# Multi-Asset Credit

## Market background

Against the backdrop of rising sovereign bond yields, the fourth quarter was a mixed period for global credit markets. Assets with floating-rate coupons delivered the best total returns, as these offered protection from the rise in yields. Assets such as collateralised loan obligations (CLOs) and leveraged loans, both in the Europe and the US, benefited. In addition, credit spreads in these markets continued to tighten over the period, particularly in the US given the positive economic growth outlook.

In other areas of the credit market, high-yield bonds in Europe meaningfully outperformed those in the US, with spreads tightening more in the former as US high-yield spreads were already close to the tightest levels seen in the past decade. Corporate bonds in the US also faced a more significant headwind from a larger rise in government bond yields than that seen in Europe. In the investment-grade space, European assets again outperformed the US, with the latter posting a negative total return over the quarter given the sharp rise in Treasury yields. Credit spreads ended the period tighter in both markets.

Despite the mixed performance seen in the fourth quarter, all credit markets posted positive returns in 2024. CLOs and loans were the top performers, followed by high-yield and investment-grade bonds.

## Performance

The Strategy produced a positive absolute return over the quarter, underperforming its cash-plus benchmark* but performing in line with the broader credit market.

The main driver of the portfolio's absolute performance was exposure to assets with floating-rate coupons, as these helped to shield investors from the rise in sovereign bond yields. Within floating rate asset classes, performance was led by US and European loans. This reflects the portfolio's significant exposure to these assets, with carry and a tightening of credit spreads in the loan market also boosting returns. Similarly, structured credit (CLOs) added to performance thanks to a combination of carry and spread tightening.

Other contributors to performance included bank capital exposure, where spreads tightened over the quarter, as well as both the European investment-grade and emerging market high-yield bond market, led by real estate issuers in the latter.

The main detractor from performance was exposure to investment-grade issuers in the US. Despite the portfolio's low allocation to this area of the credit market, the sharp rise in US Treasury yields offset a slight tightening of spreads. For similar reasons, exposure to US high-yield bonds detracted slightly from performance.

## Portfolio activity

We increased the portfolio's allocation to leveraged loans in both the US and Europe, driven by their attractive carry and better downside characteristics compared to high-yield corporate bonds. We also continued to increase exposure to structured credit (collateralised loan obligations, CLOs), capitalising on compelling valuations relative to traditional corporate debt.

As spreads in the US investment-grade market are near the multi-decade lows, we reduced exposure reflecting the limited upside potential. We maintained our preference for short-duration high-yield bonds, leveraged loans, and select areas of specialist credit that provide a favourable mix of carry and downside protection.

We continue to selectively use credit derivatives to add incremental downside protection to the portfolio.

*Where performance is gross of fees, returns will be reduced by management fees and other expenses incurred. Net performance is net of highest institutional segregated portfolio management fee.
Not all securities held have been discussed. For further information on how the overall strategy performed during the period covered, please reference the relative performance noted in the Performance review section.

Past performance does not predict future returns; losses may be made.

## Outlook and strategy

Credit markets are navigating a tug-of-war between attractive all-in yields and unquestionably tight spreads (expensive valuations). So far, the yield component has been the clear winner – as evidenced by sustained inflows into the asset class – despite investment-grade (IG) and high-yield spreads sitting at multi-decade lows. Strong credit fundamentals have supported these markets, but unprecedented demand was the primary driver of spread compression in 2024.

Given the tight (expensive) valuations in traditional US investment-grade and high yield debt, we see greater opportunities in specialised segments of the credit market. Structured credit remains attractively priced relative to corporate credit, particularly CLO mezzanine tranches. Similarly, agency mortgage-backed securities (MBS – securities issued by US government-sponsored organisations such as Freddie Mac or Fannie Mae) offer compelling relative value compared to both investment-grade corporates and segments of the high-yield debt market. Agency MBS spreads are among the few credit asset classes where credit spreads are wide relative to history (i.e., valuations are historically attractive), driven by weak supply/demand dynamics and elevated rate uncertainty — factors we expect to normalise in the coming year. Additionally, we favour leveraged loans over high-yield debt given their higher carry, even accounting for potential further rate cuts.

Regionally, we see more compelling bottom-up opportunities in Europe, where spreads across various asset classes remain significantly wider than their US counterparts. However, our focus is on defensive sectors, given the region's weaker growth outlook and limited upside potential in cyclical sectors. The banking sector has been a standout performer, and we expect this outperformance to continue in 2025, albeit at a more measured pace.

As we begin 2025 with historically tight credit spreads, a disciplined focus on bottom-up selection and a dynamic approach to positioning will be critical to navigating the challenges and opportunities ahead.

## Specific risks.

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