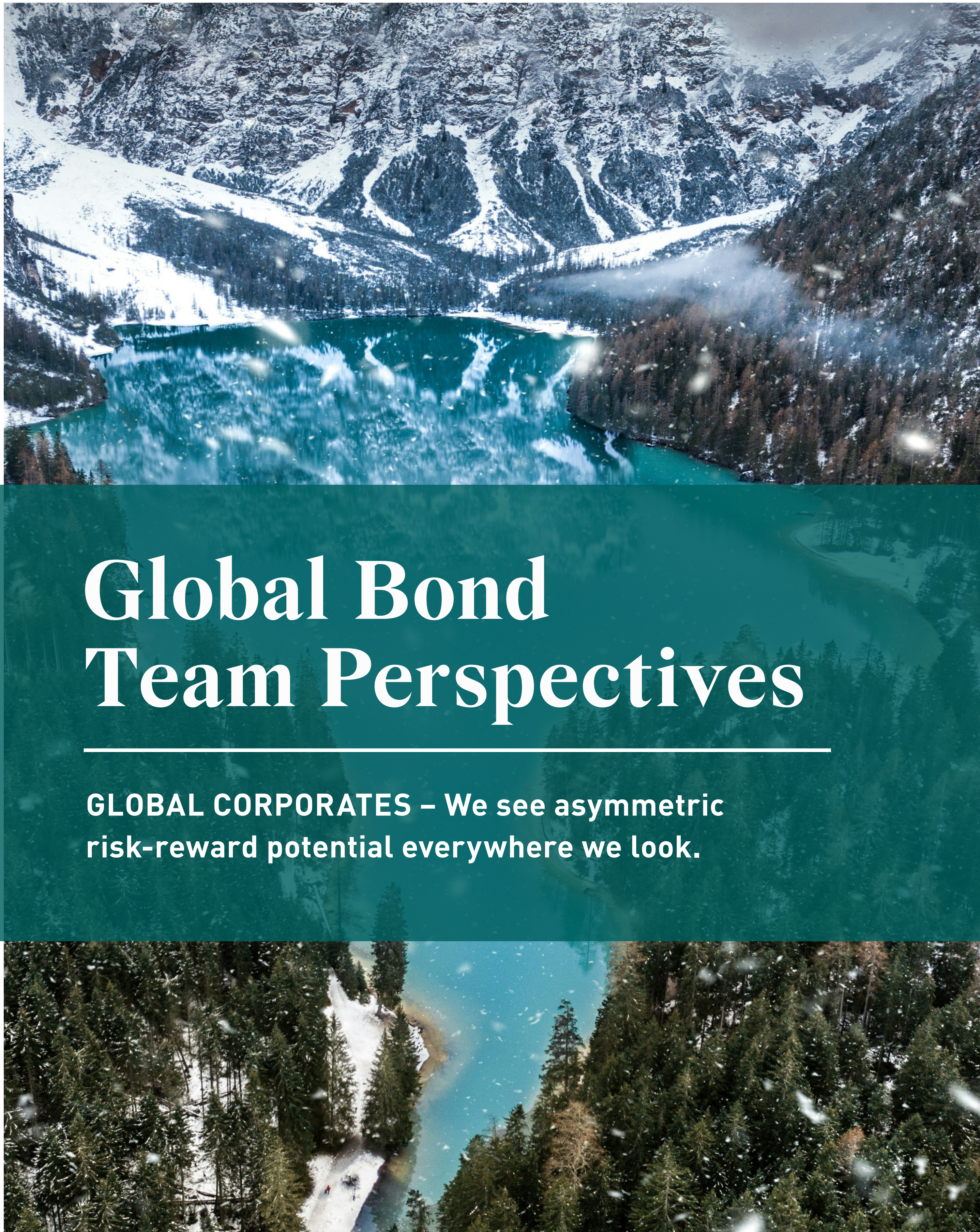
LOOMIS | SAYLES

DECEMBER 2024



Global Bond Team Perspectives

GLOBAL CORPORATES – We see asymmetric risk-reward potential everywhere we look.

Bull Points

1. Corporate earnings remain solid
2. Technical demand for corporate bonds persists
3. Fed likely to continue to cut, albeit at a slower pace

Bear Points

1. Credit valuations even more expensive
2. US GDP estimated to grow sub 2% in 2025
3. Global growth ex-US remains subdued
4. Trump policies likely to increase volatility

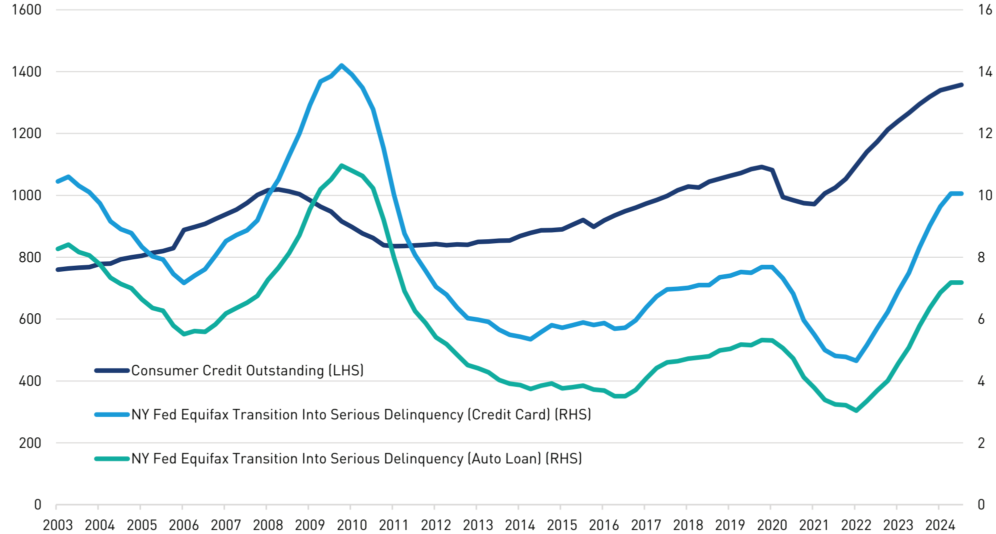
Outlook

When assessing global corporate bonds, it is important to focus on the health of US corporate issuers given their large size in the asset class. Despite our concerns coming into the year that the significant tightening in financial conditions and drawdown of household excess savings since early 2022 would result in a noticeable slowdown in US economic activity, GDP growth remains buoyant. After a sluggish 1.6% growth rate in 1Q24 due to weak exports and inventory build, the previous two quarters posted robust 3% growth. While market expectations for 2025 call for a more muted approximated 2% trend rate, our view remains that strong consumer spending and business investment continue to power the economy. While the uptick in credit card and subprime auto loan past dues that we have warned of in the past is concerning (see **Exhibit 1** below),

EXHIBIT 1

OUTSTANDING CREDIT & DELINQUENCIES

Source: Bloomberg, data as of 30 September 2024.



The chart presented above is shown for illustrative purposes only. *Some or all of the information on this chart may be dated, and, therefore, should not be the basis to purchase or sell any securities. The information is not intended to represent any actual portfolio. Information obtained from outside sources is believed to be correct, but Loomis Sayles cannot guarantee its accuracy. This material cannot be copied, reproduced or redistributed without authorization.*

other consumer indicators such as University of Michigan consumer sentiment and retail sales have improved over the past few months. Why has this strength persisted? The lagged effect of monetary policy tightening has simply not dented earnings enough yet, at least in the large cap space, to ignite a surge in layoff announcements and a resultant decline in consumer and business spending. Following a US earnings recession from 4Q22 to 2Q23, earnings have grown rather robustly every quarter since. The bottom line is for the US economy, if people have jobs, they spend. While the past due factors mentioned above and the negative impact from inflation on spending are worth monitoring, credit card balances in the lower income cohorts continue to grow. The upper income cohort remains unfazed, incessantly benefiting from the continued positive wealth effect.

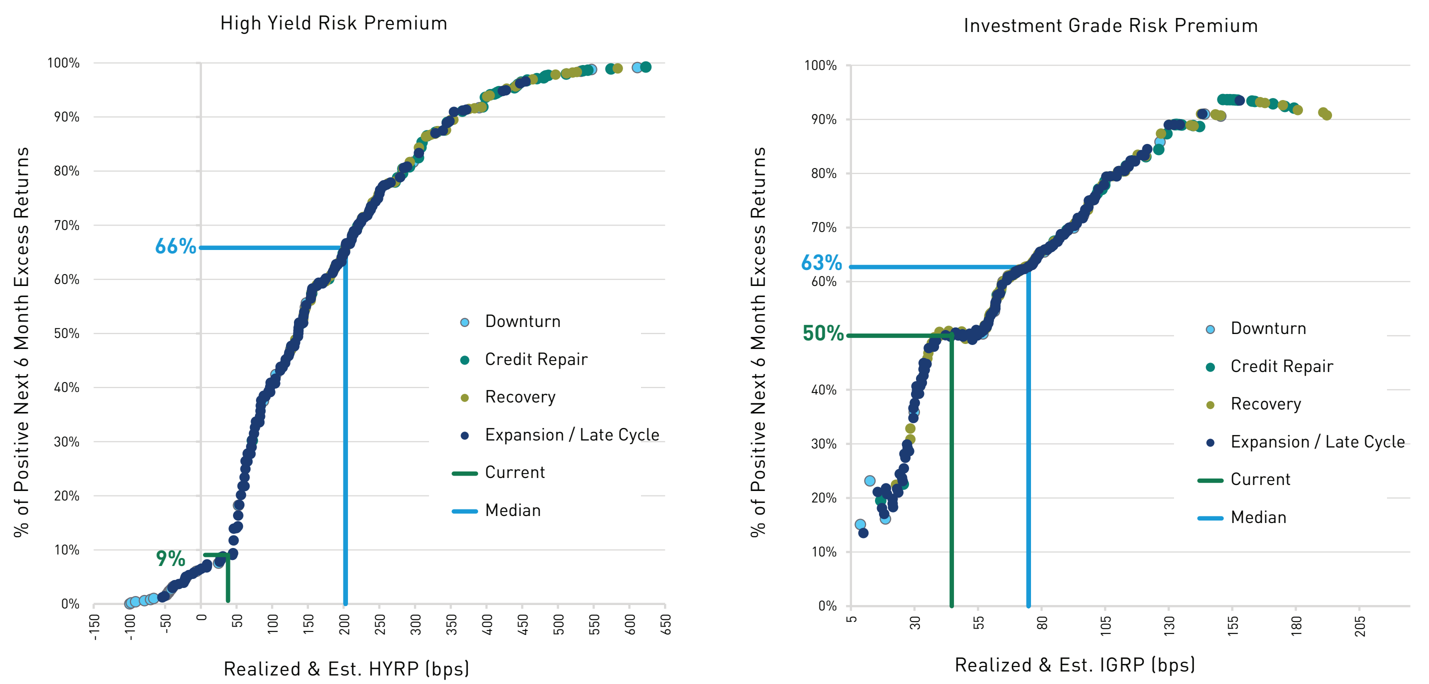
Further, with the reelection of President Trump and Republicans in full control of Congress, many expect a boost to growth as US tax cuts are extended, regulations are relaxed, and animal spirits are potentially rekindled. This may come to fruition, but we believe the reality is that there are far too many unknowns regarding Trump policies to have a high level of conviction. Most market commentators expect risk assets to behave similarly to 2017 when Trump first came in to office. GDP growth for major world economies, ex US, was growing strongly then led by China. The problem is that the global economic backdrop is far different now. While European growth has improved a bit, it remains well below trend, and China is in a markedly different place now. We are concerned that in this environment some of Trump's proposed policies regarding taxes, immigration, and tariffs could lead to even higher fiscal deficits, higher volatility, inflation, and less Fed rate cuts. Case in point, the fed fund futures market is now only pricing in 2.8 cuts by the end of 2025, down substantially from the 4.8 expected the day before the election. With fewer rate cuts in the offing, markets might be less willing to accept even further fiscal expansion, and with the introduction of sizable tariffs, yields could move sharply higher and create volatility across risk assets, in our view. When considering richly priced corporate credit valuations, this does not seem like a reach. At the very least, we should expect increased dispersion across geographies and industries within corporate credit to present some interesting opportunities (see **Exhibit 2** below).

EXHIBIT 2
US INVESTMENT GRADE SPREAD DISPERSION

Source: Bloomberg, data as of 11 November 2024.

As we have discussed in past notes, our favored valuation tools are our proprietary investment grade and high yield risk premium models, which attempt to calculate the available risk premium in markets after accounting for forward looking loss estimates. These models unfortunately continue to signal that the available premium is rather small in an historical context, and it has weakened further over the past few months, especially in high yield (Our proprietary "s curve" charts (**Exhibit 3**) suggest the probability of positive excess returns in credit over the next 6 months as 50% in IG and only 9% in high yield).

EXHIBIT 3 **HIGH YIELD RISK PREMIUM & INVESTMENT GRADE RISK PREMIUM**



Source: Loomis Sayles, data as of 31 October 2024.

There is no guarantee that the investment objective will be realized or that the strategy will generate positive or excess return. Markets may behave very differently than history suggests, and it is not possible for any methodology to accurately identify and interpret all relevant market events. There is no guarantee that investment strategies based on risk premia and related analysis will be successful.

Other valuation metrics such as 'corporate spread as a % of yield' and 'IG valuation by regime' result in a similar conclusion (please see **Exhibits 4 and 5** below).

EXHIBIT 4
BLOOMBERG BAA CORP, USD OAS AS % OF YIELD TO WORST (YTW)

Source: Bloomberg, data as of 30 September 2024.

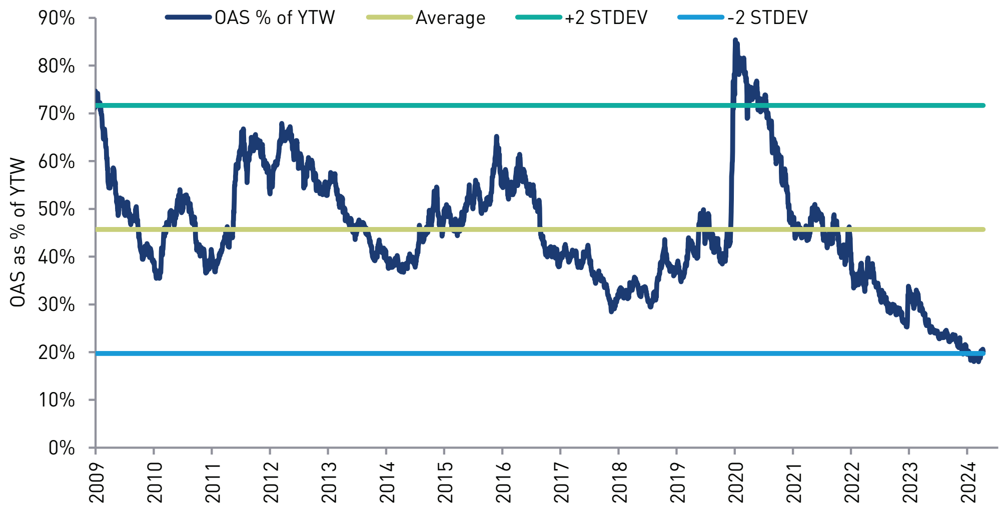
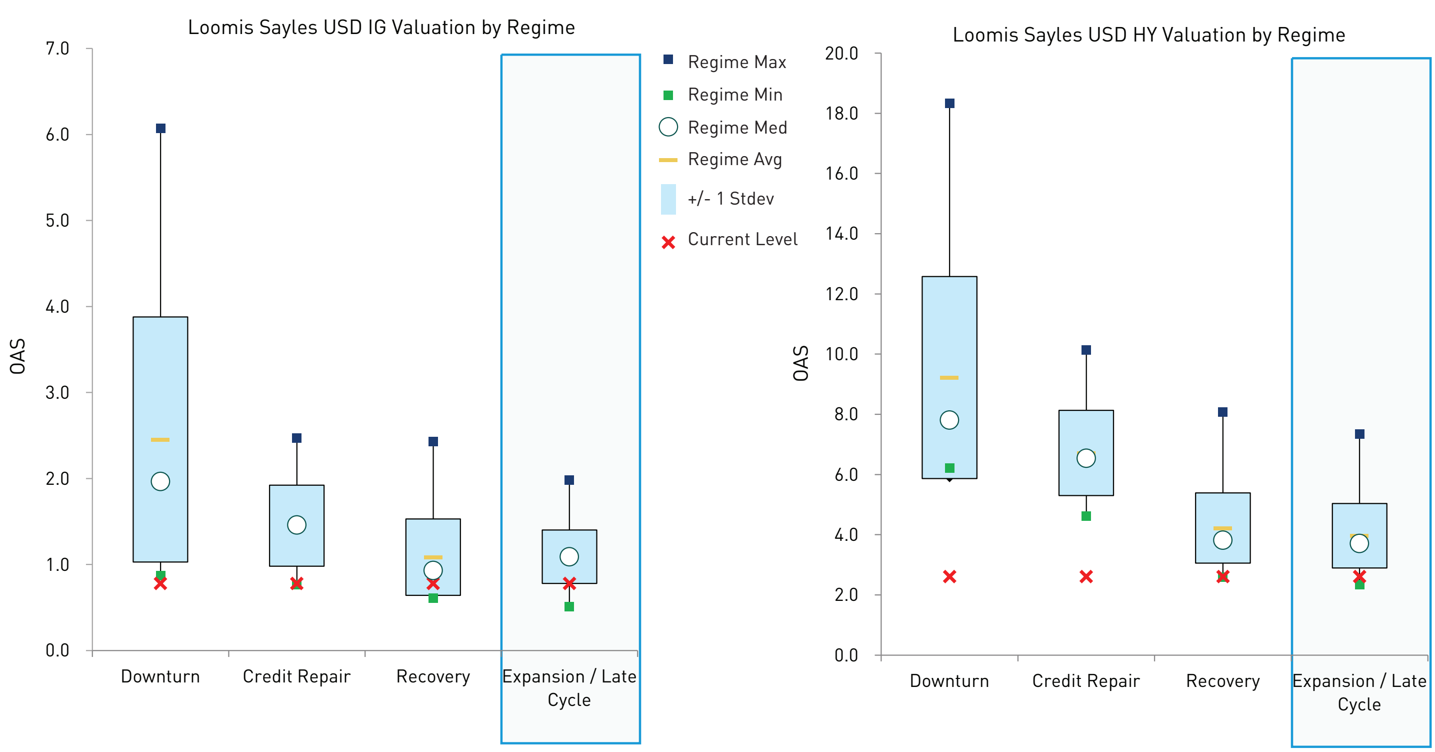


EXHIBIT 5 **LOOMIS SAYLES US DOLLAR INVESTMENT GRADE & HIGH YIELD VALUATION BY REGIME**



Source: Bloomberg, data as of 30 September 2024.
Used with permission from Bloomberg Finance L.P.

The insatiable demand for credit given the all-in yields on offer has continued to provide a strong tailwind. Couple that with the euphoria of the Trump trade and we have spreads near the tightest levels in the past 25 years. We continue to feel that this technical grab for yield has pushed corporate bond spreads tighter than fundamentals warrant. We anticipate volatility as Trump policies could disrupt the market.

AUTHOR

SCOTT SERVICE, CFA

Portfolio Manager, Co-Head of Global Fixed Income

Important Disclosures

Charts are illustrative for presentation purposes only as a sampling of risk management tool output. *Some or all of this information on these charts may be dated, and, therefore, should not be used as a basis to purchase or sell any securities. The information is not intended to represent any actual portfolio managed by Loomis Sayles.*

Indices are unmanaged and do not incur fees. It is not possible to invest directly in an index.

While the analysis provided may be shared with one or more investment teams, it is not the only input into the investment process for any strategy and therefore should not be viewed as a primary source of investment decisions, which are a function of many variables.

The analysis is based on historical data and does not predict future results. Therefore, the use of this type of information to make investment decisions has inherent limitations. There is no guarantee that future experience will be similar. The analysis reflected in this presentation is limited to certain periods. We make no representation that the experience of any other periods is comparable.

Past performance is no guarantee of future results.