. Equities reached 15.1% as of the end of July, up from 12.9% as of June 2025, with Frontline more than doubling over the year contributing to the growth.

Analysis of the whole capital structure is an important part of the stock selection process, with the team looking to understand where the value is and how best to take advantage of the opportunity. A proper understanding of the debt structure and the covenants is vital to being comfortable taking risks in the higher yielding issues and can help the team add value. A good example was the purchase of bonds and equity in Rathbones, the wealth manager. The managers were scaled back in the new issue, but their analyst demonstrated that they could create a synthetic convertible bond by buying into the equity as well, which they have done.

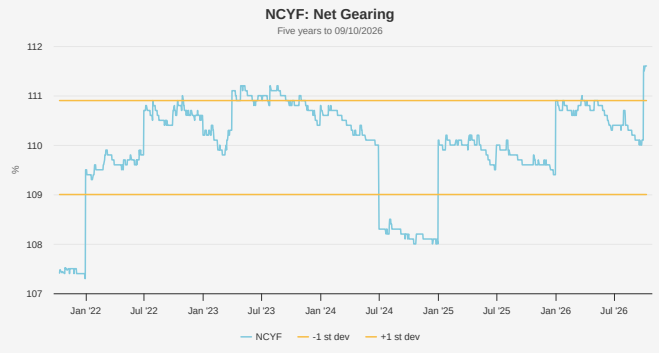
As noted, market expectations for rate hikes are creating some volatility the managers can take advantage of. They argue rates are likely to stay higher for longer, and this should mean that some 'zombie' companies buckle as the rates they pay rise or fail to come down. This should bring opportunities for the managers to invest at higher rates. In fact, any rate hikes would mean even improving credits might find they have to pay the same or higher yields when refinancing, meaning NCYF might be able to generate the same yield from a higher credit quality portfolio. They stress that whatever the volatility in markets, the key to their approach is consistency: looking for opportunities s to enhance performance without trying to shoot lights out, a conservatism which helps moderate the risks of investing in the highest yielding credits.

One trend over the past year to note has been for more of the portfolio to be invested in sterling debt: sterling assets rose from 69.4% in June 2025 to 75.5% as of the end of July 2026. This is a function of higher rates available in sterling, with interest rates higher in the UK than the EU or US, and more opportunities at the stock level. This allocation follows the opportunity rather than being a macro call, although overseas exposure is not hedged, which would reduce the income earned, so the managers have to consider the outlook for the currency.

Gearing

The managers have consistently employed a meaningful level of gearing to help hit their yield target in recent years. Gearing is taken through a short-term unsecured loan facility of £50m, of which £40m has been drawn down, and as of the end of August stood at 10.2% according to Morningstar data. The cost of debt is a spread of 1.4% over the SONIA interbank rate which more or less tracks the Base Rate, plus a charge of 0.45% on the daily drawn down amount. Leveraging up the portfolio counteracts the impact of costs and allows a higher dividend to be paid straight through to shareholders, although it does mean NAV volatility will be higher. The ability to use bank debt in this way differentiates investment trusts from open-ended funds, which can only use it for short-term purposes. Along with investing into less liquid issues, it is one of the ways NCYF uses the closed-ended structure to the full to enhance its ability to generate a high income for investors.

NET GEARING



Source: Morningstar

Past performance is not a reliable indicator of future results.

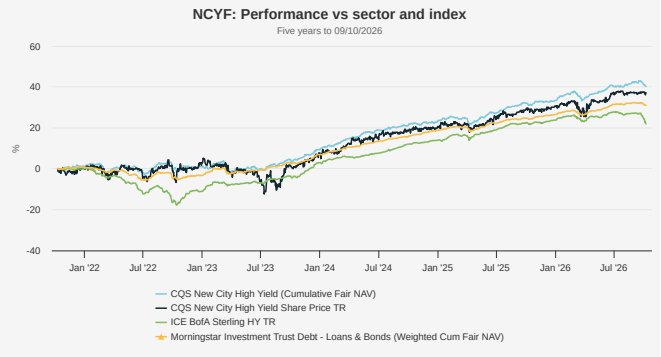
Performance

The most relevant performance metric for investors is the income performance via the **Dividend**. NCYF is unabashedly an income fund, and Darren and Franco's main aim is to maintain and grow the income, which means meeting a portfolio yield of 9.5% after charges, or c. 10.6% gross. The strategy is largely buy and hold, with a low portfolio turnover,

the managers looking to reduce trading costs, which are higher for less liquid issues. That said, they do trade, usually with the aim of enhancing the income when opportunities come up.

Over the past five years, the NAV total return has been 41.7%, ahead of the weighted average return in the Morningstar Loans & Bonds sector and a sterling high yield index. While this latter is not a benchmark, and the trust has no benchmark, we think it provides some useful context.

FIVE-YEAR PERFORMANCE



Source: Morningstar

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NCYF's returns annualise to 7.2%, i.e. below the income earned. The NAV per share, excluding dividends paid, has fallen c. 10.8%. To some extent, this reflects the impact of rising interest rates which have led to falls in the prices of bonds over this time. Bonds bought above par will realise losses if held to maturity, while if the managers have traded out of bonds to chase yield they may have taken a capital loss. However, if we look back long enough, this dynamic has worked in the trust's favour in the past, in periods of falling rates. For example, between March 2009 and May 2013, the NAV per share rose from 38p to 64p, above the 48p issue price. Additionally, in late 2020 to early 2021, credit spreads narrowed considerably and NCYF achieved NAV per share gains in addition to the dividends paid.

One of the key features of investing in the highest yielding bonds is it naturally brings down the duration of the portfolio, i.e. it's sensitivity to interest rates. This means that if we get the forecast rate hikes over the coming months, NCYF's portfolio should see a muted impact (although some impact). However, any impact would only be permanent if the bonds had initially been bought above par, or if they were sold, otherwise the price move would revert on maturity. Permanent loss of capital can also come from defaults. Over the financial year ending 30/06/2026, the portfolio saw its holding in air freight financing business Priority Logistics 1 enter liquidation due to pressure of fuel costs and lower flight activity. This was an exceptionally high yielding instrument with a 12.625% coupon which didn't pan out. Consumer lending Holdco Garfunkelux was also sold at a significant loss as it faced severe refinancing pressure. However, overall, the team's record of avoiding defaults is good, with the evidence being the NAV performance achieved over multiple cycles while hitting a very high yield target.

Credit risk has tended to be correlated to equity markets over time, and additionally Darren and Franco invest 5-10% in equities. These equities will pay a high yield, but also help with capital growth. For example, shipping company Frontline delivered a 112% return over the year ending 30/06/2026, with its dividend hiked from $1.34 a share to $3.13. In fact, Frontline's success helped push the equity exposure to c. 14% as of year-end, above the higher end of the usual range. On the other hand, equities also bring downside exposure too. However, if the coupons on the high yield debt are high, then investors continue to receive an offsetting return when equity markets fall, dampening the impact, as long as the managers avoid defaults. As a result, even in 2022, when equity markets stumbled and bond markets sold off, NCYF's performance was fairly resilient, as the below chart of annual returns shows, although this was also buoyed by a high weighting to dollar debt. NCYF has occasionally generated modestly negative total returns in recent history, in 2018 and in 2020. However, there have been exceptional years which have made this back. While the total return chart therefore looks volatile, the income performance has been very stable, as we discuss in the **Dividend section**.

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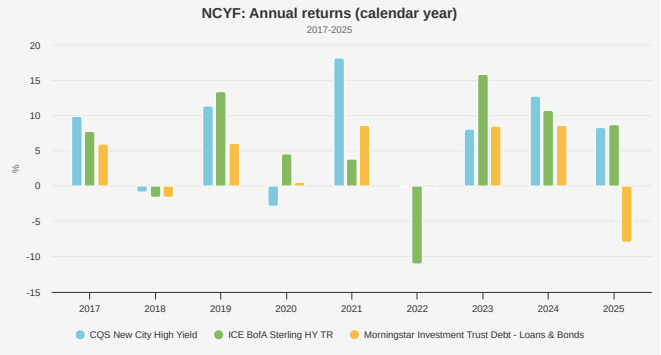
ANNUAL RETURNS



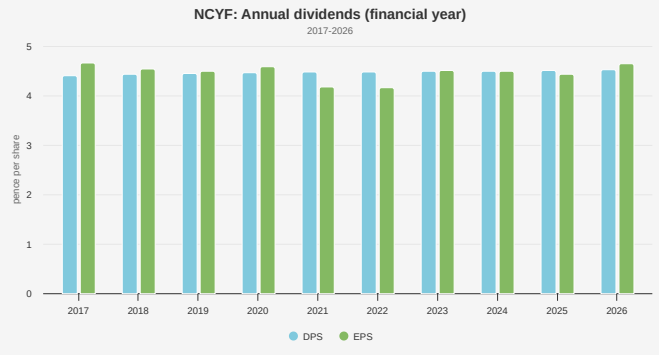
Source: Morningstar

Past performance is not a reliable indicator of future results

Dividend

Last year's dividend of 4.52p per share equates to a historic yield of 8.9% at the time of writing. This very high yield, net of fees, is a key attraction of the trust, as well as the consistency with which it has been increased year on year. In fact, NCYF will qualify for the AIC's Dividend Hero award if it raises its dividend for one more year, which the board states it intends to do. It would be the 20th consecutive year of raising the dividend, a particularly impressive feat for a bond fund given that bond yields rise and fall over the course of an economic cycle, and testament to the flexibility afforded by the investment trust structure. We note though, that while the increase has been regular and consistent, the rate has been behind inflation in recent years.

DIVIDENDS PER SHARE



Source: CQS, Morningstar

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The company pays quarterly dividends, with the fourth being a larger payment. For the financial year ending 30/06/2026, it paid a total of 4.52p per share. This dividend was covered 1.03x by earnings, which means there was a payment made to the revenue reserves. The latter was worth 0.56x the annual payout. While earnings can rise and fall from year to year, NCYF has made a net contribution to the revenue reserves over the past ten years.

Darren's ability to maintain the dividend over the medium to long-term will rely on his ability to take advantage of the smaller, less liquid and riskier issues which allow the

portfolio to generate such a high yield. The immediate outlook is for rate hikes, which could increase yields in absolute levels, and mean that even borrowers in a stronger position might end up paying the same or higher yields when they refinance. As such, we think this would be a helpful environment for the trust's strategy. Additionally, if rate hikes lead to financial pressures on some borrowers, there could be the opportunity to achieve some very high yields. Darren and Franco fish in a part of the pond that larger and open-ended funds struggle to access, which gives them a structural advantage, but nonetheless good credit analysis on individual issuers will remain critical as the portfolio owns many of the highest-yielding credits which by definition means they are viewed by the market as highly risky.

Management

NCYF is currently managed by co-managers Darren Toner and Ian 'Franco' Francis. After almost two decades as sole manager of the trust, Franco is stepping away in May 2027, with Darren to succeed him after a 12 month transition period.

Darren is a senior portfolio manager at CQS within the Multi Asset Credit team, and Head of Global High Yield and Financials strategies. He also manages the open-ended CQS Dynamic Credit Multi Asset fund. As such, he has deep knowledge and experience of the specialist areas of the credit market which NCYF invests in.

Darren notes there is a high degree of crossover between NCYF and the other multi-asset credit funds run by the team, and Franco has been drawing on the same research by the same team of 40 asset class specialists and analysts as he has, while he has personally worked with Franco for 15 years. Therefore, for the most part there really shouldn't be much change to how the portfolio has been run, although Darren notes his different mandates mean he has tended to trade a bit more than Franco, so at the margin he may be inclined to take profits more frequently and add a bit more capital growth potential. As NCYF is a closed-ended fund, Franco has been able to invest in some smaller and less liquid credits which would not work in an open-ended fund, but this just means Darren will have a little extra flexibility on this portfolio. When the transition period ends, Franco will remain available to the company as a consultant for a period of approximately three years.

Discount

NCYF has consistently held a premium rating over the past five years, with investors willing to pay above the NAV per share for the high dividend yield and strong track record of dividend growth. With the yield at 8.9% and the premium at 7.5%, over 2/3 of a year's income return would be sacrificed if a new investor bought the shares and they derated to par and were sold, which shouldn't be a major issue for a long-term investor but does mean they reduce their attractions to an investor with a short-term time horizon. The one period it traded on a discount came in 2023 when market conditions hit demand for most trusts in the sector. While brief, it would have led to significant share price losses in the short-term for any who sold, emphasises there are risks to buying on a premium, particularly for those with a shorter time horizon.

That said, we think the premium rating should persist as long as the high yield can be maintained. In the short-term, rate hikes are expected in the UK, US and Europe. This should boost yields available in the market, while higher rates lasting for longer increases disruption at the company level and could lead to more differentiation in yields on offer. In the longer run, we think the managers' track record of maintaining the yield through past down-cycles is sound, and the strategy allows them to invest in the least liquid and under-researched areas of the market in order to maintain the yield. Equally, board and manager are well aware of the importance of their dividend record to the shares' appeal, so are highly incentivised to keep their track record going.

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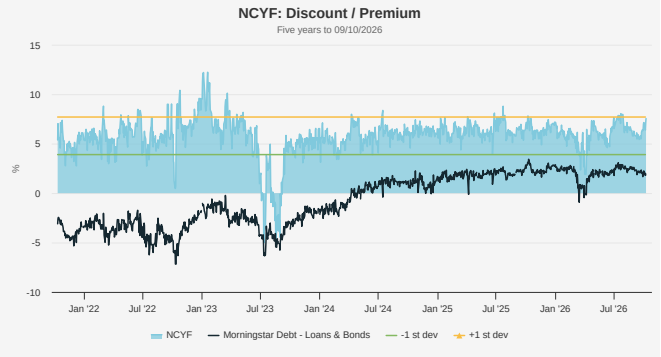
DISCOUNT / PREMIUM

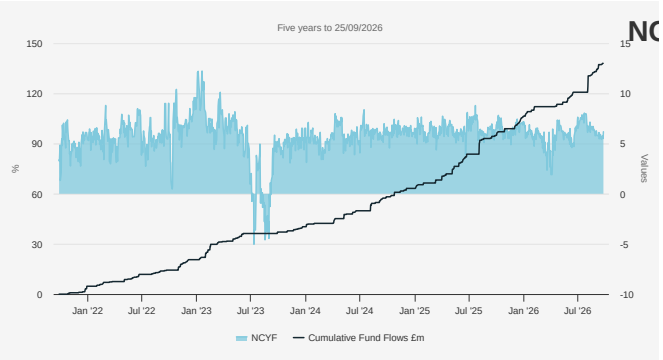


Source: Morningstar, Kepler calculations

Past performance is not a reliable indicator of future results.

The board has issued a substantial amount of shares in recent years, and prefers to do so when the premium is at or above 5%. This is so that the costs don't fall on existing shareholders – the fund has to pay a spread on new investments which tend to be wide on less liquid issues, while there are fees to be paid and revenue reserves per share fall when new shares are issued. The chart below shows the steady growth in the size of the portfolio over the past five years, with c. £138m of capital raised. In the long run, if the fund grew large enough it could threaten the ability to invest in the smaller issues at reasonable size, although the manager tells us they could absorb inflows of at least this size again and as such we don't view it as a concern.

SHARE ISSUANCE



Source: Morningstar

Past performance is not a reliable indicator of future results.

Charges

NCYF's latest ongoing charges ratio (OCF) is 1.11%, calculated as of 30/06/2026. This includes a tiered management fee. On the first £200m of total assets the fee is 0.8%, and falls to 0.7% on the next £100m and 0.6% thereafter. At the time of writing total assets sit at £367m, which implies an ongoing management fee of c. 0.74%. The OCF makes NCYF more expensive than BIPS, which has an OCF of 0.86%, but cheaper than all other members of the AIC Debt – Loans & Bonds sector. We note the impact of OCFs is already included in the NAVs rather than being an additional cost paid by shareholders, and NCYF has outperformed BIPS over three, five and ten year periods.

ESG

The board notes that CQS New City High Yield Fund (NCYF) prioritizes shareholder value by generating strong financial returns within appropriate risk limits. Regarding sustainability, NCYF relies on the framework established by manager Manulife CQS, directing portfolio managers to evaluate environmental, social, and governance factors. This approach acknowledges that companies mismanaging these issues face heightened long-term risks to commercial viability. Given NCYF's focus on smaller debt issuances, roughly 43% of holdings held an official MSCI ESG rating at the last annual reporting date, making NCYF less suited for investors requiring sustainability information.

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