

## Learning from Past Trends: Insights for the Future

I will not write a conventional review of 2025, nor will I focus on performance metrics. That exercise is already well covered by research houses and credit strategists, who dissect returns across asset classes through the lens of macroeconomic, monetary, and political developments. Broadly speaking, 2025 was a year in which certain outcomes were largely anticipated, others wrong-footed investors, and select segments offered pockets of value for real-money investors and opportunistic hedge funds able to deploy capital with timing and conviction.

Crucially, in my opinion, 2025 should not be analyzed in isolation. A proper assessment requires evaluation over a longer-term period, extending four to five years back to the post-COVID period, in order to understand market technicals, positioning, and global capital flows over the years. The strong total and excess returns delivered in 2023 and 2024—years during which a U.S. recession was widely and wrongly forecast following aggressive monetary tightening but ultimately failed to materialize—largely offset the drawdowns of 2022. Ignoring that recovery in those years would materially distort the interpretation of 2025 valuations, risk premia, and investors' behavior.

Without these premises, any attempt to make sense of 2025 might result in a flawed understanding.

The same perspective applies to credit markets. Their evolution in 2025 cannot be fully understood without accounting for the stellar returns of the previous two years and residual effects (negative) of the late 2020 and 2021 leverage-finance euphoria, as well as the volatility driven by political uncertainty and shifts in U.S. policy expectations (well announced in 2024). These factors continue to influence spreads, issuance dynamics, and risk appetite well beyond their initial occurrence. In the past three years, uninvested cash has carried prohibitively high opportunity costs.

Throughout the year which is now drawing to a close, investors were frequently confronted with conflicting signals across growth, inflation, fiscal and monetary policies. Yet, when assessed objectively, many trades considered value opportunities, were not undermined by weak fundamentals per se. Rather, the challenges lay in asymmetrical risk-reward profiles: compressed spreads, limited upside, and deteriorating downside protection resulted in sub-optimal values, even where underlying credit quality or macro fundamentals remained (or seemed to remain) broadly intact. Some investors did not sufficiently reassess their sectoral and geographic asset allocations.

Strategies tailored exclusively to return enhancement, without adequate risk balance, proved inherently fragile. Critically, the investment style remained unchanged entering 2025, despite the need for a more balanced approach.

So, what genuinely surprised us? I will be brief and selective.

- 1) The US yield curve steepened over the year, though the long end remained anchored near the lower bound of market expectations. The U.S. 10-year Treasury yield, widely expected to reach 5%, failed to breach that level. Elevated government deficits and term premia had limited upward impact (the curve failed to offer more term premium today for the uncertainty tomorrow presents), suggesting that forward inflation expectations and real yield dynamics dominated market pricing. In contrast, the 10-year Bund yield traded above the most pessimistic forecasts despite successive ECB rate cuts, highlighting a latent fragility in the European yield curve. This divergence between U.S. and German long-end yields underscores the differing sensitivities of the two curves to fiscal positioning, central bank signaling, and cross-border capital flows. As far as Japan is concerned, the 10Y JGB yield is the highest since 1999 in a correction that started around July 2023.
- 2) Credit spreads and indices remained everywhere tight throughout 2025 despite forecasts of decompression, with the notable exception of the tariff-driven volatility in April. Some investors and analysts attributed this resilience to strong corporate fundamentals and healthy balance sheets. In reality, the situation appears more nuanced. Facing limited opportunities for genuine value or hard pressured for achieving results, many investors chased returns indiscriminately, operating under the assumption that “everything rally.” The chase for yield often occurred without sufficient consideration of credit spreads, leaving credit portfolios exposed.

The sobering reality is that numerous companies in HY began to struggle under high leverage, challenging their ability to service debt. Tail risks in credit are now evident across multiple industrial sectors (even those traditionally considered safe). In these cases, elevated debt levels have been the primary driver of underperformance and subsequent price declines in debt securities. Opportunistic and distressed investors have been able to capitalize on this environment; however, their strategies frequently conflict with traditional credit holders, resulting in disputes both in court and through extrajudicial resolutions. Credit tail risks should serve as a reminder to reassess current holdings and future investment strategies rather than to be ignored.

In the leveraged loan space, many participants failed to recognize that a core segment of the market was effectively becoming a repository for higher-risk, high-yield issuers. These issuers often offered tight spreads, yet

the associated credit risks were underappreciated or overlooked. The pressure on borrowers to refinance the liabilities remained often a drag on balance sheet liquidity, interest expenses and technicals, while decelerating earnings and negative cash flows drove further tiering. CLO portfolios have functioned as the primary conduit for allocating higher-risk credits in loan and floater bond formats—many of which would have been more appropriately held within private debt mandates at yields around 10% and not at 4,5% where CLO vehicles were buyers. Many painful liability management exercises (LMEs) and haircuts could have been avoided in idiosyncratic credit cases which, taken together, risk evolving into a broader market trend. Volatility in some HY names had a more disruptive impact on portfolios than initially expected. Another surprise.

- 3) Structured products are a fundamental pillar of global credit markets, spanning retail lending, consumer finance, commercial real estate, and high-yield credit. In the United States, the asset class has benefited from consistent regulatory and institutional support and has recorded sustained growth since 2008, the year of the Global Financial Crisis. In contrast, the European securitization market has lagged significantly, contracting for much of the past decade. Only recently have the European Council, the Eurogroup, and the ECB formally acknowledged the urgency of revitalizing securitizations in Europe. The primary impediment to market development has been prudential regulation, particularly capital requirements imposed on banks and insurers that were insufficiently aligned with the actual risk profile of securitized assets. This year marks an important shift, as policymakers have begun to recognize the need for a more proportionate and risk-sensitive regulatory framework.

For years, sophisticated investors (look, for example, at the asset managers who promote ETFs for securitizations) have anticipated this inflection point, advocating for regulatory reform and investing heavily in the analysis of granular, asset-level data to accurately assess quality and risk of the pools under management. By contrast, other market participants have been slower to adapt and are only now reshaping their investment strategies to accommodate new products, evolving market structures, and renewed funding needs. These “delays” among certain credit investors are difficult to justify and may contribute to elevated near-term volatility. New entrants, in particular, will require time to develop the technical expertise necessary to navigate an asset class characterized by complex structures, distinct market technicals, and episodic volatility. At present, entry points in several structures appear suboptimal, with spreads tight and compressed. The key risk at this stage is both the deterioration of the underlying assets and potential

downgrades of tranches within the capital structures—a development that, even if limited or contained, could be sufficient to deter new investors and insurers participation in the asset class. The securitized products opportunity set is broadening, but the risks are rising alongside it. For example, the legal documentation governing certain capital stacks appears insufficient to protect the IG and HY mezzanine tranches, as it is skewed in favor of the equity, the most subordinated tranche. In the CLO market, tiering pressures among managers are already emerging (the NAV levels tell the story; the market never had similar dispersion in 2.0 world), with some mezzanine tranches struggling to clear as bid–ask spreads widen between buyers and sellers.

Have we consistently invested in CLOs under the assumption that active management enhances the intrinsic value of securitized products? Throughout 2025, certain CLO managers disregarded repeated warnings and numerous cautions about deteriorating credit fundamentals in companies that would not be classified as financially conservative. The lack of available paper in primary and secondary and the repricings definitely influenced the choices of PMs.

- 4) Amid persistent uncertainty over economic growth, global trade fragmentation, fiscal sustainability concerns in Western economies, Central Banks cutting rates despite still-elevated inflation, rising credit risks, questions around the monetization of AI investments, and emerging stress in private credit markets, it is unsurprising that gold delivered its strongest rally in years in 2025. Forecasts stayed very short of the target. However, this move should not be interpreted merely as a reaction to fear or cyclical uncertainty. Rather, it reflects a deeper and more structural shift in global capital allocation. Investors are increasingly reallocating capital away from assets whose returns are highly dependent on financial leverage, policy support, or optimistic growth assumptions, and toward assets perceived as stores of value with limited duration risk and no reliance on counterparties.

In this context, gold is benefiting not only from declining official real rates, but also from a reassessment of portfolio construction in an environment where traditional diversification “stocks vs bonds” has weakened. The reallocation toward real assets signals a loss of confidence in the stability and predictability of financial assets, and suggests that the current gold rally is underpinned by long-term strategic flows rather than short-term positioning or risk aversion.

I conclude with literature, a source I find consistently resonant and ever pertinent. The “Proustian lesson” for investors is that habit—models, narratives, and historical analogies—can dull perception by forcing the present to resemble the past.



The greatest risks and opportunities arise when markets change and familiar frameworks no longer apply. Successful investors are those able, even briefly, to suspend habit, perceive what is genuinely new, and act before novelty is absorbed into consensus.

This requires intellectual ability, constant questioning of assumptions, and attention to anomalies rather than averages. Habit provides efficiency, but unexamined habit breeds complacency. Alpha, and risk management, ultimately depend on the ability to see before the market explains.

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