LOOMIS | SAYLES

TEAM VIEWS
March 2025

Global Bond Fixed Income Team Views

By the Loomis Sayles Global Bond Fixed Income Team

SECTOR	OUR CURRENT VIEW	OUR ANTICIPATED STRATEGY
CREDIT		
Global Corporates	Relative credit beta had remained at the lower end of our risk spectrum as of quarter end and prior to "Liberation Day" on rich valuations with potential for a very volatile macroeconomic backdrop. Credit fundamentals have been fine, but trade war is likely to cause pain. While credit valuations have improved in the first two weeks of April, spreads are still just median for this stage of the credit cycle and suggests there is much room for widening in a downturn, in our view.	We are starting to increase credit beta in portfolios, but selectively, adding names we like in oversold areas like energy. We will continue to look for mispriced securities and add into further weakness. We still remain overweight communications and tech on a combination of positive issuer specific stories and general defensive nature of the industries. Banking remains a top overweight. Underweight consumer cyclicals (e.g. retailers and autos)
High Yield	While forward looking loss estimates are relatively subdued, our high yield allocation remains near historic lows given the limited risk premium available and relative value versus investment grade. Amidst the post quarter end volatility, the value proposition for high yield has improved, although is still not broadly attractive. We remain cautious of potential stress to come from the lagged effects of the recent tightening cycle with lower quality, more interest sensitive companies the most vulnerable. We remain patient and await a better buying opportunity ahead.	We ended the quarter with minimal high yield corporate exposure across accounts, although since the quarter ended we have begun establishing positions in select BB-rated names. We remain low in HY corporates relative to history but will look to incrementally add as specific opportunities arise. Note, high yield exposure includes Brazil and South Africa local rates positions.
Securitized	In Agency MBS, valuations are attractive and technicals have improved with a marginal uptick in bank buying, although uncertainties persist regarding regulatory changes under the new administration. We believe residential real estate performance should be contained given a structural lack of supply, record home equity and conservative underwriting.	Overweight high carry securitized credit, mainly in short non-agency MBS, and select aircraft ABS senior bonds. Trimmed our overweight to free up capital for potential corporate buys. We expect this to be a source as volatility persists and corporates cheapen.

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CURRENCY		
US Dollar view	The story of US exceptionalism is increasingly under threat, and diverging fiscal policies and weaker global growth may see the currencies of developed countries make further headway against the dollar, in our view.	Underweight USD
Developed	While an infrastructure and defense spending ramp up led by Germany may be slow to materialize as an economic boost, Western Europe's resilience in the face of a dent in the global trade environment is likely to be greater than what we would have assumed coming into 2025. Solid wage growth and strong capex pipeline in Japan support a growth recovery.	Overweight EUR, JPY, GBP
Emerging	EM and global trade-sensitive economies still could struggle to attract sizable capital flows.	Underweight CNY on geopolitical risks, decline in goods exports, and risk of growth shortfall. Closely watching BRL (high carry, cheap valuations, some fiscal improvement)
YIELD CURVES		
Duration	Rising global risks and the threat of weaker global growth has pulled forward the markets expectation for rate cuts and we are biased slightly long overall duration, led by USD and looking for potential areas to add, with a particular eye on EUR and GBP duration. However, global fiscal concerns still act as a counter to lower rates.	Extended a what was a modest US duration overweight post quarter end Took profits on a JPY duration underweight post quarter end
Local EM Markets	We believe select local EM markets are currently attractive where proactive central bank tightening has resulted in high (ex-ante) real yields	Overweight EM duration: S. Africa, Brazil, and Indonesia
KEY RISKS		
	Unexpected distortions from uncertainty and trade policy could see a rising number of stressed corporations raise risk of a broader credit cycle downturn, in our view. Changes to the fiscal, trade, and immigration landscape in such a short period creates potential volatility revealing unpredictable areas of stress. Geopolitics: any change (ceasefire or escalation) in the Ukraine, Middle east, or other conflicts will have market implications.	As valuations adjust, we will look for opportunities to add risk in interest rates, currency and credit

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KEY RISKS Credit Risk, Issuer Risk, Interest Rate Risk, Liquidity Risk, Non-US Securities Risk, Currency Risk, Derivatives Risk, Leverage Risk, Counterparty Risk, Prepayment Risk and Extension Risk.

Commodity, interest and derivative trading involves substantial risk of loss.

Markets conditions are extremely fluid and change frequently.

Diversification does not ensure a profit or guarantee against a loss.

Any investment that has the possibility for profits also has the possibility of losses, including the loss of principal.

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OUTLOOK

- It is a cliché of military history that it is easier to start a war than to end one, and the war one starts may not be the war one gets. We will see if the same themes apply to trade wars in coming months, but a trade war analysis is not the only lens by which Liberation Day can be viewed.

- The US tariff hikes are largely being analyzed in trade policy terms, which in isolation would imply a stronger US dollar. While there are differing opinions across Loomis Research and the portfolio teams, another way to organize thinking about currency consequences is to consider the tariff hikes as a fiscal policy tightening, and then employ portfolio theory. This analysis points to the conclusions we wrote about last month: weaker equities, lower yields, lower oil prices, and a weaker USD.

- The US government needs money. Total net Treasury debt is 100% of GDP, or $30T. Revenues are in the 17% of GDP range, spending is about 24%. The deficit is 7% of GDP. So what to do? Spending cuts are the first resort, but the Polymarket bettors have grown more pessimistic since the beginning of the year, and now place only a 25% probability that Doge, etc. can cut as much as $250bn from spending. Some sell-side bank guesses are materially lower, at $60-100bn, or about 0.25%-0.35% of GDP. This is not enough, in our view. We believe the alternative is to go after transfer payments… Medicare, Medicaid, and Social Security …in a serious way, but this is politically fraught, and we think meaningful cuts here will take some time. So where to get money? Taxes! But how?

- There is approximately zero appetite for a bipartisan tax and spending package along the lines of the Bowles-Simpson proposal of 2010 (which failed) in a deeply divided, tax-averse Congress. But there is one kind of tax that can be enacted by Presidential decree: tariffs. The initial average tariff proposed on Liberation Day was about 22-23%. This was estimated as a 1.5%-2.0% of GDP fiscal tightening. This would raise serious cash, but probably slow the economy into recession via supply shocks, lost purchasing power, and negative wealth effects. We doubt that this will ultimately be the effective rate, but a baseline of 10% on everything with much higher rates for China is where we might see the policy settle. So perhaps we are looking at an ultimate effective rate of 12-15%. Stay tuned. This is not equivalent to a Value-added tax (VAT) but it rhymes. We believe consumers ultimately pay most of it, like a VAT (incidence attribution is complicated).

- Current policy settings and portfolio positioning look like the opposite of what we saw in the first Reagan administration, in 1980-82. Then we had a massive fiscal ease (tax cuts, defense) and an even more massive monetary tightening (Volcker!). US equities and bond markets were massively under-owned by the rest of the world (RoW) after the 1970s inflation decade. The USD rose for four years.

OUTLOOK

- Lastly, US equities and the dollar may be re-rated lower by overseas investors, who could demand a higher risk premium to invest. Team America is changing its brand. As Leo Lewis wrote in the London Financial Times, writing from Tokyo (two of the largest overseas pools of capital) globalization, rules based international order, and Pax Americana are out. Mercantilism, isolationism, and protectionism are in. Larry Fink of BlackRock noted that the US has become an engine of volatility rather than an absorber of volatility. Higher risk premia seem reasonable.

- We remain bullish Treasuries, bearish equities and credit, (but are starting to buy in specifically wider industries), bearish oil, and bearish USD. The US economy may narrowly evade recession if enough tariffs are rolled back, but near-zero GDP growth looks plausible. Headline inflation will have to absorb 100bp of supply shock effects. The Fed may cut four times, starting in June, as hard data soften. We believe less liquid assets are likely to become even less liquid.

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