

Relative Value Across the Credit Continuum

Transcript

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Guillermo Felices, PhD, Global Investment Strategist, PGIM Credit: So the increased complexity means that relative value must be assessed across the full credit spectrum. Similar risks can appear in different forms in public and private credit markets in order to meaningfully assess the asset class, one has to assess relative value across three key layers.

The first one is, basically the point of purchase, or more of a bottom-up approach. In this case, basically private credit value is expressed through origination and also through other characteristics like structure, covenants, collateral, and underwriting discipline. And in public markets, price signals become more important because they are more transparent and they are more accessible through primary and secondary markets.

The second layer is a cross-market comparison, so more of a top-down relative value assessment, where we compare similar risks across public and private credit markets. And the idea here is to assess how the same risk is priced once differences in liquidity, in structure, and volatility are taken into account.

And then the third layer is portfolio construction. We need to make sure that we meet the needs of our investors in terms of illiquidity preferences, but also in terms of risk preferences. Anchoring the private allocation using investors' illiquidity tolerances allows the optimization to become less sensitive to opaque and sometimes uncertain private market assumptions, like returns and volatility. And once those private allocations are set, the public credit piece provides flexibility, an opportunity to liquidity manage, and, also, the ability to rebalance portfolios.

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