COLUMBIA THREADNEEDLE
INVESTMENTS

Your success. Our priority.

In Credit

1 FEBRUARY 2021

David Oliphant
Executive Director,
Fixed Income

Contributors

David Oliphant
Macro / Government bonds, Investment Grade Credit

Angelina Chueh
Euro High Yield Credit, Emerging Markets

Chris Jorel
US High Yield Credit, US Leveraged Loans

Katherine Nuss
US Investment Grade Credit

Kris Moreton
Structured Credit

Justin Ong
Asian Fixed Income

Doug Rangel
Municipals

Charlotte Edwards
Responsible Investments

Jake Lunness
Commodities

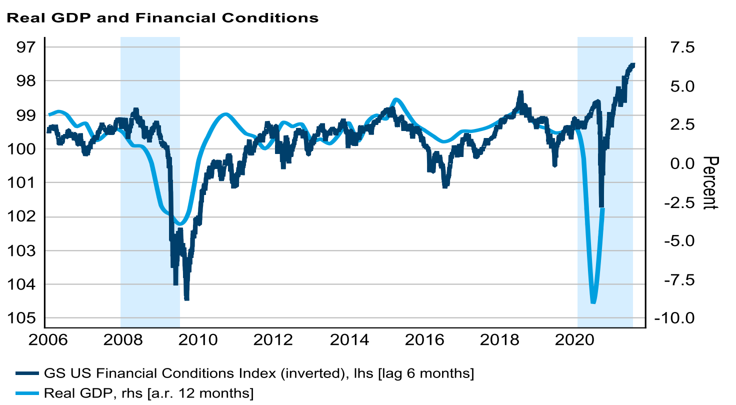
Reddit in the news.

Markets at a glance

	Price / Yield / Spread	Change 1 week	Index MTD return	Index YTD return
US Treasury 10 year	1.08%	-1 bps	-1.1%	-1.1%
German Bund 10 year	-0.51%	0 bps	-0.4%	-0.4%
UK Gilt 10 year	0.33%	2 bps	-1.8%	-1.8%
Japan 10 year	0.06%	1 bps	-0.3%	-0.3%
Global Investment Grade	103 bps	3 bps	-0.8%	-0.8%
Euro Investment Grade	94 bps	4 bps	-0.1%	-0.1%
US Investment Grade	103 bps	2 bps	-1.2%	-1.2%
UK Investment Grade	98 bps	1 bps	-0.9%	-0.9%
Asia Investment Grade	228 bps	-6 bps	0.1%	0.1%
Euro High Yield	362 bps	18 bps	0.5%	0.5%
US High Yield	384 bps	9 bps	0.4%	0.4%
Asia High Yield	581 bps	-2 bps	-0.1%	-0.1%
EM Sovereign	324 bps	-3 bps	-1.2%	-1.2%
EM Local	4.3%	-6 bps	-1.1%	-1.1%
EM Corporate	323 bps	-2 bps	-0.1%	-0.1%
Bloomberg Barclays US Munis	1.0%	-7 bps	0.6%	0.6%
Taxable Munis	2.1%	-1 bps	-0.1%	-0.1%
Bloomberg Barclays US MBS	18 bps	-3 bps	0.1%	0.1%
Bloomberg Commodity Index	173.43	1.2%	2.6%	2.6%
EUR	1.2085	-0.3%	-0.7%	-0.7%
JPY	104.95	-0.9%	-1.3%	-1.3%
GBP	1.3691	0.2%	0.3%	0.3%

Source: Bloomberg, Merrill Lynch, as at 29 January 2021.

Chart of the week: Real GDP and Financial Conditions (2006-2020)



Source: Macrobond, as at 25 January 2021.

Macro / government bonds

The trend higher in yields has paused. Inflation expectations have stopped rising in what has been thus far the theme for fixed income markets.

As mentioned, though the risk to inflation is heightened by recent US political developments it faces substantial ongoing secular forces that will we feel keep such prices rises in check. These forces include technology, demographics, deunionisation, globalisation as well as the more immediate issues that Covid-19 brings to bear. In last week's FOMC meeting. Chairman Powell was dismissive on upside inflation risk and said any pick-up would be transient. His concern is more about downside rather than upside risk; Fed support is expected to continue **(see 'chart of the week').**

Last week, there was a raft of recent economic data. This showed that the US economy expanded at an annualised rate of 4% in the last three months of 2020, which was broadly in line with expectations. Meanwhile continuing jobless claims slowed to the lowest rate since this pandemic began. The US is also having some success in rolling out vaccinations with around 9% of the population inoculated; the UK has outperformed this with around 14% of citizens inoculated.

In Europe, the roll out has been slower with disputes about supply and halted progress in a number of places. Datawise in Germany inflation rose to 1.6% y/y while the unemployment rate came in at 6%. Fourth quarter GDP data was also better than expected as was the case in Spain and France.

Investment grade credit

Corporate bond spreads have mirrored the trend in government bond yields.

So, while rates markets stabilised somewhat, credit spreads have widened somewhat in the last week. This take the global IG spread out to 103bps over government bond yields. We remain modestly constructive about the prospects for the market. This is driven more by accommodative policy conditions, better economic news, and the expectation of improving credit metrics than it is about valuations. Indeed, after the rally of the last few months spreads are through both shorter- and longer-term averages.

We are in the midst of corporate reporting season, which seems to have been constructive. Meanwhile, the primary market is expected to remain relatively light after the deluge of issuance last year.

High yield credit

US high yield bond prices declined modestly over the past week as macro uncertainties and equity volatility weighed on the market, as did the continued wave of supply. The ICE BofA US HY CP Constrained index returned -0.10% and spreads were 6bps wider. Capital markets remained active for a fourth consecutive week as issuers capitalize on historic low yields. In particular, $12.8bn priced over the week which increased January's volume to $52.5bn, making it the most active January on record. Topically, high yield investors were shielded from this week's GameStop drama as none of the issuer's outstanding bonds are large enough for index inclusion. The asset class experienced its 7th outflow over the last eight weeks with a $1.3bn withdrawal.

European High Yield (EHY) spreads widened back out (+18bps) last week as the market experienced some decompression as well as outflows (-€73m), though mainly via ETFs (-€57m). Market volatility came on the back of the equity market turmoil on heavily-shorted stocks, as well as vaccine roll-out concerns and country disputes. The primary market remained healthy for EHY with an additional €8bn of bond issuance, mainly focused on single Bs. Deals included TeamSystem (Italian IT services), THOM Europe (French jewellery), BioGroup (French labs) Assemblin (Swedish mechanics), TalkTalk, and Thames Water and were generally massively oversubscribed. This bring the year-to-date figure to €16.4bn, about 6% lower than last year.

In company specific news, Schaeffler, the German auto parts manufacturer, reported pre-released numbers showing the auto industry is doing pretty well as earnings were up 8% in Q4. Rolls Royce announced a higher than expected cash burn for 2021 at €2bn (vs. expected €1bn), with the market appearing to take the news in its stride.

Even with the recent spread widening, the market continues to display good two-way pricing. There is a sense that Covid complacency is creeping into the market as Covid names have, relatively, not underperformed as much of late. This is even in spite of the recent news flow pointing to a tougher near-term prognosis.

Leveraged loans

Leveraged loan prices were lower as well amidst equity volatility and elevated capital market activity. Leveraged loan prices decreased $0.18 to $98.11 over the past week, with the average price for BB loans decreasing $0.07 to $99.66, Single B loans decreasing $0.21 to $99.31, and Split B/CCC decreasing $0.17 to $88.91. For context, the average price of the J.P. Morgan Leveraged Loan index rose $1.17 year-to-date through 1/20 and is down $0.16 since. Primary market activity surged with the week's $40.3bn of issuance the fifth highest weekly issuance on record. Inflows continued, albeit at a declining rate, with a $740m inflow.

Structured credit

Mortgages were mixed as rates bull flattened slightly last week. Higher coupons outperformed lower coupons, and Ginnies continued to underperform conventionals with nearly every coupon lower in price despite the rally. Expectations for the Biden administration to follow through on former President Obama's 25bps reduction in the FHA's annual mortgage insurance premium are rising. A cut would reduce borrower costs for an FHA mortgage and increase the borrower's incentive to refinance. FHA mortgages have the highest delinquency rate currently at roughly 15%. Story bonds (loan balance, fico/ltv and seasoned) saw high demand as did extension protection stories.

Emerging markets

Hard currency spreads tightened in -3bps while corporate spreads tightened in only -1bps. Local returns were positive on back of FX performance. Flows remained strong into the asset class with $3.9bn of which almost 60% went into hard currency were from institutional investors.

In central banks news, Colombia and Chile, both kept rates unchanged (0.5% and 1.75%), as expected. This was even after an unexpected jump in inflation, in the case of Colombia. New issuance continues at a strong pace, from both sovereigns and corporates, from the likes of Saudi Arabia and Movida (Brazil car rentals).

In country specific news, Chinese PMI indices announced over the weekend are showing that the economic recovery is starting to lose some steam as all measurements came in lower than expected (and were already marked down from the last figures). With Chinese New Year coming up next week any improvement in the figures will have to wait. Brazil's unrest continues to grow. Brazil's transport group (National Confederation of Transport and Logistics Workers) has advised members to join the trucker strike on 1 February (the issue is the lack of a minimal freight rate, which had been agreed by the government in 2018). This comes on top of the general unrest in the country given the disappointment of how Bolsonaro and his government have been handling the pandemic.

In EM corporate specific news, Ecopetrol has offered to buy Colombia's stake in a $7.7bn utility (Interconexion Electrica or ISA). This is good news for the country as it would provide funds to reduce the country's budget deficit. Colombia has been discussing asset sales though, up to now, no action was expected until 2022, at the earliest. It should be noted that Ecopetrol is 88% owned by the government.

Asian fixed income

The People's Bank of China (PBOC) made a net liquidity withdrawal of CNY78bn on 26 January 2021 instead of making a liquidity injection that is normally expected prior to the Chinese Lunar New Year holidays (11–17 February). This raised concerns that the PBOC is embarking on a faster-than-expected tapering, which resulted in a funding squeeze through the week. While the PBOC injected CNY100bn of 7-day reverse repo to ease market anxiety, the short-term rate in China remained elevated on concerns that monetary policy could be tighter over the near term.

Ms. Gina Raimondo, the nominee for the Secretary of the US Commerce Department stated during her Senate confirmation hearing that the department will maintain a tough stance on China in the technological sector. With reference to the ongoing sanctions on Huawei, Ms. Raimondo stated that the US Administration will take measures to protect US interests from China's interference. However, she refrained from commenting whether the US Commerce Department will remove Huawei from the department's blacklist. On a related note, SEMI which is an industry association that represents companies in the electronics design and manufacturing supply chain sector, has urged the US Commerce Secretary to review the export control policy implemented by the Trump Administration. SEMI raised the request to the Biden Administration to cut down the backlog of license applications.

S&P revised the ratings outlook of Vedanta Resources Ltd (VRL) from negative to stable. VRL has announced an open offer to acquire an additional 10% in the 55%-owned Vedanta Ltd. If this transaction is successful, VRL's higher ownership in Vedanta Ltd will enhance its access to the subsidiary-level cash. This will support VRL's ability to meet is debt maturities over the next 12 to 18 months.

Commodities

The Commodity Index rallied 1.2% last week. Energy markets rose by 1.1%, with crude down a marginal 0.1%. Natural gas rallied 4.4%, partially recovering from last week's sell-off, following warmer weather forecasts.

Industrial metals declined by 2.6%. This was driven by the declining pace in China's manufacturing recovery. Zinc was the worst performer, with a 5.1% decline, high LME stockpiles (+45% on the month) were a key driver of this.

Grains rallied by a hefty 6.2% as corn surged 9.3% to 7-year highs following China's purchase of 6 million tonnes from the US, last week. Another 2 million tonnes of purchases are also expected in the near term. Wheat and soybeans also performed strongly up 4.5% and 4.4% respectively, as rains in South America are delaying harvesting.

The silver index rallied 5.3% last week following a surge in speculative buying from Reddit users. The forum's users aim to gain exposure through a silver ETF (backed by physical delivery) then forcing physical delivery of silver into the fund's vaults, subsequently triggering a short squeeze on the market. Silver, like GameStop was targeted due to the high volume of short positions in the market. The iShares Silver Trust saw just under $1bn of inflows this Friday. Gold was down -0.5% on the week.

Responsible investments

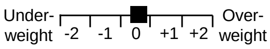
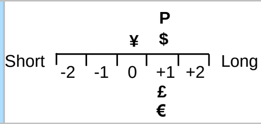
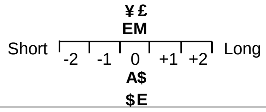
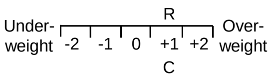
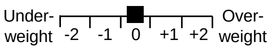
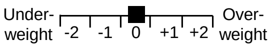
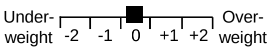
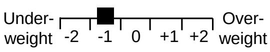
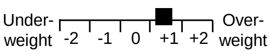
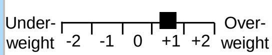
Last week President Biden self-proclaimed Wednesday (27 January) as 'Climate Day'. In his first week in office Biden has now signed more than 36 executive orders, more than any other US President in that time frame. He addressed climate change as a national priority, in line with the need to battle the pandemic. There were highlights to note in his announcement on Wednesday that have indicated the beginning of the end for the fossil-fuel era. Those include blocking funding for fossil fuel projects abroad, considering climate in federal permits (making it harder to permit fossil fuel infrastructure while making it easier to permit renewable energy projects), and most notably the order for the federal government to start buying electric cars in volume.

Other key announcements last week came from the auto sector with the likes of Volkswagen and General Motors both promising specific zero emission targets. General Motors hopes to have all its global operations and vehicles completely carbon neutral by 2040, aided by aiming to sell zero-emissions-only models by 2035. Volkswagen are working to close the gap with Tesla and aim to have 6-8% of total global sales come from its electric vehicles.

Summary of fixed income asset allocation views

Fixed Income Asset Allocation Views

1st February 2021

Strategy and positioning (relative to risk free rate)		Views	Risks to our views
Overall Fixed Income Spread Risk		▪ 2021 has started with continued positive credit performance – and not for nothing: fundamentals in 2021 should continue to improve as economic activity normalizes amid more widespread vaccination. ▪ Despite this outlook, valuations matter. Most spread sectors are well inside long-term averages. ▪ We have likely already seen peak liquidity in financial markets. We do not expect material tightening in financial conditions next year, but spreads at these levels no longer offer cushion for unforeseen hiccups. ▪ We have a modestly positive outlook but realistic returns are lower than in 2020.	▪ Moving to neutral, risks are two-sided. ▪ A recovering economy propels spreads to all-time tights. ▪ The recovery gets bungled by vaccine delays, geopolitical interruptions, or a limping back to normality in the services sector
Duration (10-year) ('P' = Periphery)		▪ Renewed virus concerns and economic disruption to keep nominal growth subdued ▪ Reflation credibility still low, although risks from fiscal policy ▪ Fed QE and high personal savings underpin demand for treasuries ▪ ECB bond buying scheme supports Eurozone market ▪ Duration remains best hedge for further risk asset correction	▪ Vaccine development pace exceeds expectations, permitting rapid normalisation ▪ Permanent fiscal policy shift rebuilds reflationary credibility ▪ Fiscal largesse steepens curves on issuance expectations ▪ Risk hedge properties deteriorate
Currency ('E' = European Economic Area)		▪ A Biden presidency should see a weaker dollar through the reduction of trade war risk premium. ▪ Longer term, expensive valuations and twin deficits presage a weaker Dollar	▪ Fiscal gridlock continues in the US, which undermines growth and risk sentiment ▪ Extension of Covid restrictions in Europe and accommodative ECB policy
Emerging Markets Local (rates (R) and currency (C))		▪ Favourable advanced economy policy settings support EM assets in near term ▪ EM real interest rates relatively attractive, curves steep	▪ Sharp escalation in global risk aversion ▪ EM funding crises drive curves higher and steeper
Emerging Markets Sovereign Credit (USD denominated)		▪ EM economies have been given very long leashes to respond to COVID: deficits and debt have skyrocketed with no plans for reigning them in. Any slowdown will likely exacerbate these 'back burner' issues. ▪ Valuations are still a slight benefit to EM, particularly EM HY credits. ▪ Low yields, lots of liquidity, and global recovery still could provide tailwinds for EM in 2021.	▪ A replay of 2013 occurs with a taper tantrum or swift appreciation of the USD ▪ Growth scars from COVID persist and hurt commodity prices & ability to grow out of deficits. ▪ Governments show little willingness to address deficits post-COVID.
Investment Grade Credit		▪ IG companies continue to adapt well to the economic environment, given that they are the best-in-class operators in their industries. ▪ Valuations are the biggest drawback: with spreads this tight, widening could very quickly more than offset carry. ▪ Technicals remain strong, especially as global investors survey the universe of high-quality assets and see extremely low government bond yields.	▪ IG bonds further cement their place in global investors' portfolios as safe assets, replacing government bonds. ▪ Management teams eschew M&A and shareholder return in order to continue to pay down debt during the recovery.
High Yield Credit		▪ Spreads are inside LT averages, even adjusting for the better quality of today's index. But higher yields give more cushion than slightly higher quality bonds. ▪ The ability to access financing has dramatically improved the prospects for many companies, especially for COVID-affected industries. ▪ The positive effects of easy financial conditions hit HY later than higher quality sectors, and tighter conditions will hit HY first.	▪ Upside risks include: intensified reach for yield keeps drawing new investors, M&A lifts HY companies into larger IG conglomerates. ▪ Downside risks include:travel & leisure habits slowly revert to pre-COVID, commodity sell-offs, or financial conditions suddenly tightening.
Agency MBS		▪ Fed buying has overwhelmed highly negative fundamentals, as seen by the near-zero spreads in bonds the Fed buys and poor performance elsewhere. ▪ Fed buying cannot be expected to increase in 2021, exposing negative fundamentals and valuations ▪ Prepays remain and will remain high, with >70% of mortgages having incentive to refinance.	▪ Housing activity slows considerably and prepays move back down to normal levels, without denting households' ability to service mortgages. ▪ The Fed maintains or increases MBS purchases next year.
Non-Agency MBS & CMBS		▪ RMBS: Housing has been a major outperformer in this recovery, as demand rises and inventory remains low. Strong household balance sheets amongst homeowners has kept fundamentals strong as well. However, many of these bonds are now call-constrained. ▪ CMBS: vaccine news reminded investors that a post-COVID world will exist, and CMBS short covering has been fast & furious.	▪ Changes in consumer behaviour in travel and retail last post-pandemic. ▪ Work From Home continues full-steam-ahead post-pandemic. ▪ Built-up savings from fiscal stimulus/enhanced unemployment benefits are drawn down and mortgage forbearance increases.
Commodities		▪ o/w Copper vs Aluminium ▪ o/w Lead vs Zinc ▪ o/w Soybeans vs Corn and Wheat ▪ o/w refining margins (o/w products, u/w Brent) ▪ u/w Sugar ▪ u/w WTI	▪ Oil production disruption

Important information: For use by Professional and/or Qualified Investors only (not to be used with or passed on to retail clients). Source for all data and information is Bloomberg as at 01.02.2021, unless otherwise stated.

The material in this publication is for information only and does not constitute an offer or solicitation of an order to buy or sell any securities or other financial instruments to anyone in any jurisdiction in which such offer is not authorised, or to provide investment advice or services. Offerings may be made only on the basis of the information disclosed in the relevant offering documents and the terms and conditions under the relevant application forms. Investment involves risk. You are advised to exercise caution in relation to this material. Please refer to the relevant offering documents for details and the risk factors. Past performance is not a guide to future performance. This is an advertising document. The value of investments and any income is not guaranteed and can go down as well as up and may be affected by exchange rate fluctuations. Your capital is at risk. This means that an investor may not get back the amount invested. The analysis included in this publication have been produced by Columbia Threadneedle Investments for its own investment management activities, may have been acted upon prior to publication and is made available here incidentally. Any opinions expressed are made as at the date of publication but are subject to change without notice and should not be seen as investment advice. Information obtained from external sources is believed to be reliable but its accuracy or completeness cannot be guaranteed. The mention of any specific shares or bonds should not be taken as a recommendation to deal. This document includes forward looking statements, including projections of future economic and financial conditions. None of Columbia Threadneedle Investments, its directors, officers or employees make any representation, warranty, guarantee, or other assurance that any of these forward looking statements will prove to be accurate. This document may not be reproduced in any form or passed on to any third party in whole or in parts without the express written permission of Columbia Threadneedle Investments. This document is not investment, legal, tax, or accounting advice. Investors should consult with their own professional advisors for advice on any investment, legal, tax, or accounting issues relating an investment with Columbia Threadneedle Investments. This document and its contents have not been reviewed by any regulatory authority.

Issued by Threadneedle Investments Singapore (Pte.) Limited ["TIS"], ARBN 600 027 414. TIS is exempt from the requirement to hold an Australian financial services licence under the Corporations Act and relies on Class Order 03/1102 in marketing and providing financial services to Australian wholesale clients as defined in Section 761G of the Corporations Act 2001. TIS is regulated in Singapore (Registration number: 201101559W) by the Monetary Authority of Singapore under the Securities and Futures Act (Chapter 289), which differ from Australian laws. Issued by Threadneedle Investments Singapore (Pte.) Limited, 3 Killiney Road, #07-07, Winsland House 1, Singapore 239519, which is regulated in Singapore by the Monetary Authority of Singapore under the Securities and Futures Act (Chapter 289). Registration number: 201101559W. This advertisement has not been reviewed by the Monetary Authority of Singapore.

Issued by Threadneedle Portfolio Services Hong Kong Limited 天利投資管理香港有限公司. Unit 3004, Two Exchange Square, 8 Connaught Place, Hong Kong, which is licensed by the Securities and Futures Commission ("SFC") to conduct Type 1 regulated activities (CE:AQA779). Registered in Hong Kong under the Companies Ordinance (Chapter 622), No. 1173058.

Issued by Threadneedle Asset Management Limited (TAML). Registered in England and Wales, Registered No. 573204, Cannon Place, 78 Cannon Street, London EC4N 6AG, United Kingdom. Authorised and regulated in the UK by the Financial Conduct Authority.

This document is distributed by Columbia Threadneedle Investments (ME) Limited, which is regulated by the Dubai Financial Services Authority (DFSA). For Distributors: This document is intended to provide distributors with information about Group products and services and is not for further distribution. For Institutional Clients: The information in this document is not intended as financial advice and is only intended for persons with appropriate investment knowledge and who meet the regulatory criteria to be classified as a Professional Client or Marketing Counterparties and no other Person should act upon it.

Columbia Threadneedle Investments is the global brand name of the Columbia and Threadneedle group of companies. columbiathreadneedle.com