

High Yield remained resilient

Rate Shock Reversed Spread Gains

Global high yield delivered a negative return in the third quarter, driven by a widening of credit spreads from 283bp to 312bp, while ongoing carry income helped absorb part of the spread widening. Spreads tightened through most of the quarter on robust fundamentals and low default rates, but widened markedly towards quarter-end as a rate shock, heavy primary supply and renewed geopolitical tension weighed on risk appetite. This resulted in a benchmark return of -2,13% in Q3 and a year-to-date return of -0,64%.

Interest rate uncertainty dominated the quarter. Early in the quarter, U.S.-Iran de-escalation and the reopening of the Strait of Hormuz briefly eased concerns over energy supply. Rising energy prices fed through to inflation expectations, particularly in Europe, where euro area inflation reached its highest level in nearly three years and expectations of further ECB hikes pushed government yields higher. In the United States, the Federal Reserve kept rates on hold, but hawkish dissent emerged within the committee under new Chair Kevin Warsh. For much of the quarter, credit proved remarkably resilient to higher rates.

Primary issuance was dominated by refinancing, with a growing share from BB-rated issuers as investors increasingly prioritized solid balance sheets. That resilience broke as the U.S. 10-year Treasury yield rose above 5% for the first time since 2007 and Brent crude surged following attacks on Saudi energy facilities. Together, these moves made unexpected monetary tightening the dominant concern for credit markets. Heavy new issuance and outflows from high yield funds added to the pressure. U.S. spreads widened more than European spreads, and stress was concentrated among the lowest-rated issuers, with U.S. CCC spreads crossing 1,000bp for the first time since March 2023. With rates at elevated levels, refinancing has become the primary credit risk, raising the importance of active credit selection.

Regional Tilt and Quality Delivered

The portfolio delivered a return of -1,57% after costs in Q3, which was 0.56 percentage points ahead of the benchmark. Year-to-date, the portfolio has returned -0,94% after costs, 0.30 percentage points behind the benchmark.

Relative performance was primarily driven by regional allocation and credit quality. The underweight in U.S. high yield and the overweight in European high yield contributed positively, as European spreads proved more resilient. The overweight in Nordic high yield added further, as the region held up well during the late-quarter widening. The underweight in CCC-rated issuers was a meaningful contributor, as stress centered on the lowest-rated issuers with elevated refinancing risk. Financials also added value. AT1 bonds and banks were supported by solid capitalization and higher net interest income, while debt collection companies continued to improve collections.

At the sector level, the underweight in energy weighed on relative performance, as higher oil prices supported earnings outlooks and credit spreads across the sector. A significant share of the energy issuers in the benchmark is excluded under the fund's ESG criteria, so the portfolio did not fully participate in the sector's strength. The underweight in communications contributed positively, while materials and mining holdings gave a mixed contribution over the quarter.

Throughout the quarter, the portfolio maintained a disciplined approach focused on companies with robust balance sheets and stable earnings, which provided resilience during the sell-off. With government yields at elevated levels and refinancing risk rising, the portfolio remains defensively positioned. It keeps an underweight in the lowest-rated segment, a preference for European and Nordic high yield over U.S. high yield, and a continued emphasis on issuer selection based on fundamental credit analysis.

Strategy

Ethical High Yield Value Bonds invests in global corporate bonds, cf. the fund's prospectus. Bond selection is based on the value approach, meaning that the team focuses on bonds issued by companies with healthy long-term earnings power and strong balance sheets as well as an expected ability to service outstanding debt. The portfolio is diversified across sectors, regions and credit ratings. At least 2/3 of the portfolio are invested in High Yield bonds. Up to 15% may be invested in corporate bonds issued by companies operating in Emerging Markets.

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