Credit Markets Face Headwinds

The market

The European credit market faced a challenging third quarter of 2026. Credit spreads widened across both investment grade and high yield segments following the significant spread tightening observed during the second quarter.

The escalation of the conflict between the United States and Iran led to higher oil and gas prices, increasing inflationary pressures and prompting the ECB to further tighten monetary policy. As a result, European government bond yields moved sharply higher, with the yield on the 10-year German government bond rising by more than 70 basis points.

At the same time, economic growth prospects were dampened by higher energy costs and tighter financial conditions. Nevertheless, economic indicators continued to show surprisingly resilient performance.

Corporate bond supply was solid in the third quarter with record high levels of issuance in what is generally a quiet summer period. Net issuance was also positive.

The quarter was therefore characterized by rising interest rates and wider credit spreads, while the European economy continued to demonstrate greater resilience than initially feared.

The portfolio

Portfolio returns were negative in the third quarter.

The negative return was driven by a combination of wider credit spreads and higher government bond yields. The ongoing coupon income provided some offset, but it was insufficient to fully compensate for the losses.

BBB-rated bonds were the best-performing rating segment during the quarter. Their lower duration relative to higher-rated bonds provided some protection against the sharp rise in government bond yields. More broadly, changes in government bond yields were the primary driver of performance during the third quarter, leading shorter-duration bonds to outperform.

Within financials, subordinated debt delivered stronger returns than senior debt, supported by investors' continued appetite for spread products despite the broader market weakness.

The Investment Grade funds delivered negative excess returns relative to their benchmarks during the third quarter of 2026.

The funds' negative excess returns relative to their benchmarks can primarily be attributed to an overweight position in the utilities and financial sectors.

While an overweight to financial companies contributed negatively to returns, the security selection within the sector contributed positively with an overweight to shorter dated subordinated capital instruments.

Participation in new bond issues also contributed positively to performance.

The outlook for corporate bonds remains constructive at the beginning of the fourth quarter. Following the rise in government bond yields and the widening of credit spreads during the third quarter, all-in yields have increased to levels not seen since the summer of 2024.

Higher yields also improve reinvestment opportunities as coupons are received and bonds mature. Combined with resilient corporate fundamentals and supportive technical conditions, the higher yield environment provides a more attractive starting point for future returns.

Strategy

Responsible Corporate Bonds invest in global companies. The bonds are selected from companies with stability or improvement in their creditworthiness and have attractive loan terms. These are good and solid companies with a mature business model and a strong market position. The financial profile is characterized by moderate indebtedness and stable cash flow generation. The investment strategy is based on disciplined risk management with prudent risk diversification across sectors, credit ratings, types of debt, regions, and maturities.

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