IG Fixed Income Recap

September 2024

A monthly review of IG Fixed Income Sectors

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Performance recap for the month

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	bps	bps	%	%
	OAS	**OAS change**	**Total Return**	**Excess Return**
IG Corporate Market	88	-4	1.77	0.48
Intermediate	78	-3	1.30	0.25
Long	106	-6	2.70	0.92
A Finance	78	-5	1.60	0.43
BBB Finance	120	-4	1.64	0.46
A Industrials	63	-7	1.87	0.49
BBB Industrials	107	-2	1.71	0.40
BBB-A basis	44	5		
EM USD	242	-18	1.76	0.55
IG	107	0	1.33	0.06
HY	465	-51	2.49	1.38
Asia	147	-2	1.45	0.36
Latin America	377	-12	2.48	1.19
High Yield	297	-2	1.62	0.70
CCCs	680	-81	4.29	3.39
Euro Agg Corporate	115	-1	1.23	0.11

USD IG Corporate Market

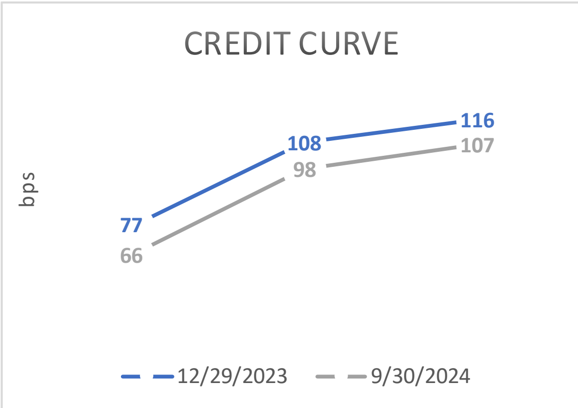
By Elizabeth Henderson, CFA

Rally month for Corporates

Risk assets rallied last month as the Fed cut rates 50 bps and China surprised with a stimulus announcement. Also, economic data was in line to stronger in September, giving the market more comfort. New issue supply continued to surprise to the upside. As we enter earnings season, it’s interesting to see estimates unchanged (since June) at a revenue level for the S&P 500 for calendar year 2024, whereas earnings are projected to be slightly lower (10% growth vs. 11%; data per Factset on 9/27/24). The slightly lower earnings growth estimate is driven by weaker commodity prices largely due to China.

Source (table above): Bloomberg, AAM

IG Fixed Income Recap



Sector Relative Value

There was a number of RV adjustments based on spread movement, especially CCCs which tightened materially. Utilities outperformed Financials and Industrials. The Long end remains rich vs. its historic average. Consumer sectors outperformed last month as Energy underperformed. BBB rated Industrials are historically a little rich vs. As with BBB Industrials looking more attractive vs. BBB Utes over the LTM.

Looking at sectors relative to broad Industrials (LTM noted otherwise 5+ year history) (bold=new; strike-through = no longer valid vs last month):

- Z scores >1.5: Aerospace/Defense, ~~Construction Machinery~~, Cable, Media, ~~Integrated Energy~~, ~~Electric Utilities~~, Health Insurance, **Supermarkets, Independent Energy, Health Insurance**
- Z scores <-1.5: Metals & Mining, Diversified Materials, Food and Beverage, Midstream, ~~Wireline~~, **Electric Utilities** (LTM)**, Retail, Consumer Products**

Source (graph): Bloomberg, AAM

Technicals and Rating Changes

New bonds issued in Sept tightened an average of 8 bps while the OAS was 4 tighter.

High Grade bond supply in September was **higher than expected** at $171B, **35% higher than the average issuance in Sept** over the past 4 years (2019-2023; ex-2020). Supply continues to surpass monthly estimates.

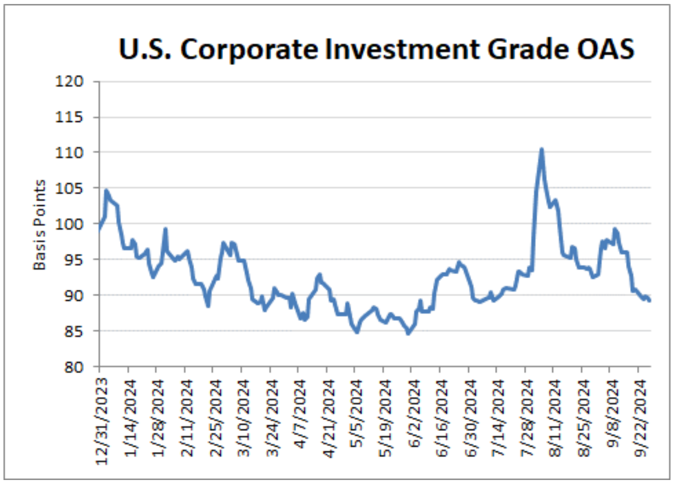
The **average daily trading volume for HG bonds** was higher than last month ($41B vs. 33B/day for cash) and for HY bonds as well ($17 vs. 12B/day). This is **54% higher** for HG and 38% higher for HY **vs. last year**.

New issue supply is expected to be around **$90-100B in October**, in line with historic averages.

Source: AAM, JPM, Bank of America

Rating changes (rising stars/fallen angels) Source: Bloomberg:

- *Fallen angels: VF Corp*
- *Rising stars: Warner Music Group*



Ticker level performance

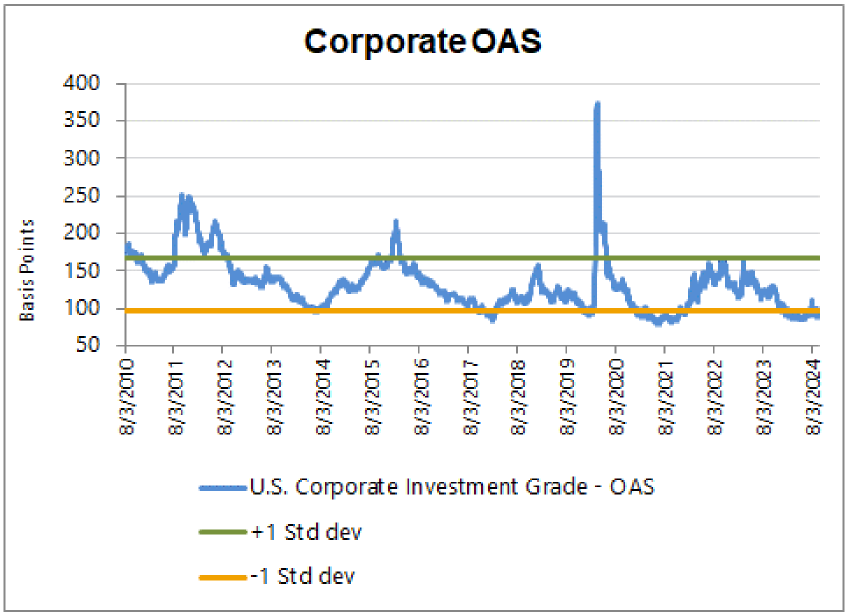
The following shows the top and bottom performing issuers based on excess return per unit of duration. This list excludes those with market values less than 0.04% of the Corporate Index. AAM's analysts have provided an explanation for issuer performance.

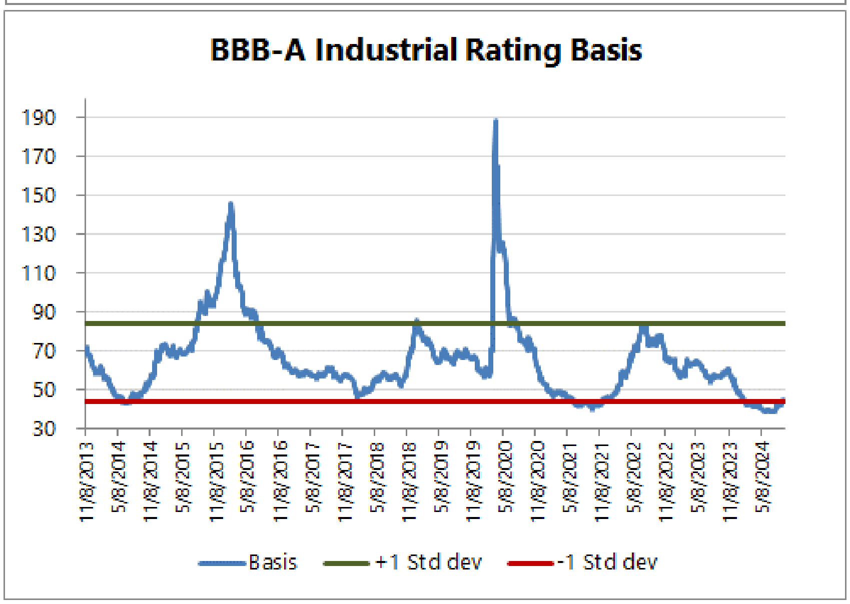
Top 15 tickers	Tickers	Sector	ER (%)	MV%*	Duration	Notes
1	**KRC**	Office REITs	1.25	0.04	5.1	Office CRE exposure; rate cuts
2	**BXP**	Office REITs	1.01	0.13	4.7	Office CRE exposure; rate cuts
3	**PCG**	Electric	1.62	0.49	7.9	Rates, AI demand, nuclear, receding wildfire risk = positive tone for utes
4	**CEG**	Electric	2.03	0.09	10.1	Microsoft nuclear PPA
5	**BHF**	Life	1.50	0.04	7.8	Equity market recovery
6	**BABA**	Retailers	1.91	0.15	10.0	China stimy
7	**FRT**	Retail REITs	0.91	0.04	5.1	Office CRE exposure; rate cuts
8	**LVS**	Gaming	0.59	0.05	3.6	China stimy
9	**MTNA**	Metals and Mining	1.06	0.08	6.4	Hopeful rebound in steel prices
10	**ORCL**	Technology	1.39	0.93	9.1	Guidance, growth targets above expectations
11	**ARE**	Healthcare REITs	1.25	0.15	8.49	Life science CRE exposure; rate cuts
12	**PRU**	Life	1.28	0.21	8.73	ULSG reinsurance deal, continues to reduce tail risks/ vol
13	**XEL**	Electric	1.51	0.32	10.84	Rates, AI demand, nuclear, receding wildfire risk = positive tone for utes
14	**MTB**	Banking	0.46	0.10	3.4	Office CRE exposure; rates cuts
15	**NGGLN**	Electric/Gas	0.82	0.04	6.0	Rates, AI demand, nuclear, receding wildfire risk = positive tone for utes

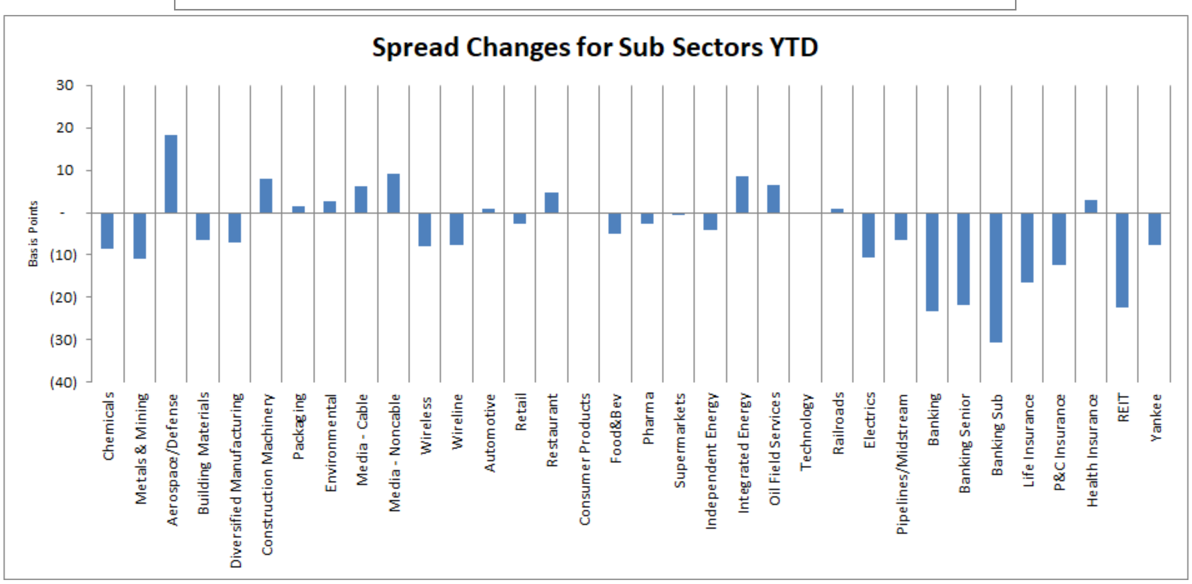
Bottom 15	Tickers	Sector	ER (%)	MV%	Duration	Notes
1	**TELVIS**	Media Entertainment	-5.14	0.04	10.7	Moody's places Negative Outlook on Baa3 rating due to fundamental issues
2	**ALLY**	Banking	-0.94	0.11	4.4	Weaker than expected guidance; asset quality
3	**GM**	Automotive	-0.67	0.71	4.7	Equity downgrade, European peers warning, China
4	**F**	Automotive	-0.52	0.63	4.2	Equity downgrade, European peers warning, China
5	**OXY**	Independent	-0.67	0.26	6.3	Weaker commodity fundamentals; high beta
6	**OBDC**	Finance Companies	-0.24	0.05	2.5	Asset sensitivity; rate cuts; debt issuance
7	**APTV**	Automotive	-1.05	0.05	11.8	Equity downgrade, European peers warning, China
8	**DVN**	Independent	-0.61	0.11	7.9	Weaker commodity fundamentals; high beta
9	**OVV**	Independent	-0.39	0.07	6.3	Weaker commodity fundamentals; high beta
10	**CHTR**	Cable Satellite	-0.58	0.53	9.6	Liberty Broadband related M&A could result in additional debt issued to refi
11	**FANG**	Independent	-0.43	0.16	8.63	Weaker commodity fundamentals; high beta
12	**APA**	Independent	-0.29	0.05	9.1	Weaker commodity fundamentals; high beta
13	**CVECN**	Integrated	-0.27	0.04	9.8	Weaker commodity fundamentals
14	**NTRS**	Banking	-0.10	0.07	3.8	Asset sensitivity; rate cuts
15	**LNG**	Midstream	-0.11	0.04	4.5	Likely heavy issuer in intermediate term

Source (graph, table data): Bloomberg, AAM

Market graphs (Source: Bloomberg, AAM)







Structured Products

By Chris Priebe and Mohammed Ahmed

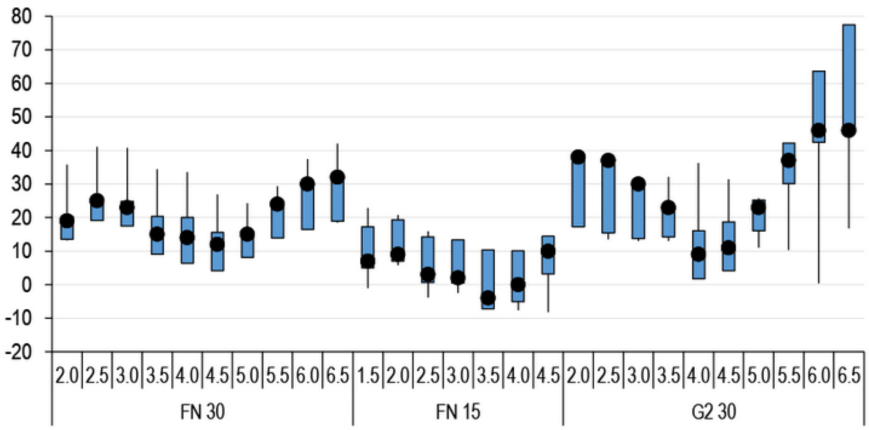
AGY MBS finally underperformed while CMBS outperformed

Rating Changes

Rating changes continued to be negative for CMBS conduit and single-asset deals in September. Conversely, more ABS deals were upgraded than downgraded in September, continuing a four-month trend.

Figure 1: Mortgage spreads reversed much of the gains they had seen heading into the FOMC

Current, 1m, and 6m Treasury OAS ranges across the TBA stack in our research beta model. The black dots represent the current OAS, the blue boxes represent the 1m range, and the black lines represent the 6m range (as of 9/26/2024)



Source: J.P. Morgan

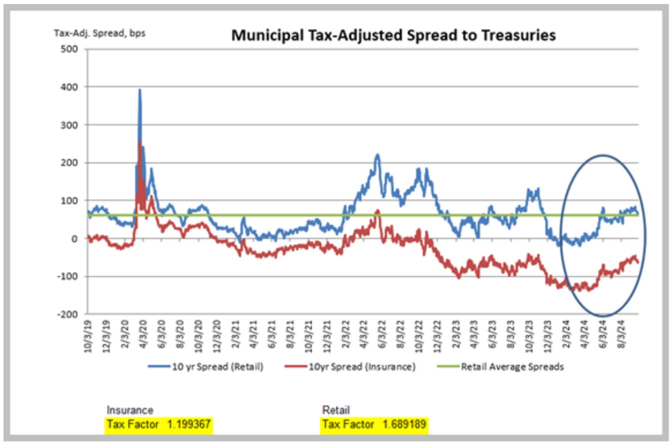
The AGY RMBS sector underperformed US Treasuries for the first time in months. Current coupon MBS spreads tightened on the month from 132 to 128 but lagged in excess returns. This was a month of great anticipation for the Fed and that kept investors on the sidelines. Spreads hovered near 122 pre and post fed for days until vol popped the last few trading sessions and MBS lagged. **AGY MBS excess -2 bps**

The CMBS market was the top performer in Structured. A few conduits and SASB deals hit the market that were attractive in spread and credit, supporting spreads as deals were able to get done. We are seeing cash enter from the sidelines from investors who have been underweight. This buying stabilized spreads and helped CMBS outperform. Given most deals have been shorter to garner investor interest, we finally saw a conduit 10-year price with elevated hotel exposure. **CMBS excess +23 bps**

The ABS market snapped back to positive returns after a flat August. ABS supply has hit over $260B on a record-breaking pace and might pass $300B by year-end. ABS new issuance in September was well spoken for, as all deals were well oversubscribed which led to tighter spreads and outperformance. Cards and autos were the top performer (+9 bps respectively) while Rate Reduction lagged a little (+5 bps). **ABS excess +8 bps**

Using the JPM CLOIE index, **CLO** return was positive (0.7%) in September driven mostly by carry. While CLOs outperformed US Loans, they underperformed fixed rate, 1–3 year Corporates (0.9%).

Sources: Bloomberg Index, JPM



Municipal Bonds

Source: Greg Bell, CFA, CPA

IG tax-exempts exhibited a firmer tone despite heavy supply. Expect spreads to weaken in October. Taxable muni spreads have been stagnant and supply technicals remain supportive.

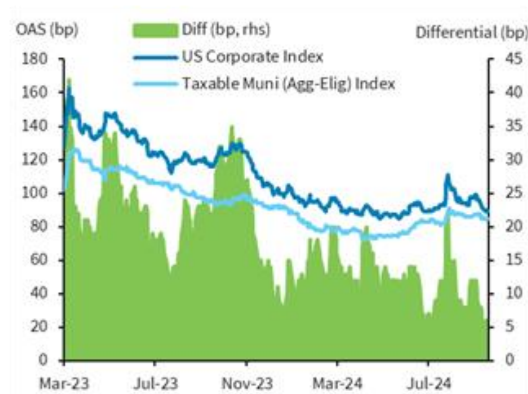
Tax-exempts Heavier supply in September did not derail the firming in yields in the tax-exempt sector. Following declines in yields in both July and August, September produced yield declines across the curve in sympathy with the rally in the Treasury market. Overall, with the exception of the front end of the curve, tax-exempt yields fell almost in line with taxables, with declines of 16, 11 and 12bps in 3, 10 and 30yrs, respectively. Treasury yields fell by 23, 12 and 8bps in 3, 10 and 30yrs, respectively.

However, the heavy supply cycle over the last three months is pressuring relative valuations for the sector to weaker levels. Since July 1st, tax-adjusted spreads in 3, 10 and 30yrs are wider by 17, 33 and 20bps in 3, 10 and 30yrs, respectively. New issue supply during that timeframe has produced a total of $135B, with $44.63B of that total coming in September. The average issuance over the last 10yrs for these three months is $103.8B. September's supply represented a 44% increase on a year-over-year basis.

Looking forward, October is expected to see another $50B in issuance. Issuers appear motivated to clear as much of their calendar as possible before the general election in November. Consequently, we could see technicals pressure relative valuation to weaker levels. Muni-to-Treasury ratios and tax-adjusted yield spreads in 10yrs begin the 4th quarter at 68.75% and negative 66bps, respectively. After exhibiting weakness over the first week of August, taxable munis performed well into month-end. On an OAS basis for the index, spreads widened to a month-high of 91bps on 8/6/24 before tightening 7bps over the balance of the month to end the month at 86bps. When reviewing trades and secondary offerings, spreads down the curve 7yrs and shorter saw the strongest performance, with spreads tighter by 7 to 8bps. The balance of the curve was essentially unchanged. Supply technicals remain supportive for the sector. New issuance remained light during August, with only $2.86B. Although that's a year-over-year increase of 10.2%, it remains at an anemic pace of only 5.8% of overall issuance.

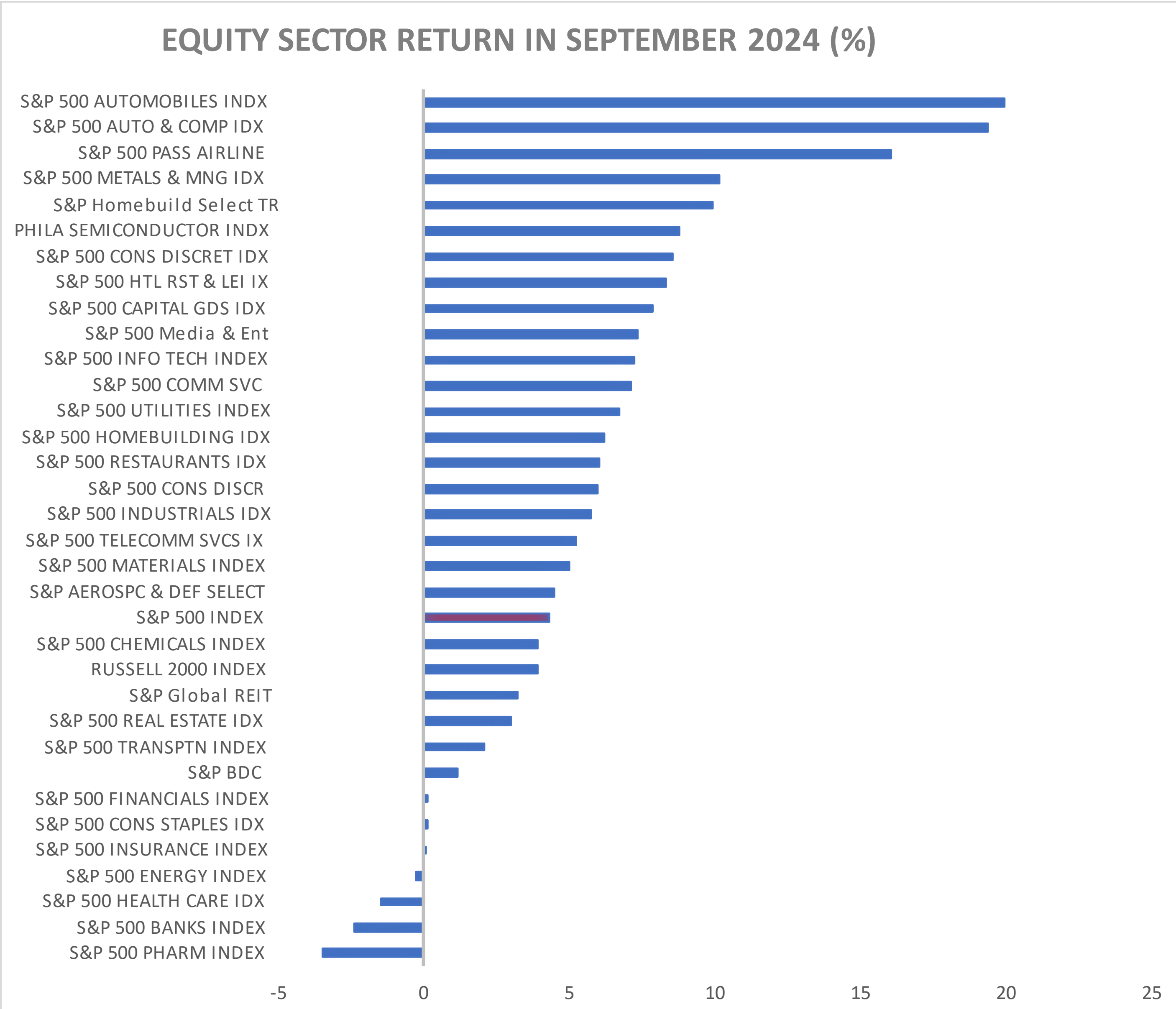
Taxable muni spreads have largely been stagnant over the last month, with a slight firming bias. The taxable muni OAS of the Bloomberg AGG index tightened modestly by 1bps to finish the quarter at 85bps. When reviewing trades and secondary offerings, spreads across the curve were essentially unchanged for the month.

Supply technicals remain supportive for the sector. New issuance remained light during September, with only $2.4B issued. That resulted in an anemic 5.4% of total issuance. On a year-over-year basis, September's supply was an increase of 135% versus September 2023.



Source: Bloomberg, Barclays; first graph above: Bloomberg, Refinitiv MMD (market information as well)

Other Asset Classes



Source: Bloomberg, AAM