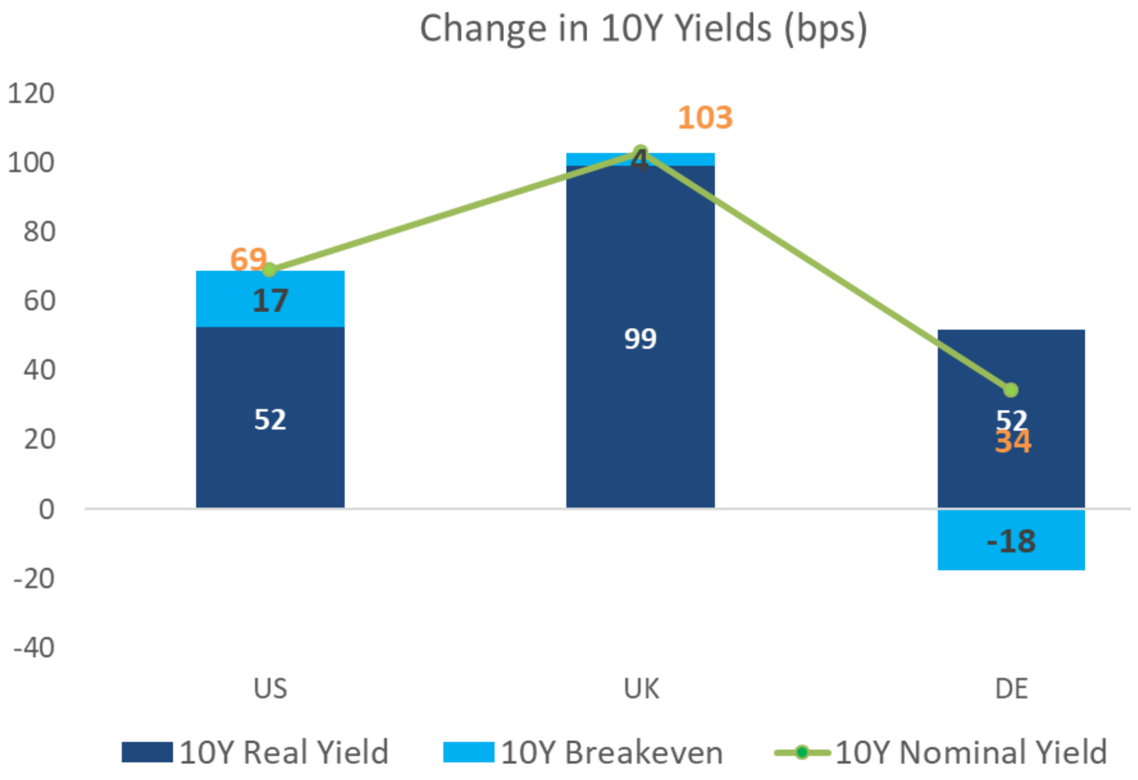
SECOR Asset Management

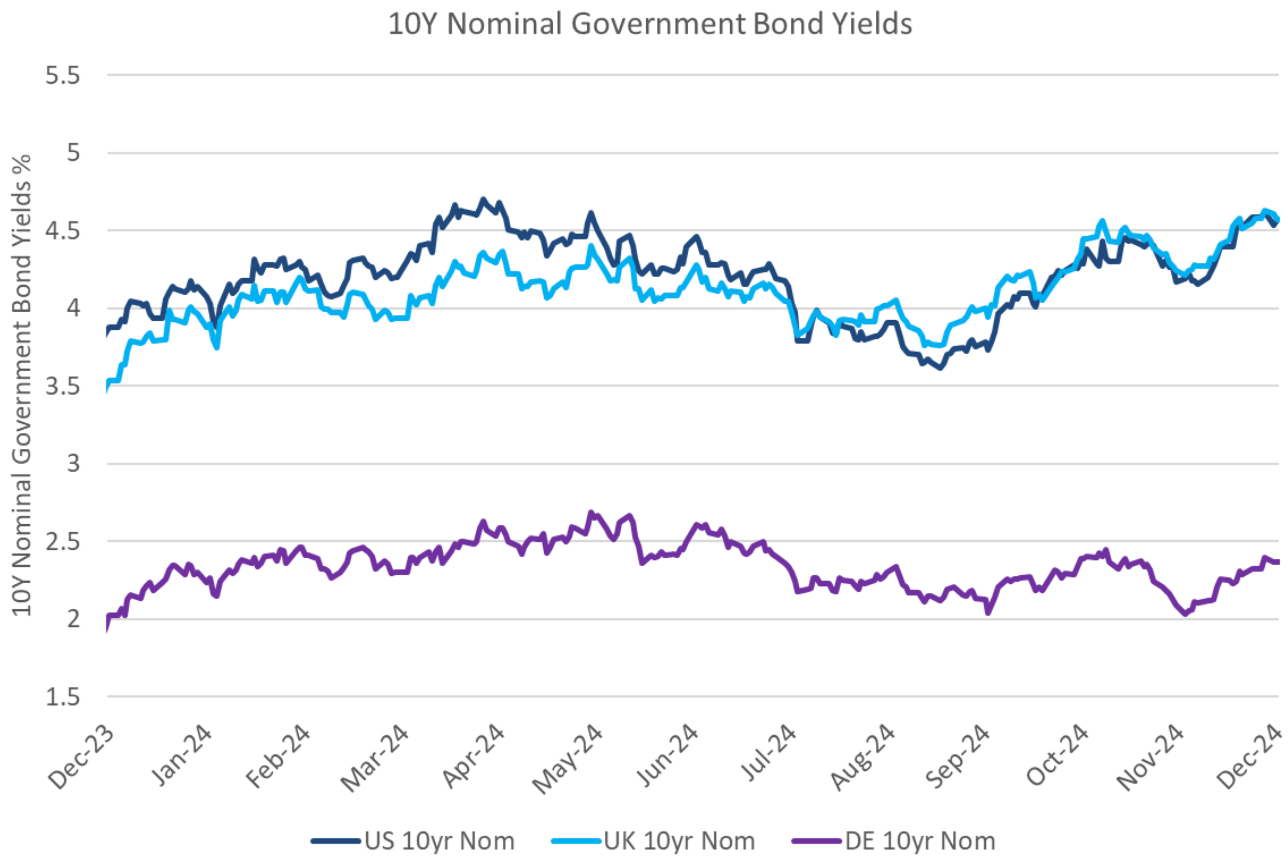
2025 Q1 Rates Outlook

29 January 2025

Interest Rates Higher Through 2024

2024 rates markets were characterized by softening inflation, rate cuts and steepening of the curve





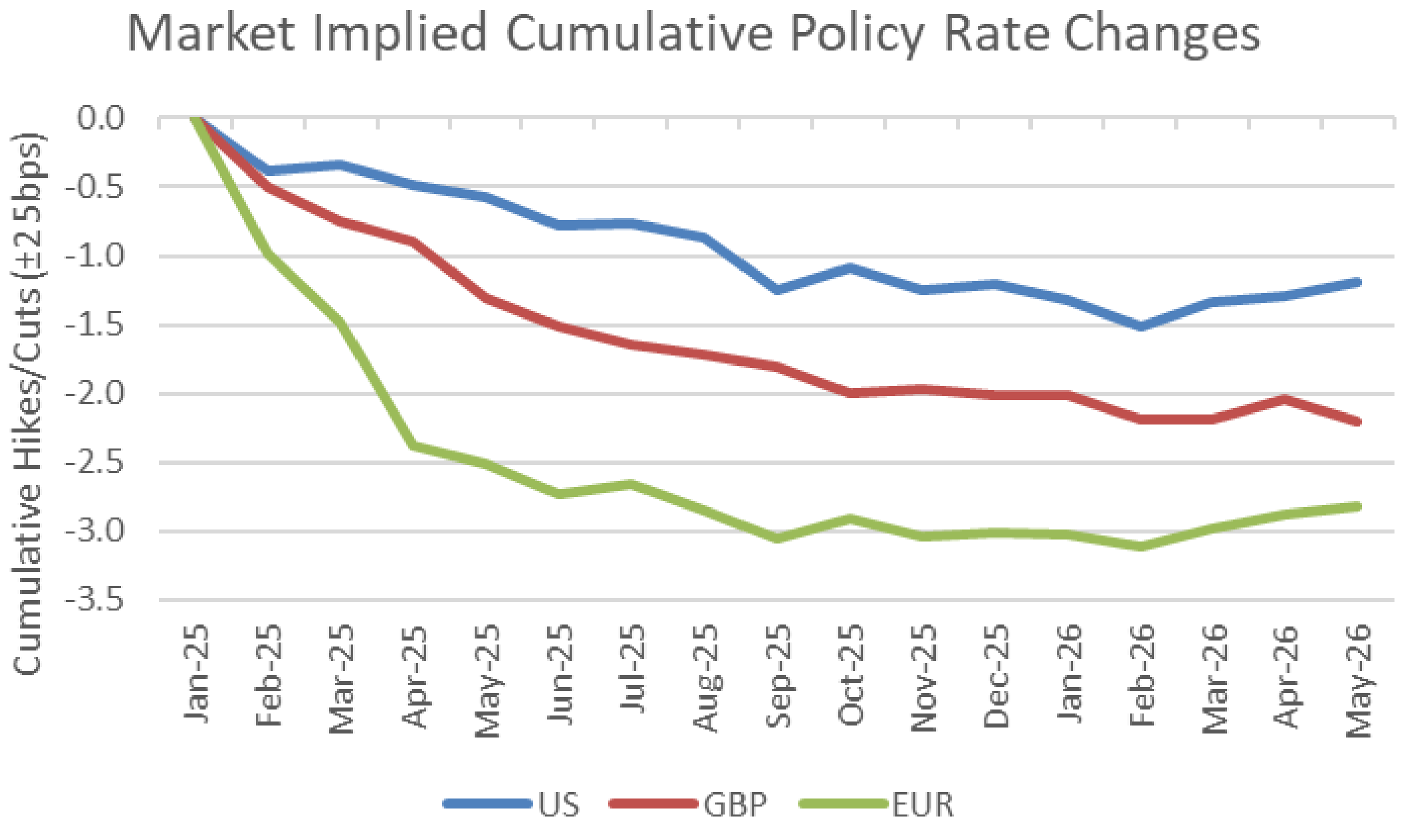
Source: SECOR, Bloomberg. As of Dec 2024.

2025 Overview

- US policy impact may lead to higher yields and volatility through fiscal expansion via extension of tax cuts, tighter immigration policy and tail risk of broad-based tariffs
- US tariffs have cast a shadow on EU growth prospects
- Central banks will continue to cut rates at a moderate pace
- Global QT is not in lockstep: US to end in Q1, UK and EU to continue
- Special Topic: Dutch Pension Reform
- Trade Opportunities
  - *Curve trade – Growth outlook drives the extent of curve steepening*

Market Implied Policy Rates

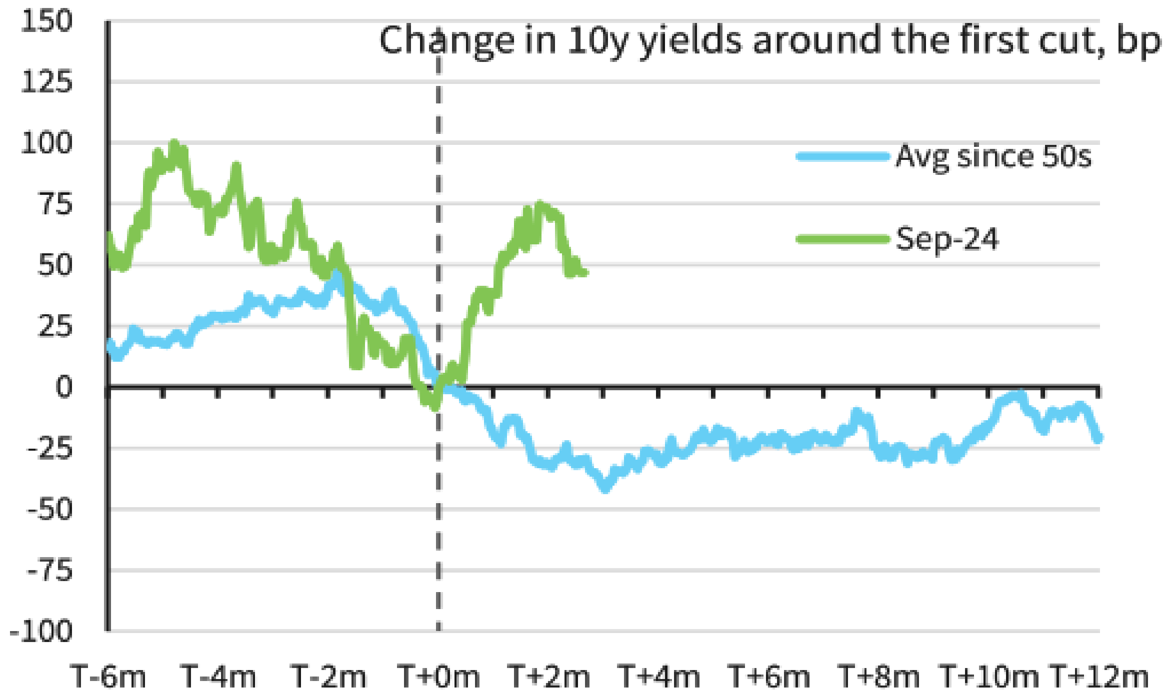
- Markets are currently pricing in moderate cuts over 2025
- Potential setup for more steepening in EUR vs US



Source: SECOR, Yield Book. As of Dec 2024.

US Rates

- Even as the Fed eases further, many of the forces arguing for elevated long-term yields should remain in place: High neutral rate, elevated rate volatility, inflation risk premium, and large net issuance
- Trump 2.0 creates significant uncertainty about the scope of easing, the neutral rate and term premium. Proposed policies have uncertain and conflicting effects on the outlook



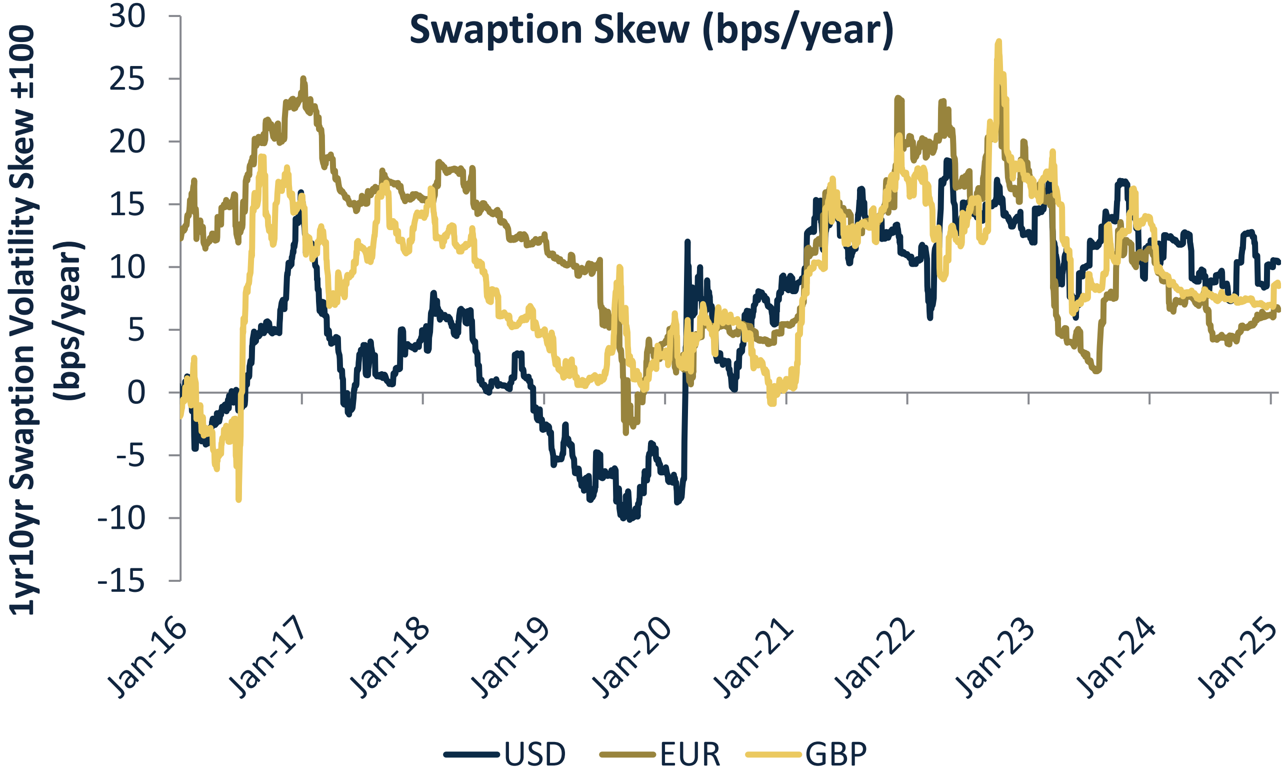
Source: Barclays

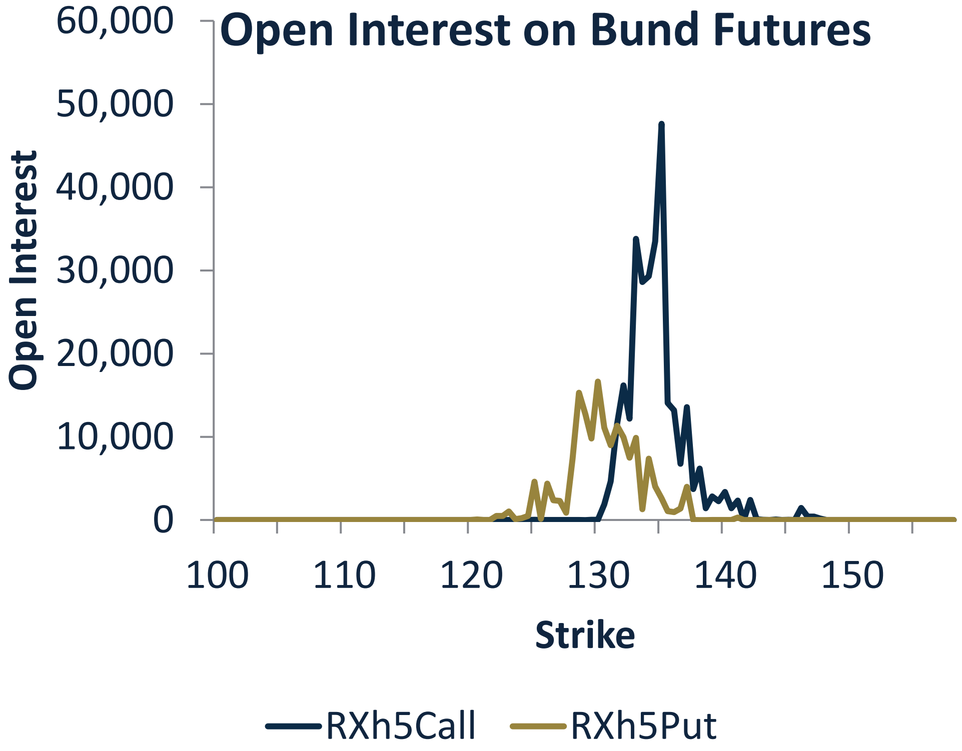
EUR Rates

- Weakening labor market and easing inflation will raise likelihood of cuts
- While the prospect of fresh trade tariffs is now closer than before, with President Trump taking office, there remains considerable uncertainty over the timing and scale of these trade restrictions
- ECB Governing Council commentary since the December meeting has shown a broad consensus on a few issues:
  - Rate cuts likely in 2025
  - Will follow meeting-by-meeting data-dependent approach
  - Current market pricing is broadly fair and little need to be accommodative

Markets are positioned short duration

- 1Y-into-10Y Volatility Skew = +100 Payer Vol – 100 Receiver Vol
- US skew off from Nov. 2024 high but remains elevated. UK and EUR skew has crept up as global yields rose.
- Open interest on Bund Calls 2x Puts which is the highest ratio we've seen in years. Last quarter was close to 1:1.



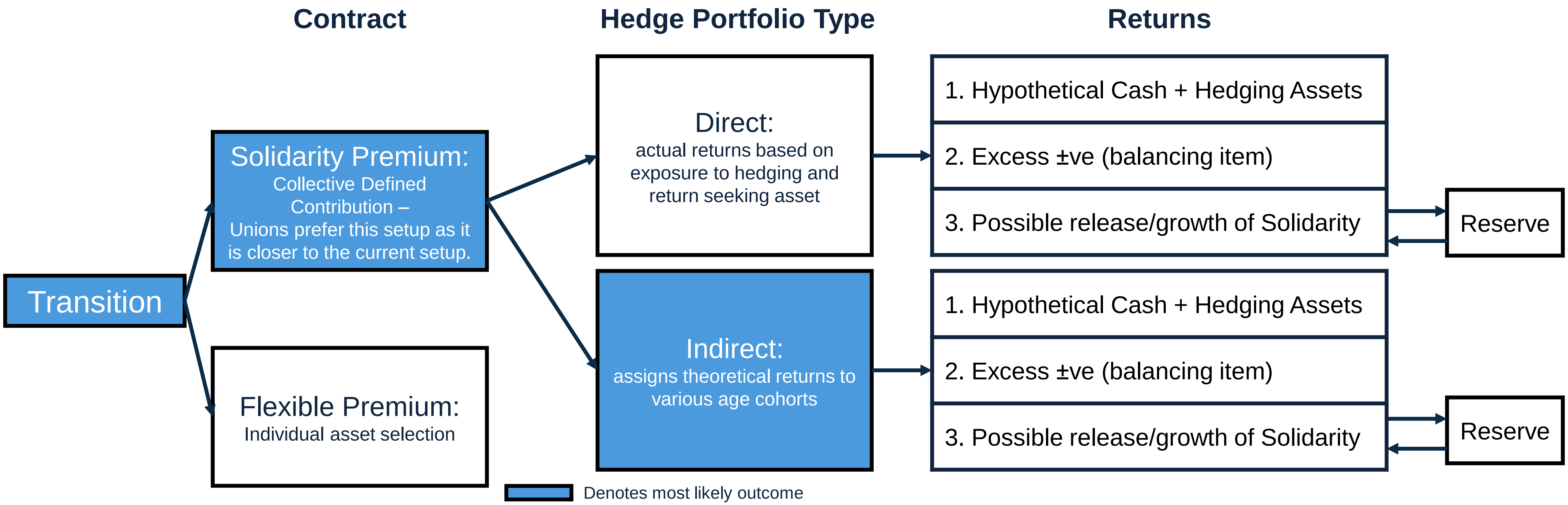


Source: SECOR, Barclays Live, Bloomberg. As of Dec 2024.

Special Topic: Dutch Pension Reform – Impact on EUR Rates

Background of Dutch Future of Pensions Act: 'Wet toekomst pensioenen' (Wtp)

- Existing and future pension savings will transition from Defined Benefit (DB) to Defined Contribution (DC) by 1 January 2028
  - DNB suggesting that 97% of pensions will convert into the new pension system (Unilever's Progress fund is one large exception)
  - 2023 survey conducted by De Nederlandsche Bank (DNB) suggests majority prefer for Solidarity Premium Scheme (SPR)



Sources: DNB, PIMCO, State Street, Barclays, BNP Paribas, PIMCO
For illustrative purposes only

Pre/Post Transition Timeframe

- Tight matching until transition to protect surplus may lead hedge ratios to rise or remain stable in 2025
- Timely execution to new matching portfolio after transition is key

How much time does the market have to absorb this?

Before Transition Date

- Coverage ratio key driver for expected Wtp pension
- FTK continues to apply

Risky to restructure LDI portfolio before transition date

After Transition Date

- Theoretical Matching Return method most popular
- Any mismatch between LDI portfolio and Matching Return allocation falls into Excess Return and will therefore be distributed unevenly over age cohorts

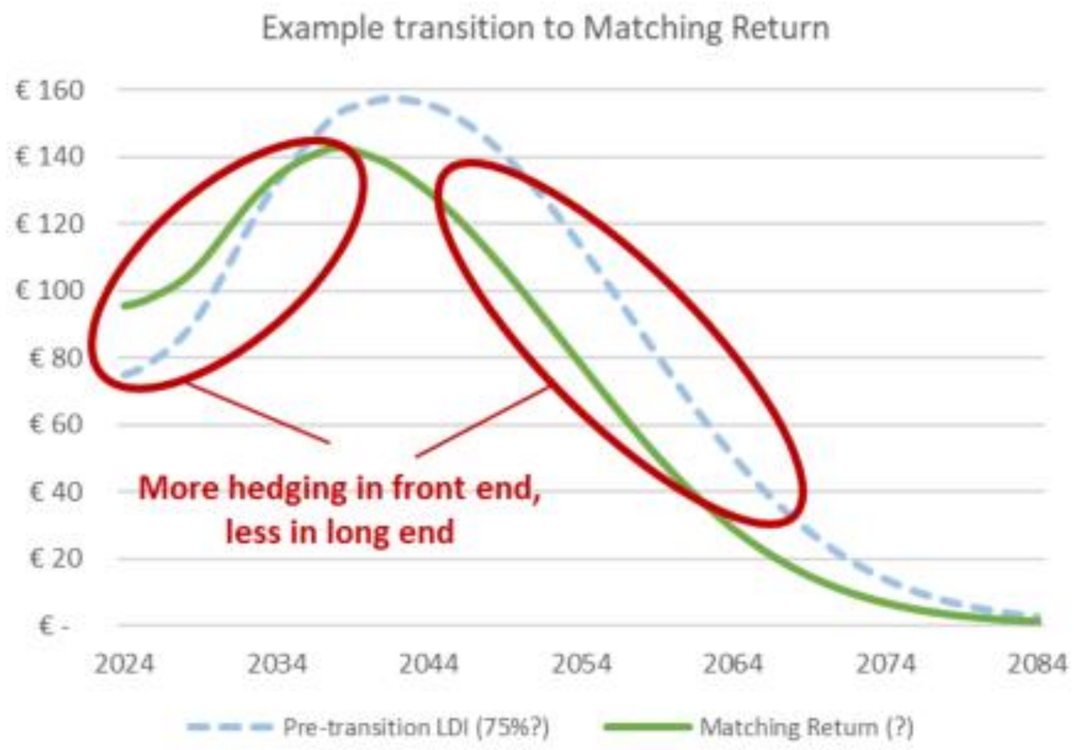
LDI portfolio needs be restructured before, or very soon after transition date

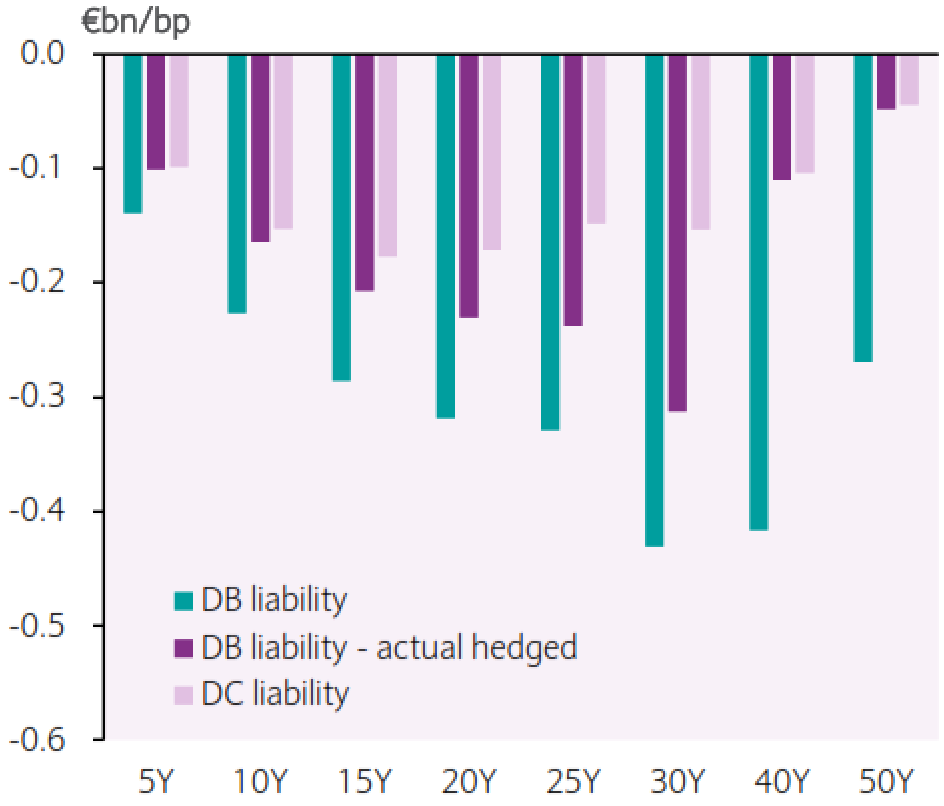
Trading needs to happen on or very close to the transition date?

Sources: DNB, PIMCO, State Street, Barclays, BNP Paribas, PIMCO

Potential Shift in Hedging Assets

- Matching assets shift from longer end to shorter end
  - Elder members need more shorter-dated hedging
  - Younger members require less hedging with longer duration

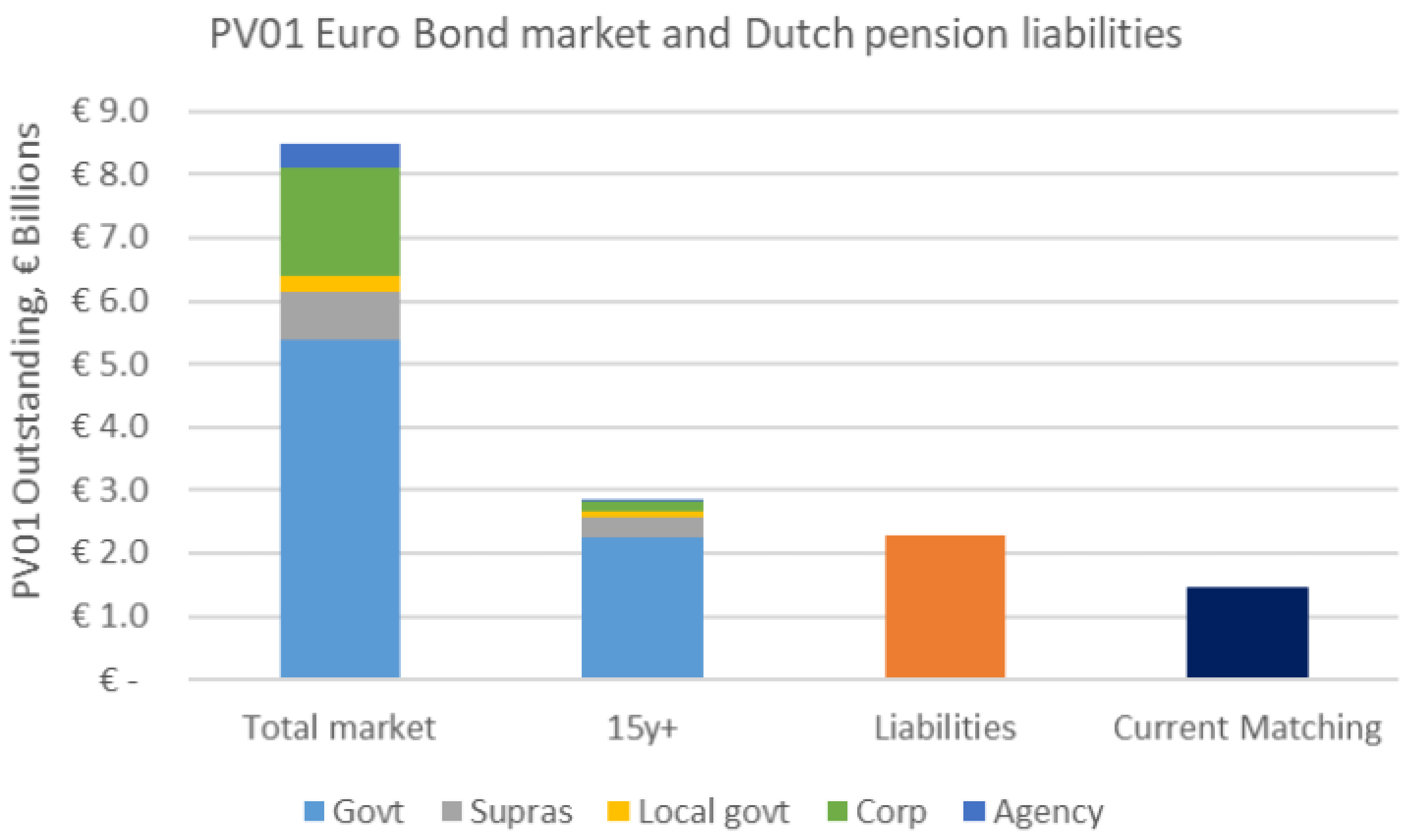




Sources: DNB, PIMCO, State Street, Barclays, BNP Paribas, PIMCO. As of Dec 2024.

Pre-Transition Market Positioning

- Largest Dutch pensions using more swaps to hedge liabilities
- Swaps more skewed in long end due to scarcity of long-dated EUR bonds



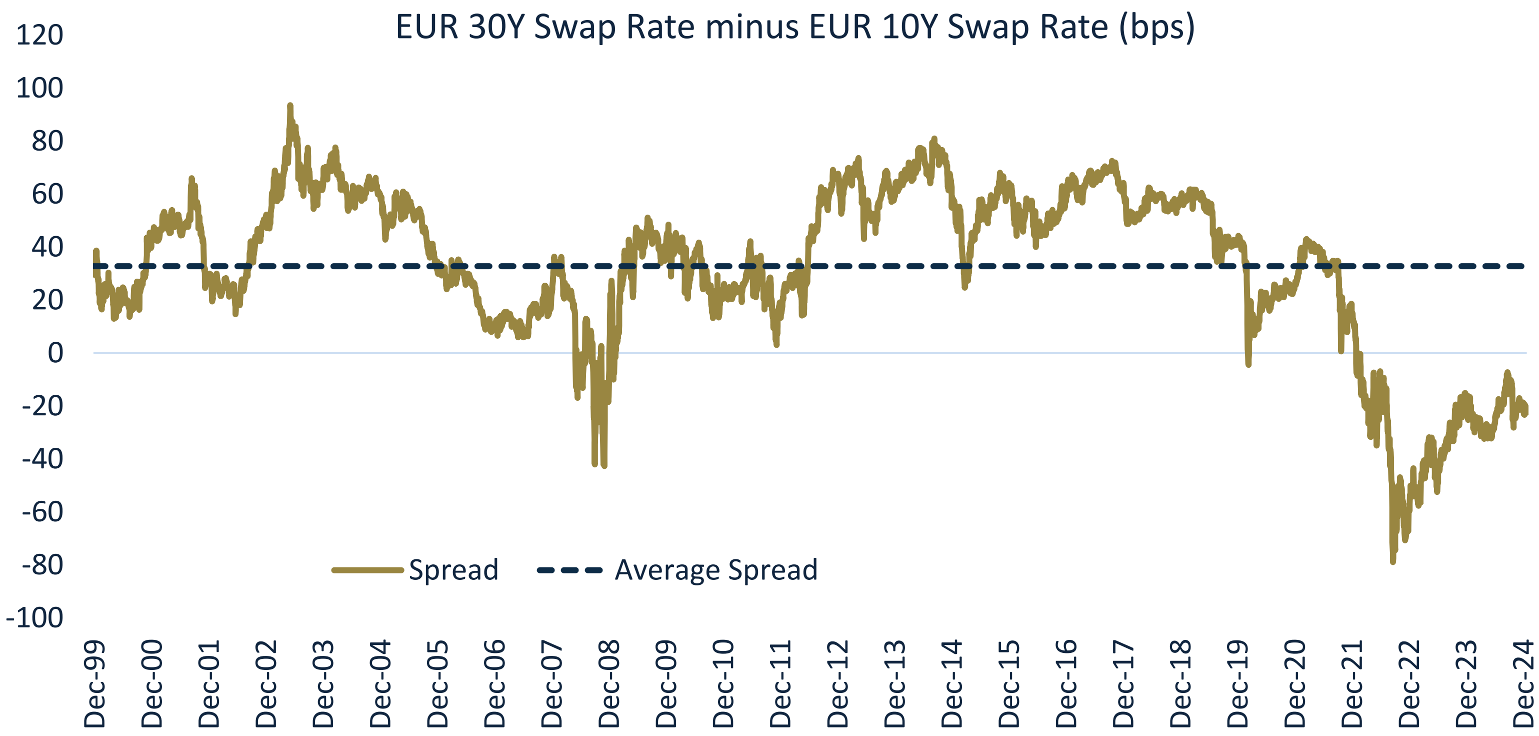
	DV01 - physical (€m)	DV01 – derivatives (€m)
ABP	44%	56%
PFZW	35%	65%
PMT	28%	72%
BpfBoouw	32%	68%
PME	33%	67%

	Proportion hedged with swaps
5y	30%
10Y	35%
15Y	45%
20Y	65%
25Y	70%
30Y	70%
40Y	90%
50Y	90%

Sources: DNB, PIMCO, State Street, Barclays, BNP Paribas, PIMCO. As of Dec 2024.

EUR Curve Steepening

- Long-dated 10s30s curve remains negative – which is abnormal to history
- Expecting some normalization post ECB hiking cycle and ECB QE in long maturity bonds
- Some further normalization if pensions unwind long dated hedges with no buyers in 2027



	10s30s Spread bps
Current	-22.2
Historical Average	32.82
Historical Median	38.80
Current Percentile Rank	0.08
Current Z Score	(1.79)
Min	(78.98)
Max	93.60
GFC (change)	(21.15)
COVID (change)	(11.42)
Euro Crisis (change)	(1.90)

Sources: DNB, PIMCO, State Street, Barclays, BNP Paribas, PIMCO. As of Dec 2024.

Swap Spread Implications

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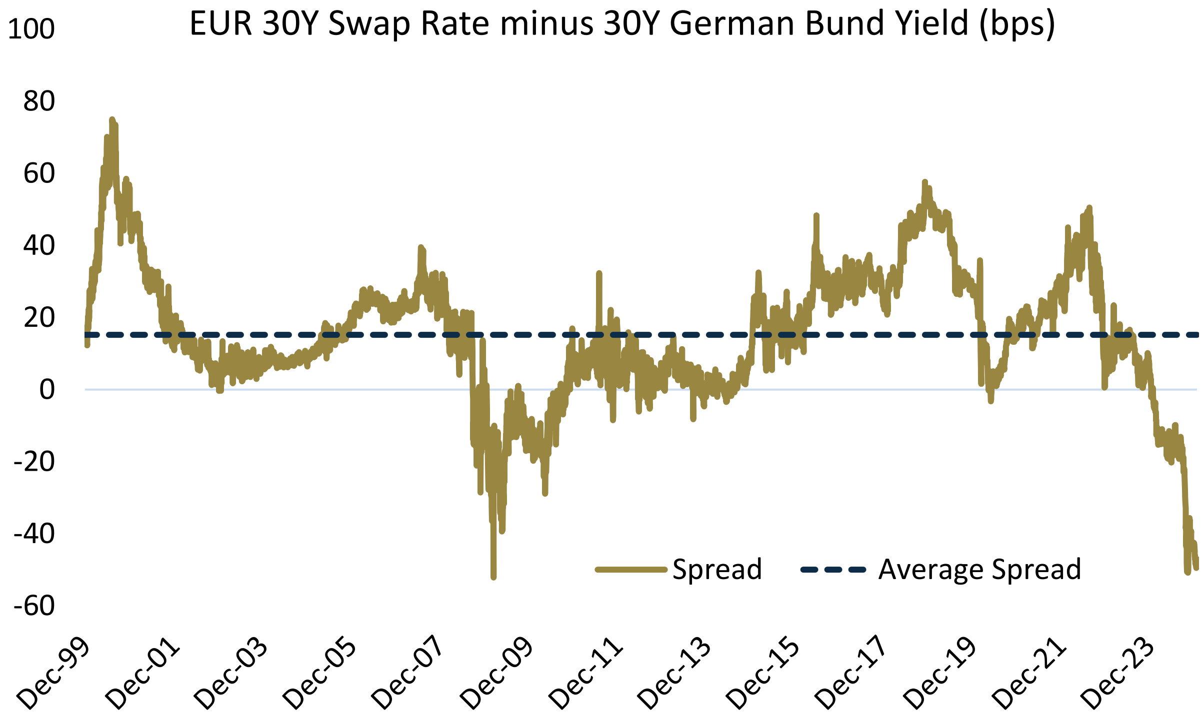
- Long-dated swap spreads have been decreasing as more swaps were used to hedge liabilities
- A portion of this could reverse and increase swap rates relative to bonds
- Mars is currently underhedged which may help with surplus if swap rates increase

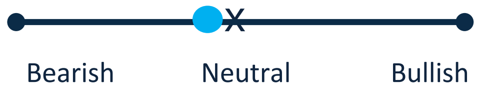
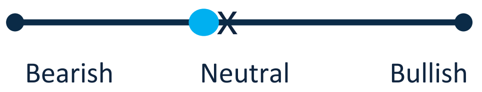


	Swap Rate minus Bond Yield (bps)	3m Rolling Correlation	3m Rolling Beta
Current	-47.9	0.98	0.82
Historical Average	15.24	0.94	0.87
Historical Median	13.95	0.97	0.91
Current Percentile Rank	0.00	0.60	0.30
Current Z Score	(3.48)		
Min	(52.20)	(0.22)	(0.26)
Max	75.00	1.00	1.56
GFC (change)	(21.15)		
COVID (change)	(11.42)		
Euro Crisis (change)	(1.90)		

Sources: DNB, PIMCO, State Street, Barclays, BNP Paribas, PIMCO. As of Dec 2024.

Rates Summary

Rates Summary Page

Factors	Comments	Historical Range
Valuations and Fundamentals	▪ Fiscal supply anticipations remain high (steeper curves) ▪ Inflation has come closer to central bank targets (lower to neutral rates) ▪ Markets positioning shorter in the long end with additional cuts for 2025	
Technicals	▪ More opportunities for steepening in Europe ▪ Swap spreads continue to grind lower in the interim but dependent on fiscal supply ▪ European swap spreads may widen towards Y/E due to Dutch Pension Reform	
Macro Impact	▪ Inflation is trending down but still a lingering risk. Central bank policy still pertinent but markets watching how tariffs and other fiscal policy plays out. Markets continue to monitor economic data prints to determine policy path which should be supportive of volatility in the near term. ▪ Fed now watching labor markets more closely	
Overall	▪ 9-to-12 month view vs Fwds is generally neutral to slightly bearish for US	

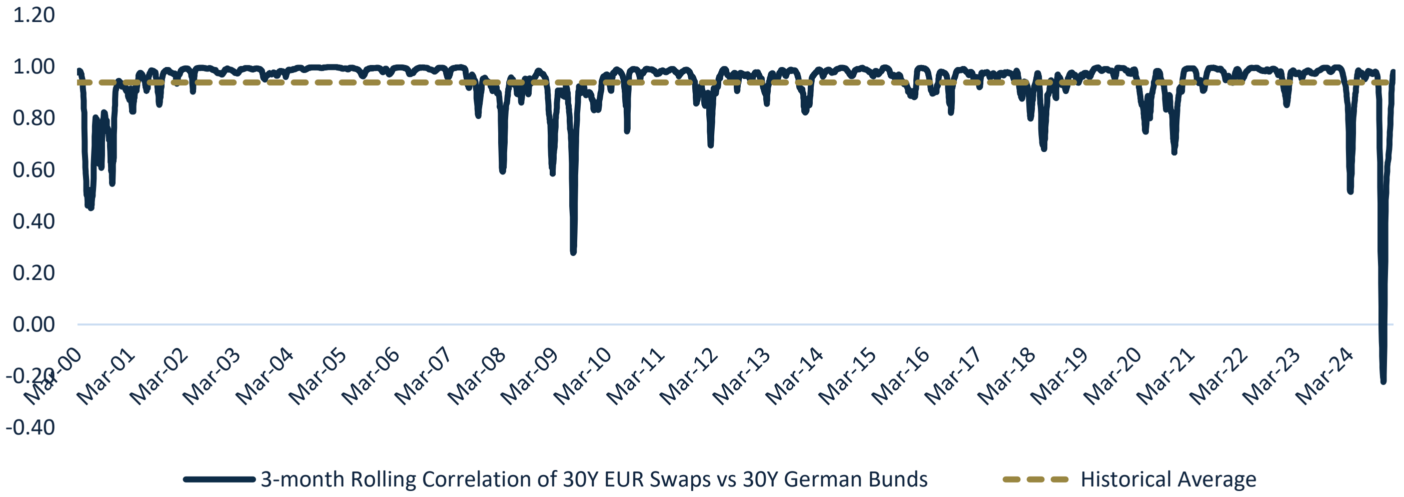
● Current Quarter

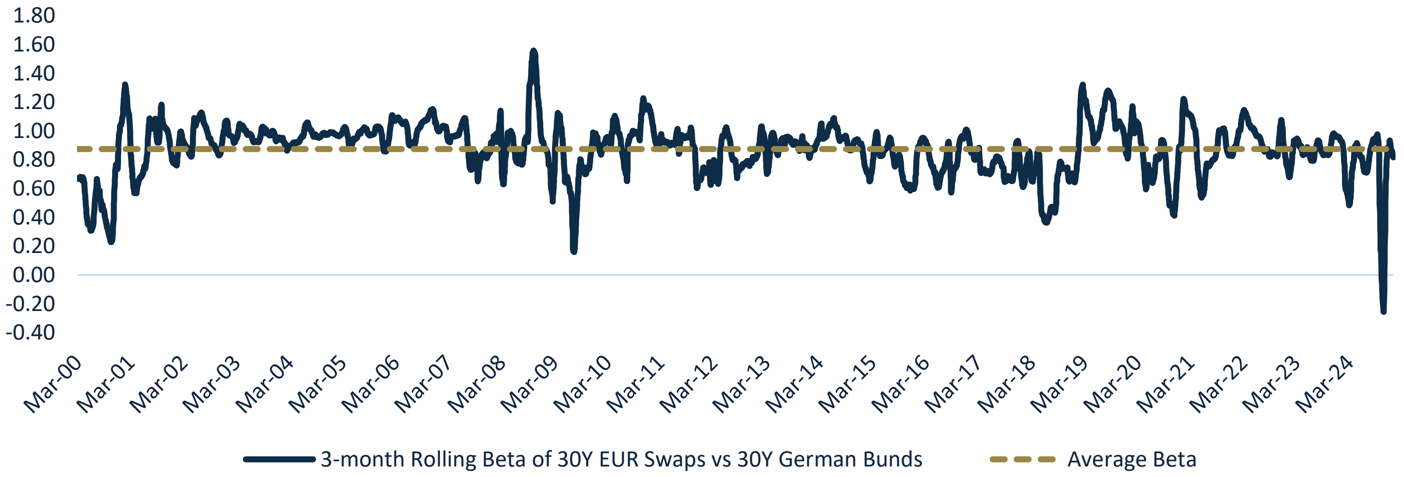
X Last Quarter

Appendix

Historical 30Y Swap to Bond Correlation and Beta

- Generally close to correlation and beta of 0.9 but can diverge at times





	3m Rolling Correlation	3m Rolling Beta
Historical Average	0.94	0.87
Historical Median	0.97	0.91
Current Percentile Rank	0.60	0.30
Min	(0.22)	(0.26)
Max	1.00	1.56

Sources: DNB, PIMCO, State Street, Barclays, BNP Paribas, PIMCO. As of Dec 2024.

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Equity investments involve a high degree of risk. Equity securities may decline in value due to factors affecting securities markets generally, and equity securities generally have greater price volatility than debt securities/investments. Equity securities of certain jurisdictions may experience more rapid and extreme changes in value and may be affected by uncertainties such as international political developments, currency fluctuations and other developments in the laws and regulations of countries in which an investment may be made. There can be no assurance that return objectives will be realised and investors could lose up to the full amount of their invested capital. Fees and expenses may offset the trading profits.

Debt investments (such as, but not limited to, investment grade, high yield, emerging market debt, asset backed securities and insurance linked securities) involves special considerations and certain risks, including risk of default and price volatility, and such securities are regarded as being predominantly speculative as to the issuer's ability to make payments of principal and interest.

LDI and equity overlay strategies may invest and trade in many different market strategies and instruments (including securities, non-securities and derivatives) and may employ different investment, hedging, leverage and arbitrage methodologies, so the risks of those would be material to understanding the risks and benefits of the portfolio. Counterparty and ISDA arrangements may pose potential risk. Furthermore, derivative strategies may be exposed to the risk of market disruptions, volatility, and governmental interventions.

Illiquid investments (such as, but not limited to, private credit, private equity and infrastructure):

General/Loss of capital. Investment involves a high degree of risk. There can be no assurance that return objectives will be realised and investors could lose up to the full amount of their invested capital. Fees and expenses may offset the trading profits.

Limited liquidity. Investments in private markets may result in restricted liquidity since withdrawal rights are limited and interests are not freely transferable or redeemable. There is unlikely to be a secondary market for private market investments interests.

Volatility. Investment techniques used may include the use of leverage and derivative instruments such as futures, options and short sales, which could amplify the possibilities for both profits and losses and may increase volatility.

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Modelling Assumptions:

Forward looking return, volatility, and correlation assumptions have been derived by SECOR, and are based on a combination of: a) the historic performance of each asset class based on what we consider to be appropriate indices or suitable proxies, and over a period that we consider to be appropriate in light of prevailing market conditions (typically 10 years); and b) our judgement in relation to how historic performance, and its various components, may differ in the future. This may include, for example, ad-hoc adjustments to reflect our view that markets are over or under valued.

The resulting assumptions are assumed to be appropriate for asset and liability projections over the medium to long term i.e. 10 to 20 years or longer, and are net of all ongoing management costs and fees.

Expected returns for an asset class are generally built up from and include an allowance for our projected return on cash, inflation, spreads, risk premiums, liquidity premiums, potential losses, valuation adjustments, alpha for active management, management fees, other ongoing costs, and any other factors that we may consider are appropriate for the asset class and/or prevailing market conditions. Expected returns generally do not allow for SECOR advisor or fiduciary management fees, or any transition or rebalancing costs between asset classes or an existing portfolio.

A material risk factor is that the projected returns modelled are underpinned by historic market returns combined with SECOR's assumptions on future market returns, meaning that the projected net returns used for modelling portfolios may not be realised within expected timeframes.

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