PARTNERS CAPITAL

Insights 2023

Asset Class Investment Strategies

Liquid Credit

Major Trends

Credit yields repriced sharply higher in 2022: Due to a combination of rising rates and wider spreads, yields moved significantly higher across liquid credit last year. US high yield finished 2022 with a yield of 9.0%, more than double the yield of 4.2% at the end of 2021. Leveraged loans finished the year with a yield of 10.8%, compared to just 5.3% a year prior.[1]

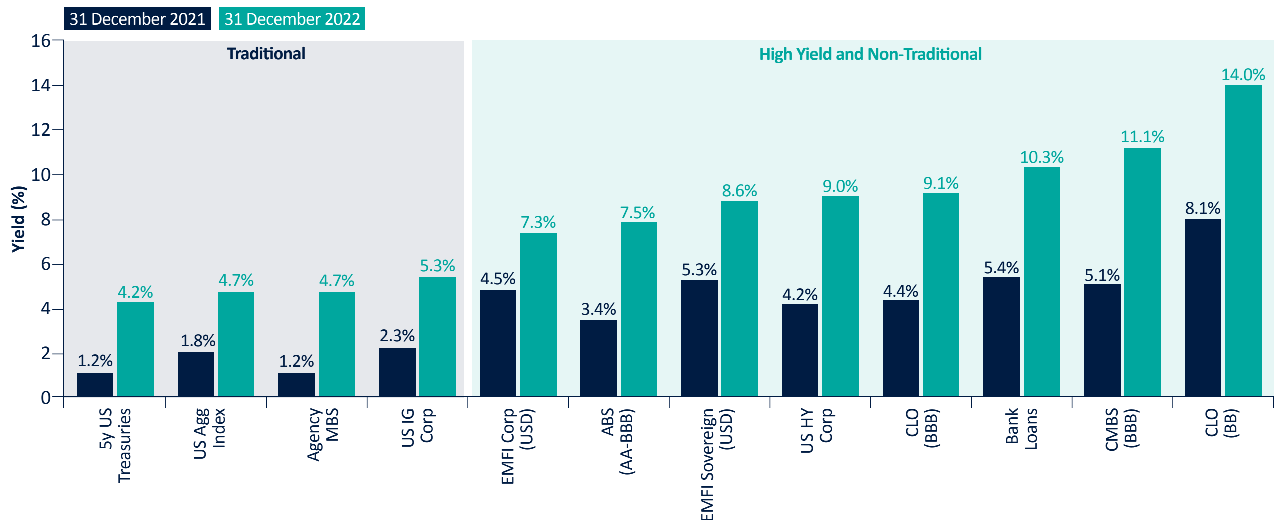
Potential rise in default rates: While default rates remained low in 2022 at just 1.7% for high yield bonds and 1.6% for leveraged loans,[2] we expect default rates to increase modestly to 3-5% in 2023 due to softening growth and rising interest rates. We anticipate that defaults may continue to rise throughout 2024, as they often lag the economic cycle. As a result, we are focusing investments in those areas of the credit market that we believe to be best insulated from higher defaults.

Higher yields provide resiliency to market stress: The Barclays Aggregate Bond Index had its first instance on record of two consecutive negative years in 2021-2022 (data dating back to 1976), and its worst single calendar year of performance in 2022. Historically, the index has produced positive returns in 16 of 21 years that the US 10-year yield increased, with the additional yield from interest rate increases overcoming the negative price impact on bonds.

Golden Rules

- Use a bottom-up approach to identify attractively valued sub-sectors over the economic cycle
- Employ a dynamic approach to asset allocation, as sub-sector selection is a significant driver of returns and market pricing can change quickly
- Partner with specialists with deep knowledge of a sub-sector's credit fundamentals, market technicals and legal documentation
- Focus on niche, capacity constrained sub-sectors marked by complexity to uncover additional value
- Use custom vehicles where appropriate to maximise flexibility and allow for control of sub-sector exposures

Exhibit 1
Higher Yields Across Liquid Credit



***Source:** Barclays, DoubleLine*

1 Yields quoted based on Barclays US Corporate High Yield Index yield-to-worst, and Credit Suisse Leveraged Loan Index yield-to-3-year-call
2 Default Rates. Source: JP Morgan, as of Dec 2022, includes distressed exchanges

Sub-Strategy Attractiveness

Residential Mortgage Bonds: Positive view. We are focused on seasoned non-agency bonds in this sector. While US home prices have come off their peak and may face modest declines in the coming months, the Case-Shiller Home Price Index is still 41% higher than in January 2020,[3] which provides significant cushion for seasoned residential mortgage loans against further economic weakness.

Opportunistic / Event Driven Credit: Positive view. While outright distressed activity remains low, access to credit markets was limited in 2022 and that will likely persist into 2023. An increasing number of stressed issuers should lead to a strong opportunity set for opportunistic lenders, as more companies will need to address their challenged capital structures.

CLO Debt: Positive view. We see attractive value in mezzanine CLO debt. The BB index is trading at an average dollar price of 85 and a 14.0% yield-to-maturity, while the BBB index has an average price of 91 and a yield-to-maturity of 9.2%.[4] The structural subordination within these CLO tranches provides resilience against impairment outside of extreme scenarios, though we expect some degree of mark-to-market volatility in the interim.

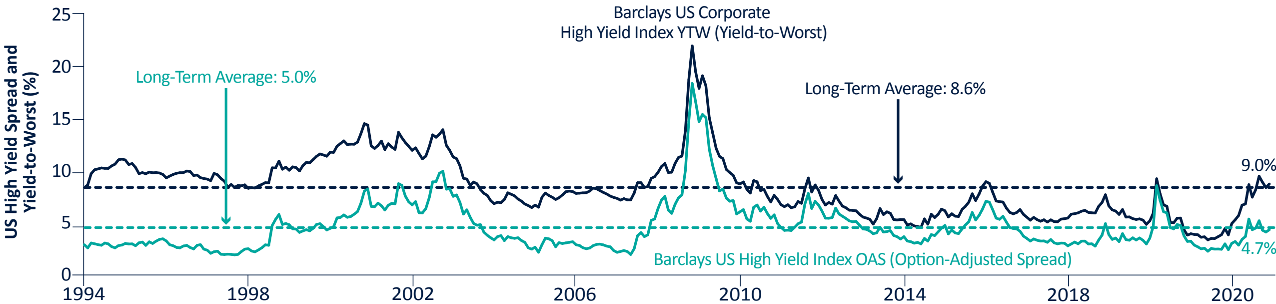
High Yield: Neutral view. Corporate credit spreads have widened far less than structured credit. While we are constructive on high yield total returns given the higher starting yields, we believe there are relatively more attractive risk-adjusted opportunities elsewhere in credit markets.

Leveraged Loans: Neutral view. We were positioned overweight in floating rate leveraged loans going into 2022, which insulated our portfolios from the rise in rates, as loans declined -1% over the calendar year while US and Global high yield indices were down -11%.[5] However, this year we have shifted to a neutral view due to concerns about fundamental trends in the loan market and an expectation that interest rates will not rise beyond what is priced in the forward market.

Emerging Market Debt: Neutral view, which may turn positive over the course of the year. We closely monitored emerging market debt in 2022, evaluating opportunities in areas of potential value such as distressed Chinese real estate debt. To date, we have refrained from making outright long investments in EM debt but will continue to monitor for opportunities in the new year.

Exhibit 2

High Yield Pricing Roughly At Long-Term Average



***Source:** Bloomberg, Barclays*

3. Home Price. Data Source: S&P Dow Jones and St. Louis Federal Reserve, latest data point as of October 2022
4. CLO Data. Source: JP Morgan CLOIE Indices, as of December 31, 2022
5. Leveraged Loan and High Yield Index. Source: Bloomberg, Barclays. Leveraged Loan performance based on Credit Suisse Leveraged Loan Index. High Yield performance based on Barclays US and Global High Yield indices.

Liquid Credit
continued

Asset-Backed Securities: Mixed view. We are positive on the outlook for aviation securities, which we expect to recover as travel activity rebounds further internationally. We are more cautious on domestic, consumer and auto loans, as consumers may come under pressure with rising costs and a weak economy.

Commercial Real Estate Credit: Neutral view. Some segments of commercial real estate face challenging fundamental trends, most notably retail. However, we see attractive value in niche lending situations, particularly in sectors with more favorable backdrops such as multi-family.

2023 Strategic Priorities

- **Position in higher-quality assets:** Our current preference is for securities with structural credit enhancement, avoiding subordinated or first-loss exposures. Where no structural credit enhancement is available, we have focused on higher-quality fundamental profiles that we believe are resilient to weakness in corporate credit markets. In order to shape our exposures, we utilise customised fund-of-one vehicles that allow us to directly influence allocations across credit sectors.
- **Exploit opportunity set in structured credit:** While corporate credit realised negative performance in 2022, spread widening was relatively modest compared to areas of structured credit. We now see attractive yields relative to the fundamental risk in areas such as RMBS, CLO debt, and aviation, which we access through strategic asset manager partnerships.
- **Prepare for upcoming stressed and distressed opportunities:** The opportunity set for distressed investing has been limited over the past five years, with the exception of a brief spike in defaults related to Covid. While our macroeconomic base case is not for a severe recession, we expect defaults to increase over the coming 12-24 months and are preparing to increase our exposure to stressed and distressed credit if the opportunity presents itself.
- **Continued focus on emerging managers:** We actively seek out early-stage managers where we can negotiate terms, structure customised vehicles with increased control and transparency, and access niche or capacity constrained strategies. In 2022 we invested in an emerging long/short credit fund and a new launch multi-strategy credit fund with a focus on convertibles. Both produced strong performance for the year.

Long-Term Expected Return

Exhibit 3

Based on our 10 year forecasts, we target the following long-term expected returns for Liquid Credit

	Liquid Credit
Risk-free Rate	3.5%
Risk Premium	3.0%
Illiquidity Premium	–
Manager Alpha	1.0%
Total Return	**7.5%**

The beta return of 6.5% for Liquid Credit represents coupon income of 8.9% p.a. on average over the next 10 years, with 4.0% annual defaults at 40% recovery rate detracting -2.4%.

Hypothetical return expectations do not represent actual trading and are based on simulations with forward looking assumptions, which have inherent limitations. No representation is being made that any investor will or is likely to achieve returns similar to those shown. Such forecasts are not a reliable indicator of future performance.

Your capital is at risk and you may not get back the full amount invested.

DISCLAIMER

Copyright © 2023, Partners Capital Investment Group LLP

Within the United Kingdom, this material has been issued by Partners Capital LLP, which is authorised and regulated by the Financial Conduct Authority of the United Kingdom (the "FCA"), and constitutes a financial promotion for the purposes of the rules of the Financial Conduct Authority. Within Hong Kong, this material has been issued by Partners Capital Asia Limited, which is licensed by the Securities and Futures Commission in Hong Kong (the "SFC") to provide Types 1 and 4 services to professional investors only. Within Singapore, this material has been issued by Partners Capital Investment Group (Asia) Pte Ltd, which is regulated by the Monetary Authority of Singapore as a holder of a Capital Markets Services licence for Fund Management under the Securities and Futures Act and as an exempt financial adviser. Within France, this material has been issued by Partners Capital Europe SAS, which is regulated by the Autorité des Marchés Financiers (the "AMF").

For all other locations, this material has been issued by Partners Capital Investment Group, LLP which is registered as an Investment Adviser with the US Securities and Exchange Commission (the "SEC") and as a commodity trading adviser and commodity pool operator with the Commodity Futures Trading Commission ("CFTC") and is a member of the National Future's Association (the "NFA").

This material is being provided to clients, potential clients and other interested parties (collectively "clients") of Partners Capital LLP, Partners Capital Asia Limited, Partners Capital Investment Group (Asia) Pte Ltd, Partners Capital Europe SAS and Partners Capital Investment Group, LLP (the "Group") on the condition that it will not form a primary basis for any investment decision by, or on behalf of the clients or potential clients and that the Group shall not be a fiduciary or adviser with respect to recipients on the basis of this material alone. These materials and any related documentation provided herewith is given on a confidential basis. This material is not intended for public use or distribution. It is the responsibility of every person reading this material to satisfy himself or herself as to the full observance of any laws of any relevant jurisdiction applicable to such person, including obtaining any governmental or other consent which may be required or observing any other formality which needs to be observed in such jurisdiction. The investment concepts referenced in this material may be unsuitable for investors depending on their specific investment objectives and financial position.

This material is for your private information, and we are not soliciting any action based upon it. This report is not an offer to sell or the solicitation of an offer to buy any investment. While all the information prepared in this material is believed to be accurate, the Group, may have relied on information obtained from third parties and makes no warranty as to the completeness or accuracy of information obtained from such third parties, nor can it accept responsibility for errors of such third parties, appearing in this material. The source for all figures included in this material is Partners Capital Investment Group, LLP, unless stated otherwise. Opinions expressed are our current opinions as of the date appearing on this material only. We do not undertake to update the information discussed in this material. We and our affiliates, officers, directors, managing directors, and employees, including persons involved in the preparation or issuance of this material may, from time to time, have long or short positions in, and buy and sell, the securities, or derivatives thereof, of any companies or funds mentioned herein.

Whilst every effort is made to ensure that the information provided to clients is accurate and up to date, some of the information may be rendered inaccurate by changes in applicable laws and regulations. For example, the levels and bases of taxation may change at any time. Any reference to taxation relies upon information currently in force. Tax treatment depends upon the individual circumstances of each client and may be subject to change in the future. The Group is not a tax adviser and clients should seek independent professional advice on all tax matters.

Within the United Kingdom, and where this material refers to or describes an unregulated collective investment scheme (a "UCIS"), the communication of this material is made only to and/or is directed only at persons who are of a kind to whom a UCIS may lawfully be promoted by a person authorised under the Financial Services and Markets Act 2000 (the "FSMA") by virtue of Section 238(6) of the FSMA and the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (including other persons who are authorised under the FSMA, certain persons having professional experience of participating in unrecognised collective investment schemes, high net worth companies, high net worth unincorporated associations or partnerships, the trustees of high value trusts and certified sophisticated investors) or Section 4.12 of the FCA's Conduct of Business Sourcebook ("COBS") (including persons who are professional clients or eligible counterparties for the purposes of COBS). This material is exempt from the scheme promotion restriction (in Section 238 of the FSMA) on the communication of invitations or inducements to participate in a UCIS on the grounds that it is being issued to and/or directed at only the types of person referred to above. Interests in any UCIS referred to or described in this material are only available to such persons and this material must not be relied or acted upon by any other persons.

Within Hong Kong, where this material refers to or describes an unauthorised collective investment schemes (including a fund) ("CIS"), the communication of this material is made only to and/or is directed only at professional investors who are of a kind to whom an unauthorised CIS may lawfully be promoted by Partners Capital Asia Limited under the

Hong Kong applicable laws and regulation to institutional professional investors as defined in paragraph (a) to (i) under Part 1 of Schedule to the Securities and Futures Ordinance ("SFO") and high net worth professional investors falling under paragraph (j) of the definition of "professional investor" in Part 1 of Schedule 1 to the SFO with the net worth or portfolio threshold prescribed by Section 3 of the Securities and Futures (Professional Investor) Rules (the "Professional Investors").

Within Singapore, where this material refers to or describes an unauthorised collective investment schemes (including a fund) ("CIS"), the communication of this material is made only to and/or is directed only at persons who are of a kind to whom an unauthorised CIS may lawfully be promoted by Partners Capital Investment Group (Asia) Pte Ltd under the Singapore applicable laws and regulation (including accredited investors or institutional investors as defined in Section 4A of the Securities and Futures Act).

Within France, where this material refers to or describes to unregulated or undeclared collective investment schemes (CIS) or unregulated or undeclared alternative Investment Funds (AIF), the communication of this material is made only to and/or is directed only at persons who are of a kind to whom an unregulated or undeclared CIS or an unregulated or undeclared AIF may lawfully be promoted by Partners Capital Europe under the French applicable laws and regulation, including professional clients or equivalent, as defined in Article D533-11, D533-11-1, and D533-13 of the French Monetary and Financial Code.

Certain aspects of the investment strategies described in this presentation may from time to time include commodity interests as defined under applicable law. Within the United States of America, pursuant to an exemption from the US Commodity Futures Trading Commission (CFTC) in connection with accounts of qualified eligible clients, this brochure is not required to be, and has not been filed with the CFTC. The CFTC does not pass upon the merits of participating in a trading program or upon the adequacy or accuracy of commodity trading advisor disclosure. Consequently, the CFTC has not reviewed or approved this trading program or this brochure. In order to qualify as a certified sophisticated investor a person must (i) have a certificate in writing or other legible form signed by an authorised person to the effect that he is sufficiently knowledgeable to understand the risks associated with participating in unrecognised collective investment schemes and (ii) have signed, within the last 12 months, a statement in a prescribed form declaring, amongst other things, that he qualifies as a sophisticated investor in relation to such investments.

This material may contain hypothetical or simulated performance results which have certain inherent limitations. Unlike an actual performance record, simulated results do not represent actual trading. Also, since the trades have not actually been executed, the results may have under- or over-compensated for the impact, if any, of certain market factors, such as lack of liquidity. Simulated trading programs in general are also subject to the fact that they are designed with the benefit of hindsight. No representation is being made that any client will or is likely to achieve profits or losses similar to those shown. These results are simulated and may be presented gross or net of management fees. This material may include indications of past performance of investments or asset classes that are presented gross and net of fees. Gross performance results are presented before Partners Capital management and performance fees, but net of underlying manager fees. Net performance results include the deduction of Partners Capital management and performance fees, and of underlying manager fees. Partners Capital fees will vary depending on individual client fee arrangements. Gross and net returns assume the reinvestment of dividends, interest, income and earnings.

The information contained herein has neither been reviewed nor approved by the referenced funds or investment managers. Past performance is not a reliable indicator and is no guarantee of future results. Investment returns will fluctuate with market conditions and every investment has the potential for loss as well as profit. The value of investments may fall as well as rise and investors may not get back the amount invested. Forecasts are not a reliable indicator of future performance.

Certain information presented herein constitutes "forward-looking statements" which can be identified by the use of forward-looking terminology such as "may", "will", "should", "expect", "anticipate", "project", "continue" or "believe" or the negatives thereof or other variations thereon or comparable terminology. Any projections, market outlooks or estimates in this material are forward –looking statements and are based upon assumptions Partners Capital believe to be reasonable. Due to various risks and uncertainties, actual market events, opportunities or results or strategies may differ significantly and materially from those reflected in or contemplated by such forward-looking statements. There is no assurance or guarantee that any such projections, outlooks or assumptions will occur.

Certain transactions, including those involving futures, options, and high yield securities, give rise to substantial risk and are not suitable for all investors. The investments described herein are speculative, involve significant risk and are suitable only for investors of substantial net worth who are willing and have the financial capacity to purchase a high risk investment which may not provide any immediate cash return and may result in the loss of all or a substantial part of their investment. An investor should be able to bear the complete loss in connection with any investment.

All securities investments risk the loss of some or all of your capital and certain investments, including those involving futures, options, forwards and high yield securities, give rise to substantial risk and are not suitable for all investors.