High Yield Corporate Bonds

Limited Net Supply Despite a Surge in Issuance

Now may be an ideal time to move up in quality while reducing exposure to lower quality, cyclical bonds.

The high yield market has seen a meaningful increase in gross supply, but net supply remains limited as the majority of issuance has been refinancing activity. Tight spreads have been supported by favorable technical dynamics and strong fundamentals, including low default rates and healthy issuer fundamentals. However, we expect more challenging dynamics in capital intensive sectors like communications, highlighting the need for selectivity. Our strategy emphasizes quality, while reducing some exposure to cyclical sectors.

Sector Commentary

- We continue to see a high share of secured issuance in the market, representing 41 percent of volume this year, partially driven by issuers refinancing loans in the bond market.
- Credit spreads have averaged 318 basis points in 2024 and ended April at just 299 basis points. Spreads are in the 10th percentile of historical valuations dating back to 1994, but they are supported by favorable technical and fundamental dynamics.
- The par-weighted default rate in the high yield index is 2.4 percent, which is below the historical average of 4.0 percent. Fundamentals have been supportive of low default activity as many borrowers carry largely fixed-rate debt, which has allowed interest coverage to stay at healthier levels than in recent history.
- Yields continue to present attractive value, particularly in BB-rated and B-rated bonds.

Investment Themes

- High yield returns were positive through April 30, but interest rate volatility returned as Treasury yields backed up, detracting from performance. CCCs outperformed BB-rated and B-rated bonds due to their limited volatility, but we expect higher quality to outperform once the Fed's easing cycle is more clearly in sight.
- Returns were positive across most industries, but idiosyncratic risks weighed on some sectors. In communications, competition, high capital expenditure requirements, and weakness in some of the largest companies' capital structures, caused the sector to return -4.2 percent year to date. The top two performing industries were energy and consumer non-cyclical.
- Current yield to worst across sectors continues to look attractive, except for communications. We believe now presents an ideal opportunity to move up in quality while reducing exposure to lower quality, cyclical bonds.

By Thomas Hauser and Maria Giraldo

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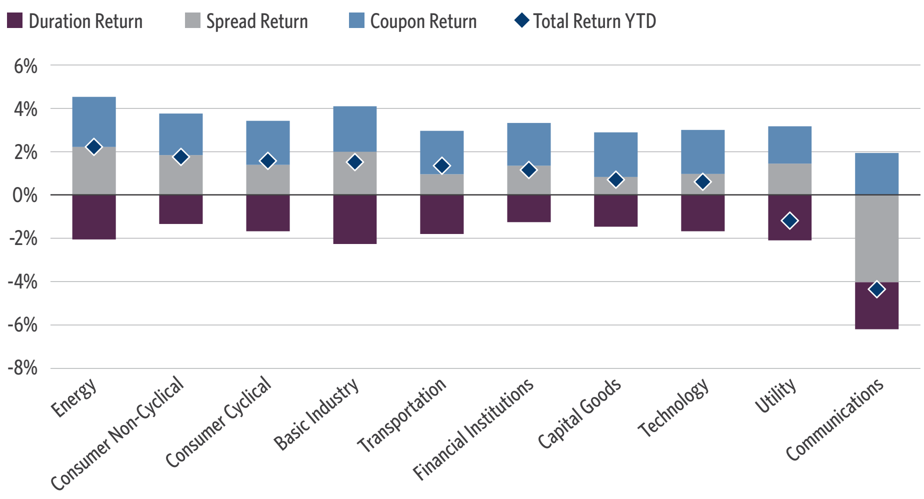
Carry and Spread Tightening Supported Positive Returns

YTD Returns through April 30, by Industry



Source: Guggenheim, Bloomberg. Data as of 4.30.2024. Attribution returns are estimates and omit other sources of return including roll down and index constituent changes. Past performance does not guarantee future results.