In Credit

12 May 2025

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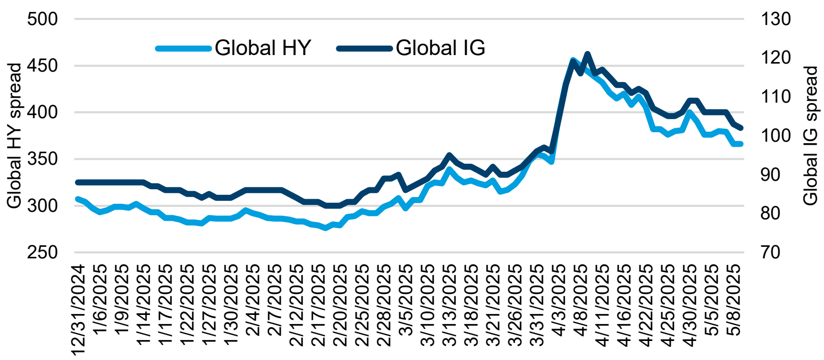
Easing trade tensions, rising risk markets

Markets at a glance

	Price / Yield / Spread	Change 1 week	Index QTD return*	Index YTD return
US Treasury 10 year	4.44%	13 bps	-0.6%	2.4%
German Bund 10 year	2.62%	9 bps	1.3%	-0.5%
UK Gilt 10 year	4.62%	11 bps	1.0%	1.5%
Japan 10 year	1.46%	19 bps	-0.1%	-2.5%
Global Investment Grade	102 bps	-4 bps	-0.2%	1.4%
Euro Investment Grade	104 bps	-4 bps	0.8%	1.0%
US Investment Grade	102 bps	-4 bps	-0.8%	1.6%
UK Investment Grade	95 bps	0 bps	1.0%	1.8%
Asia Investment Grade	145 bps	-1 bps	-0.3%	2.0%
Euro High Yield	367 bps	-16 bps	0.7%	1.5%
US High Yield	353 bps	-7 bps	0.6%	1.5%
Asia High Yield	494 bps	-9 bps	-0.7%	2.2%
EM Sovereign	314 bps	-10 bps	0.0%	2.3%
EM Local	6.1%	1 bps	3.5%	7.9%
EM Corporate	279 bps	-6 bps	-0.5%	1.9%
Bloomberg Barclays US Munis	4.0%	-2 bps	-0.5%	-0.8%
Taxable Munis	5.2%	3 bps	-1.6%	1.2%
Bloomberg Barclays US MBS	38 bps	-4 bps	-0.6%	2.5%
Bloomberg Commodity Index	252.20	1.4%	-3.0%	5.6%
EUR	1.1127	-0.4%	4.0%	8.7%
JPY	147.73	-0.3%	3.2%	8.1%
GBP	1.3182	0.3%	3.0%	6.3%

Source: Bloomberg, ICE Indices, as of 9 May 2025. *QTD denotes returns from 31 March 2025

Chart of the week: Risk market rally – credit spreads year-to-date



Source: ICE BofAML and Bloomberg, as of 12 May 2025

Macro/government bonds

Tariff policy was the major theme last week. US Federal Reserve chair, Jay Powell, stated that the Fed would like to see greater clarity on trade policy as it held rates steady. Powell noted that US economic resilience was allowing the Fed to be patient on rates. Markets reacted to his cautious messaging by scaling back their expectations of future cuts this year from three to two 25bps moves.

Meanwhile, the Bank of England cut interest rates by 0.25% to 4.25%. It noted that inflation had declined but was still above target. The vote to cut was split 5-4: two policymakers voted for a 0.5% cut in rates, while two voted to maintain rates at 4.5%. The range of views reflects the current lack of clarity around both global and domestic developments. The market scaled back its expectations of monetary easing from three to two 25bps rate cuts by the end of December.

In tariff news, on Thursday the Trump administration announced a trade deal with the UK. The latter secured a reduction in car tariffs from 25% to 10%, while tariffs were also reduced on UK steel and aluminium exports. Then, over the weekend, US Treasury Secretary, Scott Bessent, and Chinese Vice Premier, He Lifeng, announced a significant reduction in bilateral tariffs. The US will reduce tariffs from 145% to 30%, while China will reduce its levies from 125% to 10%. The news delivered a further boost to risk-on sentiment at the market open on Monday morning.

Investment grade credit

Investment grade spreads continued to tighten at a modest pace. The global index has seen spreads tighten from a year-to-date wide of 121bps on 8 April to end last week at 102bps, according to data from ICE indices. As with other ‘risk’ markets, IG has been supported by signs of a descalation of trade friction, including the aforementioned positive comments around the US and Chinese relationship and a trade deal between the UK and the US. The market was also aided by a widely expected reduction in interest rates in the UK last week.

Year-to-date, spreads are wider with a significant dispersion between the weaker performance of the US dollar market versus its euro-denominated cousin. The US has seen spreads widen by 24% year-to-date, while the euro is barely changed with a 3% widening in spreads in the same period. More defensive sectors including utilities, telecoms and healthcare have held up the best.

High yield credit & leveraged loans

US high yield bond valuations were again stable over the week, as markets absorbed positive trade headlines, resilient economic data and solid earnings. Notably, spreads have fully reversed the widening seen since ‘liberation day’. The ICE BofA US HY CP Constrained Index returned 0.19% and spreads tightened 7bps to +371bps. The index yield-to-worst was unchanged at 7.73%. According to Lipper, US high yield bond retail funds saw a $1.6 billion contribution, meaning the asset class has recouped 33% of the withdrawals seen in early April.

US leveraged loan prices rose $0.2 over the week and have retraced around 66% of the decline from 2025’s peak. This came as the market benefited from the ongoing Fed pause and mild inflows. The average price of the S&P UBS Leveraged Loan index increased to $95.8. Retail floating rate funds saw a second consecutive – albeit modest – contribution with a $59 million inflow.

It was another strong week for European HY as tariff news showed a positive change in direction. With the improved atmosphere, EHY returned 0.45% as spreads tightened 16bps to 367bps, and yields fell 15bps back to 6.3%. Inflows improved (+€142 million), but this was solely due to managed accounts as ETF net flows were flat. The primary market was robust with €4.4 billion in new corporate issuance, which was largely refinancings as well as some new money. Global payments firm Shift4 came with a €680 million offering as part of its funding for the acquisition of Global Blue. This was seven times oversubscribed with pricing coming in at 5.5% from an IPT of 6%.

The US-UK agreement for a flat 10% tariff on auto was a boost for Jaguar Land Rover and Aston Martin, both of which had announced a halt on shipments to the US in April. This now matches the tariff on US autos imported into the UK. The agreement also opens the possibility for potential deals with continental Europe.

In credit rating changes, gaming company Playtech was downgraded to BB- by S&P on the back of reduced scale and diversity for the business following the disposal of Snaitech.

EHY defaults have moderated as the 12-month trailing number fell to 3.5% due to an absence of defaults in March. Looking forward, we have increased our one-year default forecast from 3.8% to 5.1% and the two-year default forecast from 7.2% to 8%. This largely reflects the timing effect of ongoing restructuring transactions drawing closer to completion, but also the prevailing tariff uncertainty. Balance sheets in general remain well termed out and we expect modest downward pressure on the forward default outlook, with many of the larger recapitalisation transactions expect to conclude in the coming months.

Asian credit

The JACI index delivered negative returns of 22bps for the week, with higher rates (negative returns of 41bps) offsetting the spread compression (positive returns of 19bps). Meanwhile, JACI IG returned -32bps while HY posted a +44bps return.

Success in the US-China trade talks establish a framework for further discussions. For a 90-day period, China has agreed to reduce the tariffs on US goods to 10%, down from 125%, while the US will cut tariffs on Chinese goods to 30%, down from 145%.

Also in China, the country announced a package of monetary policy stimulus, marking its first response to the US tariff escalation in early April. The The People's Bank of China lowered the seven-day reverse repo benchmark rate by 10bps to 1.4%. The RRR (Required Reserve Ratio) was also reduced by 50bps, which released around CNY1 trillion ($139 billion) in liquidity into the banking system. The Pledged Supplementary Lending (PSL) facility, which serves as low-cost financing for policy banks, was also cut by 25bps. Additionally, a new relending quota of CNY1.1 trillion was also set up to support elder care, services consumption and equipment/consumer goods trade-in, and to provide lending to small-medium enterprises and agriculture.

In India, the supreme court ruled that JSW Steel's resolution plan for Bhushan Power & Steel (BPSL) did not meet the provision of the Insolvency and Bankruptcy Code (IBC). As such, the court has directed the National Company Law Tribunal (NCLT) to liquidate BPSL. This is a negative development because JSW Steel acquired BPSL in March 2021 and had made additional investment in it to increase its capacity from 2.75mt to 4.5mt by the end of 2024. Both creditors (banks and other lenders) and JSW Steel itself are likely to seek a review of the supreme court order.

Also in India, according to Reuters, Adani Group representatives have reportedly met with US officials with regards to the US Department of Justice's indictment of Gautam Adani, Sagar Adani and Vneet Jain on bribery charges. The representations are seeking the dismissal of the indictment.

Emerging markets

Emerging markets (EM) benefitted from encouraging US trade policy signals and market optimism last week. Sovereign credits returned 0.32% in US dollar terms and spreads tightened by -11bps on the week. High yield credits drove returns (+0.79% in US dollar terms), outperforming investment grade sovereigns (-0.17%). High yield credit spreads tightened by -22bps on the week. Venezuela, Ecuador, Ghana and Senegal outperformed. Local currency returns were negative (-0.16% in Us dollar terms), ending a run of positive performance.

Romanian bonds were the largest underperformer last week, following the rerun of the first-round presidential election and ensuing political uncertainty. The far-right candidate, George Simion, secured 41% of the vote, while Bucharest mayor, Nicușor Dan, secured 21%. They will proceed to the run-off vote on 18 May. Both Romanian bonds and the local currency sold off, with 10-year spreads widening 16bps and prices decreasing by 4% on the week.

In Saudi Arabia, crown prince Mohammed bin Salman is preparing to welcome Donald Trump this week. Oil prices have slumped by more than 20% in March, reaching $60.3 per barrel. Saudi Aramco's net income fell by almost 5% over the quarter and free cash flows failed to cover dividends. Saudi complex bonds remained stable due to the general strength of the credit.

S&P raised Ghana's credit rating after the new administration revealed plans to cut spending following a debt restructuring in late 2024. Ghana's long-term foreign debt rating has moved from 'SD' to 'CCC'. The International Monetary Fund (IMF) also affirmed that they see Ghana's fiscal adjustment path as credible, with debt-to-GDP estimated at 55% versus a previous IMF estimate of 67%. Spreads compressed by -90bps on the week.

Tensions between India and Pakistan eased over the weekend as the Trump-brokered ceasefire between nations held. Pakistani bonds maturing in 2036 tightened by -88bps on the week.

There was no sovereign issuance last week. Key central bank meetings this week will be in Mexico, where the policy rate is expected to be cut by 50bps.

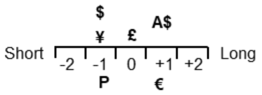
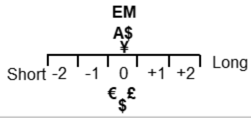
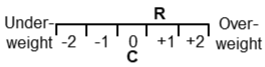
Responsible investment

The European Commission (EC) has given market players until the end of May to feedback on the Sustainable Finance Disclosures Regulation (SFDR). This anti-greenwashing regulation has evolved since it came into force in March 2021, and could be set for further change with the EC's wider sustainable rulebook also under review. The aim of the renovated regulation is to simplify the framework and enhance its usability while still preventing greenwashing.

Labelled bond issuance for April was the lowest April the market has seen since 2020, with just over $55 billion in new bonds, according to Bloomberg. First quarter issuance was still strong, and a quieter month does often follow. Although anti-ESG agendas are growing in popularity across the US, European-based issuance continues to dominate and shows no signs of a slow down when it comes to sustainable debt.

Fixed Income Asset Allocation Views

12th May 2025

Strategy and positioning (relative to risk free rate)		Views	Risks to our views
Overall Fixed Income Spread Risk		▪ Since the US tariff announcements on 2nd April, corporate credit spreads have dramatically widened, market volatility has soared, and the 10-year Treasury has sold off by over 30 basis points. The group took this opportunity to buy credit risk. ▪ The group discussed how they are improving their portfolio's resiliency to this uncertainty, as well as how they are looking to take advantage of further repricing. ▪ **The group upgraded to a neutral outlook on credit risk overall, upgrading their views on corporate credit and downgrading Emerging Markets credit.** ▪ The CTI Global Rates base case view is that the pace and magnitude of additional cuts is uncertain and dependant on growth, inflation and labor market data.	▪ Upside risks: the Fed achieves a soft landing with no labour softening; lower quality credit outlook improves as refinancing concerns ease; consumer retains strength; end to Global wars ▪ Downside risks: Fed is not done hiking and unemployment rises, or the Fed pivots too early and inflation spikes. Restrictive policy leads to European recession. China property meltdown leads to financial crisis. 2024 elections create significant market volatility.
Duration (10-year) ('P' = Periphery)		▪ Longer yields to be captured by long-run structural downtrends in real yields ▪ Inflation likely to normalize over medium term, although some areas will see persistent pricing pressures	▪ Inflationary dynamics become structurally persistent ▪ Labour supply shortage persists; wage pressure becomes broad and sustained ▪ Fiscal expansion requires wider term premium ▪ Long run trend in safe asset demand reverses
Currency ('E' = European Economic Area)		▪ Dollar has been supported by US growth exceptionalism and depricing of the Fed while the ECB looks set to embark on a cutting cycle. ▪ Dollar likely to continue to be supported into year end, where a Trump presidency looks most likely, and with it a return to tariffs and America First policy.	▪ Central banks need to keep rates at terminal for much longer than market prices, to the detriment of risk and growth and to the benefit of the Dollar
Emerging Markets Local (rates (R) and currency (C))		▪ US weakness can enable EM currency performance. ▪ Inflation normalisation and currency strength allows EM central banks to stimulate domestic demand. ▪ Risk premium to leak out of local bond curves.	▪ Global risk aversion restores bid for US dollar. ▪ Weaker oil environment requires fiscal premium among exporters ▪ Higher global term premium.
Emerging Markets Sovereign Credit (USD denominated)		▪ Despite valuations becoming more attractive in the past month, the group has downgraded the sector to a negative outlook because of worsening fundamentals. ▪ The group maintains discipline regarding valuations, rotating into more compelling opportunities as they arise. ▪ Tailwinds: Strong primary market and growth outlook, ratings trends, dollar retracement. ▪ Headwinds: US tariff and trade policy, global trade destruction, weaker net supply, lower oil prices, higher debt to GDP ratios, wider fiscal deficits and slow restructurings.	▪ US trade policy aggression strengthens USD against EM currencies. ▪ EM policy makers constrained by currency pressure; rates remain tight. ▪ Fiscal concerns leak into local risk premia.
Investment Grade Credit		▪ Spreads have widened to levels last seen in Q3 2023. In this new valuation environment, the group has covered their underweight to IG credit risk. ▪ The group upgraded their outlook due to this recent spread decompression. This outlook was only increased to neutral, however, because the same tariff uncertainty driving this repricing is also worsening the fundamental and technical backdrop. ▪ Earnings season is kicking off with large banks; results and commentary from issuers will be important indicators of future global corporate stress.	▪ Tighter financial conditions lead to European slowdown, corporate impact. ▪ Lending standards continue tightening, even after Fed pauses hiking cycle. ▪ Rate environment remains volatile. ▪ Consumer profile deteriorates. ▪ Geopolitical conflicts worsen operating environment globally.
High Yield Bonds and Bank Loans		▪ Given the more compelling valuations, the group has added high yield credit risk and upgraded their outlook on the sector. ▪ This outlook was only increased to neutral, however, because the same tariff uncertainty was driving this repricing is also worsening the fundamental and technical backdrop. ▪ When earnings season begins in a few weeks, the group will be monitoring issuers' forward guidance and insights into tariff-related industry differentiation.	▪ Lending standards continue tightening, increasing the cost of funding. ▪ Default concerns are revised higher on greater demand destruction, margin pressure and macro risks ▪ Rally in distressed credits, leads to relative underperformance ▪ Volatility in the short end of the curve, eroding potential upside where we are positioned for carry.
Agency MBS		▪ Agency MBS has underperfomed during the recent volatility. ▪ This sector has been a source of cash because it has decent liquidity compared to the rest of the securitised market. The group has pared down the Agency MBS position to fund opportunistic credit purchases. ▪ The group remains positive on Agency MBS because the carry and convexity are still attractive, and pre-payment risk is low because of the elevated mortgage rates. Prefer call-protected Inverse IO CMO's, a large beneficiary of aggressive cutting cycle.	▪ Lending standards continue tightening even after Fed pauses hiking cycle. ▪ Fed fully liquidates position. ▪ Market volatility erodes value from carrying. ▪ More regional bank turmoil leads to lower coupons to underperform.
Structured Credit Non-Agency MBS & CMBS		▪ The group reduced high quality carry positions to fund opportunistic credit purchases. ▪ RMBS: Spreads wider MoM. Fundamental metrics, like delinquencies, prepayments, and foreclosures remain solid overall. On the margin, housing affordability is improving. ▪ CMBS: Spreads wider MoM. Stress continues with the highest delinquencies in office, but multi-family is increasing/Continue to monitor health of new issue market. ▪ CLOs: Spreads wider MoM driven by ETF outflows. Defaults remain low but CCC buckets are rising with lower recoveries. ▪ ABS: 60+ Day delinquencies are elevated, driven by inflation and credit score drift. Spreads tighter over the past month; the group prefers higher quality, liquid securities.	▪ Weakness in labour market ▪ Consumer fundamental position (especially lower income) weakens with inflation and Fed tightening. Consumer (retail/travel) behaviour fails to return to pre-covid levels ▪ Student loan repayments weaken consumer profile more than anticipated, affecting spreads on a secular level. ▪ High interest rates turn home prices negative, punishing housing market. ▪ Cross sector contagion from CRE weakness.

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