

Monthly Spotlight

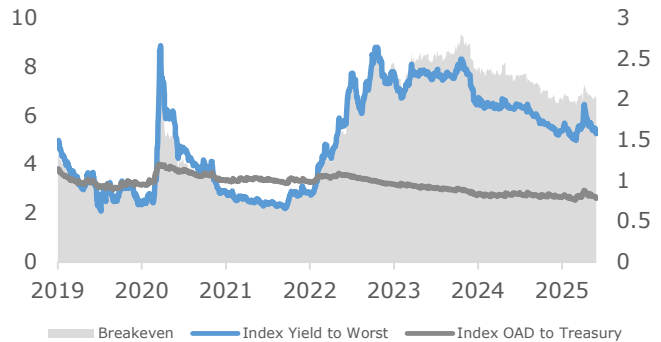
Attractive Breakeven Cushion in European High Yield

As of the end of May, the European High Yield index delivered a return of over 1.3%, fully erasing the losses from March and reaching new highs for the year at 2.30%.

Despite this strong performance, the European High Yield market continues to offer an attractive medium and long-term opportunity, considering that default rates are expected to remain contained and breakevens still provide a cushion of 201 basis points. This is illustrated in the chart on the right, which shows the Pan-European high yield bond index (with the left axis reflecting Yield to Worst and Option Adjusted Duration, and the right axis showing the breakeven).

The current carry provides a substantial buffer against potential increases in yields before investors would begin to experience negative total returns over a 12-month period.

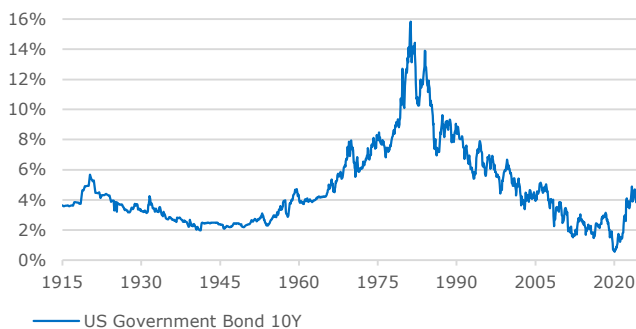
Pan-European High Yield (Euro)



Breakeven: The amount yields can increase before returns turn negative.

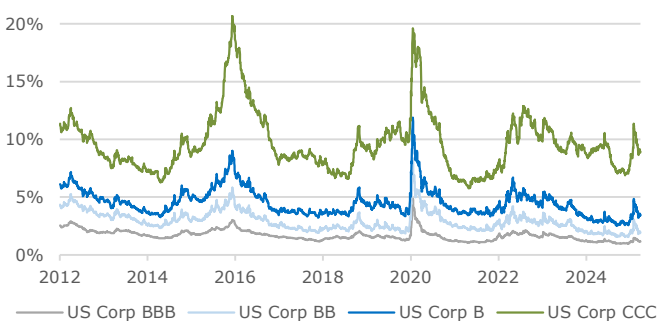
Rates Perspective

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

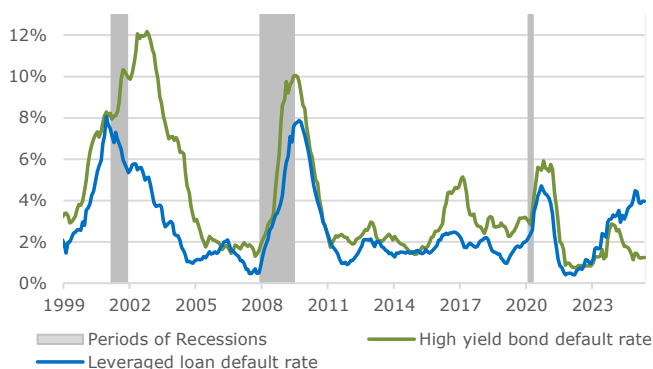


Corporate Perspective

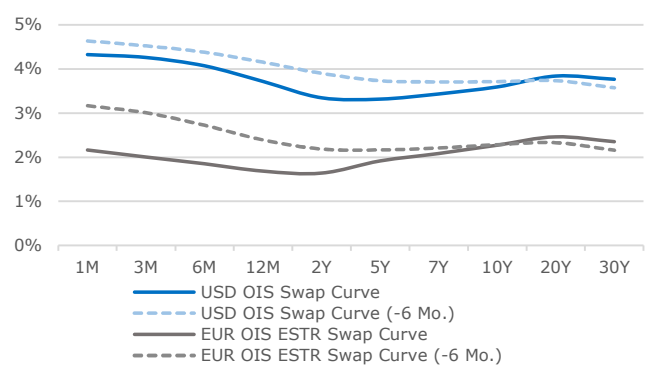
3) US Corp. Rating: Credit spreads (OAS) of lower rated high-yield bonds widened disproportionately.



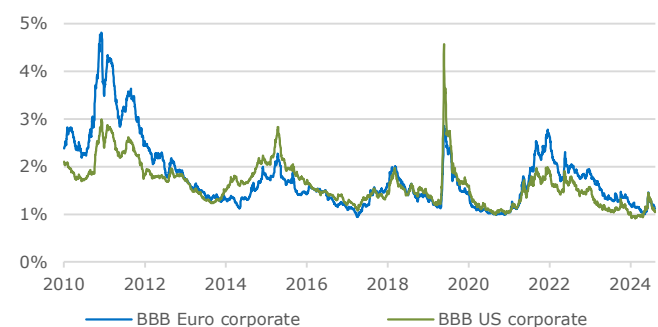
5) Default Rates: HY bond default rates have been structurally higher (Ø4.0%) vs. loans (Ø2.7%).



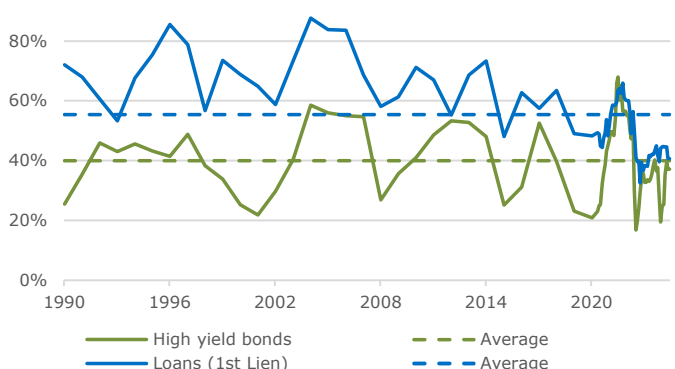
2) Interest Swap Curve: The USD and EUR curves are V-shaped with minima around 2Y maturities.



4) EU vs. US: EU credit spreads (OAS) are now at similar levels than in the US.



6) Recovery Rates: Recovery rates of leveraged loans are higher (Ø55%) 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	37	-9
AA	49	-12
A	76	-14
BBB	115	-22
BB	197	-57
B	349	-62
CCC	896	-104

Global high yield (bps)

	curr	Δ month
US HY	331	-63
EU HY	326	-44
Asia HY	575	-29
EM HY	418	-57

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

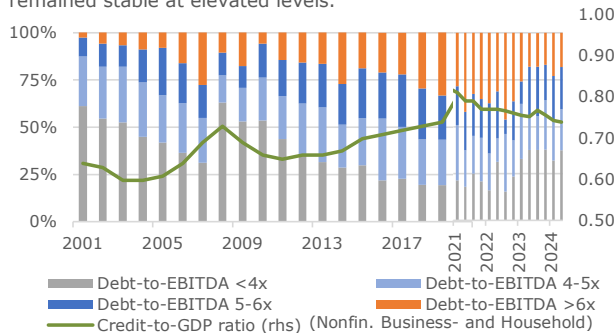
CDS spreads (bps)

	curr	Δ month
CDX IG - US	56	-11
iTraxx IG - EU	58	-10
CDX HY - US	351	-56
iTraxx XO - EU	300	-50

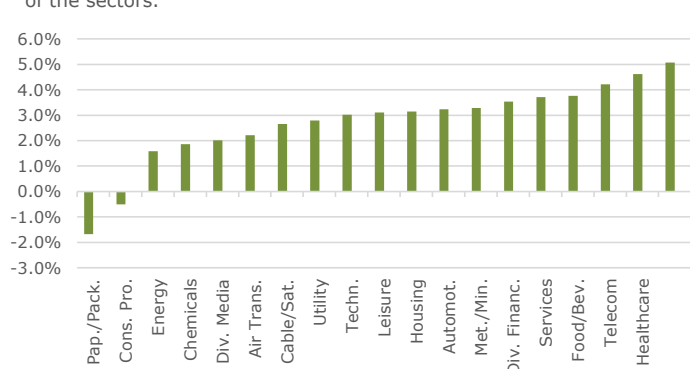
Loans and CLOs yields (bps)

	curr	Δ month
US Loan	796	-19
CLO AAA	567	-1
CLO BBB	795	-1
CLO BB	1095	-1

7) US Leverage: Debt-to-EBITDA ratio of US companies remained stable at elevated levels.

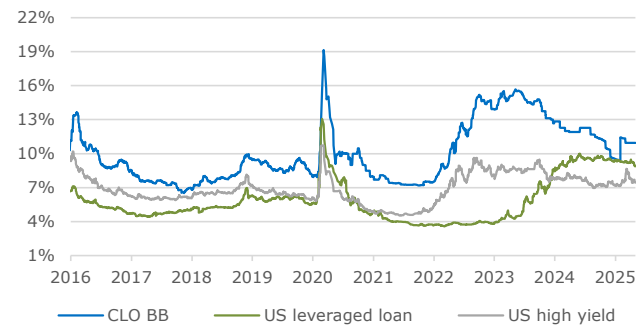


8) YTD Sector High-Yield Returns: Positive YTD results across most of the sectors.



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 have tightened thanks to gradual post-COVID recovery and US inflation easing.



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



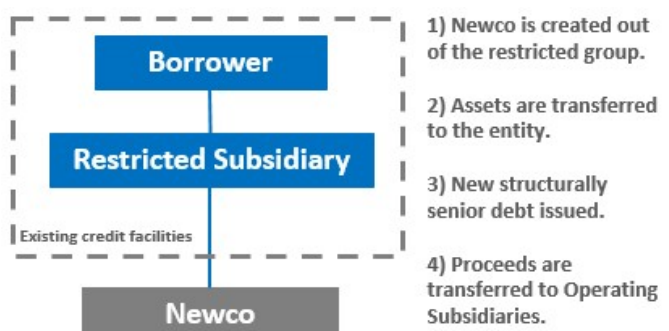
Education Corner - Series: AIM Credit Analysis (15)

Liability Management Exercises: Asset Drop-Downs

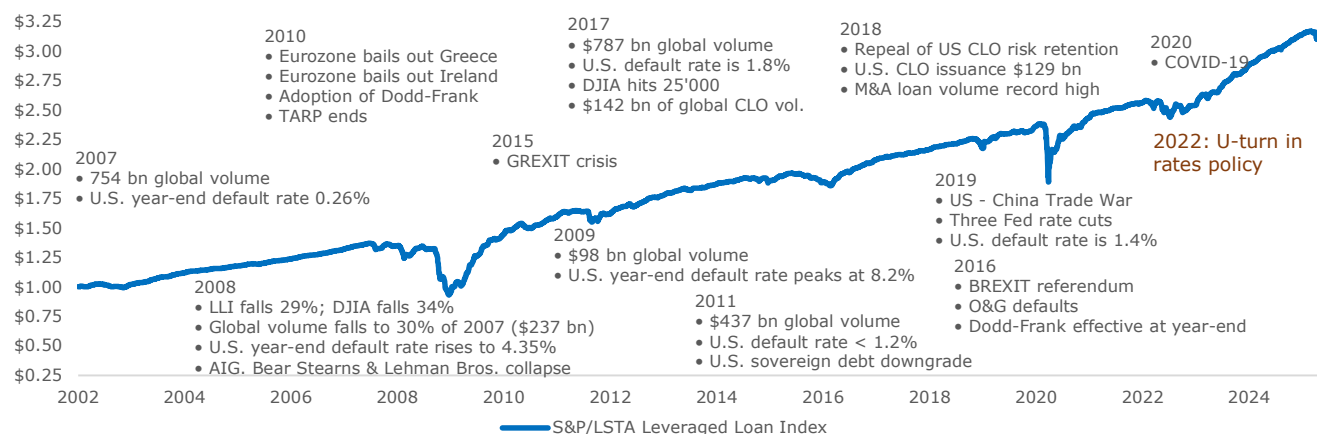
Last month, we explored the growing prevalence of Double-Dip structures in liability management exercises (LMEs). This month, we will take a closer look at another sophisticated liability management tool: Asset Drop-Downs. Famously utilized in high-profile restructurings such as Caesars Palace and J. Crew, Asset Drop-Downs involve transferring assets out of the credit group, thereby making them potentially available as collateral for new lenders.

These transactions typically involve transferring a borrower's assets to an unrestricted subsidiary. The company then issues new debt, securing it with the now unencumbered collateral and effectively subordinating the excluded lenders to a second lien position. This structure provides distressed companies with an effective means to raise additional capital by establishing a new priority claim on the transferred assets.

Asset Drop-Down Example



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

Alpinum 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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