Credit Chronicle

Market review from Ninety One's Developed Market Credit team

Market review

After a challenging Q1, credit markets staged a broad-based recovery in Q2, resulting in positive returns for the first half of 2026. All parts of the asset class posted positive returns over Q2, as a stronger appetite for risk drove a tightening of credit spreads. Dispersion remained a defining theme across credit markets, in part explained by divergent sovereign bond market moves. US Treasury yields rose on inflation concerns and a hawkish Federal Reserve, while European yields fell as oil prices eased on optimism around a resolution to the US-Iran conflict, easing the pressure on inflation. European assets outperformed their US counterparts in most credit asset classes.

Within the specialist credit markets, lower-rated CLOs performed well in both the US and Europe as spreads tightened materially. Having offered protection during the Q1 sell-off, higher-rated CLO tranches lagged in Q2, although returns were still positive. Bank capital (AT1s) recovered strongly following the March sell-off, with spreads tightening significantly. Loans also performed well, with European loans outperforming the US reflecting greater spread compression in the former. The US agency mortgage-backed securities (MBS) market delivered small positive returns as spreads were broadly unchanged – as a long-duration, high-quality market, it could not keep pace with the spread-driven rally. Among the more mainstream markets, high-yield (HY) debt outperformed investment grade (IG), reflecting the risk-on tone. European HY led the segment, with spreads tightening substantially given the sharp fall in oil prices. The same regional pattern held in the IG market, with Europe outperforming the US, driven by the contrasting moves in underlying sovereign yields.

Current snapshot

We believe that credit markets are driven by three Compelling Forces and that a careful assessment of each of these is essential for exploiting evolving market inefficiencies and building a robust credit portfolio. Here's our current view:

Compelling force	**Fundamentals** Fundamental strength	**Valuations** Attractiveness of valuations	**Technicals** Supply/demand dynamics
US high yield	Grey	Red	Grey
European high yield	Orange	Red	Grey
US investment grade	Grey	Orange	Orange
European investment grade	Orange	Red	Light teal
US loans	Orange	Grey	Grey
European loans	Orange	Grey	Light teal
Bank capital	Grey	Red	Light teal
Corporate hybrids	Grey	Red	Grey
EM corporate credit	Grey	Red	Grey
Short-duration high yield	Grey	Red	Grey

Key: Worst ← Red, Orange, Grey, Light teal, Dark teal → Best

For illustrative purposes only. For further information on the investment process, please see the important information section.

Where to focus and what to avoid

- We are defensively positioned and continue to rotate away from European markets that are more heavily exposed to energy prices.
- We have limited exposure to segments most at risk of AI disruption, favouring higher quality opportunities such as insurance sector issuers and select bonds issued by BDCs, which still look appealing on a longer-term relative value basis.
- We are cautiously positioned in US investment-grade debt as issuance from hyperscalers (AI data centre providers) is tipping the supply/demand balance, although relative value in this segment is improving.
- In the high-yield market – where there is wide dispersion – we prefer specialist segments such as structured credit and bank capital over the most compressed parts of high yield (notably BB rated credit), where comparable yields are available at meaningfully better credit quality. In addition, loans continue to offer significant pick-up relative to high yield, even for the same issuers.

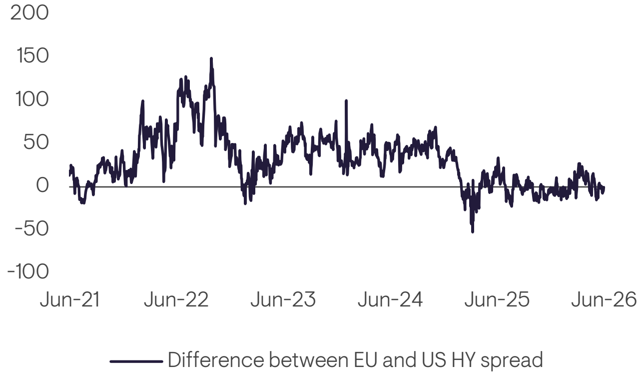
Sector by sector

High yield

US	- -	-	0	+	+ +
Fundamentals			●		
Valuations	●				
Technicals			●		
EUR	**- -**	**-**	**0**	**+**	**+ +**
Fundamentals		●			
Valuations	●	○			
Technicals			●		

An empty circle denotes our view in the previous quarter, if it differs.

Spreads between Europe and the US have converged



Source: Bloomberg, June 2026. Indices used are Bloomberg Pan-European HY (Euro) OAS and Bloomberg US HY OAS.

The quarter started just after the peak in high-yield spreads – 374bps in the US and 320bps in Europe. The expectation of conflict easing in the Middle East – driven by signs the US administration was keen for a resolution – combined with a strong earnings season in the US led to a rapid recovery and compression in spreads. By the end of June, spreads in both the US and European high-yield indices had compressed, but absolute returns were impacted by shifting dynamics in rates markets. In addition, after three years of Europe offering a significant spread pick-up over the US, the two markets have recently traded very similarly on a relative-value basis (as seen in the chart). This reinforces our view that value in high-yield investing is not a regional call right now, but more about monetising the dispersion within the market.

While the easing of the conflict-related inflationary shock was enough to see European rates stabilise and end the quarter c.10bps lower, US rates remained under pressure from strong economic data and the arrival of Warsh as Chair at the US Fed. This resulted in European high-yield outperforming meaningfully, with total returns of 4.1% compared with 2.5% in the US. It was a classic risk-on environment with the CCC rated segment outperforming, particularly in Europe. The US market continues to be shaped by AI-related new issue supply, with a pick-up in growth financing: data centres and AI infrastructure have been largely financed in USD. Fundamentals remain good overall, and defaults continue to track at low levels. While stress in the tech sector has been well flagged, it only underperformed very marginally during the high-yield market recovery in Q2.

Global loans

US	- -	-	0	+	+ +
Fundamentals		●			
Valuations			●		
Technicals			●		
EUR	**- -**	**-**	**0**	**+**	**+ +**
Fundamentals		●			
Valuations			●		
Technicals				●	

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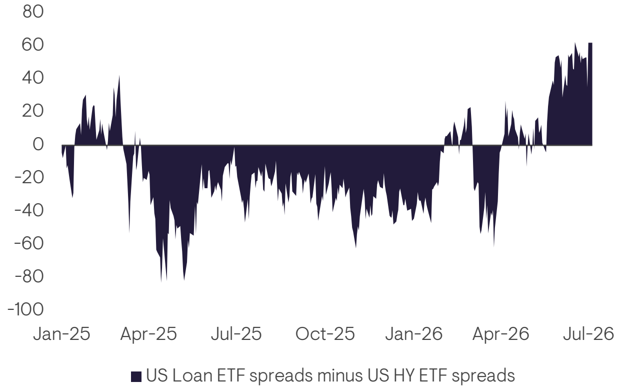
US loan spreads are now wider than US high yield



Source: BofA, June 2026.

A strong quarter for loans saw US and EUR loans return 1.9% and 2.9% respectively – more than offsetting the AI-induced software sell-off seen in Q1 and bringing year-to-date returns to 1.5% and 1.9% respectively. Returns were positive in each month of the quarter, with April particularly strong (US loans +1.3%; EUR loans +1.9%) as tensions around the Iranian conflict eased. In June, renewed weakness in software loans was a headwind to returns (US loans +0.1%); US software loan spreads widened 74bps in June to a new high of 825bps, bringing loan index spreads to 499bps. Prices were also negatively impacted, with US single-B loan prices down to US$96.3, although the market is increasingly discerning between the strong and the weak in the software sector. This software-driven weakness was also a key driver of the notable divergence between the primary US loan ETF (BKLN) and US HY ETF (HYG), as seen in the chart above, reflecting dynamics we outlined here.

While pressure is rising in software sector loans, the loan market overall remains reasonably healthy. The loan new issue market remained active, with US loan issuance of US$79bn (US$24bn net) in June, bringing the year-to-date total to US$438bn – on par with gross volumes in 2025 but with net issuance 14% higher year on year. This steady backdrop was also reflected in fund flow data, with US loan funds reporting US$1.2bn of inflows in June, US$2.4bn in May, and US$915mn in April, suggesting that the challenges being priced in the software space have yet to weigh materially on investor demand for the asset class.

Developed market credit indicator: Credit Chronicle

Investment grade

US	- -	-	0	+	+ +
Fundamentals			●		
Valuations	○	●			
Technicals		●	○		
EUR	**- -**	**-**	**0**	**+**	**+ +**
Fundamentals		●			
Valuations	●				
Technicals				●	

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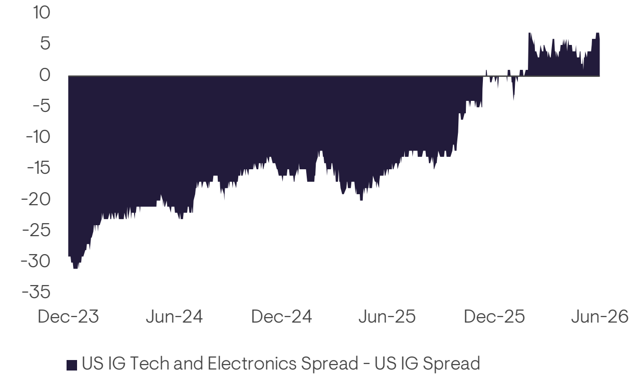
The tech sector has underperformed the broader IG market



Source: ICE BofA, June 2026. Spread is OAS to government.

US and European investment grade spreads tightened by 14bps and 17bps respectively over Q2, offsetting some of the widening seen into end-March. European investment-grade (IG) returned 2.8% over the quarter, ahead of 1.4% for US IG, with the gap driven by the Euro rates market outperforming US rates rather than any difference in spread performance. Some of the weakness in areas linked to AI and software disruption that had weighed on the market in Q1 unwound during the quarter: Business Development Companies (BDCs) notably drove outperformance in financials as investors priced out much of the systemic tail risk they had previously feared.

The prevailing theme of 2026 – AI-driven disruption and the associated capex boom – continued in Q2, with a shifting supply dynamic driven by ongoing hyperscaler new issuance. On average, hyperscalers have already accessed the market to raise around US$25bn annually from 2020-2024. However, as capex needs have ramped up, Meta raised US$25bn of issuance in the last quarter alone, matched by similarly sized US$25bn deals from SpaceX (post-IPO) and Nvidia. While Google's equity raise offset some of its funding requirements, other issuers turned to non-USD debt markets to absorb the additional volume, with jumbo deals issued in JPY, EUR and CAD, and Amazon separately accessing CHF and CAD markets. This trend looks set to continue, with data centre growth increasingly funded through separate financing vehicles issuing investment-grade and asset-backed security (ABS) debt, sometimes backed by implicit or explicit hyperscaler guarantees – keeping this exposure off the hyperscalers' own balance sheets.

Structured credit

Senior CLOs (AAA/AA)	- -	-	0	+	+ +
Fundamentals			●		
Valuations		●			
Technicals				●	
Mezzanine CLOs (A-BB)	**- -**	**-**	**0**	**+**	**+ +**
Fundamentals		●			
Valuations		●			
Technicals			●		

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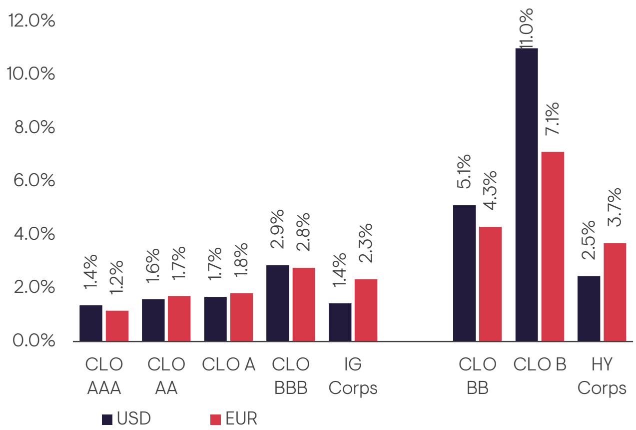
Lower-rated CLOs recovered in Q2



Source: ICE, JP Morgan. 30 June 2026. Chart shows Q2 total returns in local currency. JP Morgan for CLOs and ICE BofA Indices for corporate bonds.

The general theme of Q2 for CLOs was one of recovery from the wide spreads prompted primarily by conflict in the Middle East. Non-investment grade tranches performed particularly well, with JP Morgan data showing 7.1% and 11.0% returns for EUR and USD single-B rated tranches for example.

Investors also remained focused on risks from AI disruption to software related loans. After an initial broad-based sell-off across loans in that sector in Q1, the market appeared to differentiate more clearly between perceived winners and losers in Q2, and that fed into dispersion in CLO tranche pricing dynamics as well. A rare impairment of a rated CLO tranche captured market attention in Q2. A tranche of a 2018 vintage European deal that had been rated single B was downgraded to D by Fitch in June after noteholders agreed to reduce their outstanding principal amount; the tranche was redeemed below original par following poor performance of the underlying portfolio. This was the first loss for CLO debt investors in any European deal issued since the GFC. More losses are likely in the European market, and several have already been recorded in the US market. However, historical loss rates for CLOs remain low, and comparable to those of similarly rated corporate bonds. CLOs continue to offer very attractive spreads relative to their credit risk, though selectivity remains key.

Developed market credit indicator: Credit Chronicle

Specialist credit

Bank capital	- -	-	0	+	+ +
Fundamentals			●		
Valuations	●				
Technicals				●	

EM corporate debt	- -	-	0	+	+ +
Fundamentals			●		
Valuations	●				
Technicals			●		

Corporate hybrids	- -	-	0	+	+ +
Fundamentals			●		
Valuations	●				
Technicals			●		

Short-duration high yield	- -	-	0	+	+ +
Fundamentals			●		
Valuations	●				
Technicals			●		

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Corporate hybrids (perps) extended their strong run through H1 2026, again outperforming their historical beta to senior credit even through the energy shock. Around €39bn has been issued so far this year – almost double the same period last year – taking net supply to €25bn (vs just €8bn for all of 2025) and pushing outstanding hybrid capital to €211bn, extending the recovery from three years of consolidation. Utilities still led gross issuance, but the more important shift is breadth, with consumer goods, telecoms, oil & gas and real estate all in positive net-supply territory. Real estate is on track for its first year of net growth since 2021. Debut issuers now account for roughly a third of H1 supply, spanning autos, food & beverage, forestry and utilities infrastructure, while reverse-Yankee issuance from US names is running at a record pace (US companies issuing in an overseas market in a foreign currency). Sub-senior spreads sit near record tight levels (expensive) – the IG hybrid-senior differential is around 80bps at the index level. While index-level valuations look unappealing, bottom-up opportunities still exist, with hybrids offering better carry than a large proportion of the high-yield market in particular.

The **bank capital** sector, or AT1s, posted a strong second quarter with a USD-hedged return of +4.3% (Q1: -1.0%) – the strongest quarterly return for the asset class since Q3 2024 – bringing year-to-date total returns to +3.3%. The rebound was driven by a strong monthly return in April (+2.6%), when the asset class recovered swiftly from the March risk-off move amid the US-Iran conflict, with May and June returns adding further gains. Returns over the quarter were driven by both price appreciation and carry/income, with spreads tightening by approximately 66bps and fully retracing the Q1 widening. Market conditions remained supportive: Q2 saw 15 new AT1s issued by European banks across USD, EUR and GBP totalling approximately €12.4bn equivalent. Demand for new issues remained robust across issuers. Furthermore, all 14 AT1s coming up for call in Q2 were called, with two issuers tendering ahead of the call date, a trend we expect to continue. Given the strong rebound and with spreads now back at tight levels, we expect returns over the second half of the year to be driven primarily by carry/income rather than further spread tightening. Selectivity remains key given current valuations.

The **EM corporate debt** asset class (JPMorgan CEMBI BD) returned 2.4%, led by high-yield issuers which returned 3.5%, with investment-grade companies posting a 1.7% gain. Spread tightening was the primary driver of returns, with all sectors and regions delivering positive returns.

Credit market performance, Q2	Return (US$ hedged) %	Yield-to-worst %	Spread	Duration
US high yield	2.5	7.2	275	3.1
European high yield	4.1	5.4	270	3.0
US investment grade	1.4	5.2	76	6.5
European investment grade	2.8	3.5	78	4.5
US loans	1.9	8.9	499	0.1
European loans	2.9	8.3	529	0.2
Short duration high yield	2.4	7.0	309	1.7
CoCos	4.3	5.8	214	3.7
Emerging market corporate debt	2.4	6.0	162	4.1

Past performance is not a reliable indicator of future results, losses may be made. Please see important information section for information on indices.

Sources: US high yield = BofA US High Yield (HUC0); European high yield = BofA EUR High Yield (HE00); US investment grade = BofA US Investment Grade (C0A0); European investment grade = BofA EUR Investment Grade (ER00); US Loans = JP Morgan US Loans Index; European Loans = JP Morgan European Loans Index; Short Duration High Yield = BofA 1-3yr Global High Yield (H1WN); CoCos = BofA Contingent Capital Index (COCO); EMCD = JPM CEMBI BD. Spread is OAS over government. All as of 30 June 2026.

General risks

The value of investments, and any income generated from them, can fall as well as rise. Where charges are taken from capital, this may constrain future growth.

Past performance is not a reliable indicator of future results. If any currency differs from the investor's home currency, returns may increase or decrease as a result of currency fluctuations.

Specific Risk(s)

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.

Glossary

Alpha: outperformance of a reference index or market through an investment manager's active investment decisions.

Bank capital: additional capital held by banks to absorb losses under duress. Cheaper and quicker for banks to issue than equity. Helps banks to improve their capital ratios.

Bank preference securities: issued by banks to meet their required capital ratios. These have characteristics of both equities and bonds. The securities are perpetual (with call features), pay dividends, and are subordinated relative to other forms of debt.

Callable bonds: bonds that can be redeemed by the issuer prior to the maturity date of the bonds. The issuer may look to issue new bonds at a lower coupon.

Carry: the net-of-cost return earned by owning a security – a 'carry trade' might involve borrowing at a low interest rate to invest in a security offering a higher interest rate to earn the additional 'carry'.

CLO: collateralised loan obligations are bonds that are backed by pools of (typically sub-investment grade) corporate loans. Several bonds of varying risk and return characteristics are usually issued against each pool of loans. Lower-risk, 'senior' tranches have higher priority claims on the cash flows from the loans but offer a lower yield than the lower-rated 'junior' tranches, which are the first to suffer losses if the underlying loans underperform.

Corporate hybrids: subordinated debt of investment-grade issuers. They combine characteristics of bonds (payment of coupon) and of equities (no maturity date or very long maturities) and are typically rated a few notches lower than the same issuers' senior debt. Usually callable by the issuer five or 10 years after issue.

Coupon: the regular interest payments a bondholder receives from the issuer of the bond.

Credit rating: a score awarded by an independent rating agency to indicate the financial strength of the issuer of a bond, and the potential for it to default on interest and principal payments. The top credit rating is 'AAA'. The lowest rating to be considered 'investment grade' is 'BBB'. Below 'BBB', bonds are termed 'sub-investment grade' or 'high yield'. The higher the credit rating of the issuer of the bond, the higher the 'quality' of the bond.

Credit spread: the difference between the yield offered by a corporate bond and the yield offered by a sovereign (government) bond of an equivalent maturity. This is the reward the investor gets in return for taking on a greater level of risk than they would if they just invested in the sovereign bond.

Credit risk: see *Default risk*.

Currency swap: a swap is an agreement between investors to exchange future cashflows, such as interest payments. In a currency swap, the parties to the agreement exchange future cash flows of different currencies.

Default risk: the risk that the issuer of a bond may not be able to meet interest payments or repay the money it has borrowed. The lower the credit rating of the issuer, the greater the risk of it defaulting on its debt and the greater the risk of the investor suffering an investment loss.

Duration: a measure of how much a change in interest rate will impact a security's market value. There is an inverse relationship between interest rates and bond prices.

Emerging market credit: bonds issued by companies from emerging markets (e.g. China, Brazil). Can be rated high yield or investment grade. Largely US dollar-denominated, although a small local currency corporate bond market exists.

Excess return: the total return of the bond minus the return attributable to changes in underlying treasury yields of an equivalent maturity.

Extension risk: the risk that the bond issuer will seek to delay when it pays back the amount it has borrowed from bondholders.

Fallen angel: an investment-grade bond issuer that has subsequently had its debt downgraded to a high-yield credit rating.

Floating-rate notes: the floating nature of coupon provides protection in a rising interest rate environment. Issued by both investment-grade and high-yield borrowers. These are typically shorter duration (up to five years).

Interest rate risk: see *Duration* above.

Leveraged loans: loans that are structured, arranged and administered by at least one commercial or investment bank. Typically issued to support a merger or acquisition or to finance company growth. Sub-investment-grade rated. Typically, the coupon is a floating rate rather than fixed.

Maturity: The date the issuer will repay the bondholder.

Subordinated debt: debt that is repaid only after other debt has been repaid (i.e. comes further down in the order of priority for repayments) in the event of the issuer of the debt falling into financial difficulties.

Synthetics: highly liquid financial instruments that artificially simulate other credit market investments. Instruments can be related to a single corporate, or to a whole credit index. Allows for efficient implementation and hedging.

Total return: the investment return on a bond which takes into account a change in credit spread and a change in the yield of the underlying treasury of an equivalent maturity.

Yield: the return investors earn for owning a bond to maturity. This is a function of the price paid for the bond, the coupon, and the time to maturity.

Important information

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