

# Credit Outlook 2023

## Guillaume Desqueyroux, Fund Manager

2022 has been a torrid year for risk assets where quite a few certainties have been more than challenged or simply written off. "Doubt is not a pleasant condition, but certainty is absurd" as cold-blooded Voltaire reminds us.

While recession is already/nearly here in the UK/Europe, it still seems premature in my opinion to extend into too much duration. You do not want to fight the Fed too early either. While I'm cognisant that the front end of the yield curve will keep bearing the pressure of any remaining hikes, the strong pick-up you can get in the short part of the curve justifies the risk. There are two ways to view the credit markets for next year, each with their own compelling arguments.

For those who see the glass half empty, the Budget in November has confirmed the astronomical level of Gilts to be issued by the UK government despite the various fiscal measures. You can also add the negative technical of quantitative tightening (QT), where the BoE keeps selling corporate bonds. The former pushing risk-free rates higher, the latter widening the spread. And a similar pattern can be defined for the ECB and various governments, where central bankers will gradually test the markets for QT.

If you see the glass half full, you will point out the current valuations reflecting the already higher rates and spreads represent a great opportunity to lock in impressive yields while reallocating your portfolio from riskier/uncertain assets. The flow dynamics will have to adjust to the new risk appetite given the now sizeable carry from bonds.

When focusing on fundamental research, it is important to assess the key features of a company and its potential resilience through this tough environment. Are any doubts justified or could the company even benefit from this market? Strong candidates will have a robust balance sheet and most importantly, multiple entry points in the value chain:

A diversified but also limited dependency to third-party suppliers are qualitative features that should not be overlooked. For companies that didn't fix issues in previous years, the problems may build up. 2023 is expected to be a year of more normalised defaults given the perfect recipe of a recessionary environment and higher refinancing costs for companies.

At the sector level, I think that fundamentals for financials are very appealing. While I am comfortable with their capital strength and the tailwind of higher rates, this naturally raises questions on the ability of debtors to repay loans in a cost-of-living crisis. One key area where this could become an issue is the UK mortgage market. After relatively low fixed rate periods start to end, borrowers will be exposed to significantly higher floating rates. Recent and future rate hikes will impact a third of borrowers year after year on average. This raises legitimate doubts regarding available income to repay any debt. However, the UK's decade of sluggish productivity growth may be the silver lining that keeps unemployment down over the next 18 months and keep incomes being paid. Real wages have stagnated (or fallen) and so human capital still remains relatively cheap for businesses.

Finally, financial rigor is the new motto and governments are not expected to be as interventionist as during the pandemic. Having said that, it would not be implausible for them to reconsider fiscal measures to protect consumers, borrowers, workers and companies in times of stress. To some extent, it has already started across the continent (nationalisation, mortgage aids, tax windshields, etc.) to smooth some of the recession on the horizon. So, while certainty is never certain, I remain positive that 2023 will present opportunities and unique investment ideas as we move through the year.

## Important information

### **This document is marketing material.**

The fund will invest in debt securities. The government or company issuer of a bond might not be able to repay either the interest or the original loan amount and therefore default on the debt. This would affect the credit rating of the bond and, in turn, the value of the fund. Investment in bonds and other debt instruments (including related derivatives) is subject to interest rate risk. If long-term interest rates rise, the value of your shares is likely to fall. The Fund may engage in transactions in financial derivative instruments for hedging purposes only. There is a risk that losses could be made on derivative positions or that the counterparties could fail to complete on transactions.

The value of this portfolio is subject to fluctuation and past performance is not necessarily a guide to future performance. The performance is calculated for the portfolio and the actual individual investor performance will

differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. All terms exclude costs. Fluctuations or movements in exchange rates may cause the value of underlying investments to go up or down. Do remember that the value of participatory interests or the investment and the income generated from them may go down as well as up and is not guaranteed, therefore, you may not get back the amount originally invested and potentially risk total loss of capital. Therefore, the Manager does not provide any guarantee either with respect to the capital or the return of a portfolio. The Manager has the right to close any Portfolios to new investors to manage them more efficiently in accordance with their mandates. Collective Investment Schemes are traded at ruling prices and can engage in borrowing and scrip lending. Collective Investment Schemes (CIS) are generally medium to long term investments. A schedule of fees and charges and maximum commissions is available on request free of charge from [sanlam.co.uk](http://sanlam.co.uk). A full summary of investor rights can be obtained from <https://www.linkgroup.eu/policy-statements/irish-management-company/>. Document is provided in English.

This document is marketing material. Issued and approved by Sanlam Investments which is authorised and regulated by the Financial Conduct Authority (FRN 459237), having its registered office at 24 Monument Street, London, EC3R 8AJ. The UCITS Management Company has the right to terminate the arrangements made for the marketing of funds in accordance with the UCITS Directive.

Tideway UCITS Fund ICAV an Irish collective asset-management vehicle registered under the laws of Ireland having its registered office at 1st Floor, 2 Grand Canal Square, Grand Canal Harbour Dublin 2, Ireland. The ICAV is an umbrella type Irish collective asset-management vehicle with segregated liability between funds incorporated under the Irish Collective Asset-management Vehicles Act 2015 of Ireland and authorised by the Central Bank of Ireland. The Fund Manager is Link Fund Solutions (Ireland) Limited a company incorporated under the laws of Ireland having its registered office at 1st Floor, 2 Grand Canal Square, Grand Canal Harbour, Dublin 2, Ireland which is authorised by the Central Bank of Ireland. Link Fund Solutions (Ireland) Limited has appointed Sanlam Investments UK Ltd as Investment Manager to this fund.

This document is provided to give an indication of the investment and does not constitute an offer/invitation to sell or buy any securities in any fund managed by us nor a solicitation to purchase securities in any company or investment product. It does not form part of any contract for the sale or purchase of any investment. The information contained in this document is for guidance only and does not constitute financial advice.

The fund price is calculated on a net asset value basis, which is the total value of all assets in the portfolio including any income and expense accruals. Trail commission and incentives may be paid and are for the account of the manager. Performance figures quoted are from Sanlam and are shown net of fees. Performance figures for periods longer than 12 months are annualized. NAV to NAV figures are used. Calculations are based on a lump sum investment.

Please note that all Sanlam Funds carry some degree of risks which may have an adverse effect on the future value of your investment. Any offering is made only pursuant to the relevant offering document, together with the current financial statements of the relevant fund, and the relevant subscription/application forms, all of which must be read in their entirety together with the Fund prospectus, the Fund supplement and the KIID. All these documents explain different types of specific risks associated with the investment portfolio of each of our products and are available free of charge from [sanlam.co.uk](http://sanlam.co.uk). No offer to purchase securities will be made or accepted prior to receipt by the offeree of these documents, and the completion of all appropriate documentation. Use or rely on this information at your own risk. Independent professional financial advice should always be sought before making an investment decision as not all investments are suitable for all investors.

This document contains information intended only for the person to whom it is addressed or presented (Investment Professionals, defined as Eligible Counterparties or Professional Clients), and is intended for evaluation purposes, with no licence to use the content or materials within. It must not be distributed to general public, or relied upon by Retail Investors.

The opinions are those of the author at the time of publication and are subject to change, without notice, at any time due to changes in market or economic conditions. Whilst care has been taken in compiling the content of this document, neither Sanlam nor any other person makes any guarantee, representation or warranty, express or implied as to its accuracy, completeness or fairness of the information and opinions contained in this document, which has been prepared in good faith, and to the fullest extent permissible under UK law. Some parts/sections of this document may have been compiled from external sources. Whilst these sources are believed to be reliable, the information has not been independently verified and is subject to material amendment, revision and updating, therefore no representation is made as to its accuracy or completeness. No reliance may be placed for any purpose whatsoever on the information, representations or opinions contained in this document nor shall it or any part of it form the basis of or act as an inducement to enter into any contract for any securities, and to the fullest extent permissible under UK law no liability is accepted or any such information, representations or opinions. The comments should not be construed as a recommendation of individual holdings or market sectors, but as an illustration of broader themes.

Statements in this document that reflect projections or expectations of future financial or economic performance of a strategy, or of markets in general, and statements of any Sanlam strategies' plans and objectives for future operations are forward-looking statements. Actual results or events may differ materially from those projected,

estimated, assumed or anticipated in any such forward-looking statement. Important factors that could result in such differences, in addition to the other factors noted with forward-looking statements, include general economic conditions such as inflation, recession and interest rates, political or business conditions or in the tax or regulatory framework in the UK or other relevant jurisdictions, any of which could cause actual results to vary materially from the future results implied in such forward-looking statements. No assurance can be given as to the future results that will be achieved. All of the information herein should be treated as confidential material with no less care than that afforded to the addressee's own confidential material of the most sensitive nature.

Sanlam funds mentioned in this document are only available for sale in certain jurisdictions. For the avoidance of doubt, this document is not intended to promote these Funds to any person in any jurisdiction where such promotion is not permitted under applicable laws and regulations. Potential investors should inform themselves of the applicable laws and regulations of the countries of their citizenship, residence or domicile and which might be relevant to any type of transaction in shares/units of our Funds. By accepting the terms of this disclaimer, you expressly acknowledge that you are, as the case may be, an investor who is legally or otherwise duly authorised to seek information about our Funds.