Credit Makes a Comeback

Notes from the Trading Desk - Q4 2023

After two consecutive difficult years for bonds, the final quarter of 2023 provided much-welcomed relief for fixed income investors. The market's soft or no landing expectation was bolstered by encouraging inflation data, optimistic central bank rhetoric, and a resilient economy, leading to a notable comeback for credit.

Given these big market moves, we believe the market may be getting ahead of itself, and it is still crucial to hedge against the market's overly optimistic outlook. As a result, we maintain a somewhat conservative positioning, being mindful of the strength of the consumer, particularly in Canada, and we remain cautious on some sectors that may be exposed if a soft landing is not achieved. Nevertheless, we continue to believe corporate credit in developed markets will be among the best risk-return opportunities over the coming quarters, especially as cash balances are redeployed in the market.

During Q4, our high conviction holding in telecom issuer, Rogers Communications, was a particularly rewarding return contributor across the capital structure with a great deal of exposure outside the Canadian market. Through our longstanding dealer relationships and strong credit work by our team, we were able to participate in Rogers' recent deal in late 2023, with both our existing bonds and the new issues outperforming across geographies. Credit spread compression in their subordinate hybrid securities enabled us to capitalize significant value from this high conviction issuer, and with the current yield to call being around 7%, there's more value to come.

As we enter this new year, we continue to seek attractive, well-priced deals, particularly in the Financials sector. We are also seeing attractive opportunities to take advantage of cross-market mispricing and relative value. We believe this environment is particularly good for investing in floating-rate bonds (FRNs) given elevated yield levels and our belief that the speed and magnitude of policy easing appear aggressive compared to fundamentals.

A key driver for 2024 will be the trillions of cash across developed markets and where it gets redeployed. As rates are expected to start coming down during this year, flows in and out of money market funds, GICs, and high-interest savings accounts will define asset allocation strategies. Overall, fixed income yields continue to look attractive, and with lots of issuances expected in 2024, we anticipate many opportunities for alpha generation for us as an active manager.

For more credit market themes, check out our **Credit Market Themes in 5 Charts** article for this quarter.