

CREDIT CRUNCH

Dynamic Specialized Credit Team

May 2025 Commentary



Downgrade

Moody's threw in the towel on their pristine Aaa US credit rating in mid-May, announcing after the close on Friday May 16th that they were downgrading the US by one-notch to Aa1 and joining S&P and Fitch who downgraded the US to AA+ in 2011 and 2023 respectively. In no surprise to anyone, Moody's highlighted that successive US governments have failed to reverse the trend of large annual fiscal deficits and growing interest costs as justification for the downgrade. Rating agencies are backward looking, and as a result, this downgrade was largely ignored by investors the following Monday with the S&P 500 rallying throughout the day to finish in the green and credit spreads modestly tighter. That being said, the US treasury has considerable near-term maturities that need to be refinanced which could pressure bond yields higher when considering President Trump's growing deficit spending agenda and the recent Moody's downgrade. To that end, yields on 30-year US Treasuries pushed through 5% towards the end of May, reaching levels we haven't seen since 2023, and looking further back, since 2007.

Discounts

Rising bond yields and US rating downgrades, present an interesting question – what entity has a better balance sheet, Amazon or the US Treasury? The reality is that both entities are extremely credit worthy with Amazon being in a net cash position while the US remains the most asset-rich economy on the planet by a wide margin. Investors can purchase low-coupon 30-year Amazon bonds at extremely discounted levels with some trading in the mid-50 cent on-the-dollar range. The convexity (or upside skew) offered by Amazon's bonds at these discounted levels is attractive, especially considering the bond's par claim on Amazon's assets. We have opportunistically taken advantage of higher yields and added exposure to higher quality discounted 30-year corporate bonds in select mandates.



Source: Bloomberg, as at May 29, 2025

Some bond discounts are a function of poor credit fundamentals. We highlight the bonds of US-based retailer Saks who issued 11% secured notes in December 2024 at par which have yet to pay their first coupon and are now trading at 37 cents on-the-dollar following weak earnings. In a troubling sign for bondholders, the issuer has hired financial advisors to help it explore means to raise new financing, while bondholder groups have formed and hired legal advisors themselves to protect their interests. You might find these bonds on Saks' clearance racks given their shocking 63% mark-to-market loss in approximately 6 months!

Tariff Threats

After a bumpy ride the past few months, the markets are increasingly getting accustomed to President Trump's tariff tantrums. In late May, Trump threatened to raise tariffs on the European Union to 50% by June 1st as he expressed frustration with the pace of trade negotiations. Several days later he pushed this deadline back to July 9th after a "very nice" call with European Commission Chief, Ursula von der Leyen. Investing in this uncertain climate remains challenging yet we continue to make use of such volatility to deploy capital at attractive levels. We doubt that President Trump will implement tariffs anywhere close to his worst threats, however, how long the economy or consumers can withstand this uncertainty is anyone's guess.

Portfolio Updates

We continue to add credit exposure across our portfolios as tariff rhetoric improves and recession risks get pushed out. Despite the improving market tone, economic uncertainty remains elevated and as a result, our overall positioning remains balanced. We are positioned to take advantage of opportunities as they may arise and could see modest tariff impacts begin to reveal themselves in economic data as the summer progresses.

Ultra-Short Term Investment Grade Mandates:

- The Funds continue to focus on high-quality issuers that provide stability and predictable cash flows, forming a strong foundation for the portfolio.
- High quality credit spread tightening in the month enabled the portfolio to earn an extra 27 bps vs its benchmark during the month.
- This mandate remains well-positioned to deliver competitive yields relative to cash-equivalent alternatives while offering daily liquidity and flexibility.

Discounted Investment Grade Mandate:

- In May, we added high-quality us issuers as interest rates were moving higher. We have been able to buy bonds with more than \$10 discount. The average Funds price decreased by approximately \$1 to reach \$97.28, vs an average price \$101.95 for its benchmark reinforcing the embedded tax advantages of this strategy.
- The current environment enabled us to continue targeting discounted securities in North America while maintaining a focus on high-quality issuers.

Multi-Sector Fixed Income / High Yield Mandates:

- During the month, we restructured a portion of US High Yield exposure by exiting a position in HYG, a USD high yield ETF, and reallocating proceeds into a synthetic credit position via the CDX High Yield index. This adjustment allowed our funds to maintain high yield beta while improving carry efficiency by eliminating ETF structural costs and USD hedge drag. The cash collateral from this position will be opportunistically deployed into CAD money market instruments, enhancing net yield. This shift supports our ongoing effort to express credit risk cleanly and tactically manage currency-related inefficiencies across the portfolios.
- We trimmed or exited positions in high yield issuers where price appreciation was driven largely by broader beta rather than improving fundamentals, particularly where forward EBITDA momentum appeared to be deteriorating. Meanwhile, we participated in select new issues backed by larger, better-capitalized issuers with clearer paths to free cash flow and less sensitivity to consumer demand. As US Treasury yields moved higher into month-end, we selectively added long-dated paper from high-quality issuer where we saw an opportunity to extend curve exposure.
- Our overweight in energy remains unchanged, with a focus on higher quality issuers with strong balance sheets and underweight CCC-rated issuers, given their higher sensitivity to economic slowdowns. We continue to avoid large, on-the-run issuers with “jumbo-sized” balance sheets, where competitive pressures and refinancing risk remain concerns.

Preferred Share Mandates:

- Canadian preferred shares rebounded very strongly (+5.05%) and finished the month at YTD highs as excitement around improving fundamentals (both tighter credit spreads and higher rates) and a resumption of the redemption technical dominated price action in May.
- In May, the \$600MM RY.PR.Js were redeemed on May 24th, a nice tail-wind for the market. In addition, the redemptions of BIP.PR.B, CVE.PR.G and PPL.PR.S were announced, which should prove supportive to the market.
- During the month of May, we continued to improve the liquidity profile of the portfolio and maintained portfolio beta relatively close to home.
- Performance benefited from our security selection in the insurance sector as well as the electric/pipeline sectors.

Liquid Alternatives Mandates:

- **Dynamic Credit Absolute Return Fund**
 - Continued deployment into US investment Grade credit in both secondary markets and select new issues, where valuations had improved meaningfully following April’s dislocation.
 - Additions to short-duration, yield-to-call high yield bonds issued by well capitalized borrowers, primarily in the energy and Telecommunications sectors, which offered compelling carry and optionality.
 - The Fund entered the month with a more constructive risk posture, having increased exposure to credit in late April. This positioning, built during a period of price dislocation, was rewarded with a +1.50% (series F) as markets responded positively in the month.
- **Dynamic Credit Opportunities Fund**
 - The Fund’s Attractive Income strategy added two energy bonds following the recent pullback in energy prices. We sized one position more meaningfully given its short maturity, compelling yield and a recent non-core asset sale that improved balance sheet flexibility, further strengthening what was already a well-capitalized credit. The second position reflects a more selective allocation where a visible strategic catalyst and strong free cash flow generation support our conviction in the

credit's ability to perform through the cycle. Both positions offer durable income underpinned by solid credit fundamentals and reflect our focus on idiosyncratic return drivers in a more volatile commodity backdrop.

- In the Fund's Event-Driven strategy, we exited an equity position in a name undergoing a pending acquisition, while maintaining exposure through the issuer's bonds. With the equity trading near the proposed takeout price, we saw limited additional upside relative to the timeline and execution risk. The bonds continue to offer a modest yield advantage with the added benefit of early takeout optionality should the transaction close. We view this as more a defensive way to stay positioned in the credit while preserving upside through the capital structure.
- Overall, the fund is generating an attractive yield relative to most asset classes in credit while our current high-conviction positioning remains less volatile than High Yield.

Investment Grade**Dynamic Ultra Short-Term Bond Fund****Dynamic Active Ultra Short-Term Bond ETF (DXV)**

Invests in high-quality, liquid, Investment Grade corporate bonds, and uses hedging instruments to maintain duration less than 1 year

Dynamic Active Discount Bond ETF (DXDB)

Tax-aware strategy targeting discounted 3-7 year Investment Grade bonds

Multi-Sector Fixed Income**Dynamic Credit Spectrum Fund****Dynamic Active Credit Strategies Private Pool**

Flexible mandates that target opportunities across the credit spectrum including, Investment Grade, High Yield, Hybrids, Prefs, Loans, etc.

Dynamic Active Crossover Bond ETF (DXO)

Highly focused mandate that isolates the positive dynamics of bonds residing on either side of the Investment Grade/High Yield threshold

High Yield**Dynamic High Yield Bond Fund**

Primarily invests in performing credits rated High Yield and other credit securities with similar characteristics such as Hybrids, Loans, etc.

Preferred Shares**Dynamic Preferred Yield Class****Dynamic Active Preferred Shares ETF (DXP)**

Delivers tax-advantaged income through actively managed exposure in North American Preferred Shares

Liquid Alternatives**Dynamic Credit Absolute Return Fund**

Alternative strategy designed to enhance total returns throughout a credit cycle while maintaining an Investment Grade credit rating

Dynamic Credit Opportunities Fund**Dynamic Credit Opportunities ETF (DXCO)**

Alternative strategies targeting high conviction opportunities across the credit spectrum, seeking to deliver equity-like returns with low volatility

Fund Characteristics*	Avg. Credit Rating	Yield-to-Maturity*	Int. Rate Duration	Credit Duration
Dynamic Ultra Short-Term Bond Fund	A	3.54%	0.5 yrs	1.9 yrs
Dynamic Active Ultra Short-Term Bond ETF (DXV)	A	3.57%	0.5 yrs	2.0 yrs
Dynamic Active Discount Bond ETF (DXDB)	A-	3.84%	4.3 yrs	3.8 yrs
Dynamic Credit Spectrum Fund	BBB-	5.14%	4.8 yrs	3.7 yrs
Dynamic Active Credit Strategies Private Pool	BBB-	5.04%	4.7 yrs	3.6 yrs
Dynamic Active Crossover Bond ETF (DXO)	BB+	5.07%	5.4 yrs	4.5 yrs
Dynamic High Yield Bond Fund	BB	5.63%	3.9 yrs	3.6 yrs
Dynamic Preferred Yield Class	P2M	4.15%	-	-
Dynamic Active Preferred Shares ETF (DXP)	P2M	4.15%	-	-
Dynamic Credit Absolute Return Fund	BBB+	5.36%	1.0 yrs	5.0 yrs
Dynamic Credit Opportunities Fund/DXCO	BB+	6.61%	3.6 yrs	2.8 yrs

Annualized Returns Net of Fees (%)	1M	3M	YTD	1yr	3yr	5yr	10yr	S.I.**
Dynamic Ultra Short-Term Bond Fund	0.58	0.90	1.76	4.78	5.26	3.46	2.30	2.32
Dynamic Active Ultra Short-Term Bond ETF (DXV)	0.61	0.95	1.81	4.87	5.31	3.63	-	3.10
Dynamic Active Discount Bond ETF (DXDB)	0.35	0.45	2.18	8.88	-	-	-	7.26
Dynamic Credit Spectrum Fund	1.05	-0.52	1.23	6.23	5.31	4.76	3.00	3.54
Dynamic Active Credit Strategies Private Pool	0.97	-0.32	1.47	6.60	5.50	4.90	3.20	3.13
Dynamic Active Crossover Bond ETF (DXO)	1.25	0.01	1.90	6.77	5.19	4.60	-	4.43
Dynamic High Yield Bond Fund	1.27	-0.47	1.13	5.95	5.84	6.04	3.92	5.11
Dynamic Preferred Yield Class	5.41	1.30	4.46	14.96	8.18	14.42	6.21	5.35
Dynamic Active Preferred Shares ETF (DXP)	5.43	1.45	4.60	15.21	8.21	14.49	-	6.88
Dynamic Credit Absolute Return Fund	1.50	2.66	2.90	6.31	6.16	5.87	4.53	4.99
Dynamic Credit Opportunities Fund	1.56	0.37	2.49	5.46	-	-	-	7.78

Source: 1832 Asset Management LP., data, series F and ETF performance as of May 31, 2025. *YTM before cost of borrow. Fund characteristics include hedging strategies when applicable.

**Inception dates: Dynamic Ultra Short Term Bond Fund F: 2013-09-06, Dynamic Active Ultra Short-Term Bond ETF(DXV): 2018-03-26, Dynamic Active Discount Bond ETF (DXDB): 2022-11-07, Dynamic Credit Spectrum Series F: 2012-12-31, Dynamic Active Credit Strats Pvt Plf: 2014-06-06, Dynamic Active Crossover Bond ETF (DXO): 2017-01-20, Dynamic High Yield Bond Series: 2002-04-05, Dynamic Preferred Yield Class Series F: 2013-04-10, Dynamic Active Preferred Shares ETF: 2017-01-20, Dynamic Credit Absolute Return F: 2014-01-01, Dynamic Credit Opportunities F: 2023-09-25

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