ROBECO GLOBAL CREDITS

Strong quarter for risky assets

- Markets price out Fed rate cuts on stronger economic data and stickier US inflation
- Credit spreads continue their tightening trend
- Cautious beta positioning as credit valuations are tight

Markets have repriced expectations of early rate cuts by the Fed as the US economy continues to perform well while US inflation proves to be stickier than expected. Despite government yields moving higher, riskier assets were up and credit spreads moved tighter over the quarter. Demand for credit has been extremely strong as many investors seek to lock in higher yields. We maintained our betas close to 1 and want to avoid being underweight risk as technicals are still very supportive for the asset class. We continue to see most attractive relative value in European financials and AAA-rated covered bonds.

Market developments

The defining feature of the first quarter was a substantial repricing in market expectations for monetary policy easing in coming quarters, particularly in the US. Where the markets had previously predicted interest rate cuts from the Federal Reserve (Fed) totaling around 1.5% over the course of 2024, by the end of Q1 expectations have reduced to just half that.

The reasons for such a change stems from a cocktail of stronger economic data, inflationary pressures proving stickier than expected and subsequently a somewhat less dovish messaging from central bankers. These factors meant government bond yields were pressured over the quarter, with 10-year US Treasuries and 10-year German bunds around 30 bps higher in yield.

It was, perhaps counterintuitively, a very strong quarter for risk assets. If risk assets were so enthusiastic about rate cuts in the final quarter of 2023, should they not be concerned about the prospect of less accommodative policy than originally hoped for? The S&P and Euro Stoxx both up over 10% in local terms, with Bitcoin posting a gain of almost 70% in the first quarter, would strongly suggest otherwise.

For corporate bonds at least, the prospect of a better growth outcome combined with higher yields has continued to be a highly supportive dynamic for the asset class. Demand for credit from a wide range of investors has been extremely strong as investors seek to lock in today’s higher yields. Despite heavy issuance throughout the quarter, there has been little sign of indigestion.

At the index level, spreads tightened by 24 bps for the Euro investment grade (IG) market and 9 bps for the US IG market. Within sectors, strong outperformance was seen from European real estate.

PORTFOLIO MANAGER'S UPDATE MARCH 2024

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Reinout Schapers
Portfolio Manager


Evert Giesen
Portfolio Manager

Sustainable Investing Expertise by ROBECOSAM

Portfolio positioning

Beta modestly above 1

We maintained a beta position modestly above 1 throughout the quarter, which contributed to performance as spreads tightened. Credit posted positive excess returns in each month of the quarter as generally firm economic data caused recession fears to further abate and higher government bond yields spurred ongoing demand for fixed income, with credit a primary beneficiary. While we do not see spreads as obviously cheap, we maintain a beta slightly above 1 given the incredibly strong technical backdrop for the asset class. We maintain a preference for Euro denominated credit over the USD market given relative valuations.

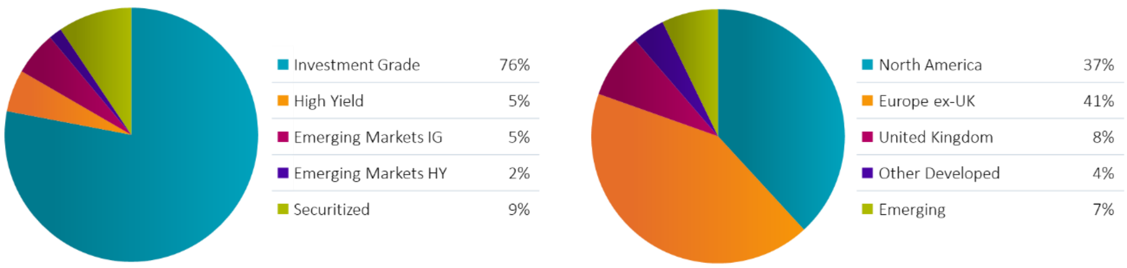
The fund remains overweight European financials, both within banking and insurance. Financials have continued to outperform non-financials since the regional bank/Credit Suisse issues of Q123. Despite this, we believe value remains given the very strong fundamental position of the sector combined with lower net issuance in 2024. Our overweight to basic industry is driven by select 'improving stories' such as Celanese, in addition to high-quality issuers such as Linde and select Emerging market issuers like Suzano and Orbia. Our overweight to communications is largely via holdings in US media companies, Warner Brothers and Paramount. While the industry faces many headwinds, we consider Warner Brothers a strong deleveraging story over time, while the current uncertainty around Paramount is likely to resolve in a way that sees spreads improve from very wide levels. Our agency overweight is driven by holdings in French state-owned utility, EDF.

The fund holds an underweight risk position to US domiciled risk/USD denominated credit, preferring exposure to the EUR market/ European issuers. This is driven by more attractive relative valuations for the European market. The US market has been tremendously well supported by robust growth data, the prospect of imminent rate cuts and overwhelming demand for fixed income at higher yields e.g. pension derisking. On the other hand, European spreads have traded at wider levels, given greater concerns around the growth outlook combined with the cessation of QE bond purchase programs.

The fund is underweight A-rated issuers, with overweights to BBB and BB credits in DTS terms. As credit has rallied, lower rated credits have compressed to their higher-rated peers. While it is not obvious this compression can go much further at an aggregate level, we still find several single-name opportunities within the BBB and BB buckets for credit improvement, rating upside and outperformance versus higher quality.

Our key risk exposures on an individual name basis are to Warner Brothers Discovery and Paramount within the US TMT space and to several financial institutions, both banks and insurers, where we hold subordinated debt.

Figure 1 - Positioning of Robeco Global Credits by segment and region



Source: Robeco. Robeco Global Credits. Data end of March 2024

Performance

Outperformance benefitting from overweight Europe and overweight financials

The fund outperformed the Bloomberg Global Aggregate Corporate Index over the quarter. With a beta of slightly above 1 over the period, the portfolio benefited only modestly from the broad tightening in spreads. The bulk of the outperformance came from issuer selection. The fund benefited from the overweight in Europe as European credit markets outperformed US credit markets over the quarter. The fund's exposures in the banking and insurance sectors added the most to relative performance. Largest positive contributors were the holdings in chemical company Braskem and insurers Athora, AEGON & Legal & General and not owning Boeing. Despite losing investment-grade status with S&P in February, Braskem bonds retraced meaningfully as multiple overseas parties appear to be looking seriously at acquiring Novonor's stake in the company. Several insurance names (Athora, Aegon and Legal & General) also made a positive contribution given the subordinated (and therefore higher beta) nature of these instruments. Zero holdings in Boeing, a meaningful corporate issuer in the USD market, benefited as the company continues to be plagued by weaker deliveries and safety concerns.

On the negative side, a modest overweight to Paramount detracted as the likely sale of controlling shareholder NAI creates meaningful uncertainty, with an Apollo led LBO a primary concern for bondholders. Warner Brothers Discovery widened meaningfully in February following the release of Q423 earnings that missed expectations on EBITDA sharply. Thames Water has further underperformed as shareholders declined to provide the required £500 mln in fresh equity to the Kemble holding company, raising fears of the company being placed into special administration. Deutsche Bank bonds lagged the rally somewhat given lingering concerns over commercial real-estate exposures within the German banking sector.

Annualized performance Robeco Global Credits						31 March 2024
	Mar/24	3-month	YTD	1-year	3-year	5-year
Robeco Global Credits (IH EUR)	**1,26%**	**0,11%**	**0,11%**	**4,48%**	**-2,78%**	**0,64%**
Benchmark (hedged into EUR)	1,15%	-0,28%	-0,28%	3,76%	-3,25%	-0,38%
Relative performance	0,11%	0,38%	0,38%	0,72%	0,48%	1,03%
Robeco Global Credits (DH USD)	**1,40%**	**0,50%**	**0,50%**	**6,64%**	**-0,80%**	**2,68%**
Benchmark (hedged into USD)	1,26%	0,10%	0,10%	5,89%	-1,30%	1,61%
Relative performance	0,14%	0,40%	0,40%	0,75%	0,49%	1,07%
Robeco Global Credits (FH GBP)	**1,37%**	**0,44%**	**0,44%**	**5,90%**	**-1,68%**	**1,72%**
Benchmark (hedged into GBP)	1,24%	0,03%	0,03%	5,14%	-2,13%	0,65%
Relative performance	0,12%	0,41%	0,41%	0,75%	0,45%	1,07%

The currency in which past performance is displayed may differ from the currency of your country of residence. Due to exchange rate fluctuations, the performance shown may increase or decrease if converted into your local currency. The value of your investments may fluctuate. Past performance is no guarantee of future results. Performance gross of fees, based on gross asset value. In reality, costs (such as management fees and other costs) are charged. These have a negative effect on the returns shown. Periods shorter than one year are not annualized. Source: Robeco. Robeco Global Credits. The oldest share class per currency is shown. Benchmark: Bloomberg Global Aggregate Corporate.

Outlook

Credit markets have embraced a soft landing

The ideal scenario for credit appears to be materializing, characterized by declining inflation and the likely avoidance of a recession. Credit markets have wholeheartedly embraced this narrative and are to a large extent priced for perfection. However, have market participants grown complacent, with risk appetite reaching high levels?
While we acknowledge the high probability of the consensus scenario, we remain mindful of the fragility of sentiment and the omnipresence of risks in a changing world. With current tight valuations and risk positioning, there is ample room for disappointment.

As long as rate cuts are likely, we judge that the technical support from central bank policy remains constructive. However, we should not anticipate another round of spread tightening after the initial rate cut. Historical data shows that even in a soft landing environment, spreads typically do not tighten further following the first rate cut.
We target a more neutral positioning in investment grade and emerging markets, focusing on generating alpha through issuer selection.

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