

# Structured credit update

## Navigating the summer months

Over the summer months, global markets continued to grind higher thanks to supportive central bank policies, expanding vaccination programmes and economic reopening. This led to prices rallying for risk assets globally, including most structured credit products – with the exception of CLOs, where spreads widened. Alongside this fundamental picture, we have seen supply technicals play a significant role in driving spreads in the structured credit market, with opposing impact in the ABS versus CLO space.

Against this backdrop, and despite widening CLO spreads, our structured credit strategies generated positive returns. This was due to a combination of factors including:

- Our diversified positioning across product types
- Holdings in high-quality assets that have robust structural features and a better margin of safety to provide more resilient performance
- Active sourcing of mispriced opportunities in primary and secondary markets
- Portfolio re-positioning in anticipation of supply driven technicals.

As we navigated the summer months, there were two prominent themes that drove our re-positioning and positive performance.

**With prices rallying across most markets, we viewed asset valuations as stretched in some areas.**

In our view, stretched asset prices can lead to spikes in volatility. We focussed on positioning our portfolios to withstand potential volatility by increasing credit quality and diversification.

Increasing credit quality is not solely about increasing exposure to higher-rated assets, but also those with more defensive profiles and stronger structures.

For example, we took part in a UK non-conforming RMBS primary market transaction where we sourced an attractive new issue with capital appreciation potential and a defensive profile given its short-dated maturity and AAA-rating.

Elsewhere, we continued to focus on bonds with robust structures. Whilst collateral performance has generally been solid over the course of the Covid-19 pandemic, the need to focus on assets with robust structures has been imperative. In areas of weakness, such as UK SME markets, the robust structure of many of these deals led to healthy performance as transactions de-risked by diverting cash flows to senior bonds, thus providing an attractive opportunity despite weaker fundamentals.

Over the summer, US primary markets were relatively active compared to Europe, which gave us the opportunity to further increase diversification in our portfolios by adding exposure to US deals.

For example, we purchased a US data centre transaction – the first green bond in the data centre space where the issuer has been developing energy-efficient data centre technology for a decade. This new issue offers exposure to what we believe to be an exciting asset class. In addition, we purchased a mortgage insurance securitisation. This transaction not only offers exposure to the buoyant US housing market, it also increases diversification in our portfolios due to the lower correlation with other holdings.

#### AUTHORS



**Tom Mowl**  
*Portfolio Manager*



**Lucy Best**  
*Institutional Portfolio Manager*

PUBLISHED  
**September 2021**

We believe exposure to these types of assets with defensive profiles and robust structures, alongside overall diversified portfolios, should help better insulate our structured credit strategies from volatility spikes.

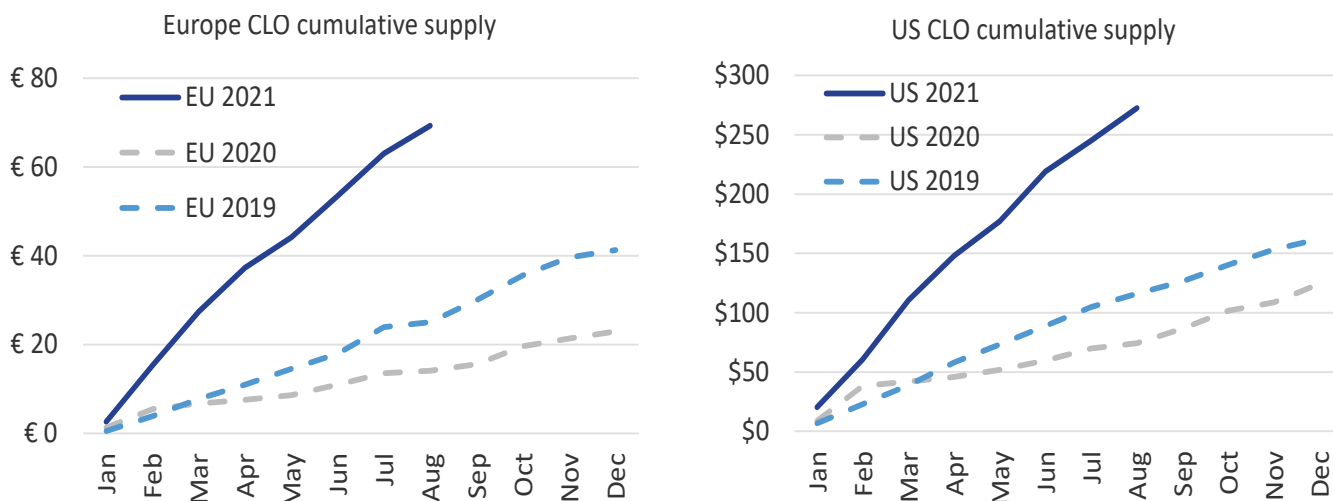
**Recent spread moves in structured credit have been driven by technicals over fundamentals during the summer months and indeed through H1 in general.**

In the ABS/RMBS markets, the relatively low supply (when compared with the strong demand) so far this year has kept spreads firm – this was particularly true in August as the market took a summer break. We were still able to selectively add value in primary and secondary markets when opportunities arose.

In the CLO market, the supply picture is quite different, with new issue, refinance and reset volumes significantly higher than in previous years (see chart 1). This heavy supply put pressure on spreads, most notably at the top of the capital structure (see chart 2).

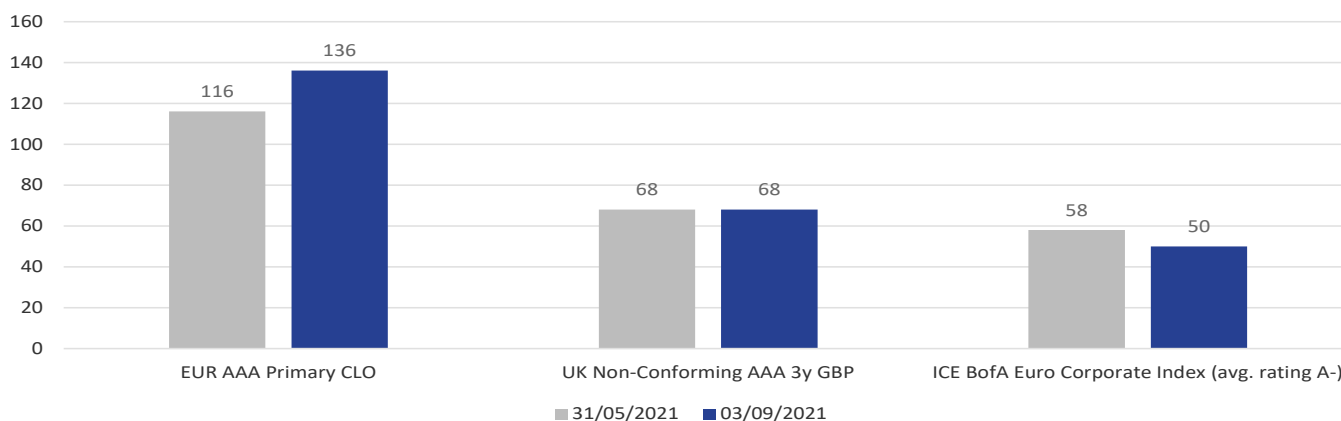
In terms of portfolio positioning, we reduced spread duration earlier this year and as higher supply led to spread widening in the new issue market, we rotated into more convex, high-grade CLO tranches whilst maintaining overall CLO exposure at the same level. This generated positive performance across portfolios and maintained our overall defensive positioning.

CHART 1: YEAR-TO-DATE SUPPLY VS. PREVIOUS YEARS



Source: LCD, as at 23 August 2021

CHART 2: HEAVY SUPPLY HAS PUT PRESSURE ON SPREADS



Source: LCD, Bloomberg, MS, Citi, BAML, as at 3 September 2021

## Outlook

As we approach the final quarter of the year, we expect the existing opportunity set to continue. ABS supply is set to pick up through September, but we believe healthy demand will absorb this new issuance and spreads will remain firm in this area. CLO supply is expected to persist at high levels, as several deals issued at wide spreads in 2020 will look to refinance over the remainder of the year, and whilst we are seeing an increase in demand, this should keep primary market spreads at relatively wide and attractive levels.

Our economic outlook is constructive, although we remain cautious entering the cooler winter period as to its impact on the spread of Covid-19. This, alongside central bank asset purchases possibly slowing in both the US and Europe, could trigger market weakness. In our structured credit portfolios, we are maintaining diversified exposure across a range of collateral types and continue to focus on high-quality assets with robust structures and defensive profiles.

This document may be produced and issued by the following entities: in the European Economic Area (EEA), by BlueBay Funds Management Company S.A. (the ManCo), which is regulated by the Commission de Surveillance du Secteur Financier (CSSF). In Germany and Italy, the ManCo is operating under a branch passport pursuant to the Undertakings for Collective Investment in Transferable Securities Directive (2009/65/EC) and the Alternative Investment Fund Managers Directive (2011/61/EU). In the United Kingdom (UK) by BlueBay Asset Management LLP (BBAM LLP), which is authorised and regulated by the UK Financial Conduct Authority (FCA), registered with the US Securities and Exchange Commission (SEC) and is a member of the National Futures Association (NFA) as authorised by the US Commodity Futures Trading Commission (CFTC). In United States, by BlueBay Asset Management USA LLC which is registered with the SEC and the NFA. In Switzerland, by BlueBay Asset Management AG where the Representative and Paying Agent is BNP Paribas Securities Services, Paris, succursale de Zurich, Selnaustrasse 16, 8002 Zurich, Switzerland. The place of performance is at the registered office of the Representative. The courts of the registered office of the Swiss representative shall have jurisdiction pertaining to claims in connection with the distribution of shares in Switzerland. The Prospectus, the Key Investor Information Documents (KIIDs), where applicable, the Articles of Incorporation and any other applicable documents required, such as the Annual or Semi-Annual Reports, may be obtained free of charge from the Representative in Switzerland. In Japan, by BlueBay Asset Management International Limited which is registered with the Kanto Local Finance Bureau of Ministry of Finance, Japan. In Australia, BlueBay is exempt from the requirement to hold an Australian financial services license under the Corporations Act in respect of financial services as it is regulated by the FCA under the laws of the UK which differ from Australian laws. In Canada, BBAM LLP is not registered under securities laws and is relying on the international dealer exemption under applicable provincial securities legislation, which permits BBAM LLP to carry out certain specified dealer activities for those Canadian residents that qualify as "a Canadian permitted client", as such term is defined under applicable securities legislation. The BlueBay group entities noted above are collectively referred to as "BlueBay" within this document. The registrations and memberships noted should not be interpreted as an endorsement or approval of BlueBay by the respective licensing or registering authorities. Unless otherwise stated, all data has been sourced by BlueBay. To the best of BlueBay's knowledge and belief this document is true and accurate at the date hereof. BlueBay makes no express or implied warranties or representations with respect to the information contained in this document and hereby expressly disclaim all warranties of accuracy, completeness or fitness for a particular purpose. Opinions and estimates constitute our judgment and are subject to change without notice. BlueBay does not provide investment or other advice and nothing in this document constitutes any advice, nor should be interpreted as such. This document does not constitute an offer to sell or the solicitation of an offer to purchase any security or investment product in any jurisdiction and is for information purposes only. This document is intended only for "professional clients" and "eligible counterparties" (as defined by the Markets in Financial Instruments Directive ("MiFID")) or in the US by "accredited investors" (as defined in the Securities Act of 1933) or "qualified purchasers" (as defined in the Investment Company Act of 1940) as applicable and should not be relied upon by any other category of customer. No part of this document may be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, in whole or in part, for any purpose in any manner without the prior written permission of BlueBay. Copyright 2021 © BlueBay, is a wholly-owned subsidiary of RBC and BBAM LLP may be considered to be related and/or connected to RBC and its other affiliates. ® Registered trademark of RBC. RBC GAM is a trademark of RBC. BlueBay Funds Management Company S.A., registered office 4, Boulevard Royal L-2449 Luxembourg, company registered in Luxembourg number B88445. BlueBay Asset Management LLP, registered office 77 Grosvenor Street, London W1K 3JR, partnership registered in England and Wales number OC370085. The term partner refers to a member of the LLP or a BlueBay employee with equivalent standing. Details of members of the BlueBay Group and further important terms which this message is subject to can be obtained at [www.bluebay.com](http://www.bluebay.com). All rights reserved.