

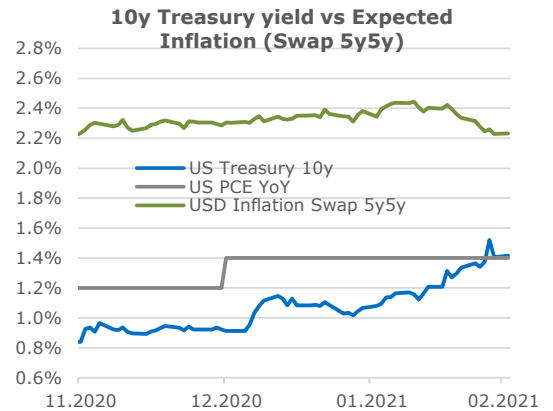
Monthly Spotlight

Real rates increased while expected inflation did not (yet) move

Since December 2020, US long-term nominal yields (US Treasury 10y) rose 60 bps, while expected inflation (US Inflation Swap 5y5y) remained flat at ~2.2%. Markets incorporate a benign outlook, but inflation will pick up significantly over the next quarters based on statistical effects (y-o-y comparison) and cyclical forces (economic recovery, lower unemployment, higher commodity prices). Therefore, we expect bouts of market volatility as rates tend to rise and equity multiples to shrink.

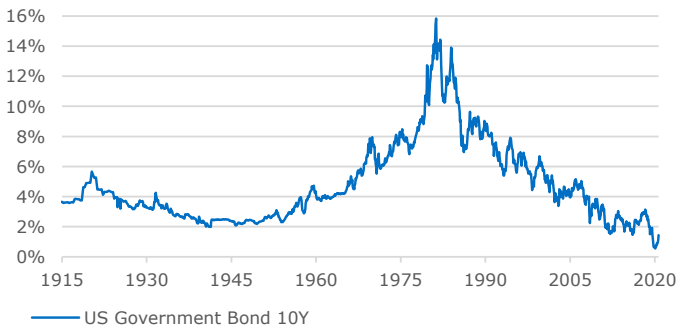
$$\text{nominal yield} = \text{real yield} + \text{expected inflation}$$

The US Fed announced that it will tolerate a temporary inflation overshoot above 2% with its recently implemented "average inflation targeting" framework. Nevertheless, should "expected" inflation move towards 3% or beyond, bond and equity markets will be challenged.

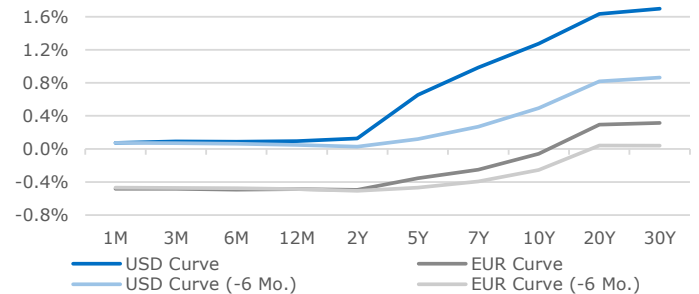


Rates Perspective

1) Historical US Treasury Yield: 10-year US government bond yield reached its 100-year low in 2020.

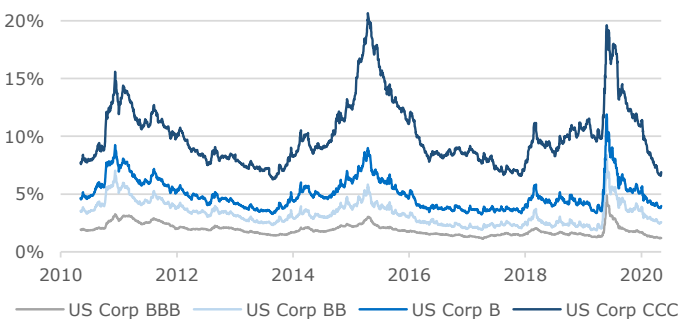


2) Interest Swap Curve: USD swap curve steepened considerably. EUR curve has steepened modestly at the long end with 20y tenor back in the positive.



Corporate Perspective

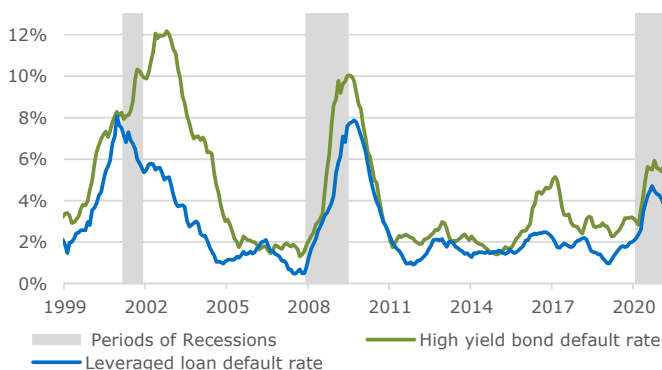
3) US Corp. Rating: Credit spreads (OAS) of lower rated high-yield bonds continued to tighten disproportionately.



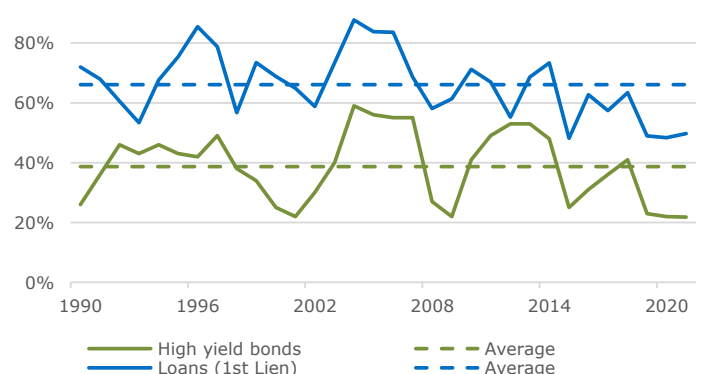
4) EU vs US: Since the March-spike, credit spreads (OAS) between the USA and EU have converged in tandem to lower levels.



5) Default Rates: Default rates of HY bonds & loans are peaking. HY bond default rates are structurally higher (Ø4.4%) vs. loans (Ø2.8%).



6) Recovery Rates: Recovery rates of leveraged loans are higher (Ø66%) vs. high yield bonds (Ø39%) due to lower severity.



OAS spread change overview across major credit asset classes - as of month end

US corporates by rating (bps)

	curr	Δ month
AAA	50	-5
AA	60	-5
A	72	-7
BBB	119	-9
BB	256	-24
B	397	-21
CCC	691	-49

Global high yield (bps)

	curr	Δ month
US HY	357	-21
EU HY	324	-26
Asia HY	745	-3
EM HY	404	-21

■ spread tightening (positive price action)
■ spread widening (negative price action)

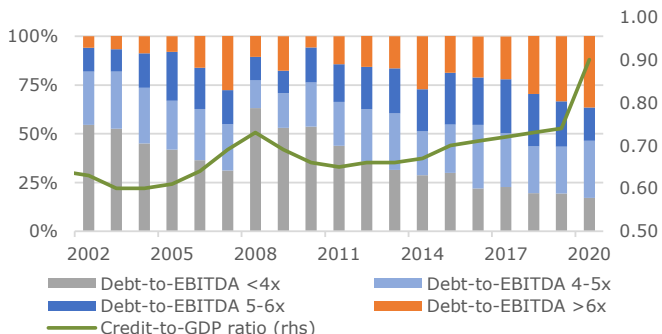
CDS spreads (bps)

	curr	Δ month
CDX IG - US	56	-0
iTraxx IG - EU	51	-1
CDX HY - US	310	-8
iTraxx XO - EU	265	-4

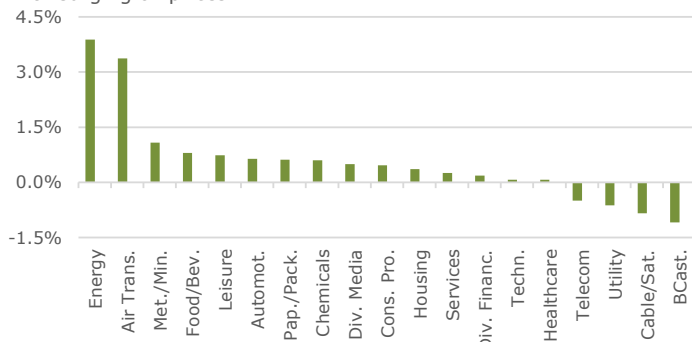
Loans and CLOs (yld, bps)

	curr	Δ month
US Loan	366	-11
CLO AAA	130	-1
CLO BBB	381	-4
CLO BB	774	+25

7) US Leverage: Debt-to-EBITDA of US companies decreased in Q1 2020, but increased to a record high in Q3 2020.



8) YTD Sector High-Yield Returns: Broadcasting, cable, telecom, and utilities faced negative price action YTD, while energy rallied with surging oil prices.

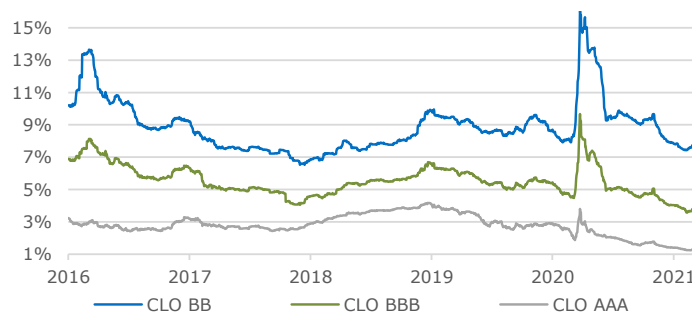


Alternative Perspective

9) Loans vs. CLO vs. HY: CLO BB yields are still wider vs Loans and HY bonds, despite the recent price increase in CLO BB.



10) CLO Yields: CLO BB yields tightened more than higher rated CLOs. CLOs offer an attractive yield premium over bonds / loans.



11) Asia vs. US: Despite a recent tightening of Asian IG spreads they continue to offer a sizeable premium vs. US IG spreads.



12) Capital vs IG: Capital Securities structurally earn a premium vs. US IG bonds. Capital Securities are dominated by the financial sector.



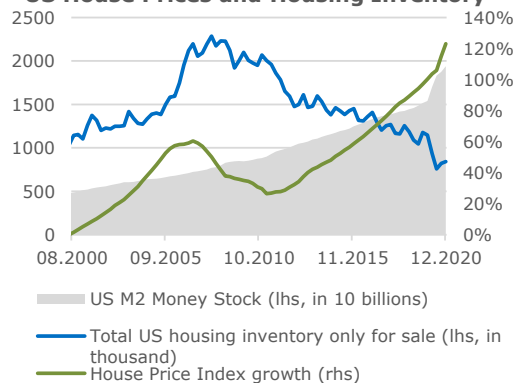
Education Corner

US house prices reach all-time high, inventories collapsed

Supply shortage in "homes for sale" combined with ultra-low mortgage rates and "staying at home" measures drove home prices to record levels. The median price of a home sold in December 2020 reached USD 340,000 (Realtor.com) – an all-time high level.

US housing inventories fell to a multi-year low level because of a variety of reasons: 1) the pandemic created job insecurity and hence, employees preferred to stay in their job, what resulted in less "mobility" and lower home sales activity. 2) More than 4 mio. homeowners with government-backed loans were in mortgage forbearance during the pandemic. Many of these homes would otherwise have hit the market. However, government policies such as the COVID hardship mortgage forbearance and a temporary halt of foreclosures prevented "forced sales" so far.

US House Prices and Housing Inventory



US Loan Index Total Return - Attractive Long Term Yield Generation



List of Abbreviations

Capital Securities (Or preferred securities): Are fixed income securities combining features of bonds and preferred stocks.

CDS: Credit default swaps transfer credit event risk to another party in exchange of a periodically paid premium. CDX index covers the US IG-, iTraxx the EU IG- and iTraxx crossover (XO) the EU HY market.

CLOs: Collateralized loan obligations are structured finance securities collateralized predominantly by a large pool of different loans.

Default Rate: Number of defaulted corporate issuers of leveraged loans and high yield bonds.

Loans: Are syndicated, public tradable loans. Synonyms are «syndicated loans», «loans», «leveraged loans» and «bank loans».

OAS: Option-adjusted spread is the yield difference of an interest paying security to the risk free rate considering embedded options.

TIPS: Treasury Inflation-Protected Securities are US government linked to the US CPI Urban Non-Seasonally Adjusted.

Up-/ downgrades: Rating actions of Moody's and S&P of up-or downgrades of US high yield bond issuers denominated in USD.

Up-/ downgrade ratio: Number of upgrades of total rating actions.

Recovery Rates: Bond issuer-weighted recovery rates express the principal and accrued interest on defaulted debt that can be recovered in percentage of face value. Example:

Expected loss rate if US HY defaults were 10%: 10% ./ Estimated average recovery rate of ~30% = -7%; Example for Loans:

Expected loss rate if US Loan defaults were 10%: 10% ./ Estimated average recovery rate of ~65% = -3.5%;

Data and Price Sources

Alpimum Investment Management

Bank of America Merrill Lynch indices

Bloomberg

The Federal Reserve

US Census Bureau

Federal Reserve Bank of St. Louis

Markit CDS indices

Moody's Investors Service

J.P. Morgan

Palmer Square indices

Preqin

S&P

Federal Housing Finance Agency

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Contact Information:
Alpimum Investment Management AG
Talstrasse 82
CH-8001 Zurich
Tel: +41 43 888 79 30
Fax: +41 43 888 79 31
alpimumim.com