Mixed US Job

- US jobs beat while unemployment rate little changed and far from the Fed's target, curve moderately flattened
- a bird's-eye view on each sub-asset class as we close 1H21
- credit vol remains subdued and correlation has finally stepped down

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Table 1: Weekly performance overview

		Change			
	02-Jul-21	1 Week	2 Weeks	1 Month	YTD
EUR IG Corp spread (bp)	83	0	0	-2	-9
BBB	95	0	0	-2	-13
IG-ex BBB	32	-1	-2	1	2
EUR HY Corp spread (bp)	294	-12	1	1	-64
BB	218	7	6	-1	-38
Capital Structure spread (bp)					
Bank AT1	310	7	-4	-10	-92
Bank Tier 2	116	0	-1	-4	-17
Corporate Hybrids	198	6	0	-7	-23
Sub Insurance	152	1	-2	-4	-23
ETF Total return					
EUR IG ETF (IEAC LN)		0.4%	0.2%	0.4%	-0.4%
EUR HY ETF (IHYG LN)		0.1%	0.0%	0.3%	2.2%
USD IG ETF (IEAC LN)		0.9%	0.2%	2.2%	-1.6%
USD HY ETF (IHYG LN)		0.5%	1.1%	1.3%	3.0%
***Cape Fixed Income Fund (EUR B Inst.)**		0.0%	0.1%	0.4%	1.3%
***Cape Fixed Income Fund (USD B Inst.)**		0.0%	0.1%	0.5%	1.7%

* as of July 1st 2021

		Change			
	02-Jul-21	1 Week	2 Weeks	1 Month	YTD
iTraxx Europe OTR (5 year, bp)*					
Main	46	0	-3	-4	-10
Xover	227	1	-13	-17	-47
Snr Fin	53	0	-3	-4	-13
Sub Fin	100	0	-7	-7	-25
CDX OTR (5 year, bp)*					
CDX IG	47	0	-4	-3	-9
CDX HY	269	-1	-18	-15	-24
Govt. bond yield (bp)					
10 year US yield	142	-10	-1	-16	51
10 year Bund yield	-24	-8	-3	-4	34
10 year Gilt yield	70	-8	-5	-10	51
10 year BTP yield	77	-15	-10	-11	23
BTP - Bund spread	101	-7	-7	-7	-11

*since index roll

Source: Bloomberg, Bloomberg Barclays, Markit as of July 2nd 2021

Our weekly publication will take a break and return end August. A big thank you to all our readers for the past 1H21 and see you soon.

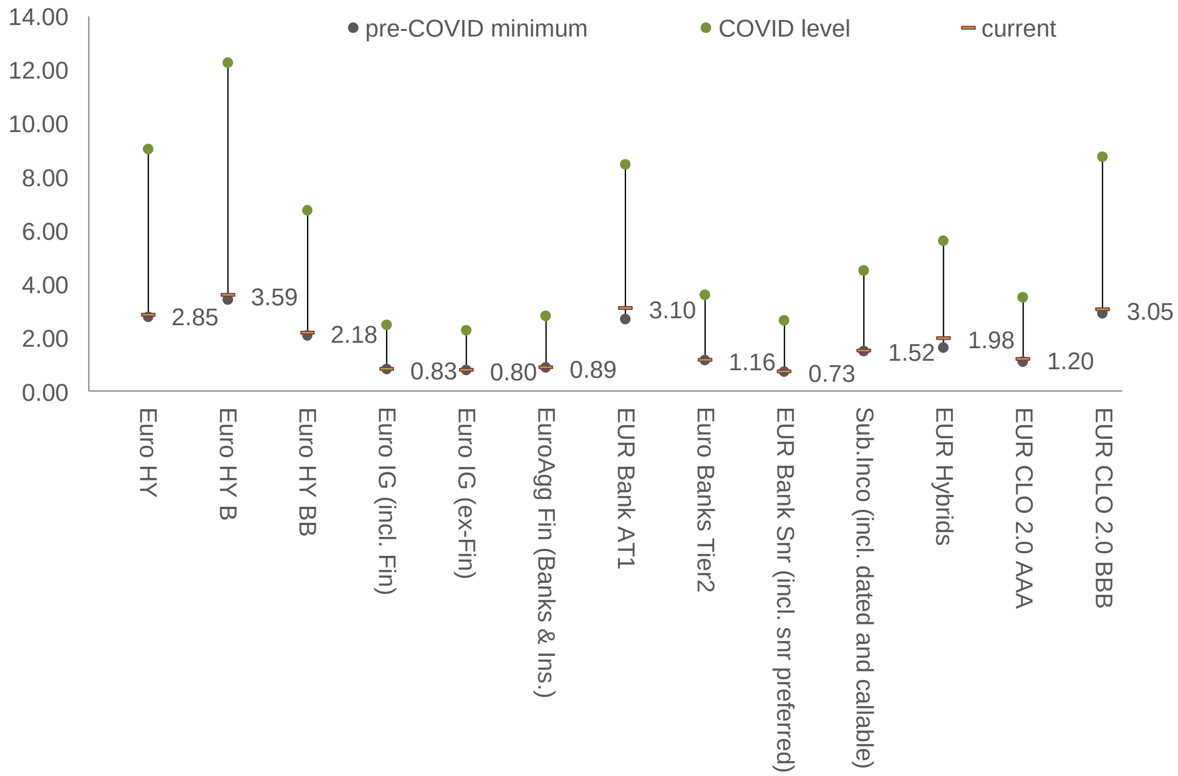
The US has added another 850k payrolls in June, coming mainly from the leisure and hospitality as well as education sector as a result of the re-opening. Regardless the beat, the survey also showed that the unemployment rate stood at 5.9%, little changed compared to January (at 6.3%) despite the significant progress in the vaccination rollout. Similarly, momentum in labor participation remains muted and well below the pre-COVID level. While this may be to a certain extent undermined by the ongoing unemployment benefits which will end in the coming months, it could also mean that there's still enduring slack in the labor market to reach the Fed's full employment target. The USD curve has moderately flattened on the data release with the 10yr now sitting slightly above 1.4%.

Since the overall spread moves were unspectacular over the week, we would give **a bird's-eye view on each sub-asset class to show where they stand as we close 1H21** (**Chart 1**). Overall Bank AT1s currently stand around a yield to call of 2.8% in EUR and 3.3% in USD. The asset class has been fast-moving for the past 2 weeks and has finally slowed down last week. Valuation on a yield basis is now inside the pre-COVID level while spread hovers around 40bps above pre-COVID level, giving some breathing room for rate movements should yield refuses to go tighter. Corporate Hybrids has been trading range-bound around 200bps in spread terms, though the Hybrid to Senior ratio remains reluctantly above its long-term average. YTD supply has been above historical trend across the universe, which has limited the secondary curve tightening potential so far, and this should be less of a concern into 2H. Sub-insurance trades around 150bps, relatively underperforming Bank Tier 2 which trades below 120bps (and inside its pre-COVID level). The relationship between the sub-insurance and the Bank Tier 2 (in both spread ratio and absolute spread differential) points to a stronger case for the prior, especially if rates curve flattening is here to stay (given that the insurance sector has a higher duration due to the nature of its liability exposure). On the senior side, the generic corporate senior bonds, as repeatedly mentioned, have limited spread tightening potential ahead and benchmark products remain in the negative territory YTD in total return terms due to the adverse impact coming from rates exposure. Therefore, different from the rest of the segments, credit selection becomes the key for performance in this area. Lastly, leveraged loans and CLOs remain "overweight" by managers with a more flexible mandate given its decent carry and limited rate risk. Current EUR AAA tranches are around 100bps and BBBs at 300bps, which screens attractive vs. some of the high beta financial debt. As liquidity is seasonally thin in summer, and since valuations are mostly tight and macro / policy news rather calm on the horizon, we think the generic spread will linger around their current level for the summer break.

A quick update on the credit derivatives market (which gives us a perspective from implied vol and correlation). **In short, reminiscent to the equity market, credit vol remains subdued and correlation has finally stepped down.** On the vol front, as uncertainty wanes both on the vaccine side and on the rates vol side (at least temporarily), both realized and implied vol have collapsed (**Chart 2&3**), suggesting an uneventful summer. On the correlation side, as discussed couple of weeks back, credit correlation has reached all time highs during the pandemic given elevated systemic risks. While still elevated in the historical context, this measure has finally peaked and came down (**Chart 4**) as the economy reopens and the level of idiosyncratic risk slowly takes over, an environment we like as it is beneficial to active non-benchmarked strategy.

Chart 1: bird's-eye view on each sub-asset class

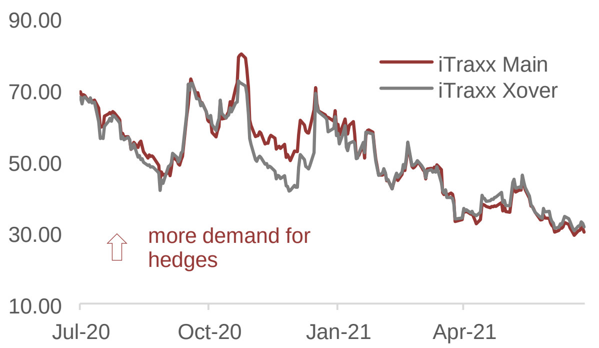
Bloomberg Barclays index, spread, in %



Source: Bloomberg as of July 2nd 2021

Chart 2: credit implied vol collapsed in EUR credit

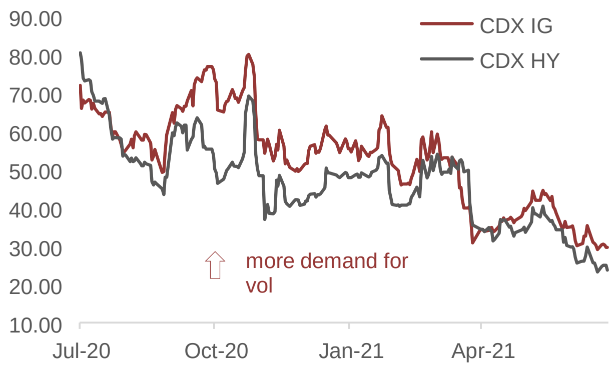
EUR IG and EUR HY CDS, implied vol, At the money, 1-month



Source: Citi velocity as of July 2nd 2021

Chart 3: … as well as in USD credit

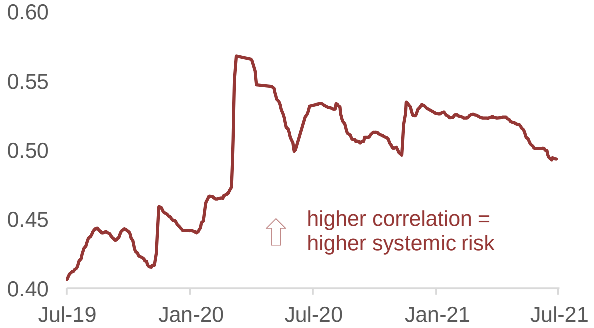
USD IG and USD HY CDS, implied vol, At the money, 1-month



Source: Citi velocity as of July 2nd 2021

Chart 4: credit correlation finally came down as systemic risk wanes

EUR IG CDS (iTraxx Main 5yr equity tranche), implied correlations



Source: Bloomberg as of July 2nd 2021

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