

# GAM Star Fund plc – GAM Star Credit Opportunities (GBP)

Marketing material for professional / institutional / accredited investors

## Macro backdrop

Subordinated debt markets were strong in January despite volatility in interest rates. Strong US employment numbers initially put pressure on interest rates. However, the tone got strong during the second half of the month following the US and UK consumer price index (CPI) numbers which were better than expected. Spreads within Additional Tier 1 (AT1) Contingent Convertible bonds (CoCos) narrowed to 270 basis points (bps), which is close to the historical tight. Credit spreads in general are at relatively tight levels compared to historical levels, but the “all in” yields remain attractive, especially when looking at the last 10 years. These yields mean that technicals within credit markets have remained robust. The second part of the month was dominated by the initial decisions of the new Trump administration. For the moment, it seems like markets in general were not too affected by those. Moreover, subordinated debt of financials was not affected by the whole DeepSeek story.

## Valuations and fundamentals

As stated above, spreads within credit market are at the tighter end of historical values. For example, AT1 credit spreads are close to the historical tightest at 270 bps above government bond rates. While this could be justified by fundamentals, we know that credit markets tend to be cyclical. As such, we believe some caution is warranted. Moreover, extension risk, which measures the percentage of AT1 CoCos priced to perpetuity or call, is currently around 6%. When market conditions are poor, it tends to peak at 100%, and when market conditions are very strong, like currently, this percentage tends to approach 0%, indicating that valuations are at their tightest. As such, from a risk-return perspective, we believe there are currently more opportunities and valuations are more attractive in Tier 2 and senior bonds from financials.

Bank Q4 earnings season kicked off strongly, with the first batch of results meeting or exceeding consensus expectations – while credit metrics remain rock solid. As an example, BBVA reported very strong earnings, closing the year with an impressive 19.7% return on tangible equity (RoTE), a Common Equity Tier 1 (CET1) ratio marginally higher at 12.9% (circa EUR 15 billion excess capital to minimum requirements), and non-performing loans (NPLs) down sequentially to 3%. The bank expects to deliver a high teen double digit RoTE in 2025.

Apart from earnings, the theme of M&A continues unabated in the European financial sector. We believe an acceleration of M&A activity in the sector should be credit positive.

## Subordinated Debt

There were six new AT1 or Restricted Tier 1 Capital (RT1) issues in January. Those represented approximately USD 4.5 billion of issuance and we saw demand of approximately USD 21 billion. As we can see, market technicals remain very strong. Issuance is expected to remain a positive technical with limited net supply as issuance is driven by refinancing of upcoming calls and maturities.



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