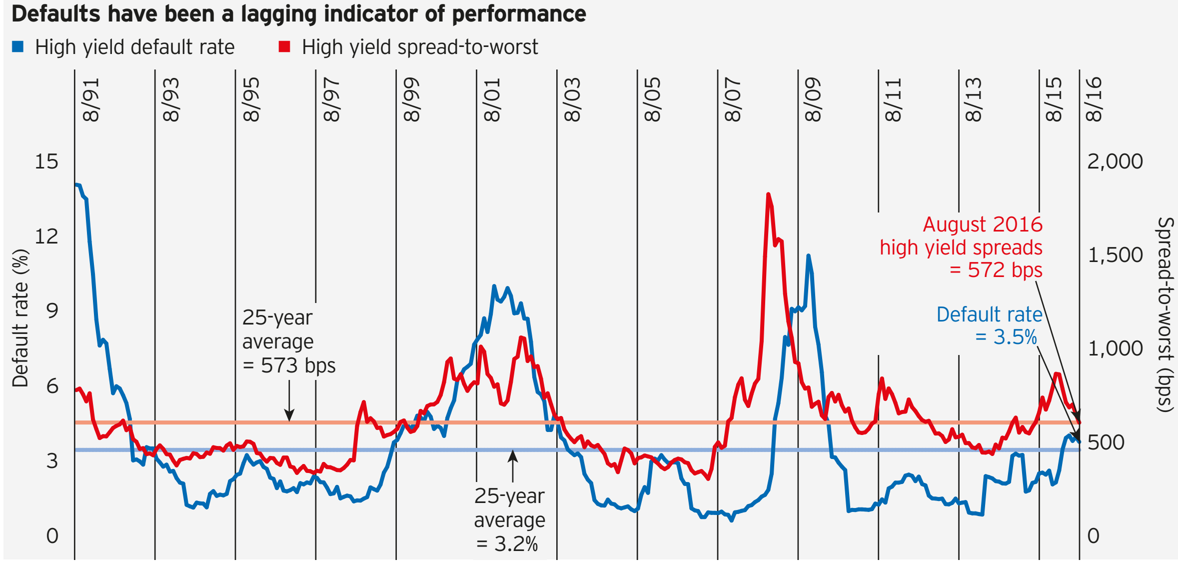
Invesco High Yield

High Yield
Snapshot

Monthly high yield bond market update: September 2016

The high yield market was strong in August, with the Barclays US Corporate High Yield 2% Issuer Capped Index gaining 2.09%. The market benefitted from an overall risk-on environment supported by a continuation of accommodating central bank behavior. Investors allocated additional assets to the high yield market, despite an outflow early in the month. Per JP Morgan, spreads ended the month at 572 bps, which is in line with the 20-year median spread level. The five-year and 10-year Treasury bonds steepened when compared to July, with the five-year rising to 1.19%, compared to 1.02% the month prior, and the 10-year to 1.58% from 1.45% the month prior. Overall, we still see value in some sectors of the market, but in our opinion, the future pace of market gains are unlikely to be as strong as we've witnessed year-to-date.

Defaults have been a lagging indicator of performance



Source: JP Morgan, as of Aug. 31, 2016

Performance by ratings[1]

Within the ratings categories:

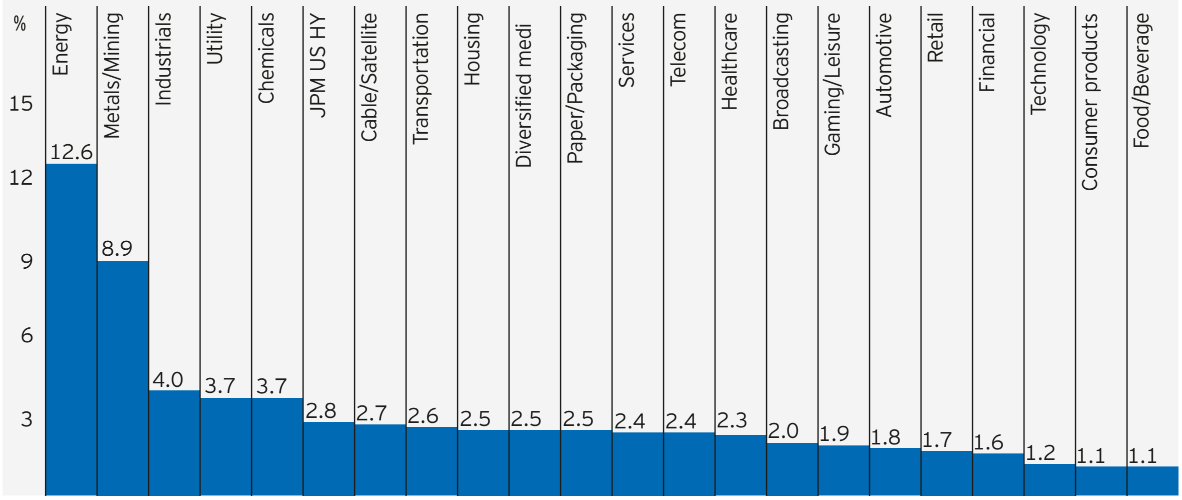
- BB-rated securities returned 1.48%
- B-rated securities generated returns of 2.28%
- CCC-rated securities returned 3.29%

Earnings trends

Second quarter earnings season has concluded. As for fundamentals overall, here are several themes we are monitoring:

- We've seen some earnings woes in the healthcare sector, mostly in the hospital and pharmaceutical areas. In general, the hospital sector has been challenged with higher operating costs and slightly lower admissions. For pharmaceuticals, pressure to halt rising drug costs, coupled with some company specific issues, have caused this area to underperform.
- The transportation sector has seen its share of weak earnings as well. We note continued pressure on heavy truck orders has resulted in weak sales for the sector. We think this pressure is unlikely to change before year-end.
- Housing results have been a bit of a mixed bag. While results have been decent overall, some investors were previously holding a more optimistic view on new sales. We continue to hear some debate about the potential impact of higher rates weighing on new home sales. In our view, one rate hike by the Fed will have little influence on the housing market.

High yield produced positive returns in August



Source: JP Morgan US High Yield Bond Index, as of Aug. 31, 2016.

Fundamentals

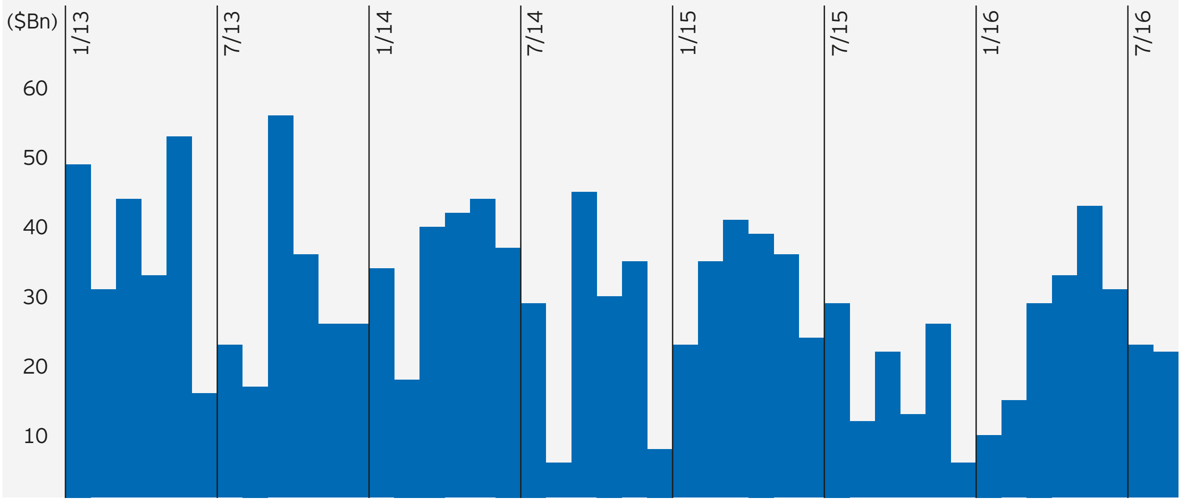
- The Barclays US Corporate High Yield 2% Is suer Capped Index finished the month with a yield-to-worst of 6.31%, a modified duration of 4.02, an option-adjusted spread of 490 bps, and an average price of 99.23.
- There was only one default in August in the high yield market which caused the par-weighted default rate to fall to 3.52% fr om 3.79% in July. Excluding energy, and metals and mining, the default rate is only 0.53%.
- Credit metrics for the overall market continue to reside in a healthy zone, in our opinion.
- Recent leverage statistics continue to increase. This increase is being driven by poor earnings within energy, and metals and mining. We don't see this trend reversing in the near-term.

Technicals[2]

- High yield mutual funds reported $1.2 billion of inflows in August, which follows a $5.2 billion inflow in July. Year-to-date, inflows have totaled $10.0 billion compared to 2015 when outflows totaled $16.6 billion.
- New issuance for August came in at $20.6 billion, the third consecutive monthly decline. Year-to-date, there has been $198 billion in new issuance compared to $230 billion in the first eight months of 2015.
- New issuance was led by refinancing activity which represented 70% of new deals followed by 14% for general corporate purposes. Year-to-date, new issuance has been led by refinancing activity, accounting for 55% o f the total volume followed by general corporate purposes which represented 24% of the total.

New issuance volume fell in June, July and August

Monthly high-yield fund flows ($bn)



Source: JP Morgan, as of Aug. 31, 2016.

Relative value

- The spread between high yield and investment grade is greater than the historical median, creating an opportunity for yield pick-up given a manageable default risk.
- High yield offers a relatively lower duration and a higher coupon, which reduces its sensitivity to interest rate movements.
- The escalation of risk premiums due to declines in commodity prices and pressure on the energy sector has created value in the overall market.

Index returns (%)

	4/16	5/16	6/16	7/16	8/16	YTD 2016
Barclays US HY 2% Is suer Cap Index	3.92	0.62	0.92	2.70	2.09	14.35
Barclays US Aggregate Bond Index	0.38	0.03	1.80	0.63	-0.11	5.86
Barclays US Treasury 5-10 Year Index	-0.08	-0.14	2.52	0.21	-0.79	5.85
JPM EMBI Global Diversified Index	1.77	-0.18	3.37	1.80	1.79	14.31
S&P 500 Index	0.39	1.80	0.26	3.69	0.14	7.82
S&P/LSTA Leveraged Loan Index	1.99	0.89	-0.15	1.64	0.70	7.84

Source: Barclays, JP Morgan, and Standard & Poor's, as of Aug. 31, 2016.

1 Barclays
2 JP Morgan

About risk

Fixed income investments are subject to credit risk of the issuer and the effects of changing interest rates. Interest rate risk refers to the risk that bond prices generally fall as interest rates rise and vice versa. An issuer may be unable to meet interest and/or principal payments, thereby causing its instruments to decrease in value and lowering the issuer's credit rating. Junk bonds involve a greater risk of default or price changes due to changes in the issuer's credit quality. The values of junk bonds fluctuate more than those of high quality bonds and can decline significantly over short time periods.

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