Global Fixed Income Perspectives

Brandywine GLOBAL
A Franklin Templeton Company

Global Market Outlook

- Inflation globally continues to move in a direction that markets are comfortable with while growth has moderated, allowing central bankers in the developed world to embark on a rate-cutting cycle.
- Investors continue to grapple with the direction of global economies as the debate intensifies over the relative strength of the US versus growth expectations for Europe and Asia. Despite the debate, the global economy appears to be normalizing from the dislocations experienced in the post-2020 landscape.
- US elections and Chinese policy responses will drive much of the story as we look forward to the balance of 2024 and will set the tone for 2025. Given the unexpected turns to date, one should not be surprised by the unexpected.

About this Publication

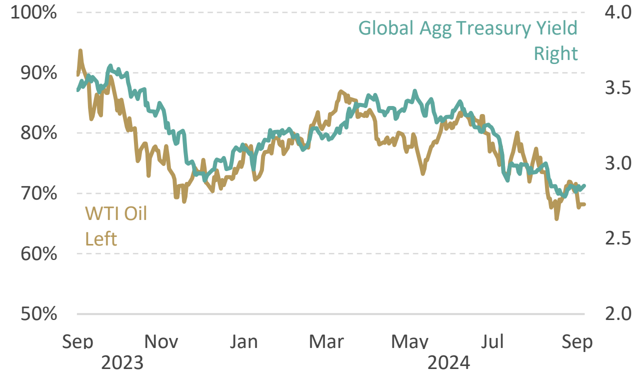
The Global Fixed Income Perspectives discusses performance and opportunities for global fixed income markets by segment.

DM	Developed Market Rates	Few indicators have been as accurate in predicting interest rates as oil prices. During the quarter, oil prices reached a three-year low, with sovereign yields following the same downward trajectory. We expect this relationships between oil prices and yields to continue.
HY	High Yield	While the high yield index has produced impressive year-to-date returns, we see no reason for the asset class to stop here. While we anticipate some moderation in US growth, we remain constructive and expect high yield to continue its positive momentum.
IG	Investment Grade	US IG spreads are near their tights for the year, while European IG spreads are closer to their median. With much of this dispersion now priced in and a potentially more accommodative European Central Bank (ECB) compared with the Federal Reserve (Fed), total returns in European IG credit may outperform US IG credit.
SP	Securitized Products	Securitized spreads have generally converged to fair value in wake of the Fed's interest rate cut. Some sectors still offer value, but we are mindful of risks. We remain constructive on segments of CRT, CLO, ABS, and CMBS ex office.
EM	Emerging Markets	Chinese policymakers were reluctant to embrace aggressive demand stimulus measures. That changed toward the end of September, with coordinated announcements. This development should be bullish for emerging markets sensitive to global growth and bearish for USD more broadly.

DM Developed Market Rates

- Oil prices hit a year-to-date high of $87 per barrel on April 5, falling over 20% since that time. Global sovereign yields, represented by the Global Treasury Index, reached a year-to-date high a month later in late May. Oil's influence on US rates is more pronounced, with 10-year Treasuries tracking oil prices closely (see FIGURE 1).
- While the copper/gold ratio has traditionally been used to gauge the balance between economic growth and safe-haven assets, oil has been a more accurate predictor this year. The decline in oil prices corresponded with a dampening of headline inflation and inflation expectations.
- Several factors influence oil prices, but this year, supply-side forces like OPEC policies and geopolitical events have played a secondary role. Instead, concerns over slower economic growth have been the primary driver pushing prices lower.
- Recently, oil prices appear to have stabilized and may trade range bound through the end of the year. In response, Brandywine Global has adopted a more neutral stance on duration across developed markets.

1 Global Sovereign Yields vs. Oil
As of 9/30/2024



Source: Bloomberg (© 2024, Bloomberg Finance LP)

HY High Yield

- High yield continues to be the best performing fixed income asset class year to date, returning just under 10% (see FIGURE 2). Over the previous two-year period, the index has generated just under 28% total returns. We see this largely as a reflection of a resilient
US economy and US consumer. While we anticipate some moderation in U.S. growth, we remain constructive and expect high yield to continue its positive momentum (see FIGURE 3).
- The high yield new issue market continues to see demand outpace supply, even with year-to-date issuance already higher than either of the previous two years. Investors have been quick to absorb new paper, even as new issue concessions dwindle toward zero. High yield corporate fundamentals like leverage and interest coverage remain in "normal" zones, and with the US economy still growing at roughly 3% annually, investors still feel comfortable allocating to high yield.
- In the short term, we do not see any reason for this trend to reverse. The US seems to be on a path for a soft-landing scenario where inflation has been tamed without material damage to labor or growth dynamics domestically. Absent material weakness from the demand side of the US labor market, we continue to favor allocations to shorter-dated high yield.

2 US High Yield Index - YTW
As of 9/30/2024

Source: Bloomberg (© 2024, Bloomberg Finance LP)

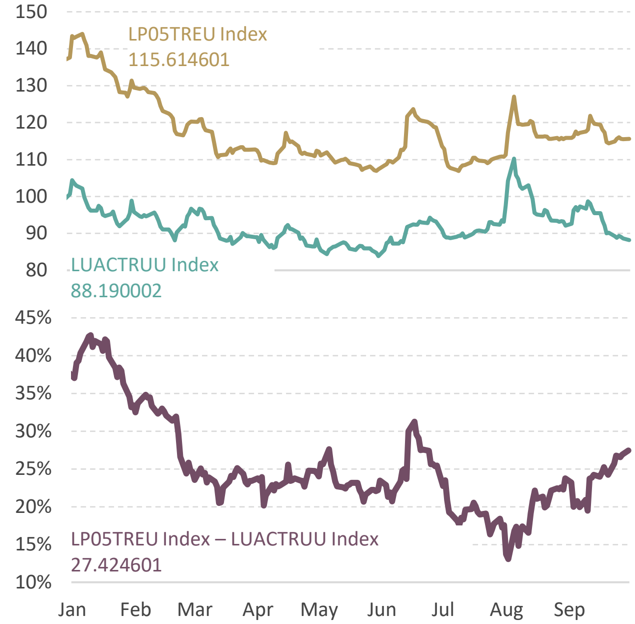
3 US High Yield Index - OAS
As of 9/30/2024

Source: Bloomberg (© 2024, Bloomberg Finance LP)

IG Investment Grade

- US Investment Grade credit spreads are approaching their tightest levels of the year, 88 basis points (bps), as the economic data looks adequate and the Fed starts on a rate cutting path (see FIGURE 4).
- European investment grade credit is trading at 116 bps, well within its median range for the year. However, Euro IG has lagged due to a) slower relative growth in Europe; b) sectoral weakness in autos after profit warnings from key players (automakers make up 6.5% of the Euro index vs. 2.4% of the US index); and c) wider OAT-Bund spreads, driven by political uncertainty in France.
- While many of the drivers of this relative weakness may already be priced in, there are still cyclical factors that could support Euro IG outperformance.
- Europe is more likely to benefit from China's stimulus measures than the US. Weaker growth across the region leaves more room for additional monetary stimulus from the ECB along with Germany, France, and Spain. The ECB has taken a more proactive stance compared with previous cycles. In a low growth, low inflation environment yields may face downward pressure, helping total returns. Additionally, recent profit warnings may serve as a final wake up call for Europe to respond with stronger state support, production subsidies, or consumer incentives.

4 US vs. European IG Corporate Spreads
As of 9/30/2024, in Basis Points (bps)

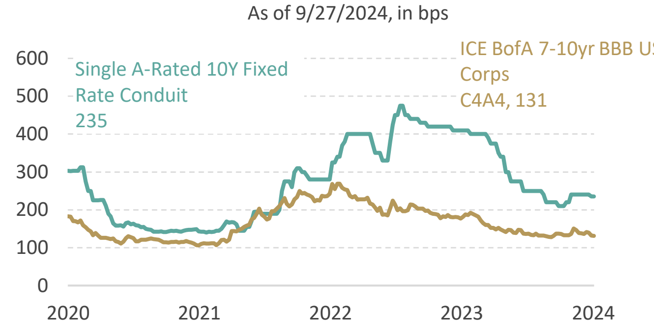


Source: Bloomberg (© 2024, Bloomberg Finance LP)

SP Securitized Products

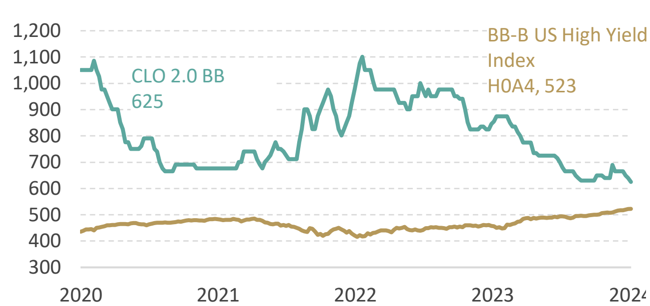
- Credit-risk transfer (CRT) securities are performing well despite increased delinquencies in recent vintages. GSE tenders and low new issuance are helpful technicals, and we expect these positive trends to continue.
- Commercial mortgage-backed securities (CMBS) should see better fundamentals amid lower interest rates but significant risks remain for office properties. We are constructive on select AAA to A rated notes (see FIGURE 5).
- Collateralized loan obligation (CLO) BBBs and BBs offer attractive yields, but with risks of credit downgrades and defaults. Lower interest rates and benign economic data should support further performance (see FIGURE 6).
- Asset-backed securities (ABS) remain attractive with short durations as structural de-levering outpaces delinquencies. We see value in some subprime auto, whole business, data center, and fiber ABS from established issuers.

5 A-Rated CMBS vs. BBB-Rated Corporate Credit Spreads to US Treasuries
As of 9/27/2024, in bps



Source: ICE Data Indices, LLC., BofA Global Research

6 CLO 2.0 BB Spreads vs. BB-B US High Yield Index
As of 09/27/2024, in bps



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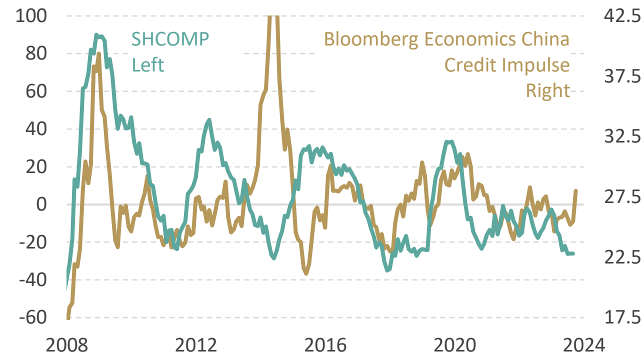
EM Emerging Markets Debt

- Following the Fed kicking off its monetary easing in September, China surprised investors with a broad-based economic stimulus program announced at the end of the quarter. Although China still faces significant structural issues, we believe stimulus measures can generate a cyclical uplift. This development should be bullish for emerging markets sensitive to global growth and bearish for USD more broadly. So far, the impact on Chinese equities has been clear, but we will be closely watching the credit impulse over the coming months to assess market impact (see FIGURE 7).
- The start of the Fed cutting cycle gives other EM central banks the green light to start cutting rates (see FIGURE 8). Markets will be watching the new Mexican president to see the policy direction she will take and whether her noted pragmatism will instill confidence. In Asia, a massive unwinding of US dollar carry trades has led to rallies in otherwise lower beta markets.
- Over the coming months, the US elections and China's growth will be critical for EM markets. China's policymakers now embrace coordinated stimulus aimed at boosting consumption, real estate, and government spending.

7 Credit Impulse (6m Lead) and SHCOMP Equity Index

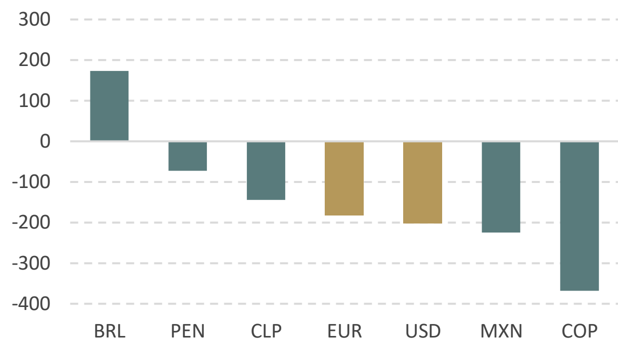
As of 2/2025, 9/2024, %yoy chg (left), % of GDP (right)



Source: Brandywine Global, Macrobond, Bloomberg (© 2024, Bloomberg Finance LP)

8 Latam Central Bank Estimated Hikes/Cuts

As of 9/30/2024, bps



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All investments involve risks, including possible loss of principal. Please note that an investor cannot invest directly in an index. Unmanaged index returns do not reflect any fees, expenses or sales charges. Past performance is no guarantee of future results.

Fixed income securities involve interest rate, credit, inflation and reinvestment risks; and possible loss of principal. As interest rates rise, the value of fixed income securities falls.

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Sovereign debt securities are subject to various risks in addition to those relating to debt securities and foreign securities generally, including, but not limited to, the risk that a governmental entity may be unwilling or unable to pay interest and repay principal on its sovereign debt. To the extent a strategy focuses on particular countries, regions, industries, sectors or types of investment from time to time, it may be subject to greater risks of adverse developments in such areas of focus than a strategy that invests in a wider variety of countries, regions, industries, sectors or investments.

The government's participation in the economy is still high and, therefore, **investments in China** will be subject to larger regulatory risk levels compared to many other countries.

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