TwentyFour
a boutique of Vontobel

Flash Fixed Income

14 July 2026

Riding the bumps in credit markets

Euro-denominated credit performed well in the first half of 2026 in the face of elevated macro risks, with subordinated financials and sub-investment grade CLOs posting some of the strongest returns across the sector year-to-date (YTD) after outperforming other segments in 2025.

Returns have not come without volatility, however, with the US-Iran war repricing rate expectations, pressuring government bond yields, and driving periods of credit spread widening as the market priced in the potential for slower growth. While credit spreads have rebounded towards all-time lows, interest rate expectations remain elevated and a number of hikes from developed market central banks this year are now seen as likely.

We view these hikes, if they do happen, as mid-cycle adjustments rather than the start of a hiking cycle. While inflation remains above target and relatively sticky, inflation expectations remain anchored and wage growth in the Eurozone is hovering around levels that are consistent with inflation at 2%. Growth has been resilient, as have labour markets, and as the geopolitical risks dissipate, we would expect oil volatility to decline.

This sets the stage, in our opinion, for a summer grind tighter in credit markets. But with macro risks still elevated and spreads on the tighter end of historical averages, active management of portfolios is key, both from a top-down and bottom-up perspective.

Digging into euro credit returns this year in more detail, we can point to several interesting trends.

Key takeaways

- Credit assets generally performed well in the first of half of 2026, despite periodic volatility driven by the Iran war and concerns about AI disruption and private credit.
- Despite broadly strong returns, credit quality has been a notable factor in some asset classes, which for us underscores the importance of credit selection in a tight spread environment.
- We see potential for credit spreads to grind even tighter over the summer, but we stress the importance of dry powder for taking advantage of any opportunities to lock in higher yields.

First, and most obviously, returns have been positive despite the instability in the Middle East and despite concerns around AI disruption and private credit. Second, spread risk has been (and we think will continue to be) preferable to duration risk. But third, the type of spread risk you are taking matters hugely to returns. BB rated high yield (HY) bonds have outperformed single-B rated HY on a total return basis, while BB CLOs have outperformed single-B CLOs. Euro Additional Tier 1s (AT1s), which are subordinated bonds issued by mostly investment grade banks, have outperformed all of the above. While CCC HY has beaten the lot, returning 4.2%, we may take this with a heavy pinch of salt after last year's -2.5% return and given the small size of the index (42 issuers).

Credit market performance

	Total return YTD (%)	Total return last 30 days (%)	Yield (%)	Duration (yrs)
EUR IG	0.60	-0.44	3.63	4.45
GBP IG	-0.04	-0.60	5.61	5.61
US IG	0.32	-0.58	5.29	6.36
EUR HY	1.90	0.24	5.40	2.90
GBP HY	3.07	0.35	8.37	2.79
US HY	2.08	0.14	7.09	2.99
EM HY	4.13	-0.20	7.40	3.90
Euro Senior Banks	0.66	-0.38	3.50	3.75
COCO	2.84	0.48	5.89	3.70

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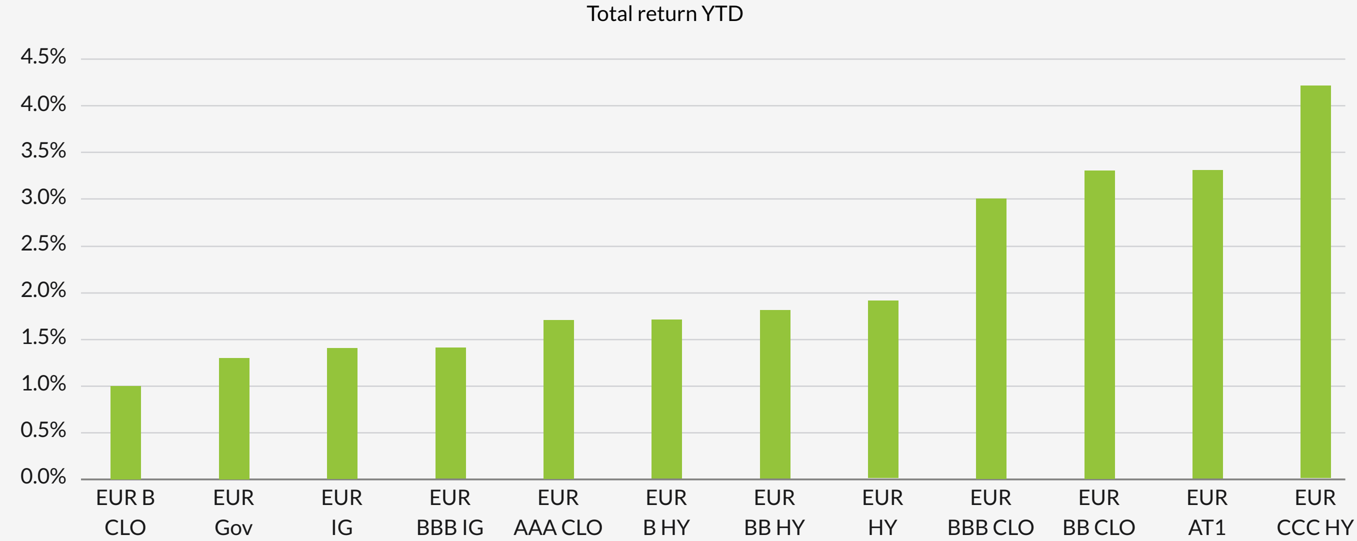
Gordon Shannon
Partner, Co-Head of Investment Grade, industry experience since 2007.


George Curtis
Partner, Portfolio Management, industry experience since 2012.

Exhibit 1: Euro credit has shrugged off periodic spread volatility in H1



Source: Bloomberg, ICE Indices, Palmer CLO Index, 14 July 2026

The YTD returns shown above in many ways depict the story we have told investors about investing in credit in current conditions (and indeed last year). We have strongly believed that credit risk has been preferable to rates risk (duration) given high all-in yields and what we have viewed as solid corporate and banking sector fundamentals. We also believe that investing across the credit spectrum, including in securitised assets such as CLOs and subordinated financials such as AT1s, can help to maximise risk-adjusted returns through the cycle. Of course, the goal is generally to seek attractive with spreads while minimising defaults, as missing the "accidents" can be key to generating excess returns given the inherent negative convexity in credit.

We can take some inspiration from our colleagues in Switzerland, who have recently dusted off their mountain bikes after a cold and snowy winter, to describe the process of investing in credit in the current environment of tight spreads.

The yield on credit is the bike's suspension. More yield equals higher credit breakeven (the level of negative price performance required to wipe out the yield over a year), which equals an increased ability to weather the lumps and bumps of the road. The overall credit risk in the portfolio is the speed you are riding. Faster speeds might be better in the short term but can be worse and more dangerous over the medium term (i.e. more difficult to control when it gets even bumpier). The route you are taking is your concentration. A smaller, narrower path leaves less margin for error. From what? A credit default, the equivalent of flipping over your handlebars. It makes sense to diversify and have multiple riders in your team but having one crash is always costly.

In this environment, when spread suspension is already compressed, we want to proceed cautiously and down lines that offer multiple exit routes. We want all our riders to make it to the finish line, so our credit selection process is focused on identifying companies that we believe are better equipped to ride out the bumpier sections. In practical terms, for us this means focusing on CLOs with clean pools from managers with strong track records, in vintages that we believe offer attractive relative value.

It also means favouring national champion banks and insurers in Europe rather than smaller challenger banks, given limited dispersion across the sector. In the corporate space we generally like strong cashflow durability, revenue visibility, and sub-50% loan-to-value paper. In all cases we want conviction in being able to hold positions through the bumps (or worse) that the market provides.

Metaphor over, the last point we would make is on the importance of dry powder, both from a top-down perspective and a bottom-up perspective. We see periodic spread volatility as both inevitable and healthy, so maintaining sufficient liquidity in a portfolio to be able to take advantage of those periods means the potential to lock in higher yields to the benefit of future returns.

Let's see what the second half of 2026 brings for fixed income managers. Happy riding.

Rates dashboard

			Change (bp)		
		Current %	1w	1m	YTD
US Treasury	2yr	4.20	0	2	72
	10yr	4.59	0	14	42
	30yr	5.12	1	22	27
UK Gilt	2yr	4.39	4	13	65
	10yr	5.02	4	18	54
	30yr	5.73	5	19	53
German Bund	2yr	2.78	2	13	66
	10yr	3.15	4	16	30
	30yr	3.66	4	12	18

			Change (bp)		
	Market projection	Current %	1w	1m	YTD
Base rate 3.75%	end-2026	3.96	2	-7	91
	end-2027	4.00	-13	0	85
Base rate 3.75%	end-2026	4.18	3	6	84
	end-2027	4.30	9	17	80
Base rate 2.25%	end-2026	2.62	3	6	68
	end-2027	2.75	10	12	85

Indicative market indices, data as at 21 July 2026. Past performance is not a reliable indicator of current or future results. Included for illustrative purposes only. Shown in local currency terms. It is not possible to invest directly into an index and they will not be actively managed. Source: Bloomberg, TwentyFour.

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