

July 9, 2025

The quarter began with a sell-off following the “Liberation Day” tariff announcement, which was promptly walked back by Trump with a three-month extension after being met with swift negative reactions from around the globe. Then, markets enjoyed a brief respite with a snapback rally in US fixed income and equities, supported by moderate inflation and resilient economic data despite ongoing uncertainty.

The pendulum swung back and Q2 ended with Congress passing the “Big Beautiful Bill” into law, more geopolitical turmoil, and a sense of wary resignation as the three-month tariff extension passed by today and got extended once again to August 1st. After blowing hot and cold on trade policy all year, markets simply shrugged at the Trump administration’s recent 25% tariff threat to Japan and South Korea among others, with the belief that these tariffs, like the others, will be rolled back in some way to some degree.

In this note we want to point out two key themes: the significant increase in fallen angels and the primary market trends we expect to materialize in the fall.

We are now in the midst of the largest downgrade cycle of fallen angels from investment grade into high yield since COVID. In fact, the last time we saw this volume of fallen angels was back in 2016 during the collapse in global energy prices. However, at that time, the downgrades were contained within the energy sector. The downgrades this time are more broad-based including sectors such as telecom and media, retail, and real estate as well as many familiar names like Warner Brothers Discovery, Ford Motor, Whirlpool Corporation, and Walgreens Boots Alliance.

While the term “fallen angel” can imply a misstep on management’s part or material headwinds that stir doubt regarding the company’s ability to repay their debt, this is not always the case. For instance, it could be a deliberate move for an issuer that might be comfortable with a more levered capital structure (ex. as a way to increase equity returns). We are seeing both types of fallen angels today – some a result of a perceived decline in the creditworthiness of the company due to operational challenges, and some that are more about balance sheet/financial optimization.

Migration of companies from investment grade to high yield (and the other way) presents good opportunities to add value through trading – particularly in our more flexible mandates. Many investors lack flexibility in their mandates and are forced to unfortunately sell fallen angels at a time when they may present the best value. Beyond this, at a high level, a greater volume of fallen angels, by definition, increases the average quality of the investment grade index while also presenting opportunities in high yield, especially when the downgrade is a result of a capital restructuring.

Heading into Q3, year to date, the performance in credit spreads globally has been supported by a demand-supply imbalance, where inflows into bonds continue to be strong while net new issuance has been quite modest. Despite higher interest rates, we haven't really seen the expected volume of M&A activity and refinancing trades that were forecasted at the start of the year. Although the volume of new issue supply is expected to remain low in July and August, we anticipate that the supply pipeline will pick up considerably from September onwards, which can present more opportunities as the market becomes more balanced.

From a positioning perspective, given the higher economic risks, we prefer to focus on duration (interest rate risk) over credit spreads at this point, maintaining a defensive credit positioning in light of tight valuations. We continue to be up-in-quality across our strategies while reducing cyclical exposures and focusing on US and European credit.

As it stands, the outcome of the Trump administration's tariff strategy has yet to materialize so approaching this evolving and persistently volatile market environment with caution and discipline is paramount. We believe our more conservative stance sets us up to take advantage of compelling opportunities as they emerge. In the meantime, we aim to continue providing investors with an effective alternative to traditional fixed income, equity, and private asset allocations.

For more updates on the credit market, read our **[Credit Market Themes in 5 Charts](#)** article for this quarter. As always, if you have questions about our market outlook or our strategies, please do not hesitate to reach out to our team.

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