High Yield Market Update

Newfleet ASSET MANAGEMENT
A Virtus Investment Partner

AUGUST 2022: OUTLOOK AND IMPLEMENTATION

- The high yield market gave back some of July's gains in August as it finished with a negative return of -2.30%, largely driven by rising risk-free rates. BBs led the way lower with a negative return of -2.92%. Bs and CCCs returned -2.27% and +0.07%, respectively. In response to a potentially more hawkish Fed, U.S. Treasury yields began to move higher, with the 10-year yield rising 55 basis points (bps) to finish August at a yield of 3.20%. Credit spreads also rose, but by a smaller amount. BB-rated credits, the most interest-rate sensitive bonds, were hit the hardest. While second quarter earnings came in better than expected and the technical picture still looks favorable due to very low issuance, these positive factors can't overcome fears of a hawkish Federal Reserve.
- The best performing industries in August were oil field services (+2.79%), refining (+.96%), transportation services (-0.19%), metals and mining (-0.26%) and other REITs (-0.71%). The worst performing industries in August were pharmaceuticals (-9.23%), health insurance (-5.15%), wireless (-4.32%), cable satellite (-4.14%) and environmental (-3.62%).

Fundamentals

- The upgrade-to-downgrade ratio, by number of issuers, increased to 2.1 in August, an increase from July's 1.7 number, and is at 2.0 through the first eight months of the year.
- The issuer-weighted default rate through August was 0.97%.

Technicals

- 2022 experienced its seventh outflow of the year as August fund flows turned negative after a positive fund flow month in July. The asset class saw $1.3 billion leave in August.
- While the primary market was more active than the previous month, only $8.1 billion of bonds priced in August. Year-to-date, we've only seen $81 billion price – 22% of what priced through the first eight months of 2021.
- Despite another month of outflows, zero fallen angels and a muted new issue calendar could not offset the rising stars and coupon reinvestments, creating a shortfall of $9.2 billion.

Pricing

- The spread on the high yield index increased 17 bps on the month to +482; however, this level is 74 bps above the month's low.
- After a rally to begin the month where the index yield-to-worst touched 7.41%, the yield-to-worst increased to 8.42%.
- The high yield index average price dropped $2.5 to $87.93 despite increasing to $91.75 mid-month.

Implementation

- As expected, August was a seasonable slow month with limited primary activity and thin secondary markets. Our activity was light to avoid the high transaction costs that are typical this time of year, but which were also worsened by the elevated volatility in U.S. Treasury rates. However, our theme remains the same – add higher quality credits with intermediate duration as we move back towards a neutral duration and look to trim some credit risk. We were able to accomplish this as rising rates led to BBB- and BB-rated securities underperforming, leading to attractive entry points. We funded our purchases with cash. With second quarter earnings now behind us, our focus will be on economic data as well as the Federal Open Market Committee and its impact on U.S. Treasury rates and high yield valuations.

Newfleet Asset Management

One Financial Plaza

Hartford, Connecticut 06103

877-332-8172

Past performance is not indicative of future results.

The **Bloomberg U.S. High-Yield 2% Issuer Capped Bond Index** is a market capitalization-weighted index that measures fixed rate non-investment grade debt securities of U.S. and non-U.S. corporations. No single issuer accounts for more than 2% of market cap. The index is unmanaged, its returns do not reflect any fees, expenses, or sales charges, and is not available for direct investment.

Newfleet Asset Management's industry trends and observations are the result of research conducted by the portfolio management / research team. These observations reflect their industry expertise and have been prepared using sources of information generally believed to be reliable; however, their accuracy is not guaranteed. Opinions represented are subject to change and should not be considered investment advice.

Investing is subject to risk, including the risk of possible loss of principal.

AR 2414316 9/2022

For Institutional Investor Use

Newfleet Asset Management is a division of Virtus Fixed Income Advisers, LLC ("VFIA"), an SEC registered investment adviser.