HIGH YIELD MARKET

INVESTMENT COMMENTARY & REVIEW

by Michael Yean

First Quarter 2021

The Bloomberg Barclays U.S. High Yield Corporate Index (Index) returned a modest 0.85% during the first quarter of 2021.

The CCC-rated cohort returned 3.58%, compared to 1.16% and -0.15% for the B-rated and BB-rated cohorts, respectively. The Index option-adjusted spread (OAS) tightened by 50 bps to +310 bps in the first quarter, while the yield-to-worst (YTW) rose slightly to 4.23% from 4.18%. By ratings, BB-rated credits now trade at an OAS of +227 bps and offer a YTW of 3.40%, B-rated credits at an OAS of +334 bps and 4.49% YTW, and CCC-rated credits at an OAS of +548 bps and 6.55% YTW. The average dollar price of the Index declined to $104.16 by quarter end.

The crosscurrents of economic recovery and sharply rising Treasury yields were evident in the varying returns by credit quality within the overall high yield market. While the Index tightened materially and offset the rise in rates, the longer-duration, most rate-sensitive BB bucket produced a negative total return. On the other hand, the lower-rated buckets, which offer greater yield and are broadly more influenced by economic activity and growth, outperformed and generated positive returns for the quarter.

Our outlook for the high yield market for 2021 remains unchanged. We continue to expect accommodative monetary and stimulative fiscal policy along with progress on COVID-19 immunizations to set the stage for an economic recovery and a constructive environment for credit. The PIA Investment Strategy Group (ISG), using the 10-year Treasury as our proxy for interest rates, continues to see 2021 bond market yields range-bound between 1.35% – 2.05%. However, the combination of accommodative policy and economic activity may also further pressure Treasury yields upwards. As such, we expect the intra-market dynamics on display in the first quarter to broadly continue, and we are positioned to take advantage of this trend.

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