In Credit

30 June 2025

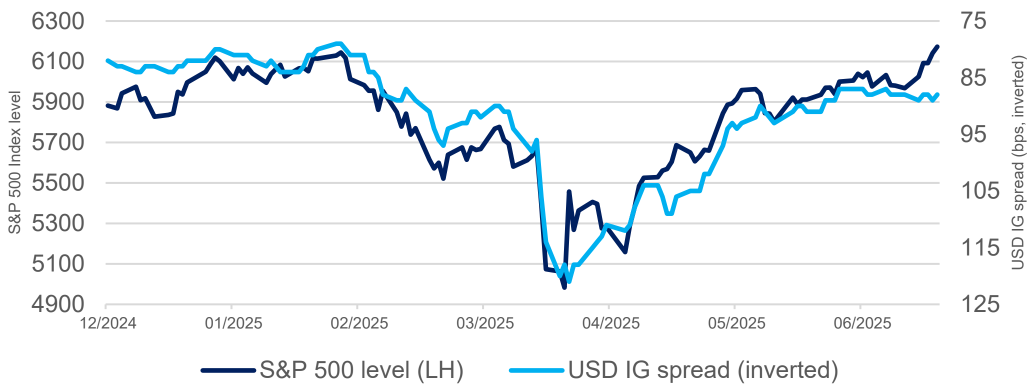
A remarkable reversal of fortune

Markets at a glance

	Price / Yield / Spread	Change 1 week	Index QTD return*	Index YTD return
US Treasury 10 year	4.25%	-12 bps	0.4%	3.4%
German Bund 10 year	2.57%	5 bps	1.2%	-0.6%
UK Gilt 10 year	4.48%	-6 bps	2.0%	2.4%
Japan 10 year	1.43%	3 bps	-0.2%	-2.6%
Global Investment Grade	89 bps	-1 bps	1.4%	3.1%
Euro Investment Grade	90 bps	-4 bps	1.6%	1.8%
US Investment Grade	88 bps	0 bps	1.3%	3.7%
UK Investment Grade	80 bps	-3 bps	2.6%	3.4%
Asia Investment Grade	140 bps	8 bps	1.3%	3.7%
Euro High Yield	335 bps	0 bps	2.1%	2.9%
US High Yield	302 bps	-11 bps	3.3%	4.3%
Asia High Yield	505 bps	5 bps	0.5%	3.4%
EM Sovereign	294 bps	-5 bps	2.8%	5.2%
EM Local	6.0%	-5 bps	7.3%	12.0%
EM Corporate	270 bps	3 bps	1.4%	3.9%
Bloomberg Barclays US Munis	4.0%	-3 bps	-0.2%	-0.4%
Taxable Munis	5.1%	-10 bps	0.1%	2.9%
Bloomberg Barclays US MBS	36 bps	-3 bps	0.8%	3.9%
Bloomberg Commodity Index	253.15	-3.5%	-2.3%	6.4%
EUR	1.1722	1.7%	8.3%	13.2%
JPY	144.08	1.0%	3.7%	8.7%
GBP	1.3699	2.0%	6.2%	9.6%

Source: Bloomberg, ICE Indices, as of 27 June 2025. *QTD denotes returns from 31 March 2025.

Chart of the week: Higher equity prices, tighter corporate bond spreads



Source: ICE BofAML and Bloomberg, as of 30 June 2025

Macro/government bonds
Simon Roberts

Due to a number of factors, we saw a fall in US bond yields last week. First, increased expectations of a rate cut by the US Federal Reserve (Fed). Second, speculation surrounding Fed leadership. Third, easing geopolitical/trade concerns. And fourth, a softer tone to US economic data:

1) In the prior week, Chris Waller, a Fed governor, had said a July rate cut was potentially in play. Fellow governor Michelle Bowman reinforced this message saying she could support a rate cut as soon as July if inflation pressures were to remain contained. She felt the impact of tariffs on inflation could be smaller than expected and noted signs of fragility in the labour market. Waller and Bowman's comments suggested that debate within the Fed was evolving from a previously cautious stance.
2) Jay Powell, Fed Chair, gave testimony to Congress last week. The markets viewed his comments as leaning towards a dovish stance as he emphasised a data-dependent approach. Speculation mounted that President Trump may name Powell's successor as Fed chair. The market believes the replacement candidate will have a bias towards easier monetary policy. Names in the hat appear to include treasury secretary, Scott Bessent; Kevin Warsh, a former Fed governor; and Kevin Hasset, director of the National Economic Council.
3) Globally, geopolitical tensions eased last week amid hopes of a durable ceasefire agreement between Isreal and Iran. Separately, although full details were not clear, China signed a trade deal with the US.
4) The final factor supporting Treasury valuations was the softer tone to economic data. Most notably, personal consumption data came in weaker than expected.

In the UK, gilt yields also fell, influenced by events in the US and domestically by softer growth and softer labour market data.

Positioning We remain constructive on US duration and retain steepening positions across markets.

Investment grade credit
David Oliphant

There has been little movement in spreads over the past couple of weeks, with the Global Corporate Bond index offering a spread of between 89bps and 91bps, according to data from ICE indices.

The market remains supported by positive 'technicals', with demand for the asset class solid, doubtless led by the attractive yields on offer. Net new issuance has not been able to keep pace with inflows. In our view, this is likely to remain the case as the primary market slows into the summer months. The **Chart of the week** plots the remarkable reversal of fortune seen in 'risk' markets – an increase in share prices in the US in the past few months and a concurrent compression in corporate bond spreads over that period.

Year-to-date, euro spreads are 11% tighter while the US dollar market has seen a 7% widening. In both cases, spreads are around one standard deviations (SDs) tight to five-year averages and around 0.7 SDs to a two-decade comparison. As such, we view spreads as expensive.

Liability driven investments

Arthur Stroij

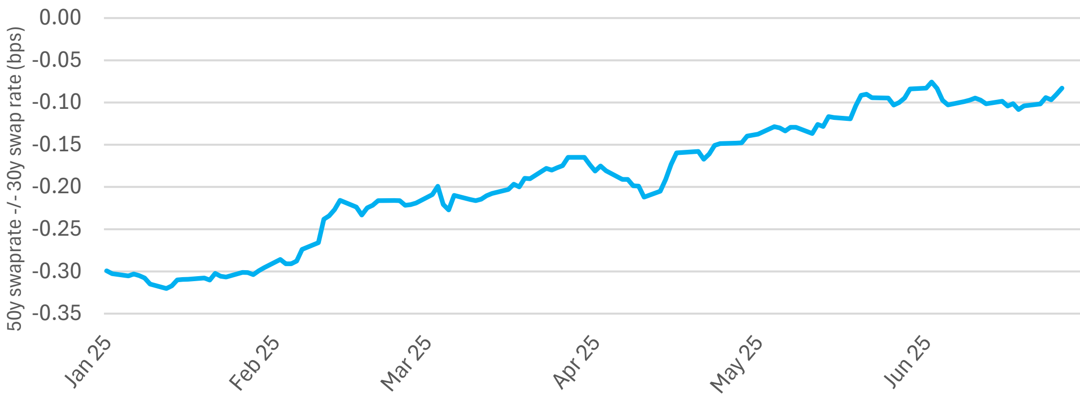
The Dutch pension landscape is undergoing a significant transformation, with approximately €1.8 trillion in assets transitioning from a defined benefit (DB) to a collective defined contribution (CDC) system. This will fundamentally alter how Dutch pension funds manage investments, and particularly their interest rate hedging strategies.

Under the CDC system the interest rate hedge will be differentiated by age cohort, leading to a net reduction in overall interest rate sensitivity. This also necessitates a shorter duration hedge, thereby reducing the need for longer-dated receiver swaps. The transition, which began at the start of this year and will continue until January 2028, is expected to trigger substantial flows in the swap market as funds adjust their hedging policies – notably around 1 January in 2026 and 2027, driven by the sheer magnitude and one-sided nature of this reduced interest rate exposure.

The impact on market liquidity is expected to be significant beyond the 30-year tenor point, potentially leading to increased transaction costs. While the impact before this is projected to be less pronounced, a notable effect on the steepness of the curve in this segment may still occur as pension funds that positioned for the transition unwind 20- and 30-year swaps. A strong consensus suggests the unwinding of receiver swaps beyond the 30-year point will exert upward pressure on swap yields, resulting in a steepening of the swap curve.

In our March 2025 LDI Market Update[1] the above market implications were highlighted. Since that update we have seen a notable steepening of the swap curve in the 30-year-plus segment (**Chart of the week 2**), which is believed to be partly caused by Dutch pension funds positioning their interest rate hedge to a shorter post-transition hedge profile by unwinding longer-dated receiver swaps.

Chart of the week 2: steepening of the swap curve in 30-year plus segment



Source: Bloomberg, as 30 June 2025

In the meantime, the Dutch regulator has acknowledged the possible market impact of the adjustment of interest rate hedges across the sector. A particular concern is the pinpoint risk

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[1] Columbia Threadneedle Investments, LDI Market Update – the new Dutch pension system and its expected market implications, March 2025

around the January transition dates and the ability of pension funds to swiftly adjust their interest rate hedge towards target after transition date. The regulator aims to enable pension funds to manage their mismatch risk by providing a period of 12 months for them to move towards their new target hedge. We believe that, although this period will provide some relief in terms of market impact, especially around liquidity concerns, and will contribute to a more orderly transition, there is still a strong incentive for pension funds to adjust their hedge towards target as soon as possible after transition.

US high yield credit and leveraged loans

Chris Jorel

US high yield bonds provided strong returns over the week alongside circa 3% equity gains, lower interest rates, strong fund inflows and declining geopolitical tensions. The ICE BofA US HY CP Constrained Index returned 0.80% and spreads tightened 11bps to +323bps. The index yield-to-worst declined to 7.08%. According to Lipper, US high yield bond retail funds saw a $3.5 billion inflow over the week, with June's inflow total approaching $4.2 billion. This was driven entirely by ETFs.

US leveraged loan prices saw modest gains given the broader risk-on tone, steady fund inflows, and resilient collateralised loan obligations (CLO) origination. The S&P UBS Leveraged Loan index average price increased to $96.4. Retail floating rate funds saw a $306 million inflow – a ninth consecutive positive observation – leaving the trailing seven-week inflow at $3 billion.

European high yield credit

Angelina Chueh

European high yield returned a steady 0.11% last week, largely on income as spreads and yields remained unchanged (335bps and 6.1% respectfully), unaffected by the Iran-Israel conflict. Under the hood, the scene was more cautious as decompression became more prominent with BBs outperforming the other rating bands. CCCs had another week of negative performance. Flows, although still positive, showed signs of slowing. The €209 million inflow was less than half the previous week. Inflows were all from managed accounts as ETFs experienced a small net negative. This brings the year-to-date net inflow to €2.8 billion, with €3 billion gross from managed accounts.

It was another busy primary week with corporate new issuance totalling €6.8 billion. This brought June's total to €19.5 billion – the second largest month since 2008 and only €1.5 billion short of the record high. There is more fun to come with talk of 10 new offerings in the wings.

In credit rating news, S&P downgraded INEOS Styrolution to BB-, bringing the rating in line with Moody's earlier downgrade in January 2024. UK debt collector Garfunkelux, which defaulted in January, saw its corporate family rating (CFR) upgraded to Caa2 by Moody's following debt restructuring. A Caa3 rating was assigned to the new senior secured bonds.

Asian credit

Justin Ong

The JACI index delivered 66bps of positive returns last week, thanks to strong Treasury returns (78bps) offsetting wider spreads (a 13bps loss). JACI IG returned 65bps while HY posted 68bps.

Tokyo-based ORIX will proceed with a share transfer agreement to sell 17.5% of its 20% stake in Greenko Energy Holdings (GEH) to AM Green Power, a wholly owned subsidiary of AM Green BV for US$1.28 billion. AM Green was established by the founders of GEH. ORIX will also invest in the convertible bonds issued by the parent company of AMG.

Vedanta Resources announced that it is arranging a term loan facility of up to $600 million from its relationship banks, of which $380 million has been committed. The facility has a four-year tenor (door-to-door) with an average maturity of around three years and is priced at a Secured Overnight Financing Rate (SOFR) of +450bps.

In Hong Kong, New World Development (NWD) has obtained written commitments from all banks for its HK$87.5 billion loan refinancing (US$11.1 billion). The agreement effectively pushes back the maturity of HK$63.4 billion, due in 2025 and 2026, by three years. The debt maturities for an additional HK$24.1 billion of loans due in 2027 and beyond remain unchanged, but NWD will add more credit enhancements and additional collateral.

In China, Xiaomi officially launched its first SUV, the YU7, which gained initial orders of 289,000 within the first hour – much stronger than when it launched the SU7 in March. The YU7 is priced at CNY253,500 (around US$54,000), which is around 4% lower than Tesla's SUV model.

Emerging markets

Priyanka Prasher

Emerging market (EM) sovereigns returned a strong 1.09% on the week and spreads tightened by -6bps. Local currency bonds returned 1.41% on the week helped by dollar weakness. On a regional basis, Africa once again led returns (+1.85%), but all EM regions posted positive returns on the week.

Markets appear to have shrugged off last week's Iran-Israel tension. Oil prices returned to pre-conflict levels of $66 a barrel for West Texas Intermediate (WTI), giving back its so-called 'escalation premium'.

On Friday, Moody's and S&P downgraded Colombia's sovereign debt rating. Moody's maintained its 'stable' outlook, whereas S&P changed its outlook to 'negative'. Spreads on 10-year bonds were barely changed, suggesting the news had been expected.

Ecuador's bonds outperformed as investor sentiment was helped by news of the arrest of a kingpin drug fugitive. President Noboa attributed his capture to recently enacted security legislation. 10-year spreads tightened by -43bps on the week.

EM primary market activity rebounded with Mexico, Slovenia, Chile, Kazakhstan, Türkiye, Peru, Uruguay and Korea tapping the markets.

Coming up Policy rate decisions will come from the Dominican Republic and Poland.

Fixed Income Asset Allocation Views
30 June 2025

COLUMBIA THREADNEEDLE INVESTMENTS

Strategy and positioning (relative to risk free rate)		Views	Risks to our views
Overall Fixed Income Spread Risk		▪ In the past month, markets have become less reactive to global trade developments and credit valuations have gotten more expensive. The group has begun reducing credit risk that was added during April's volatility. ▪ The conversation focussed on how the group is navigating this unattractive valuation environment, as well as fewer foreign investors could impact US credit markets. ▪ **The group downgraded to a negative outlook on credit risk overall, with no changes to underlying sector views.** ▪ 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 ▪ As markets have reduced the amount of cuts expected by the FED in 2025, we have used the back- up in yields to go long US duration	▪ 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)		▪ The group maintains a negative outlook as the sector's rich valuations are misaligned with trade-related fundamental uncertainty. ▪ The group maintains discipline regarding valuations and will take advantage of compelling opportunities as they arise. ▪ Tailwinds: Reduced default tail risks, ratings trend positive, dollar retracement. ▪ Headwinds: US tariff and trade policy, global trade disruption, 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 tightened significantly since the early April volatility, The group added exposure in April to cover underweights and has maintained those allocations. ▪ The group remains neutral on the sector given less attractive valuations and global trade uncertainty weighing on the fundamental backdrop. ▪ Earnings results were solid, showing historically strong credit metrics. Forward guidance was cautious as management teams struggle to quantify tariff impacts.	▪ 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		▪ The group has started reducing the risk they added during early April's dramatic spread decompression. The group remains negative on the sector because current rich valuations are misalighned with a weaker fundamental outlook.. ▪ The earnings season largely met expectations; however forward guidance skewed lower due to trade and political concerns. ▪ Despite the negative outlook on the sector, the group remains open to attractive high quality relval opportunities.	▪ 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		▪ Spreads have moved tighter in the past montth. In April, the group reduced their Agency MBS allocation 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. ▪ Mortgage rates steadily rose alongside interest rates, as home price increases and refinance applications are slowing. Purchase applications are steady at lower level. ▪ 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 maintains a large allocation of high-quality carry positions. ▪ RMBS: Spreads have tightened MoM as mortgage rates increase. Fundamental metrics, like delinquencies, prepayments, and foreclosures remain solid overall. ▪ 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: AAA spreads are tighter MoM, below-IG market is weaker. Defaults remain low, but CCC buckets are rising with lower recoveries. ▪ ABS: 60+ Day delinquencies are elevated, driven by inflation and credit score drift. Debt service ratios worsening broadly. 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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