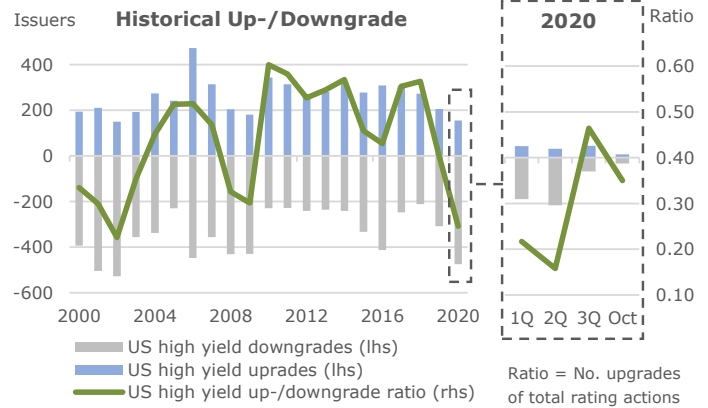


## Monthly Spotlight

### Rating downgrade avalanche has slowed down

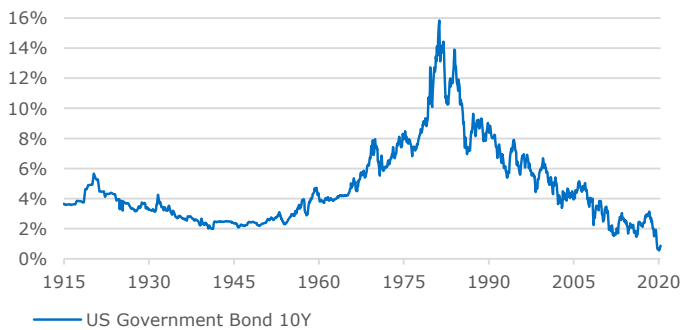
Year-to-date US high yield corporate rating downgrades accumulated to more than 475 - even surpassing the previous crisis in 2008. The up-/downgrade ratio (proportion of upgrades among total rating actions of Moody's and S&P) marked a low of 0.16 in Q2 2020 and the accumulated YTD ratio reached 0.25, a similar low level as experienced during the DotCom-Bubble burst.

Since Q3 2020, rating actions are normalizing and in October 2020 the overall downgrades shrank to only 26 issuers, which is ~90% lower compared to Q2 2020 with 208 downgrades.

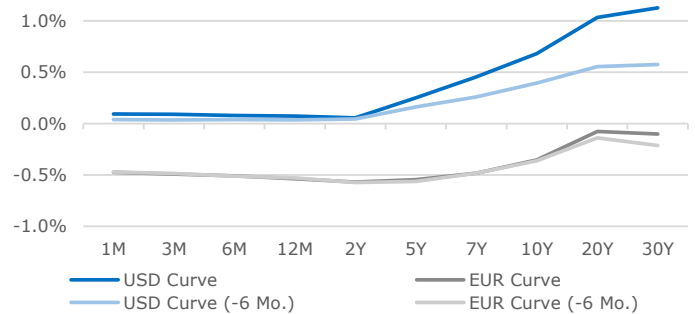


## Rates Perspective

**Chart 1:** 10-year US government bond yield is at 100 years low, as the chart below does well illustrate.

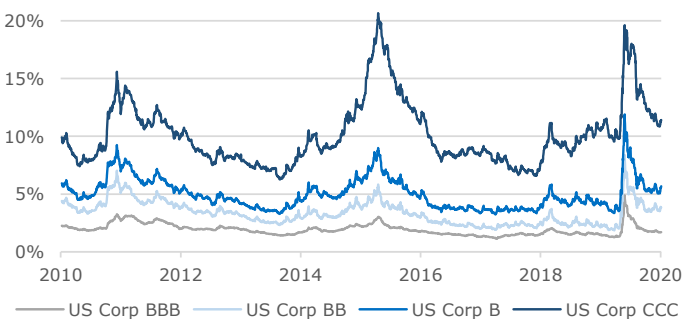


**Chart 2:** USD swap curve has steepened more than the EUR curve, implying a faster economic recovery in the U.S.

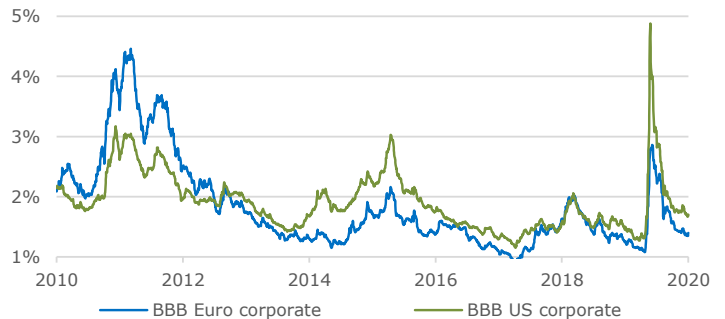


## Corporate Perspective

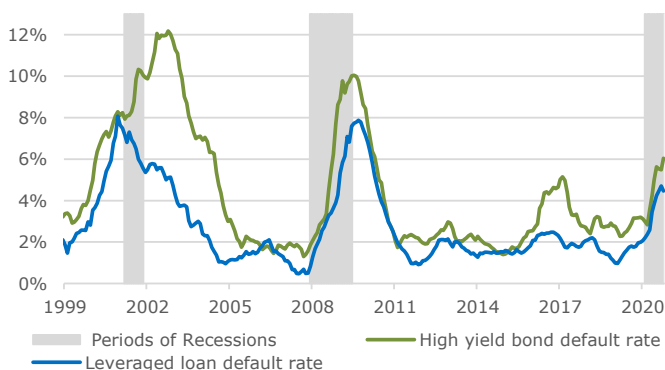
**Chart 3:** Credit spreads (OAS) of CCC-rated bonds are still elevated with energy/transport sector still in stress/distress.



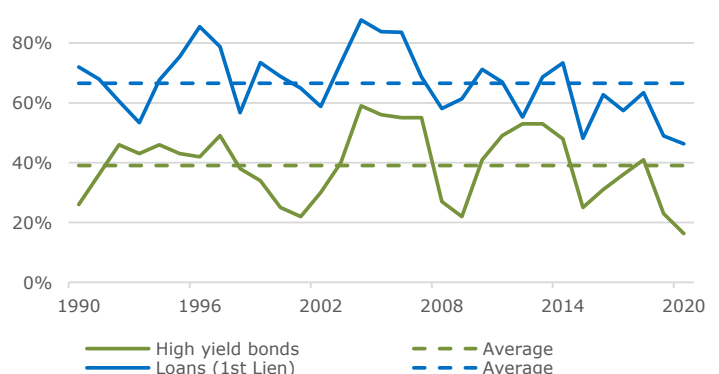
**Chart 4:** Since the March-spike, credit spreads (OAS) between the USA and EU have converged in tandem to lower levels.



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



**Chart 6:** Recovery rates of leveraged loans are higher (Ø67%) 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 monthly
AAA	72	-6
AA	82	-5
A	99	-9
BBB	171	-13
BB	384	-16
B	568	+1
CCC	1141	-11

### Global high yield (bps)

	curr	Δ monthly
US HY	532	-4
EU HY	482	+16
Asia HY	887	+23
EM HY	569	-2

■ spread tightening  
■ spread widening

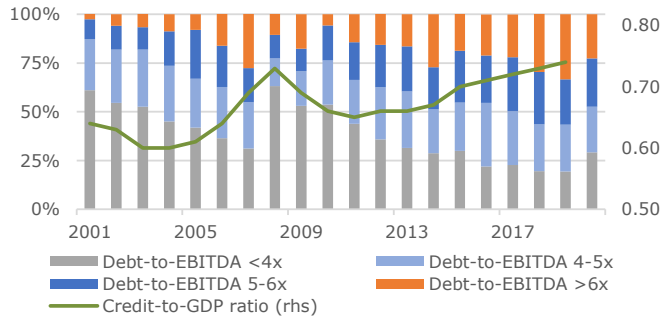
### CDS spreads (bps)

	curr	Δ monthly
iTraxx IG - EU	65	+6
CDX IG - US	65	+6
iTraxx XO - EU	421	+12
CDX HY - US	369	+24

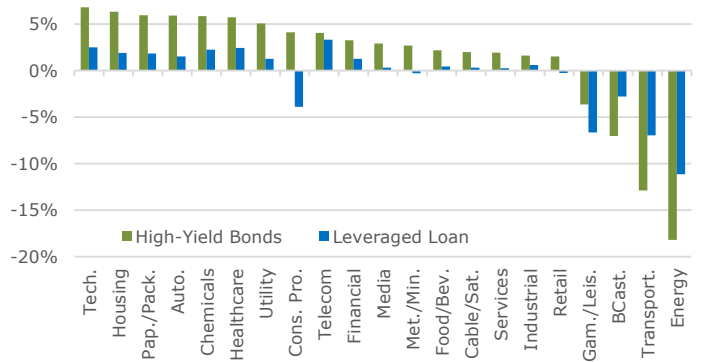
### Loans and CLOs (yld, bps)

	curr	Δ monthly
US Loan	479	-14
CLO AAA	178	+12
CLO BBB	507	+42
CLO BB	967	+54

**Chart 7:** US companies increased their Debt-to-EBITDA leverage over recent years. US Debt-to-GDP ratio is at peak level.

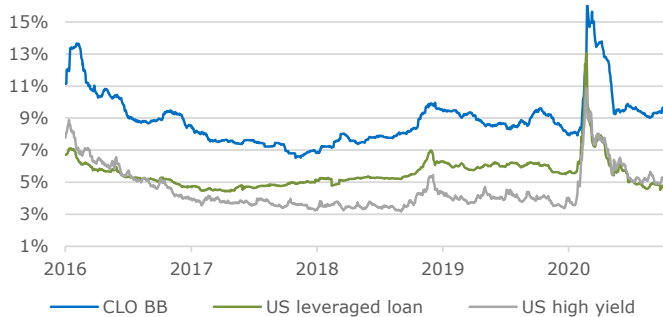


**Chart 8:** Energy and transportation performed worst YTD in %. Loans experienced smaller drawdowns vs. HY bonds.

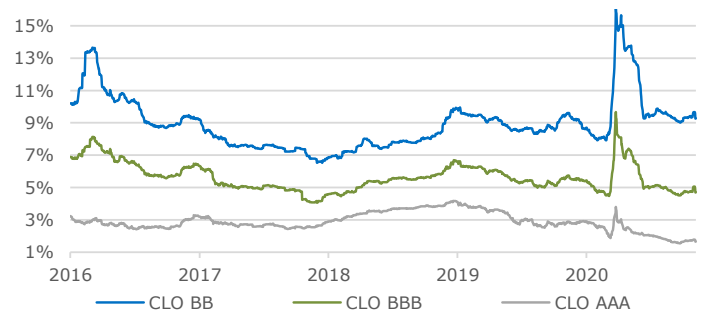


## Alternative Perspective

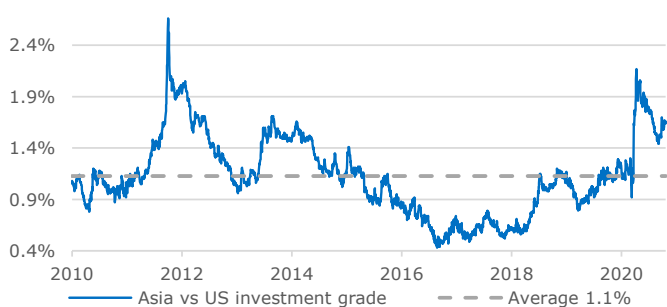
**Chart 9:** The spread of US loans and US HY bonds converged to around 5%, whereas CLO BB yield is still >9% p.a.!



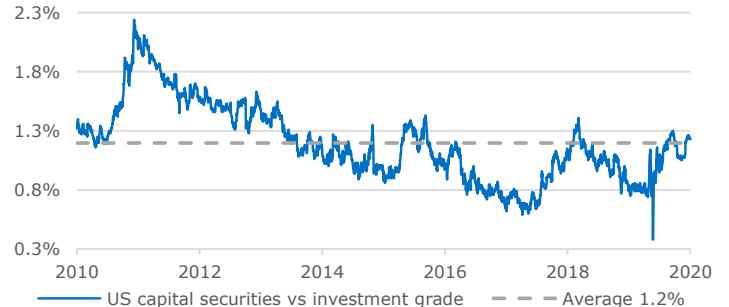
**Chart 10:** CLO yields offer a significant yield premium vs. bonds/loans, whereas BB/BBBs look particularly attractive.



**Chart 11:** Asian IG bonds pay a structural premium vs. the US. Current elevated OAS represent a buying opportunity.



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



## Education Corner

### Inflation linked Notes - TIPS

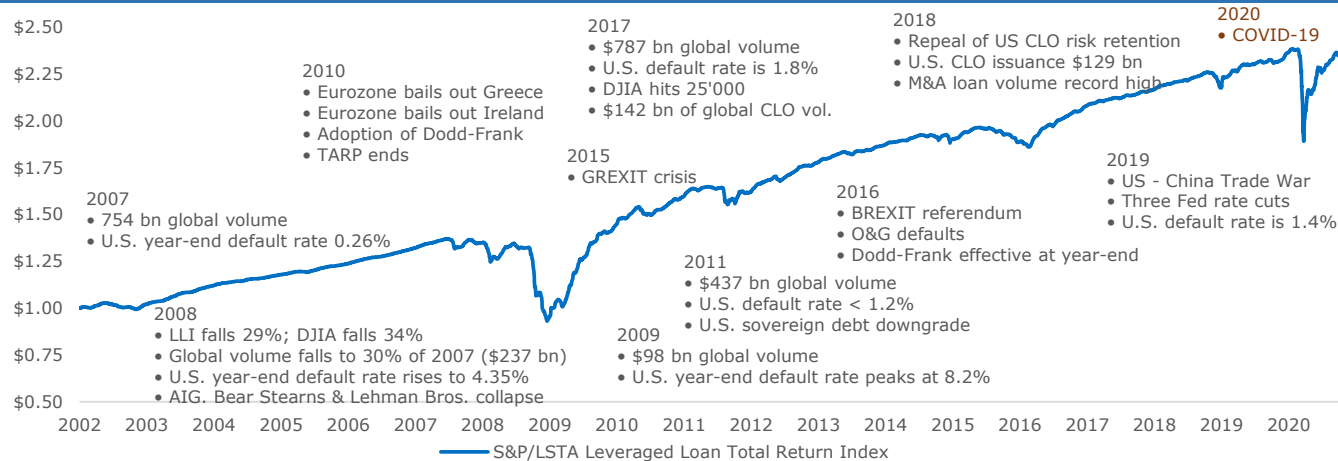
The "classic" US treasury yield represents the nominal interest rate level, whereas the inflation-linked treasury (i.e. TIPS) is an US CPI adjusted bond, indicating the real interest rate. The breakeven interest rate is considered to be the expected inflation, which currently stands at 1.8%.

$$(1 + \text{yield}_{\text{nominal}}) = (1 + \text{yield}_{\text{real}}) * (1 + \text{inflation}_{\text{expected}})$$

Rational for buying TIPS: If the investor believes inflation will trend higher than 1.8%, he prefers buying inflation-linked bonds (i.e. TIPS). On the opposite, if he believes inflation will trend lower than 1.8%, he prefers buying nominal bonds.



## 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

Federal Reserve Bank of St. Louis

Markit CDS indices

Moody's Investors Service

J.P. Morgan

Palmer Square indices

Preqin

S&P

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