

MULTI-ASSET CREDIT STRATEGY

Quarterly Investment Review

PERFORMANCE DISCUSSION

The GMO Multi-Asset Credit portfolio continued to build on strong returns in the second quarter – a period in which we also generated our first full year of performance, which we are glad to share with clients.

In the second quarter, the portfolio posted a positive return, with Emerging Debt, High Yield, and Securitized Products contributing the lion's share of returns. This very strong quarter was driven not only by a relatively strong tone in risk, but also by underlying strategy alpha engines.

Nowhere is this more evident than looking at the trailing 1-yr performance of the portfolio, of which a third was driven by GMO's Emerging Country Debt Strategy, which has generated substantial outperformance based on its bottom-up, instrument selection philosophy as well as its holdings in Venezuela.

Additional contributions to returns were generated by Structured Products (~200 bps), High Yield (~70 bps), Systematic Investment Grade (~40 bps), and Agency RMBS (~30 bps). Rates and curve positioning was a slight drag, detracting -20 bps from performance. It is worth noting that the portfolio outpaced a more traditional multi-asset credit exposure - 50% U.S. High Yield and 50% U.S. Leveraged Loans - with considerably less risk and a higher quality tilt.

This first full year is a proof statement that underlying strategy alpha engines, coupled with top-down allocation, relative value positioning and hedges, is a powerful combination.

MARKET CONTEXT

Interest rates are starting to eat into risk assets, not only from the perspective of real yields at a generational high in U.S. Treasuries, but also from the impulse of front-end expectations leading into, and following, Kevin Warsh's appointment as Fed Chair.

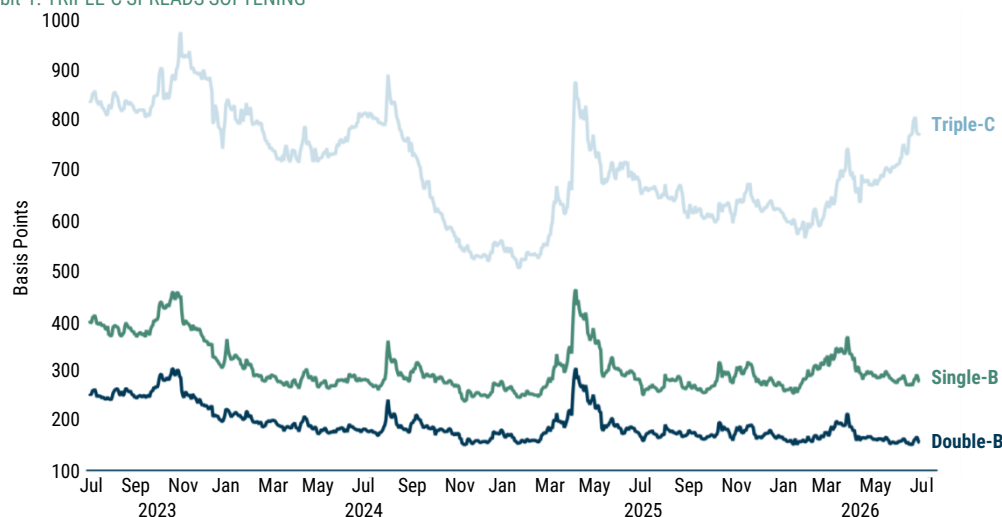
Taking the Chairman at his word, and as markets have certainly recognized, policy expectations have tightened since only a few months ago. However, perhaps as an acknowledgment of his appreciation for how his words have shifted expectations substantially, Warsh has in recent days tempered hawkishness.

The Chair tempered hawkish expectations by noting softening inflation pressure and alluded to the potential for technology to support productivity and disinflation. This seemingly abrupt change in view is consistent with policy jawboning associated with Mervyn King of the UK, who was recently appointed to an advisory role supporting a review of policy and communication.

With the current higher setting of yields, the cost of capital is beginning to eat into structures that need lower rates, refinancing, or are not cash generative. Cyclical stocks in Korea swooned, SpaceX's bond issue was a flop, and software woes continue.

On the credit side, high yield has been dragged wider by the CCC space with headline spreads up 20 bps in the latter days of the month, to roughly 280 bps. This compares with a near-term range of 250-325 bps. So, not cheap by any stretch of the imagination, but off the tights. While investment-grade spreads have softened, the move was far less noticeable.

Exhibit 1: TRIPLE-C SPREADS SOFTENING



Source: GMO, Bloomberg

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Exhibit 2: TOTAL RETURN

Total Return (%)	QTD	YTD
Bloomberg U.S. Aggregate	0.7	0.6
Bloomberg U.S. Corporate High Yield	2.5	2.0
Bloomberg U.S. Corporate Index	1.4	0.9
Bloomberg U.S. Securitized	0.6	1.0
J.P. Morgan EMBI Global Diversified	4.6	3.3
50/50 Leveraged Loans + High Yield	2.2	1.6
SOFR Index Plus 3%	1.6	3.3
MAC Blended Benchmark	2.3	1.8
Multi-Asset Credit Strategy (net of fees)	1.5	1.9

OUTLOOK & POSITIONING

We remain conservatively positioned, as has been the case for some time now. This is consistent with forward-looking expected returns in the context of both historical and loss-adjusted spreads. It is also consistent with the risk that elevated inflation keeps the Fed from easing aggressively into any equity market weakness.

With inflation elevated and necessary adjustments to fiscal sustainability relying on that to continue, we are at somewhat of a crossroads, with wages being the fulcrum. That is, wages must either rise to keep purchasing power intact and not dip further into savings that are largely exhausted, or we need to see a material decline in economic activity that may only be delayed by late-cycle consumer debt expansion, which is increasingly financed by BNPL (buy-now-pay-later) structures in private credit. This furthers the trend seen in HY and BSL of weaker credit generally moving to the private space, and legacy public markets seeing a tailwind of quality improvement.

Within the portfolio, we remain wary of spread duration and favor up-in-quality trades as well as relative value opportunities within and across credit derivatives. Our largest overweight remains the structured allocation, which is focused on seasoned positions with predictable cash flows. In addition, we have allocated to short-duration CLOs through a position in GMO's Ultra-Short Income Strategy.

Relative to underlying allocations to sub-portfolios, we are at or near our lows in Investment Grade, Emerging Debt, and High Yield, though we acknowledge their proven alpha potential and hedge betas where appropriate while still harvesting bottom-up and top-down alpha offered in underlying strategies, especially when considering total return prospects from the instrument selection.

At quarter end, approximately 66% of the portfolio was rated Investment Grade (BBB or higher), 45% of the portfolio was invested in Securitized Credit, 12.6% in High Yield, 7.5% in Investment Grade Corporates, 7.5% in Emerging Debt (including CDX hedge), 2.9% in Agency MBS, and 13.2% in U.S. Treasuries and ultra short income investments.

Given the starting point in yields, we feel comfortable with a low-risk position and focusing on carry until opportunities to deploy capital at more attractive prices or more obvious short candidates emerge. We have a penchant for being patient, while others lose theirs. Now is no different.

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ANNUALIZED RETURNS (USD, %) (QUARTER-END)

	<i>Quarter-End</i>	<i>YTD</i>	<i>1-Year</i>	<i>3-Year</i>	<i>5-Year</i>	<i>10-Year</i>	<i>Since Inception</i>
Multi-Asset Credit Strategy (net)	1.46	1.93	6.57	-	-	-	7.62
Multi-Asset Credit Strategy (gross)	1.60	2.21	7.13	-	-	-	8.18
Multi-Asset Credit Blended Benchmark	2.26	1.78	6.77	-	-	-	8.17
Value Add vs. Multi-Asset Credit Blended Benchmark	-0.81	+0.15	-0.20	-	-	-	-0.55
SOFR Index Plus 3%	1.63	3.28	7.00	-	-	-	7.06
Value Add vs. SOFR Index Plus 3%	-0.17	-1.35	-0.43	-	-	-	+0.56

RISKS

Risks associated with investing in the Strategy may include: (1) Credit Risk: the risk that the issuer or guarantor of a fixed income investment or the obligor of an obligation underlying an asset-backed security will be unable or unwilling to satisfy its obligation to pay principal and interest or otherwise to honor its obligations in a timely manner; (2) Market Risk-Asset-Backed Securities Risk: the market price of asset-backed securities, like that of other fixed income investments with complex structures, can decline for a variety of reasons, including investor uncertainty about their credit quality and the reliability of their payment streams. Payment streams associated with asset-backed securities held by the Fund depend on many factors (e.g., the cash flow generated by the assets backing the securities, deal structure, and creditworthiness of any credit-support provider), and a problem in any of these factors can lead to a reduction in the payment stream GMO expected the Fund to receive when the Fund purchased the asset-backed security; (3) Illiquidity Risk: low trading volume, lack of a market maker, large position size, or legal restrictions may limit or prevent the Fund from selling particular securities or closing derivative positions at desirable prices; and (4) Pooled Investment Vehicles Risk: Investments by a Fund in pooled investment vehicles may involve additional and/or a layering of fees, expenses, changes and other costs (including without limitation, purchase premiums and redemption fees, if any). This is not a complete list of risks associated with investing in the Strategy. Please contact GMO for more information.

Composite Inception Date: 31-May-25

Performance Returns: Performance for the year of inception is less than a full calendar year. Returns shown for periods greater than one year are on an annualized basis. To obtain performance information to the most recent month-end, visit www.gmo.com. **Performance data quoted represents past performance and is not indicative of future results.** Net returns are presented after the deduction of a model advisory fee and incentive fee if applicable. These returns include transaction costs, commissions and withholding taxes on foreign income and capital gains and include the reinvestment of dividends and other income, as applicable. Fees paid by accounts within the composite may be higher or lower than the model fees used. Gross returns are presented gross of management fees and any incentive fees if applicable. These returns include transaction costs, commissions, withholding taxes on foreign income and capital gains and include the reinvestment of dividends and other income, as applicable. If management and incentive fees were deducted performance would be lower. For example, if, before fees, the strategy were to achieve a 10% annual rate of return above its hurdle rate each year for ten years, and an annual advisory fee of 1% and incentive fee of 20% of net returns above the hurdle rate were charged during that period, the resulting average annual net return (after the deduction of management and incentive fees) would be approximately 7.20%. **GMO does not yet have a GIPS-compliant report for this composite since it has not managed accounts in this strategy for a full year.**

IMPORTANT INFORMATION

Benchmark(s): The Multi-Asset Credit Blended Benchmark is an internally maintained benchmark computed by GMO, comprised of (i) 25% Bloomberg U.S. Securitized Index, (ii) 25% Bloomberg U.S. Corporate High Yield Index, (iii) 25% Bloomberg U.S. Corporate Index, and (iv) 25% J.P. Morgan EMBI Global Diversified.

The above information is based on a representative account in the Strategy selected because it has the fewest restrictions and best represents the implementation of the Strategy.

For private bank intermediaries in Singapore and Hong Kong, these materials are intended for institutional and Accredited/Professional Investors Use Only.

ABOUT GMO

Founded in 1977, GMO is a global asset manager committed to delivering superior performance and advice to our clients. We are privately owned, which allows us to singularly focus on our sole business – achieving outstanding long-term client investment outcomes. Offering multi-asset, equity, fixed income, and alternative strategies, we invest with a long-term, valuation-based philosophical approach.

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*GMO's West Coast Hub is comprised of members of Investment, Global Client Relations, and other teams located in and around the Greater San Francisco area

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