

The Quarterly Big MAC Letter

Multi Asset Credit Outlook

Overview

- Markets are transitioning from beta-driven returns to dispersion-driven alpha, as volatility exposes underlying fundamental dispersion.
- Refinancing risk is rising as higher base rates, wider spreads and thinner equity cushions pressure weaker, highly levered issuers.
- We favor B-rated corporates across high-yield bonds and leveraged loans, alongside CLO mezzanine, where default-adjusted spreads remain attractive.

Market Backdrop

Recent escalation in the Middle East has disrupted shipping through the Strait of Hormuz, driving volatility in energy markets. While oil futures curves still point to some normalization, the Strait remains disrupted. The net effect is a near-term inflationary shock and a drag on growth, with the outlook sensitive to the duration of disruptions and uncertainty.

The European Central Bank has framed this dynamic through a baseline and two energy shock scenarios; adverse and severe. Current conditions suggest the euro area sits between the baseline and adverse scenarios, while the severe tail risk remains relevant given the potential for more persistent inflation. Even in the severe case, euro area growth remains positive, supported by domestic demand and fiscal spending in infrastructure and defense. GDP growth is projected at 0.9% in 2026 and 1.3% in 2027, compared to 0.6% / 1.2% in the adverse scenario and 0.4% / 0.9% in the severe case.

In the baseline, HICP remains above target in 2026 (2.6%) before normalizing toward 2% in 2027. The adverse case implies a temporary spike (averaging 3.5% in 2026) before easing. By contrast, the severe scenario reflects persistent second-round effects, with inflation averaging 4.4% in 2026 and remaining elevated at 4.8% in 2027 before moderating to 2.8% in 2028.

In the US, the macro impact is expected to be more contained, forecasters estimate a growth drag of around 0.5%, driven by higher energy prices and uncertainty. However, underlying fundamentals remain resilient. Labor markets continue to hold up, with unemployment around 4.3% and limited signs of deterioration.

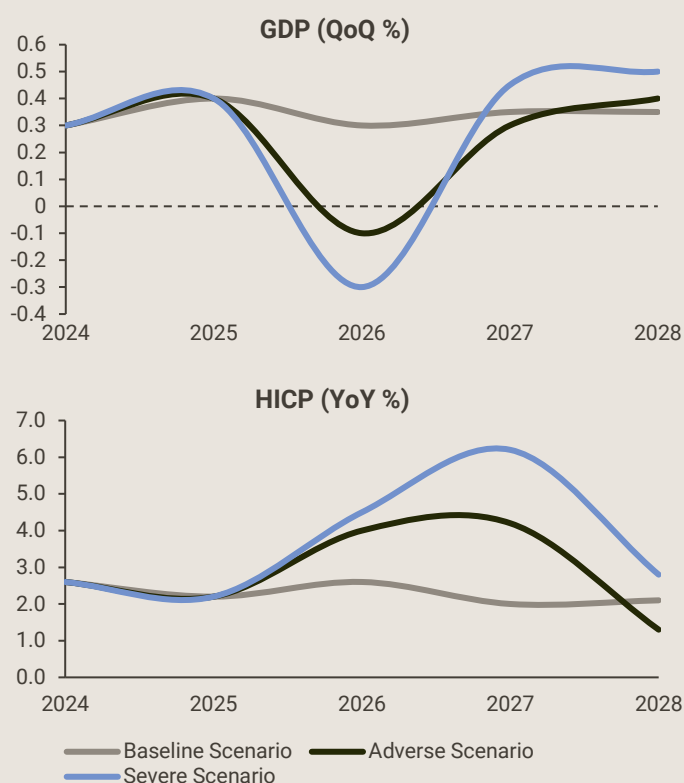
Markets are pricing a stagflationary mix of higher energy costs, softer growth and limited policy easing. In Europe, rate expectations remain sensitive to inflation persistence, with two ECB hikes currently priced and long-

end yields under upward pressure. In the US, expectations point to only modest easing, with the policy path dependent on the extent of inflation pass-through. Against this backdrop, focus has shifted to the US private credit market. Recent media focus has centered on public BDCs, now trading at around c.20% discounts to NAV, and the implementation of ~5% quarterly liquidity gates in non-traded BDC structures. While these dynamics highlight growing investor scrutiny, we do not view them as indicative of systemic risk, given gating mechanisms and moderate leverage.

Rapid growth in US private credit, with elevated leverage and weaker coverage, suggests a concentration of risk in lower-quality segments of the market, broadly in the B to CCC spectrum based on S&P private debt estimates.

Following a prolonged period of benign credit conditions and below-average defaults, the risk of a normalization in default rates is increasing. In our view, this could result in default levels in US private credit exceeding those observed in broadly syndicated loan markets (including distressed exchanges), in a tighter financial environment.

Euro Area Growth and Inflation Under Energy Shock Scenarios



Source: European Central Bank, staff macroeconomic projections (March 2026). Adverse and severe scenarios based on ECB alternative energy shock assumptions; scenario paths approximated from published charts.

Software-Led Repricing Drives Divergence in Leveraged Finance

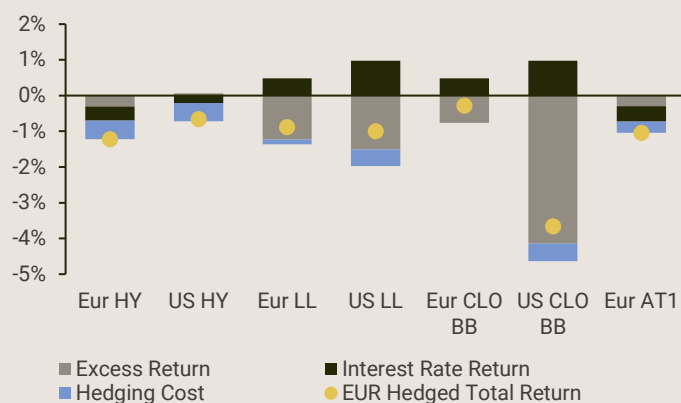
Leveraged finance markets started the year with strong momentum, with both high-yield and loan issuance front-loaded in January before fading through February and March as market conditions tightened and several LBO processes faced more challenging execution.

Recent weakness has been driven by software repricing, where equity valuations remain materially lower year-to-date, reflecting increased uncertainty around terminal values amid AI-driven disruption. This has had a direct spillover into leveraged credit, as lower equity valuations (Software equity indices still down >25% YTD) reduce cushion within capital structures for more levered issuers.

As a result, dispersion within software credit has increased. Names characterized by higher leverage, elevated loan-to-value ratios and weaker interest coverage have come under the most pressure, with secondary loan prices in some cases trading around the low-90s. While a modest rebound was observed toward the end of March, performance remains highly differentiated and sensitive to both fundamental quality and refinancing visibility.

At the same time, the broader technology landscape continues to exhibit a clear bifurcation between winners and losers. While legacy software credits face valuation pressure, strong IPO pipelines in AI and data infrastructure highlight continued investor interest (e.g. SpaceX/xAI, Anthropic and OpenAI targeting >USD 3tn combined valuations).

Q1 2026 Cross Assets Returns



Source: Capital Four calculations based on ICE BofA and S&P UBS indices. Returns shown are euro-hedged.

Positioning: Navigating Volatility Through Selective Credit Allocation

Against this backdrop, volatility measures such as VIX and VSTOXX futures continue to signal elevated uncertainty well into late 2026, underpinning a selective approach with potential for tactical opportunities.

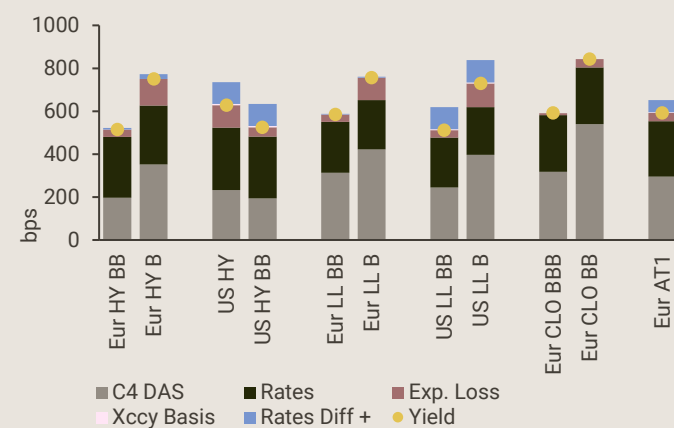
The recent repricing has improved relative value across segments of the leveraged finance universe, with improved entry points. In particular, we see value in European high-yield, where B-rated corporates offer compelling spreads relative to underlying default risk, supported by more resilient spread behavior compared to the US.

Within structured credit, we continue to favor CLO mezzanine tranches, particularly those backed by strong market value overcollateralization tests and high-quality, diversified collateral pools. Following the recent drawdown, selective allocations to diversified CLO equity are also becoming increasingly attractive as pricing is not too elevated vs. equity NAV. CLO equity continues to serve as a high-yielding diversifier within Multi-Asset Credit (MAC) portfolios, benefiting from its low through-the-cycle correlation with traditional bonds and loans.

In leveraged loans, while software-related weakness has partially reversed, performance remains bifurcated. Excluding software, loan returns are broadly flat year-to-date, highlighting the extent to which sector-specific repricing has driven index-level performance. We prefer gaining loan exposure through closed-end vehicles trading at c.10% discounts to NAV, providing an additional buffer.

Overall, we favor European B-rated corporates across high-yield bonds and leveraged loans, alongside selective allocations to CLO mezzanine tranches, where risk-adjusted returns are most attractive, while remaining selective in high-yield given the evolving macro backdrop.

Excess Spread Comparison



Source: Capital Four calculations based on ICE BofA High Yield and S&P UBS Leveraged Loan indices. Excess spread components reflect Capital Four's proprietary default-adjusted and euro-hedged methodology. As of 31st March 2026. C4 DAS: Capital Four Default Adjusted Spread

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Focused Leveraged Finance Manager*

High Yield	Leveraged Loans	Multi-Asset Credit	Structured Credit	Private Credit
Since 2001 €4.9bn AuM	Since 2013 €7.4bn AuM	Since 2010 €2.7bn AuM	Since 2019 €0.6bn AuM**	Since 2015 €8.5bn AuM

Notes

* As of March 2026.

** Includes structured credit assets under management in multi-asset credit funds and mandates

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