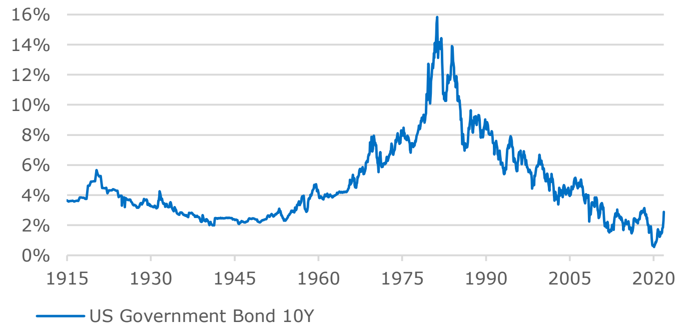
Monthly Spotlight

Short Term High Yield Rates are attractive again @ 7% p.a.

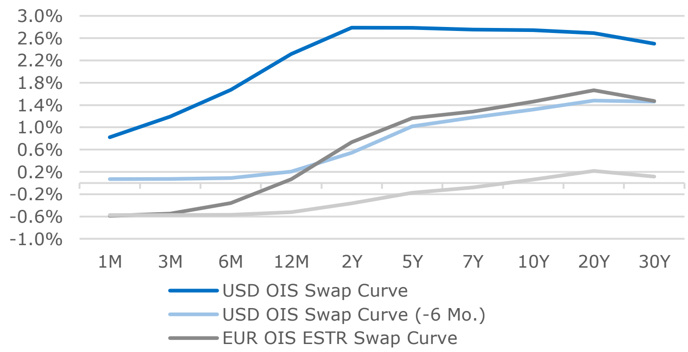
Yields of US short term low grade bonds broke through the 10-years average of 5.7% and reached a level of 6.9%. Since the Fed signalled a faster pace of interest rate increases in the coming months, investors divested longer term bonds in favour of their shorter term counterparts. The yield curve steepening by more than 200 bps over the last 6 months (please see chart 2) has been the main driver of the increase of the yield level. Another driver has been the investor's uncertainty about whether the economy and company earnings can withstand an aggressive Fed tightening to fight inflation. Absent of a severe recession ahead of us, yields on low grade bonds are back at attractive levels.

Rates Perspective

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

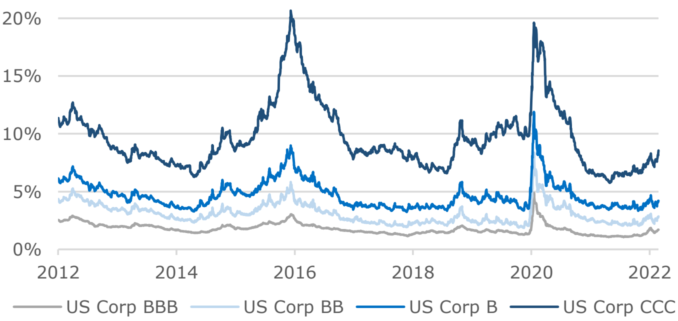


2) Interest Swap Curve: Both the USD curve and the EUR curve steepened predominantly at shorter tenors.

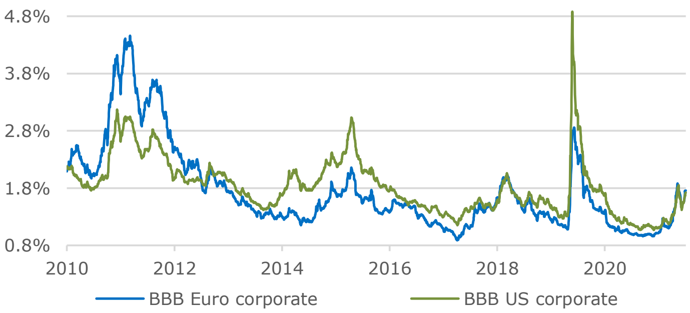


Corporate Perspective

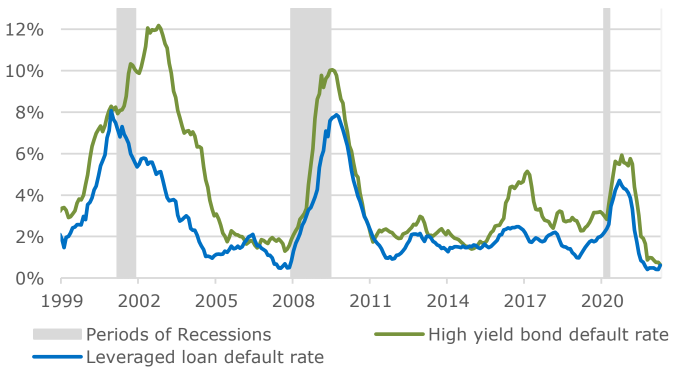
3) US Corp. Rating: Credit spreads (OAS) of lower rated high-yield bonds widened disproportionately.



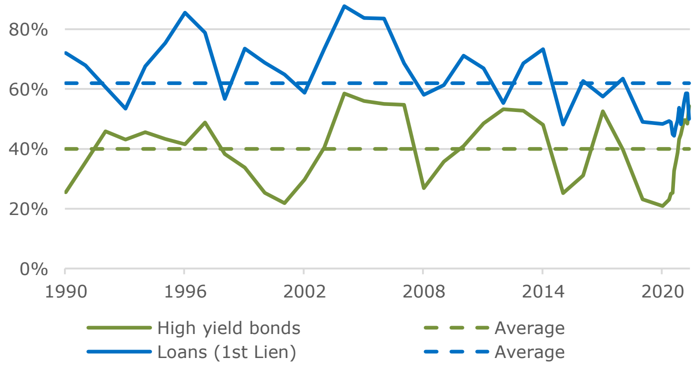
4) EU vs US: Credit spreads (OAS) between the US and EU have narrowed since the beginning of 2022.



5) Default Rates: HY bond default rates are structurally higher (Ø4.3%) vs. loans (Ø2.7%).



6) Recovery Rates: Recovery rates of leveraged loans are higher (Ø62%) vs. high yield bonds (Ø40%) 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	70	+12
AA	86	+12
A	117	+18
BBB	171	+22
BB	285	+48
B	421	+44
CCC	855	+126

Global high yield (bps)

	curr	Δ month
US HY	397	+54
EU HY	454	+54
Asia HY	1120	-172
EM HY	487	+40

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

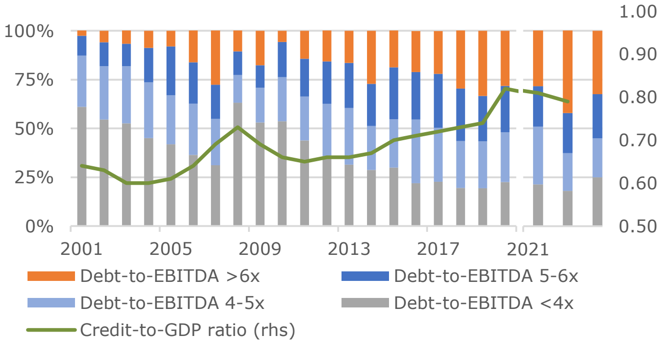
CDS spreads (bps)

	curr	Δ month
CDX IG - US	84	+16
iTraxx IG - EU	90	+17
CDX HY - US	461	+85
iTraxx XO - EU	428	+89

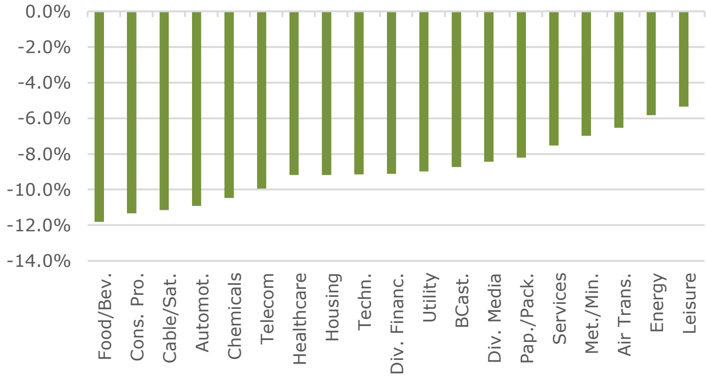
Loans and CLOs (yld, bps)

	curr	Δ month
US Loan	474	+37
CLO AAA	434	+58
CLO BBB	656	+71
CLO BB	1036	+73

7) US Leverage: Debt-to-EBITDA of US companies has remained stable at high level in Q3 2021 compared to Q4 2020.

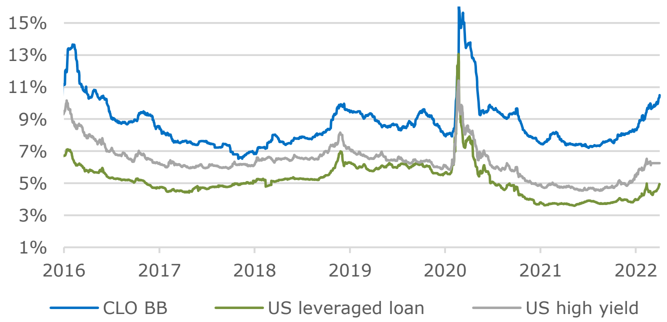


8) YTD Sector High-Yield Returns: Total return of food and beverage suffered the most.



Alternative Perspective

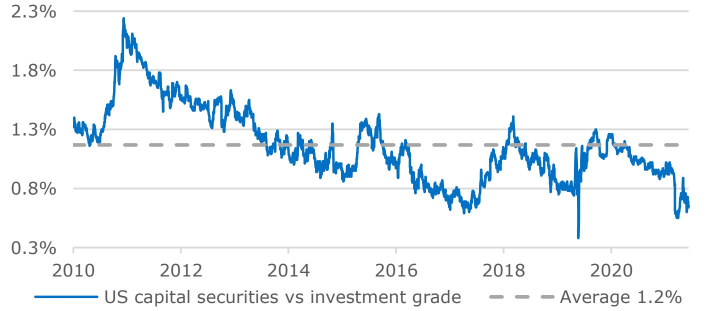
9) Loans vs. CLO vs. HY: CLO BB yields are wider vs Loans and HY bonds.



10) CLO Yields: CLOs offer an attractive yield premium over bonds and loans.

11) Asia vs. US: Asian IG spreads spiked in recent months due to the stress in the Chinese real estate development sector.

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

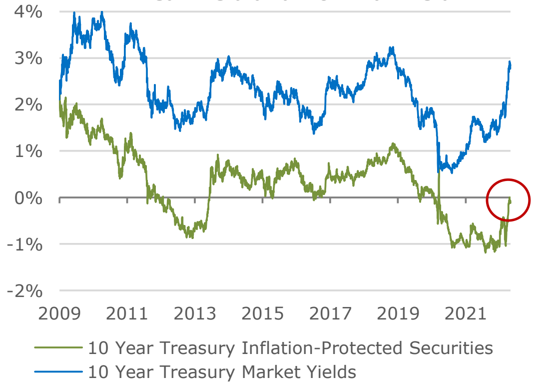


Education Corner

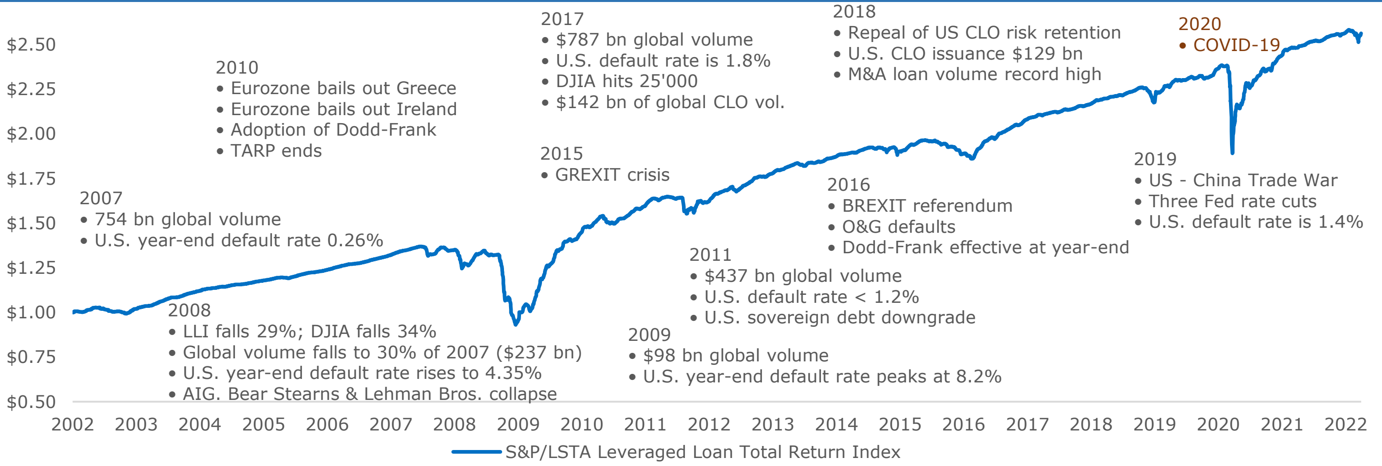
US Real Yields reach positive territory again

Yields on the 10-year Treasury Inflation-Protected Securities (TIPS) - also known as real yields because they subtract projected inflation from the nominal yield on Treasury securities - had been in negative territory since March 2020, when the Federal Reserve cut interest rates to near zero. That changed in April 2022, when real yields climbed above zero. This had been caused in anticipation of a tighter monetary policy, which is pushing yields higher. Negative real yield means that the nominal yield earned (i.e. 10-year Treasury note) is lower than the assumed inflation yield. Real interest rates of 0 will also affect the equity risk premium, which measures how much investors expect to be compensated for owning stocks over government bonds. This can be a headwind for growth stocks, where future cash flows are often more weighted and diminished when discounted at higher rates.

Real Yield and Nominal Yield



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 perdiodically 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

Alpinum Investment Management	Federal Reserve Bank of St. Louis	Palmer Square indices
Bank of America Merrill Lynch indices	Markit CDS indices	Preqin
Bloomberg	Moody's Investors Service	S&P
The Federal Reserve	J.P. Morgan	Federal Housing Finance Agency
US Census Bureau		

Disclaimer

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