

# Global Credit Income

## Quarterly Review and Outlook

As at September 2016

### Key Highlights

- The positive return was driven by a tightening in credit spreads (driving prices up) early in the quarter as the easing of global monetary policy drove markets.
- In the current low growth, low rate environment demand for higher yielding securities, including investment grade and high yield bonds, has increased.
- We believe that returns often overcompensate for credit risk, and that diversification across a large pool of lowly correlated assets will generate positive 'value-for-risk' outcomes for our portfolios.

### Strategy Positioning and Performance

The strategy outperformed its cash benchmark in the quarter returning 1.95% (gross of fees) compared to the benchmark return of 0.13%. The positive return was driven by a tightening in credit spreads (driving prices up) early in the quarter as the easing of global monetary policy drove markets. Later in the quarter sentiment turned somewhat as spreads widened as the pricing of a US rate hike and as news of the large fine imposed by the US Department of Justice for Deutsche Bank saw financial credits impacted. Combined with oscillations in oil prices, this saw some volatility return to synthetic credit indices following a previous lull.

### Market Insights

In physical credit, the Barclays Global Aggregate Corporate Index average spread moved 20 bps narrower to 1.34%, while the Barclays US Aggregate Corporate Index average spread fell 16 bps to 1.31%. The Barclays European Aggregate Corporate Index narrowed a larger 22 bps to 1.15%, reflecting the increased focus on the Deutsche Bank litigation.

US high yield credit spreads similarly moved notably tighter in the quarter with the Bank of America Merrill Lynch Global High Yield index (BB-B) spread closing at 3.98%, 1.01 percentage points down from the end of August. The high yield market continues to be impacted by increased downgrades particularly in the energy and mining sectors.

Issuance in investment grade credit returned to following the lulls pre and post Brexit. Despite continued geopolitical uncertainty and defaults remaining high, demand continues to be strong as investors seek additional yield in the current low growth environment. The impetus for accommodative monetary policy is helping to fuel the risk-on environment. There were no defaults in the strategy during the quarter.

### Credit Market Outlook

In the current low growth, low rate environment demand for higher yielding securities, including investment grade and high yield bonds, has increased. As credit conditions tighten, fundamentals deteriorate and liquidity becomes sparse, but appetite has remained resilient in the face of substantial primary supply and elevated volatility. Flows will need to continue for the rally to be durable as supply will remain heavy. In high yield credit, flows, issuance and dealer inventories continue to provide a favourable technical backdrop, valuations appear to be stretched, providing little cushion for downside surprises or rate shock related repricing. Our credit strategy and process employs a disciplined approach in the credit assessment and selection process, as issuer decisions will contribute meaningfully to overall portfolio performance. We believe that returns often overcompensate for credit risk, and that diversification across a large pool of lowly correlated assets will generate positive 'value-for-risk' outcomes for our portfolios.

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