NEWFLEET ASSET MANAGEMENT

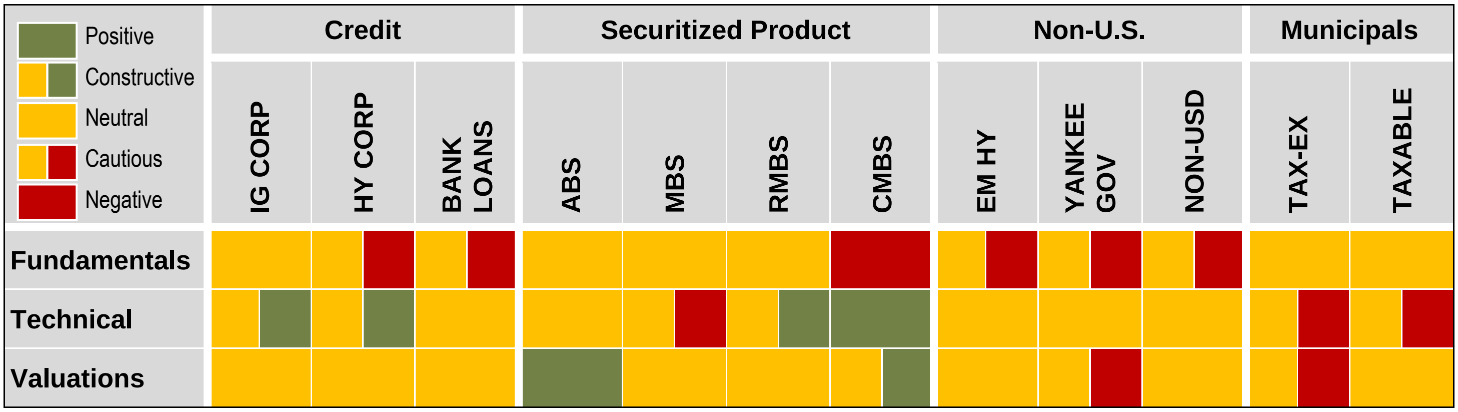
Fixed Income Sector Review

As of April 30, 2023

OBSERVATIONS ON THE MACRO ENVIRONMENT & MARKET CONDITIONS

- We are still neutral on credit markets and expect mid-to-upper single digit returns.
- We expect mostly sideways-to-small positive rate and risk markets, punctuated with bouts of volatility, amplified by a continued reduction of financial market liquidity.
- Recommendation: add, but only on weakness, and book gains.
- Key issue remains market response to the impact of central bank policy tightening on growth and inflation.
- We think the key risks are intertwined. The Fed has a big challenge: can it simultaneously vanquish persistent inflation, avoid a large recession, and save the banks on an ad hoc basis, all while minimizing the impact on economic activity?
- In addition, the future impact of prior rate hikes on banks and overall economic health remains unknown.
- Turmoil in the banking sector is one consequence of the sizeable and rapid removal of monetary policy accommodation over the past year.

SECTOR ASSESSMENTS



🟩 Positive
🟨🟩 Constructive
🟨 Neutral
🟨🟥 Cautious
🟥 Negative

	Credit			Securitized Product				Non-U.S.			Municipals	
	IG CORP	HY CORP	BANK LOANS	ABS	MBS	RMBS	CMBS	EM HY	YANKEE GOV	NON-USD	TAX-EX	TAXABLE
Fundamentals	🟨	🟨🟥	🟨🟥	🟨	🟨	🟨	🟥	🟨🟥	🟨🟥	🟨🟥	🟨	🟨
Technical	🟨🟩	🟨🟩	🟨	🟨	🟨🟥	🟨🟩	🟩	🟨	🟨	🟨	🟨🟥	🟨🟥
Valuations	🟨	🟨	🟨	🟩	🟨	🟨	🟨🟩	🟨	🟨🟥	🟨	🟨🟥	🟨

Newfleet's assessments of non-government spread sectors as of April 30, 2023. Assessments are determined by analyzing a sector's fundamental data, technical indicators, and relative valuations. Sectors (l to r): **Credit**: Investment Grade (IG) Corporate Bonds, High Yield (HY) Corporate Bonds, Bank Loans. **Securitized Product**: Asset-Backed Securities (ABS), Agency Mortgage-Backed Securities (MBS), Non-Agency Residential MBS (RMBS), Non-Agency Commercial MBS (CMBS). **Non-U.S.**: Emerging Markets HY, Yankee Government, Non-U.S. Dollar. **Municipals**: Tax-Exempt, Taxable.

SELECT SECTOR HIGHLIGHTS

Investment Grade Corporate Bonds

- Following a tumultuous March, the investment grade market returned to normalcy in April as financials, front-end bonds, and BBBs, previous underperformers, all outperformed during the month.
- Financials, which trade close to their relative wides versus industrials, remain under intense focus and will be the driver of market performance from here.
- Despite a wave of financial downgrades in the wake of the regional banking mini-crisis, upgrades outpaced downgrades again in April. Upgrades to mega-cap issuers included T-Mobile and Anheuser Busch.

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High Yield Corporate Bonds

- The high yield index was able to generate a positive return of +1% in April as fears over the banking turmoil began to abate, and as the market benefited from strong inflows and active capital markets.
- Technicals were supportive in April as high yield experienced its largest one-month inflow since August 2020 and its second largest month of new issuance in over a year. The issuance was not enough to offset the inflows and a sizable number of rising stars, creating a supply shortfall of $20.9 billion.
- April's volatility and ample supply increased liquidity, enabling us to keep moving forward with investing cash, reducing risk, and improving the overall credit quality of the portfolio. The strength in CCCs provided the bid we were looking for to reduce, while the move in rates, coupled with a few bouts of selling, allowed us to invest cash in the higher quality part of the credit curve.

Bank Loans

- Year-to-date returns for loans are +4.31% − the best four-month stretch since the start of 2019. Meanwhile, loan valuations tightened to +576 on a 3-year discount margin basis – tight to the start of the year (+645) but wide to the 10-year average (+506).
- At $5.1 billion, April was the slowest month for CLO issuance this year, and roughly half of March's level. Anticipation of a Fed pause, heightened recession risk, and difficult economics surrounding CLO creation are dampening demand. Still, five CLO transactions were announced in May at the time of this writing.
- We await the May Senior Loan Officer's Survey for insight into changes in bank lending standards. Tighter capital markets for borrowers could trigger a credit cycle contraction, potentially leading to downgrades, CLO structure stresses, and defaults.

Securitized Product

- Credit spreads for ABS, CMBS, and RMBS tightened during the month. The agency MBS market was the only securitized sector to experience wider spreads; this was due to the amount of supply expected to hit the markets after the FDIC takeover of several large regional banks.
- Muted new issue supply – especially for CMBS and RMBS – was a positive technical for the month.
- We selectively added new issue senior-tranche CMBS, as it trades cheaper than single A- and BBB-rated corporates on a spread basis.

Emerging Markets Debt

- For April, EM investment grade outperformed U.S. investment grade corporate credit. However, EM high yield still lagged U.S. high yield by 181 bps in April, which brought the YTD margin of relative underperformance to 400 bps.
- Recession fears, tightening financial markets, and banking system stresses contributed to EM high yield's underperformance, though this has produced good value for the sector. We think EM high yield credit risk spread gets attractive near 900 bps – it is now at 826 bps.
- We think overall market conditions, combined with better overall bond market value, should support positive total returns in bonds this year. Such a backdrop favors credit, including EM debt. As a result, we remain buyers on dips.

Municipal Bonds

- The municipal bond index returned -0.23% for the month, and 2.54% year-to-date as of April 27.
- According to Lipper, year-to-date outflows are now at $5.9 billion as of April 26.
- Year-to-date issuance is now down by -18.6%.

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