



## ANALYSIS

# Credit Continuum

June 2018

*Rising European volatility could lead to a reassessment of US credit exposure for European investors*

The recent return of political risk in Peripheral Europe has, we believe, changed investors' view of credit markets and the role central banks have to play. It has brought into focus the disparity between the monetary policies of the European Central Bank (ECB) and the Federal Reserve (Fed).

In our view it shows in sharp relief how the Fed, which has stopped quantitative easing, is unwinding its balance sheet and is already raising rates, has significantly more firepower to support markets if required, especially as we move towards the latter stages of the economic cycle.

While the ECB has also now signalled an end to its economic stimulus this year, we believe it is still some way behind the Fed; although central banks have in the past shown new and innovative ways of supporting risk assets, and could do so again if needed, the ECB appears to have less options than the Fed.

As a result of this monetary policy divergence, rising yield differentials between the US and Europe may begin to offset hedging costs and tempt European investors to revisit their US exposure.

However, we believe volatility is likely to be a continuing feature of markets. The Trump administration's conflict-driven stance shows no signs of abating, while political risk has also returned in Europe. In our view, this new world order is likely to feature periods of episodic volatility for the foreseeable future, therefore we remain cognisant of the ongoing need for capital preservation and diversification of risk.



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Michael manages the Muzinich Global Tactical Credit strategy. Prior to joining Muzinich in 2012, Michael was president and Head of the High Yield Division at Seix Advisors, Inc. At Seix Advisors, he was the founding partner of the high yield strategy that grew to over \$13 billion under his leadership. Previously, Michael served in various research and portfolio management capacities at American General Corp. and at Capital Holding Corporation. He earned a BA in Management Science from the University of California, San Diego and an MBA from Rice University.

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