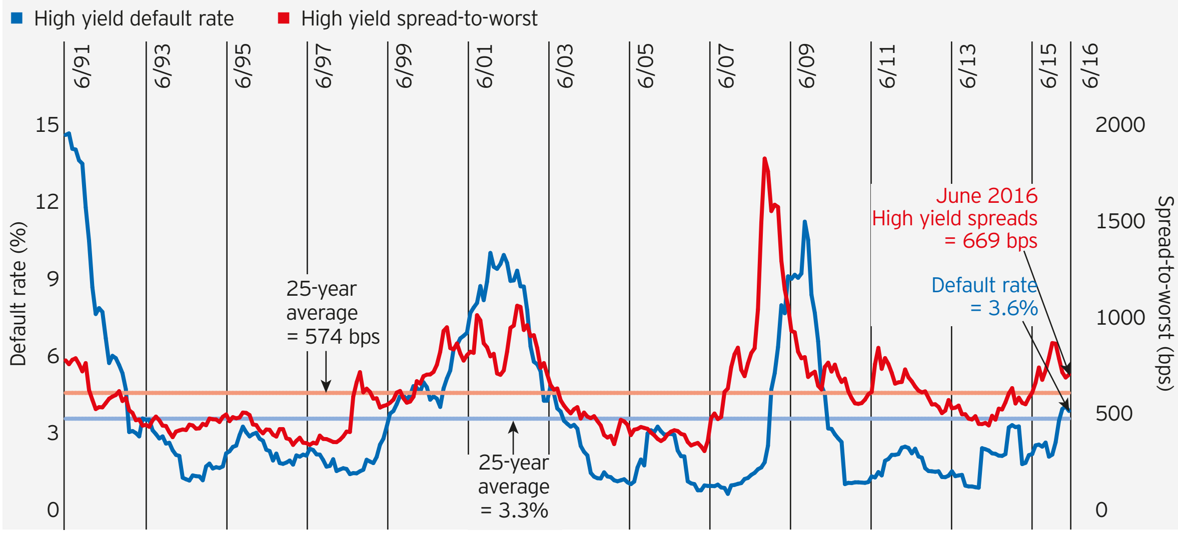
Invesco High Yield

High Yield Snapshot

Monthly high yield bond market update: July 2016

June was a volatile month in the high yield market, but the asset class was ultimately able to generate positive returns following the Brexit vote, and finish with the Barclays US Corporate High Yield 2% Issuer Capped Index gaining 0.92% for the month. The month was marked by uncertainty over the direction of the Brexit vote, as the market swung back and forth between pricing in Britain leaving or remaining. When Britain ultimately voted to leave the EU in late June, the market declined for a few days, before ultimately rallying back. Investors looked to support from the Treasury rally and the yield advantage over other asset classes as justification for adding high yield, and the market remained resilient. Per JP Morgan, spreads ended the month at 669 bps, which in our opinion still offers value. The five-year and 10-year Treasury bonds rallied and yields fell when compared to May. The five-year yield ended the month at 1.01%, compared to 1.37% at the beginning of the month, and the 10-year yield ended at 1.47%, compared to 1.85% at month beginning. The market rally amidst the growing murkiness in the global macro picture continues to support our thesis that the asset class offers attractive compensation for risks taken.

Defaults have been a lagging indicator of performance



Source: JP Morgan, as of June 30, 2016

Performance by ratings[1]

Within the ratings categories:

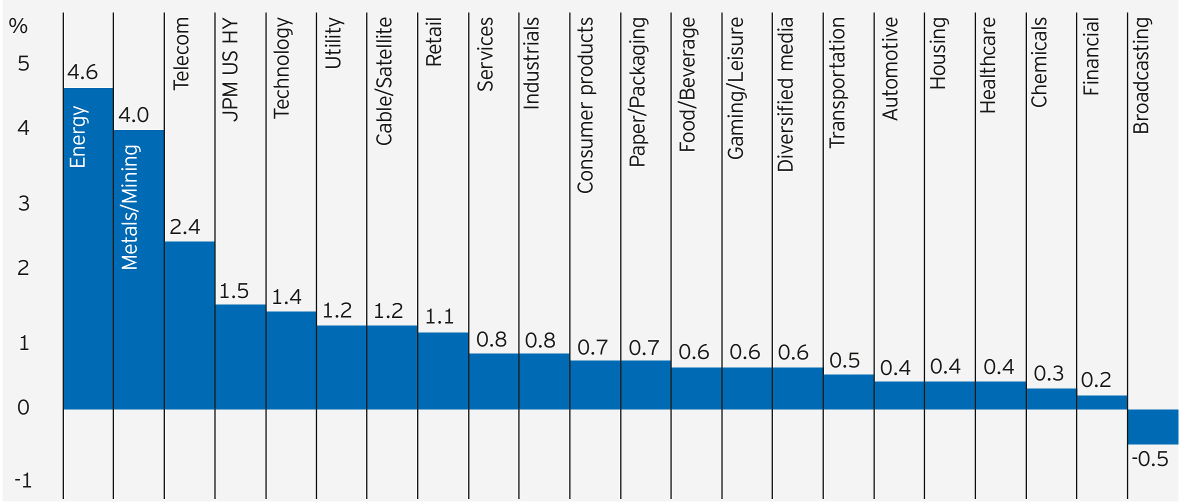
- BB-rated securities returned 0.70%
- B-rated securities generated returns of 0.81%
- CCC-rated securities returned 1.50%

Earnings trends

First quarter earnings season is behind us. As for fundamentals overall, here are several themes we are monitoring:

- We have slightly added to our positions in metals and mining. While we expect challenges to continue for the space, we do see value within some companies. We continue to see balance sheet improvement from new equity issuance and asset sales.
- We've noticed some poor earnings from some retail companies. In our view, the US is over-stored. Shifting consumer buying patterns and outdated business models coupled with high debt loads is a very bad combination. We continue to underweight this industry.
- Energy earnings continue to be quite bad. In particular, energy service companies continue to demonstrate large revenue declines and unsustainable earnings trends. However, with the recent improvement in oil prices, the strongest independent energy credits are on very solid footing. Yet, $50 oil doesn't fix all the problems in this sector and we continue to expect elevated default activity for the industry.

High yield produced positive returns in June



Source: JP Morgan US High Yield Bond Index, as of June 30, 2016

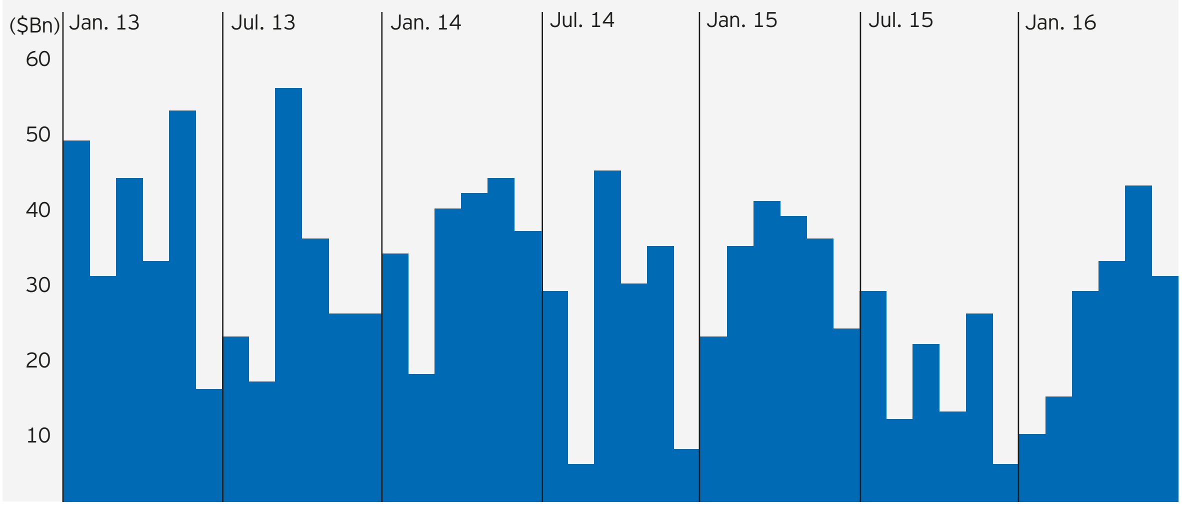
Fundamentals

- The Barclays US Corporate High Yield 2% Issuer Capped Index finished the month with a yield-to-worst of 7.27%, a modified duration of 4.26, an option-adjusted spread of 594 bps, and an average price of 95.49.
- There were two defaults in June in the high yield market which caused the par-weighted default rate to fall to 3.56% from 3.78%. Excluding energy, and metals and mining, the default rate is 0.53%.[2]
- 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 $3.4 billion of outflows during June, which marks the second consecutive month of net outflows. In 2015, outflows totaling $16.6 billion even after a record $23.8 billion of outflows in 2014.
- New issuance for June came in at $30 billion – the first drop in five months. The second quarter totaled $104 billion – the fifth highest quarterly total on record.
- New issuance was led by refinancing activity with 62% followed by 19% being used for general corporate purposes. In 2015, new issuance was led by refinancing activity, accounting for 43% of the total volume followed by 38% used for acquisition-related purposes. This compares with 54% and 26%, respectively, during 2014.

New issuance volume fell in June



Source: JP Morgan, as of June 30, 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 (%)

	1/16	2/16	3/16	4/16	5/16	6/16	YTD 2016
Barclays US HY 2% Issuer Cap Index	-1.61	0.57	4.44	3.92	0.62	0.92	9.06
Barclays US Aggregate Bond Index	1.38	0.71	0.92	0.38	0.03	1.80	5.31
Barclays US Treasury 5-10 Year Index	2.85	1.10	0.09	-0.08	-0.14	2.52	6.47
JPM EMBI Global Diversified Index	-0.18	1.91	3.27	1.77	-0.18	3.37	10.31
S&P 500 Index	-4.96	-0.13	6.60	0.39	1.80	0.26	3.84
S&P/LSTA Leveraged Loan Index	-0.65	-0.53	2.64	1.99	0.89	-0.15	5.36

Source: Barclays, JP Morgan and Standard and Poor's, as of June 30, 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.

All data provided by Invesco unless otherwise noted. Data as of June 30, 2016, unless otherwise noted.

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