



# Exploring a Multi-Asset Credit (MAC) Allocation

A MAC strategy may have benefits in a volatile, low-yield world.

September 2020

## KEY INSIGHTS

- The longer-term goal of MAC portfolios is harnessing attractive opportunities across global fixed income credit sectors and instruments.
- MAC portfolios have the potential to capture alpha through sector rotation and security selection as well as diversification as part of a broader portfolio.
- We believe that MAC portfolios should not simply invest in the highest-yielding opportunities but should focus on harnessing credit market inefficiencies.

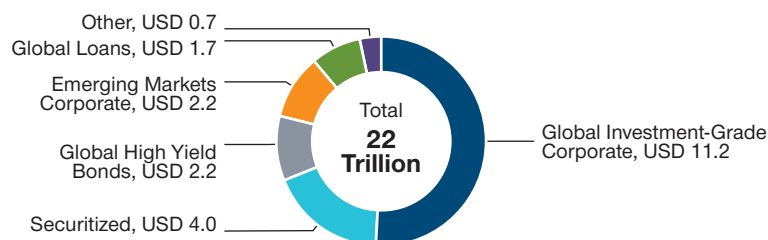
The market turmoil of March 2020 demonstrated that volatility often creates market inefficiencies, and harnessing these dislocations in credit markets requires a combination of tactical and demonstrated global analytical capabilities. While many of the initial market dislocations generated by the onset of the

coronavirus pandemic have dissipated, we anticipate that the ongoing volatility and uncertainty will create longer-term opportunities for multi-asset credit (MAC) investors.

MAC portfolios can offer the potential to capture alpha<sup>1</sup> through sector rotation and security selection as well

## Global Credit Opportunity Set

(Fig. 1) Credit segment size, in USD trillion



As of June 30, 2020.

Sources: Credit Suisse, J.P. Morgan, and Bloomberg Barclays (see Additional Disclosures).

<sup>1</sup> Alpha is the excess return of an investment relative to its benchmark.



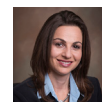
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# USD 22 trillion

Size of investible universe for MAC portfolios

as diversification<sup>2</sup> benefits as part of a broader portfolio. MAC portfolios can be designed to pursue various return and risk objectives for adroit managers who have the depth and breadth of global credit capabilities. In the current volatile, low-yield fixed income environment, investors may benefit from a more opportunistic, dislocation-oriented MAC portfolio in terms of risk level.

The investible universe for MAC portfolios is about USD 22 trillion across the range of global credit sectors, providing the flexibility to make sizable, high-conviction allocations to sectors that offer value relative to other segments, or that appear to have prices that do not align with their fundamentals.

## **Search for Total Return and Income in Low-Yield Environment**

With interest rates likely to remain at low levels for the foreseeable future, the search for total return and income from a fixed income allocation has become a top priority for many investors. MAC strategies that allow investors to target higher fixed income returns with lower volatility—albeit with higher credit risk—are in demand. The unprecedented amount of global stimulus in response to the pandemic will likely affect different credit sectors, industries, and issuers in different ways, creating an ideal environment for a strategy designed to harness dislocations.

## **Sector-Specific Knowledge Is Essential**

The key for pursuing alpha in a MAC portfolio is expertise in fixed income sectors, such as high yield, leveraged loans, investment-grade corporate, securitized,<sup>3</sup> convertible, and emerging markets credit securities. A MAC portfolio requires strong, fundamental credit analysis for effective security selection within the sectors, allowing managers to recognize and have

exposure to names that are priced inefficiently. Particularly when investing in high yield, emerging market, and securitized sectors, we believe rigorous credit analysis is essential for selecting credits that are more likely to avoid default over the investment time horizon.

Sector-specific knowledge is also essential for recognizing dislocations and relative value among those segments. This allows MAC portfolio managers to tactically rotate exposures to credit sectors that are dislocated or that offer compelling relative value or attractive absolute value as markets fluctuate.

Robust quantitative capabilities are a key component of MAC portfolio efficiency enhancement. Tools such as quantitative analysis across various market scenarios can create more risk-aware portfolio construction, assist portfolio managers with timely sector shifts, and keep overall portfolio risk within desired parameters.

## **MAC Return Objective**

Typically, the longer-term goal of MAC portfolios is aiming to harvest attractive risk-adjusted returns across a range of fixed income credit markets and instruments. In the current environment of elevated volatility and dislocations across sectors, we believe that MAC portfolios may have the potential to deliver equity-like returns with lower volatility.

The T. Rowe Price Dynamic Credit Fund is an example of a MAC strategy. In our MAC portfolios, we do not simply invest in the highest-yielding—and riskiest—sectors and issuers. Rather, we focus on finding and harnessing inefficiencies across credit markets that ultimately can deliver more optimal outcomes. T. Rowe Price already offers strategies specializing in key credit sectors, giving us the ability to leverage our extensive

<sup>2</sup> Diversification cannot assure a profit or protect against loss in a declining market.

<sup>3</sup> Securitized credit includes non-agency mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), asset-backed securities (ABS), collateralized loan obligations (CLOs), and enhanced equipment trust certificates (EETCs).

experience in credit and equity analysis to manage portfolios across sectors and regions.

### **Close Collaboration Characterizes T. Rowe Price MAC Capability**

T. Rowe Price's global fundamental research platform is at the core of our MAC capability. The close collaboration among T. Rowe Price's global credit, equity, and quantitative analysts enables our MAC capabilities to try to take advantage of credit market dislocations like those created by the market turmoil in March 2020. We empower and encourage our analysts to think as investors and to provide conviction ratings on their ideas.

We believe that there are two key components of MAC alpha generation. The first is credit selection at the issue level. The second is the flexibility

to rotate among credit sectors and subsectors to source relative value opportunities while also providing portfolio diversification benefits.

### **Extensive Application of Quantitative Tools**

The MAC team and our credit analysts work closely with our quantitative analysts, using proprietary tools to screen for relative value at the sector, industry, rating class, issuer, and security levels. The quantitative team also provides insight for enhancing optimal sector allocations and general portfolio construction, including developing return and risk expectations, measuring factor exposures, creating risk scenarios, and assessing portfolio liquidity. This work is also essential to portfolio risk management.

Look for our upcoming series of monthly Insights detailing our views on particular credit sectors.

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