



MAC mechanics

Under the hood of Ninety One's Multi-Asset Credit Strategy

With significant dispersion in valuations across the fixed income universe today, we believe that the case for adopting a dynamic approach to portfolio construction across a broad investment universe has never been clearer.

That's the approach we use when managing our Multi-Asset Credit strategy. Here, we explain what that means in practice and in the context of today's fixed income markets.

Opportunity set: a broad range of global credit markets

Rationale 1: credit markets are highly diverse

When constructing multi-asset credit (MAC) portfolios, we believe that the best results can be achieved by utilising the full breadth of the opportunity set.

In addition to the traditional building blocks such as investment-grade and high-yield credit, investors with the right expertise can find compelling opportunities in other, more specialist credit market segments such as loans, CLOs, corporate hybrids, and bank capital.

Looking across the full spectrum of credit markets in our MAC strategy universe, in any year, there is huge variation in risk and return outcomes driven by the different dynamics underlying each sub-asset class, as shown in Figure 1. This underscores the need to make use of the broad credit opportunity set and pivot towards the more attractive areas of the market as conditions evolve.

Figure 1. A broad universe with diverse returns

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
US HY	58.1%	15.1%	4.4%	15.5%	7.4%	2.5%	-4.6%	17.5%	7.5%	-2.3%	14.4%	6.1%	5.3%	-11.2%	13.5%
European HY	79.8%	15.7%	-2.6%	28.6%	10.3%	5.4%	1.6%	9.3%	6.9%	-3.3%	11.5%	2.9%	3.4%	-11.4%	12.4%
EM Credit	39.1%	12.4%	4.1%	15.7%	-0.9%	3.6%	1.1%	9.6%	6.9%	-1.3%	12.4%	7.1%	-1.4%	-14.4%	7.7%
US IG	19.8%	9.5%	7.5%	10.4%	-1.5%	7.5%	-0.6%	6.0%	6.5%	-2.2%	14.2%	9.8%	-1.0%	-15.4%	8.4%
European IG	14.9%	4.8%	2.0%	13.0%	2.4%	8.3%	-0.4%	4.8%	2.4%	-1.1%	6.3%	2.6%	-1.0%	-13.9%	8.0%
European Loans	43.4%	9.8%	0.7%	9.7%	8.6%	4.5%	5.5%	3.8%	3.6%	1.3%	4.9%	2.4%	5.2%	-3.4%	13.3%
US Loans	51.6%	10.1%	1.5%	9.7%	5.3%	1.6%	-0.7%	10.2%	4.1%	0.4%	8.6%	3.1%	5.2%	-0.6%	13.1%
Corporate Hybrids	31.2%	12.7%	3.8%	15.3%	6.4%	7.8%	-1.7%	8.5%	10.3%	-3.9%	12.7%	2.7%	1.8%	-13.3%	10.2%
Floating Rate Notes	60.0%	12.6%	-9.2%	22.3%	7.7%	3.7%	4.0%	5.0%	1.9%	-1.8%	7.1%	1.8%	6.3%	-2.5%	13.6%
Short Duration HY	44.3%	12.0%	2.7%	13.1%	6.5%	0.9%	1.2%	14.0%	5.3%	0.6%	8.7%	5.0%	5.3%	-8.6%	9.5%
Bank Capital	-	-	-	-	-	5.8%	6.9%	7.3%	14.4%	-3.7%	17.6%	6.8%	4.7%	-11.4%	5.7%
Differential (best/worst)	64.9%	10.9%	16.7%	19.0%	11.7%	7.3%	11.5%	13.7%	12.5%	5.2%	12.7%	8.0%	9.6%	14.8%	7.9%

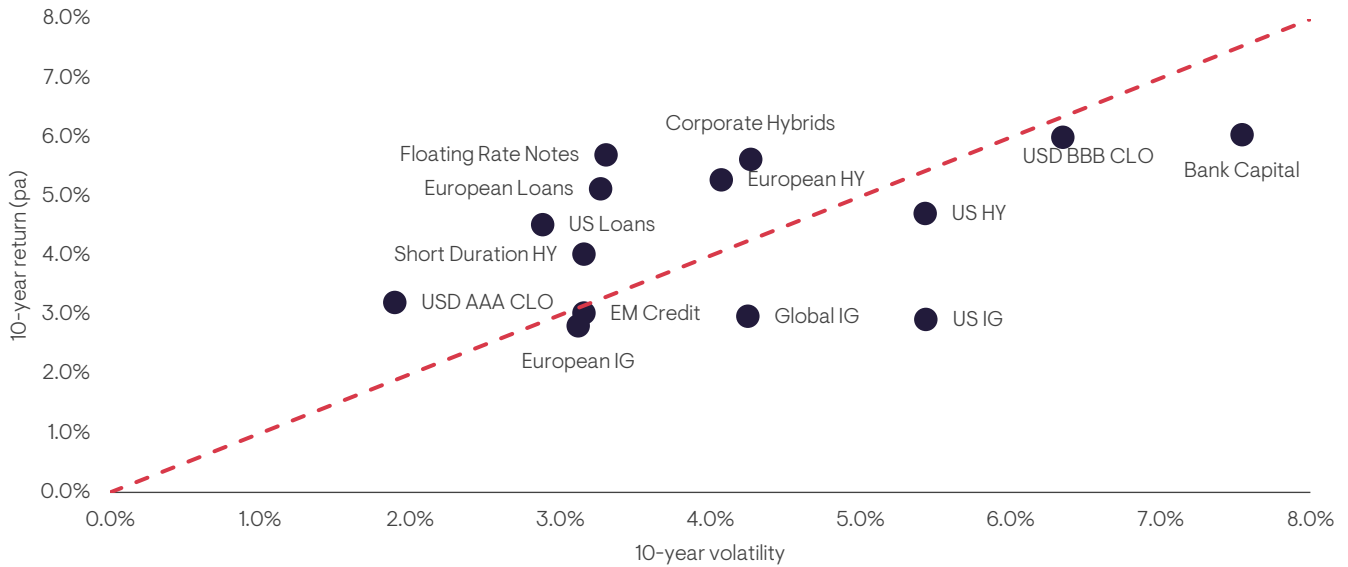
Past performance is not a reliable indicator of future results, losses may be made.

Source: Bloomberg, 31 December 2023. For a full list indices, please see the appendix. For further information on indices, please see the important information section.

Focusing specifically on more specialist credit markets, Figure 2 below highlights the variation in risk and return outcomes across these and the benefits they can provide compared to traditional credit markets.

For example, CLO mezzanine debt has outperformed the global high-yield debt market despite being several notches higher from a credit quality perspective. The table also underscores the wide dispersion in outcomes even within a sub-asset class such as CLOs – where risk/return characteristics can vary significantly across the different rating tranches.

Figure 2. Specialist credit can provide better risk-adjusted returns



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Source: JP Morgan, BofA, Ninety One, As at 12 September 2024. For a full list indices, please see the appendix. For further information on indices, please see the important information section.

Rationale 2: improved portfolio diversification

This variation in outcomes means that there are significant diversification benefits from accessing the broad opportunity set. Figure 3 shows that the more specialist credit segments have low correlations with more traditional assets, and illustrates the value they can add to a MAC portfolio. For example, CLOs, bank capital and leveraged loans have a correlation of less than 10% versus traditional global broad fixed income indices. The diversification of risk provided by allocating to assets that have low correlations with each other can lead to less variation in outcomes at a total portfolio level and ultimately aims to achieve stronger risk-adjusted returns.

Figure 3. Market correlations

	Global Broad Market Index	US IG Corporate Bonds	Euro IG Corporate Bonds	US HY Corporate Bonds	Euro HY Corporate Bonds	US IG Financial Bonds	Euro IG Financial Bonds	Bank Capital	Global IG Corporate Hybrids	Global HY Corporate Hybrids	US Leveraged Loans	European Leveraged Loans	USD CLO AAA	USD CLO BBB	US MBS	US Current Coupon MBS
Global Broad Market Index	100%															
US IG Corporate Bonds	89%	100%														
Euro IG Corporate Bonds	73%	61%	100%													
US HY Corporate Bonds	21%	39%	42%	100%												
Euro HY Corporate Bonds	15%	32%	50%	77%	100%											
US IG Financial Bonds	87%	99%	62%	41%	35%	100%										
Euro IG Financial Bonds	66%	59%	97%	51%	61%	61%	100%									
Bank Capital	7%	24%	32%	67%	81%	28%	46%	100%								
Global IG Corporate Hybrids	14%	27%	46%	66%	88%	29%	55%	74%	100%							
Global HY Corporate Hybrids	12%	26%	43%	65%	88%	28%	52%	72%	94%	100%						
US Leveraged Loans	5%	28%	29%	72%	73%	31%	39%	64%	54%	56%	100%					
European Leveraged Loans	10%	30%	33%	55%	72%	34%	42%	62%	54%	56%	81%	100%				
USD CLO AAA	6%	21%	17%	39%	35%	23%	22%	34%	21%	25%	58%	50%	100%			
USD CLO BBB	0%	9%	14%	31%	28%	9%	18%	20%	15%	20%	38%	37%	59%	100%		
US MBS	85%	78%	52%	23%	9%	79%	47%	5%	9%	7%	1%	2%	0%	-2%	100%	
US Current Coupon MBS	81%	79%	45%	12%	3%	78%	40%	0%	4%	2%	-3%	-1%	0%	-6%	82%	100%

Source: Ninety One, JP Morgan, ICE. As of 30 September 2024. For a full list indices, please see the appendix.

Rationale 3: abundant relative-value opportunities

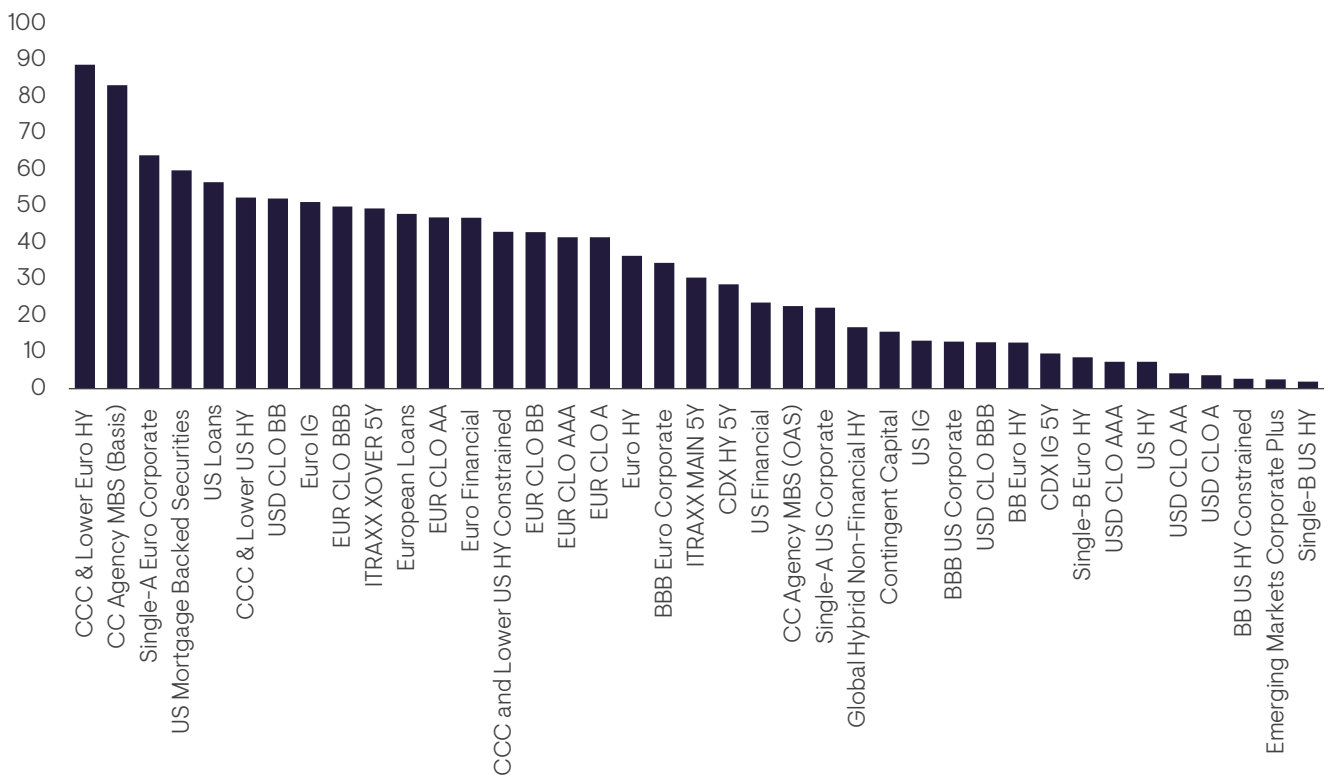
While it is important to consider the diversification benefits that assets can offer, it is equally important to consider the relative value for each of these sub-components.

Today, there is a huge dispersion in valuation across the credit spectrum, illustrating the need to build unbiased portfolios that reflect the most attractive opportunities in the credit market. Figure 4 shows that traditional credit, particularly US investment grade and high yield, looks very expensive, with spreads trading at the lower end of their historical range over the last 10 years, while there is more value in parts of specialist credit such as CLOs and mortgage-backed securities (MBS).

Equally, there is a clear valuation difference between European and US credit, highlighting the benefits of an investment approach that has the flexibility to invest globally.

There are also relatively large divergences between synthetic instruments and cash. For example, while European high-yield corporate bonds are in their 36th percentile, the comparable product in the synthetic market, iTraxx Crossover, is at its 50th percentile, making these products useful for both hedging and efficient portfolio management purposes.

Figure 4. 10-year spread percentiles of different credit sub-asset classes



Source: ICE BofA, Citi, JP Morgan as of 22 August 2024. For a full list indices, please see the appendix. For further information on indices, please see the important information section.

In practice: taking a dynamic approach to asset allocation

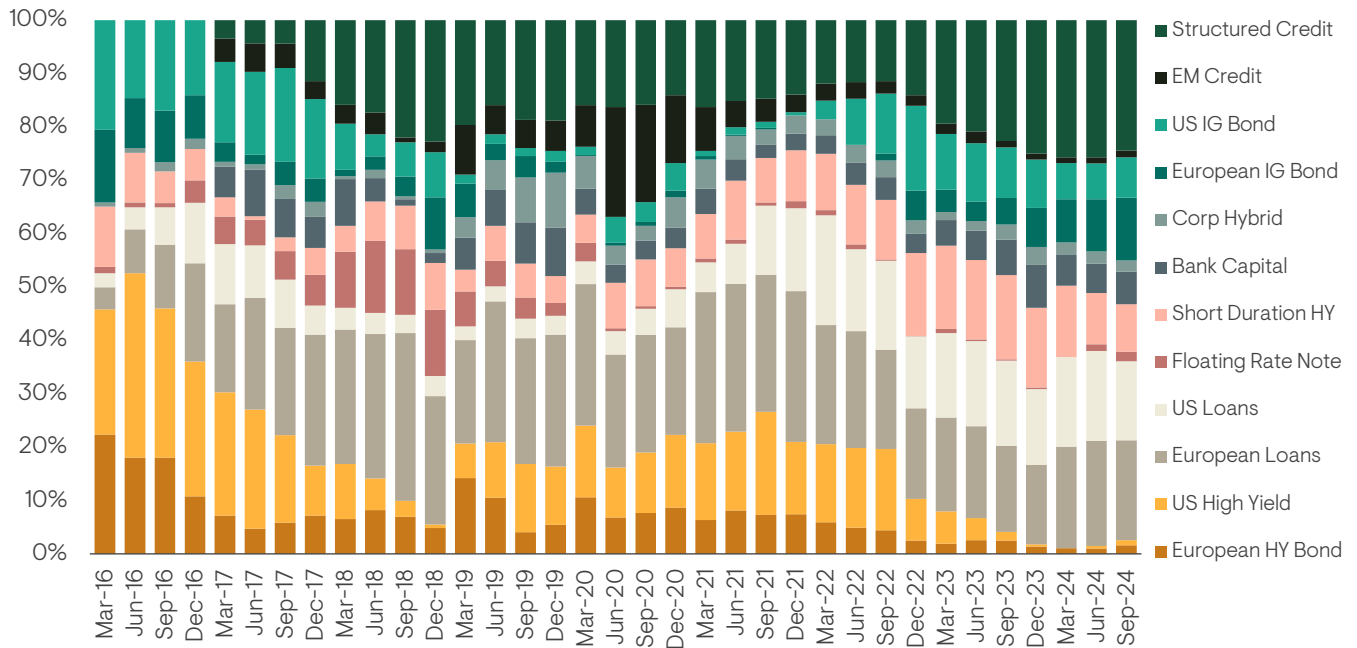
Taking all the above factors into account, when considering the optimal portfolio construction, we believe that rotating the portfolio using a dynamic approach driven by bottom-up investments is the best way to deliver a cash+ return target over the market cycle.

This dynamism allows the strategy to become more defensive when valuations are less attractive and to take on more risk when valuations improve (spreads widen).

To put that into context, today, we see similarities in credit markets between 2018 and current conditions. Despite 2018 being a year when returns for major credit markets such as US investment grade and US high yield were negative, the MAC strategy still generated a positive total return gross and net of fees. Dynamism was key to this outcome, as we actively rotated into more defensive asset classes such as AAA rated CLOs and European loans throughout the year as these offered better risk-adjusted value compared to more volatile segments such as US HY, which started 2018 at cyclical tightness from a spread standpoint. This can be seen in Figure 5.

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Figure 5. Multi-Asset Credit's dynamic positioning through time



Source: Ninety One, 30 September 2024. Since inception date: 01 January 2016.

For the purposes of displaying more coherent portfolio information cash and synthetics have been removed from charts and the residual exposure is grossed up to sum to 100%.

Today's environment of high dispersion and tighter valuations for core fixed income asset classes such as US high yield really highlights the necessity of a dynamic, unconstrained approach to credit investing. We have continued to pivot the portfolio towards higher carry holdings such as structured credit, loans and select parts of the financials market (both senior and subordinated). At the same time, as shown in Figure 5, we have taken exposure to areas of the market where spreads are nearing their tights, to zero (or close to) over the past decade, as these offer limited potential for spread appreciation nor attractive income relative to the risk. This has been most apparent in high-yield markets and select positions in corporate investment-grade, particularly in the US. Additionally, given the tight valuation in core credit markets, we have used synthetics (CDS Options) to add additional protection to the fund should spreads widen from here.

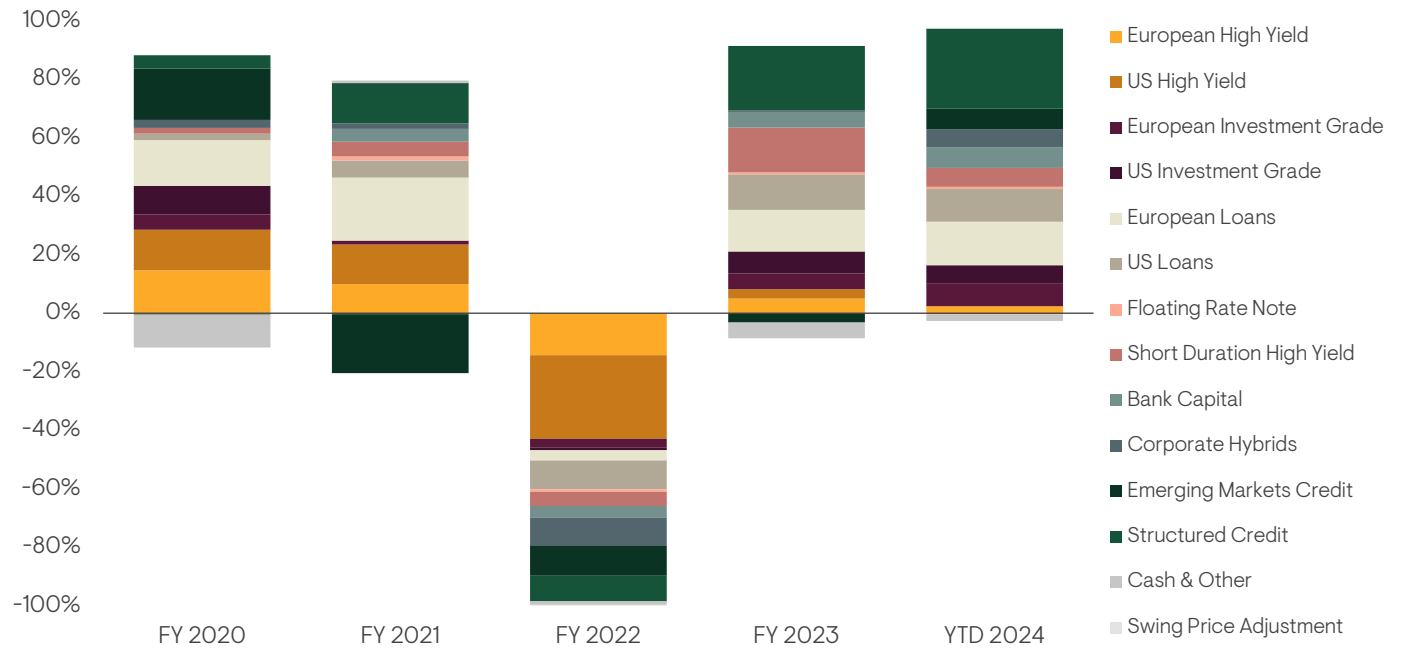
Regionally we have seen more value in European credit, given valuations are still far more attractive than their US counterparts. As Figure 3 shows, European IG is in its 51st percentile while US IG is within its 13th percentile. We are observing this on a bottom-up basis too, where EUR denominated debt continues to trade wide to its USD equivalent - even for the same issuer.

Result: smoother return path

Allocating dynamically to sub-asset classes that have a low correlation with each other, and at a time when relative valuations are attractive has delivered a smoother path of returns for investors. Figure 6 shows the return contribution for our MAC strategy on an asset class basis, which reveals the diverse nature of return drivers across different years. We believe this contributes to a return profile that is diversified and smoother than allocating in a static nature to traditional credit building blocks.

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Figure 6. Multi-Asset Credit's performance contribution by asset class

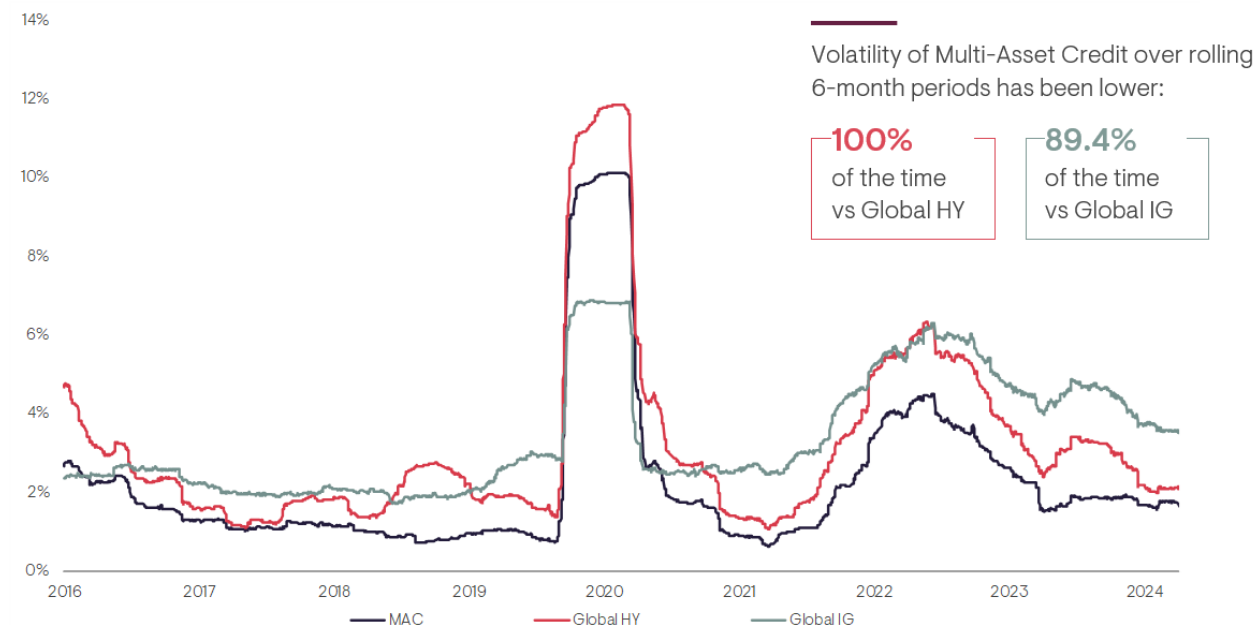


Past performance is not a reliable indicator of future results; losses may be made.

Source: Ninety One, 30 September 2024. YTD performance is calculated using a geometric compounding methodology. Based on a related portfolio with substantially similar objectives as those of the services being offered. For further information on specific portfolio names, please see the Important information section.

Effective dynamism should ultimately lead to a smoother return profile for investors relative to static allocations to core credit markets. We believe that the result of all the above factors is most clearly demonstrated in Figure 7 below. This shows that since inception at the start of 2016, the volatility of our MAC strategy over rolling 6-month periods has been lower than the global high-yield market 100% of the time, and lower than the global investment-grade market 89% of the time. Despite exhibiting lower volatility throughout the life of the strategy, the strategy offers yield commensurate with the global high-yield market with an overall credit quality that is in line with investment-grade markets.

Figure 7. A smoother return profile vs traditional credit



Source: Ninety One, 30 September 2024. Global HY represented by HWO0, Global IG represented by GOBC. Performance shown since inception on 1 January 2016. For further information on indices, please see Important Information section.

Focused on credit spreads rather than duration

A further reason for our MAC strategy displaying lower volatility via a reduced dispersion of outcomes relative to traditional fixed income assets is its focus on credit spreads rather than duration. This has been particularly apparent during periods of elevated US Treasury volatility, as we have seen over the last few years.

Launched in 2017, the MAC strategy's return profile is less beholden to the global interest-rate environment than many traditional bond funds, thanks to its flexibility to select less rate-sensitive instruments, such as floating-rate notes and structured credit. For these subsets of the market, changes in credit spreads are significantly more important than interest rate movements. The strategy's flexibility means it can seek out the best opportunities while avoiding parts of the market that are least attractive from a risk-adjusted return perspective – this is particularly relevant in the context of the high-dispersion, high-differentiation conditions we see in credit markets today.

In summary

As we highlight above, investing across a broad opportunity set including more specialist segments of the credit market that exhibit low correlations with traditional credit is key to diversifying risk at a total portfolio level. This has resulted in returns commensurate with high-yield yet with lower volatility than that of investment-grade credit, a combination that represents a significantly superior risk-adjusted solution.

General risks: The value of investments, and any income generated from them, can fall as well as rise. Costs and charges will reduce the current and future value of investments. Past performance does not predict future returns. Investment objectives may not necessarily be achieved; losses may be made. Target returns are hypothetical returns and do not represent actual performance. Actual returns may differ significantly. Environmental, social or governance related risk events or factors, if they occur, could cause a negative impact on the value of investments.

Specific risks: **Default:** There is a risk that the issuers of fixed income investments (e.g. bonds) may not be able to meet interest payments nor repay the money they have borrowed. The worse the credit quality of the issuer, the greater the risk of default and therefore investment loss. **Derivatives:** The use of derivatives may increase overall risk by magnifying the effect of both gains and losses leading to large changes in value and potentially large financial loss. A counterparty to a derivative transaction may fail to meet its obligations which may also lead to a financial loss. **Interest rate:** The value of fixed income investments (e.g. bonds) tends to decrease when interest rates rise. **Liquidity:** There may be insufficient buyers or sellers of particular investments giving rise to delays in trading and being able to make settlements, and/or large fluctuations in value. This may lead to larger financial losses than might be anticipated. **Loans:** The specific collateral used to secure a loan may decline in value or become illiquid, which would adversely affect the loan's value. Many loans are not actively traded, which may impair the ability of the Portfolio to realise full value in the event of the need to liquidate such assets.

Appendix – list of indices used

US HY = ICE BofA US High Yield Index

European HY = ICE BofA Euro High Yield Index

EM Credit = ICE BofA Emerging Markets Corporate Plus Index

US IG = ICE BofA US Corporate Index

European IG = ICE BofA Euro Corporate Index

European Loans = JP Morgan European Leveraged Loan Index

US Loans = JP Morgan US Leveraged Loan Index

Corporate Hybrids = ICE BofA Global Hybrid Non-Financial High Yield Index

Floating Rate Notes = ICE BofA Euro Floating Rate High Yield Index

Short Duration HY = ICE BofA 1-3 Year Global High Yield Non-Financial 2% Constrained Index

Bank Capital = ICE BofA Contingent Capital Index

Global IG = ICE BofA Global Corporate Index

USD BBB CLO = JP Morgan USD BBB CLO index

USD AAA CLO = JP Morgan USD AAA CLO index.

MBS indices are from JP Morgan

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