
LO Funds

Fallen Angels Recovery

Newsletter

Global Fixed Income • Fixed Income

30 November 2024

FIXED INCOME MARKET OVERVIEW

After a turbulent October, and through a month filled with political headlines, fixed income posted robust performance at an aggregate level in November. There was however marked differentiation between EUR and USD markets, with EUR markets outperforming in the government bond space but underperforming in credit as spreads moved wider toward month end. Sectoral trends were also driven by the US election result, with industrials and autos leading the tightening in the US at the expense of EUR counterparts, with EUR autos continuing to suffer after experiencing some reprieve in October. The US election headlined a busy macro month, with Donald Trump and the Republican party securing a "red sweep" across the presidency, house and senate. While Trump had the edge in betting markets heading into the vote, the scale of the Republican wave was quite unexpected. In the lead up to voting day, markets had moved to price towards this result with higher yields and rallying risk assets domestically, on the assumption of a mix of expansionary fiscal policy with disregard of fiscal deficits and increased trade tariffs. However, post-election, the selection of cabinet nominees who have voiced support for more fiscally prudent policies, particularly Scott Bessent Treasury Secretary, has been taken positively by markets, and saw rates move lower alongside continued strength in US risk assets. However, the news flow on trade tariffs remained volatile post-election in a reminder of the headline risk that came with Trump's first term. The use of trade tariff threats as a negotiation tactic will very much continue to be part of Trump presidency, and rhetoric since his victory has highlighted Mexico, Canada and China to be at threat, with concerns also spilling over into European risk assets. European assets additionally had their own bout of political headlines as German chancellor Scholz called a snap election for February. Whilst the ultimate outcome might bring some much-needed coherency to Germany's political front, it freezes any chance of policy advancement at a time when the economy continues to stumble as their fiscal business model is suffering. France also faced a fresh bout of political headwinds towards the end of the month, resulting in the government's resignation following a no-confidence vote due to the rejection of the proposed budget. Politics aside, macroeconomic developments also supported duration following the pre-election sell off, with the Fed delivering

another 25bp cut after a soft labour market report (albeit weather and strike affected). Growth data also showed signs of weakening in the US after a post summer rebound, whilst inflation continued a short-term uptick but maintained a longer-term downtrend. If anything, the months events should act as a reminder that the future path of inflation will be driven by both fiscal developments as well as the longevity of underlying growth momentum. Eurozone economic data continued to come in weak but has perhaps showed signs of bottoming in its weakest areas. Geopolitical risk spiked higher in the Ukraine-Russia conflict, with Ukraine's use of US-supplied longer-range missiles to target Russian territory after receiving clearance from Washington. The use of western supplied missiles to hit Russian occupied territory has been touted as a red line by Putin, and as a response the Russian president signed a decree lowering the threshold to trigger use of the country's nuclear arsenal. Whilst this appears to be a deterrent rather than an imminent escalation threat, the events saw a spike in volatility, so headline risk from the conflict remains. With rates actually lower now than pre-election despite the perceived 'worst-case scenario' for rates of a 'red sweep' materializing, we continue to favor duration heavy assets. But without seeing an imminent risk to spreads, despite being at tight levels, we prefer to access duration via high quality credit to collect extra carry to compensate for flat/inverted rate curves. We maintain a neutral allocation to high yield but emphasise a continued focus on selecting quality, particularly in Europe which faces ongoing growth and refinancing risks.

PORTFOLIO ACTIVITY

November saw no new Fallen Angels and one issuer returning to the investment grade universe. Iconic UK retailer Marks and Spencer's was upgraded to Baa3/BBB- by Moody's & S&P in November following continued strong operating performance. Business profile has improved as M&S has become increasingly competitive and has a clear strategic plan to continue to increase market share, reduce costs and improve margins. The improved operating performance combined with a financial policy focusing on debt reduction has led to a material improvement in financial metrics and a return to investment grade status.

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Newsletter • LO Funds - Fallen Angels Recovery • Data as at 30 November 2024

PERFORMANCE AND CHARACTERISTICS

. The fallen angel strategy is a high quality high yield strategy with an average rating of BB+; some two notches better than the high yield index.. The strategy under-performed the high yield index in November. Telecoms and retail sectors under-performed primarily through two French companies Eutelsat (Telecoms) & Auchan (Retail); probably linked more to the political uncertainty in France than any company specific events. This weakness was partially offset by the continued positive contribution from our over-weight in the real estate sector which continues to normalise as investors become more comfortable with the long-term fundamentals of the sector. In particular, Canary Wharf announced GBP900m equity funding from Brookfield to support the refinancing of its bonds due in 2025, 2026 & 2028. . Year to date

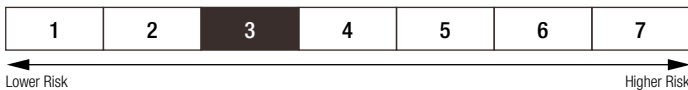
performance lags that of the high yield index but remains materially ahead of the Fallen Angel index which has underperformed the high yield index by c. 300bp this year reflecting the structural differences between the two indices. This performance supports our view of the critical importance of active management and alpha generation within this strategy. . Outlook: The recovery in the real estate since the end of last year continues albeit at a slower pace. We still expect this sector to provide a number of new Fallen Angels as while interest rates have peaked which will stabilise valuations, refinancing costs ae still high and interest cover - a key credit metric - will weaken. We are now starting to see some weakness within the consumer cyclical sectors along with the automotive industry where profit warnings have led to some negative rating actions albeit no new fallen angels.

PERFORMANCE

30.11.2024	INCEPTION	AUM	MONTH-TO-DATE	YEAR-TO-DATE	INCEPTION-TO-DATE	5 Year Ann. Return	10 Year Ann. Return
LO Funds - Fallen Angels Recovery, Syst. Multi Ccy Hdg, (USD) NA	30.11.2021	USD 389 mn	0.73%	6.96%	8.48%		
Bloomberg Barclays Global High Yield Corporate ex-EM TR HDG USD			1.03%	8.82%	11.81%		

Past performance is not a guarantee of future results. Performance is presented net of fees. AUM as of the date of the table.

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The following risks may be materially relevant but may not always be adequately captured by the synthetic risk indicator and may cause additional loss:

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Concentration risk: To the extent that the fund's investments are concentrated in a particular country, market, industry, sector or asset class, the fund may be susceptible to loss due to adverse occurrences affecting that country, market, industry, sector or asset class.

Before taking any investment decision, please read the latest version of the

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Finland. Finanssivalvonta (Fiva) - Financial Supervisory Authority (FIN-FSA), Snellmaninkatu 6, P.O. Box 103, FI – 00101 Helsinki, Finland; Website: <http://www.finanssivalvonta.fi>.

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