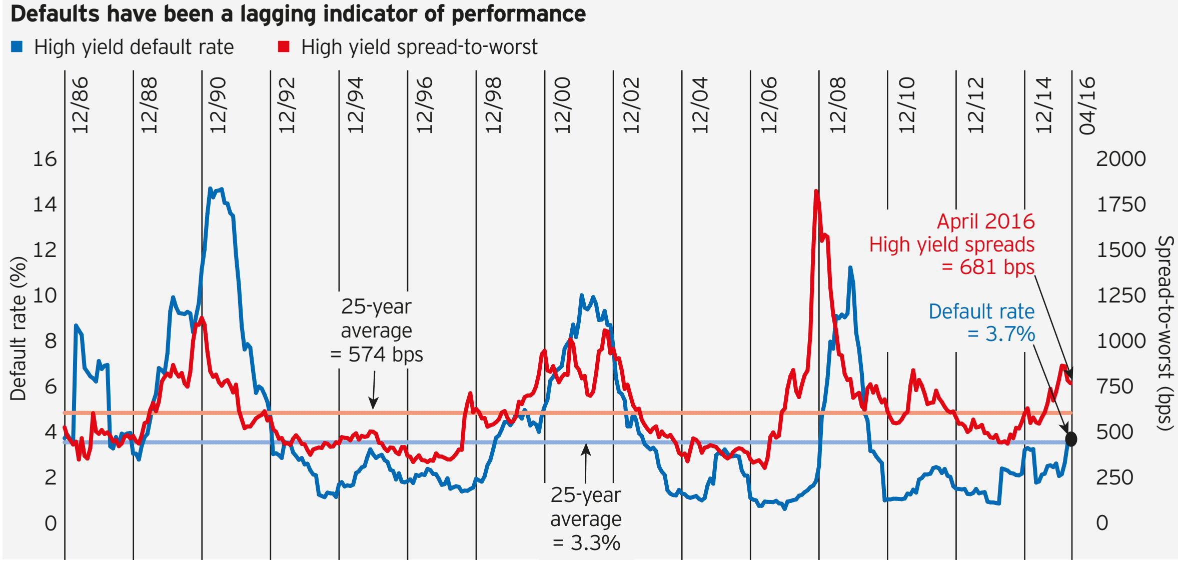
High Yield Snapshot

Monthly high yield bond market update: May 2016

Total returns in the high yield bond market were strong in April, with the Barclays U.S. Corporate High Yield 2% Issuer Capped Index gaining 3.92% during the month. Improving global macro conditions and dovish language from the Fed helped spur strong performance as investors increased exposure to risky assets, including high yield. As fears of slowing global growth subsided and most commodities showed signs of improvement, investors drove spreads tighter. Spreads, as per JP Morgan, ended the month at 694 bps, a level we believe offers value. The five-year and 10-year Treasury yields were little changed at 1.29% and 1.83%, respectively, despite intra-month volatility. With respect to default rates, the recent rally would suggest actual defaults to come in lower than previous estimates, but we note a large number of commodity-related companies continue to struggle with high debt burdens. We do note the recent recovery in oil and other commodities may make it easier for some of these companies to service their debt. Overall, we believe investors are getting compensated for the risks associated with today's market.

Defaults have been a lagging indicator of performance



Source: JP Morgan, as of April 29, 2016

Performance by ratings[1]

Within the ratings categories:

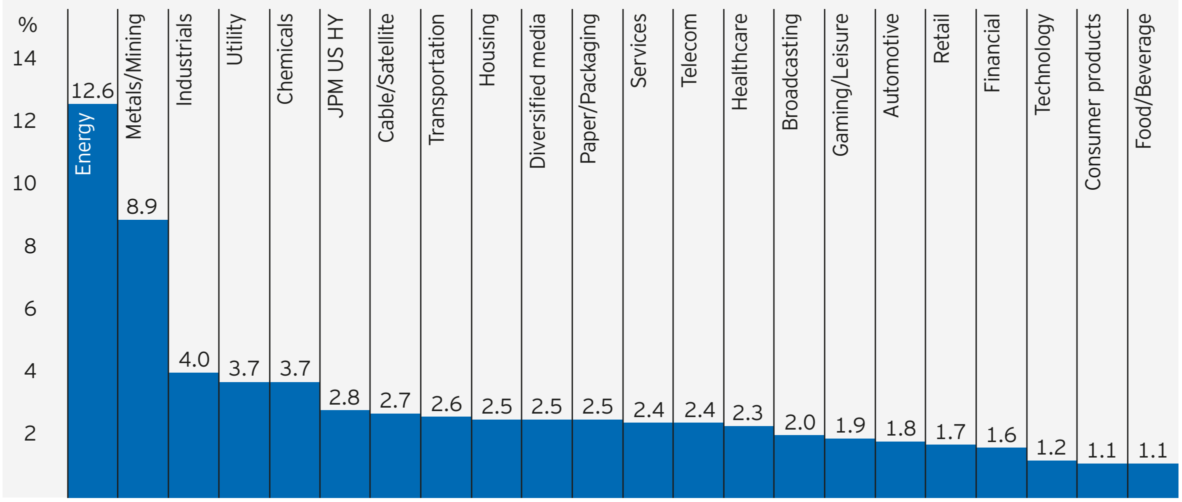
- BB-rated securities returned 2.56%
- B-rated securities generated returns of 3.77%
- CCC-rated securities returned 7.78%

Earnings trends

First quarter earnings season is coming to a close. As for fundamentals overall, here are several themes we are monitoring:

- We have added to our positions in metals and mining. Despite the overall weak fundamentals in the sector, we see value in certain credits with lower amounts of balance sheet leverage.
- Healthcare has shown mixed results. Some companies are reporting higher wage pressures for skilled labor while other costs have increased. We continue to underweight this sector given relative value concerns.
- Energy earnings have been quite poor, a surprise to no one. In particular, energy service companies continue to demonstrate large revenue declines and unsustainable earnings trends. We note no discernible improvement in fundamentals in this segment of energy and maintain our underweight to this portion of the energy sector. In contrast, we maintain our overweight to strong independent energy producers with great assets in the Permian Basin of Texas.

High yield posted strong returns in April



Source: JP Morgan, as of April 29, 2016

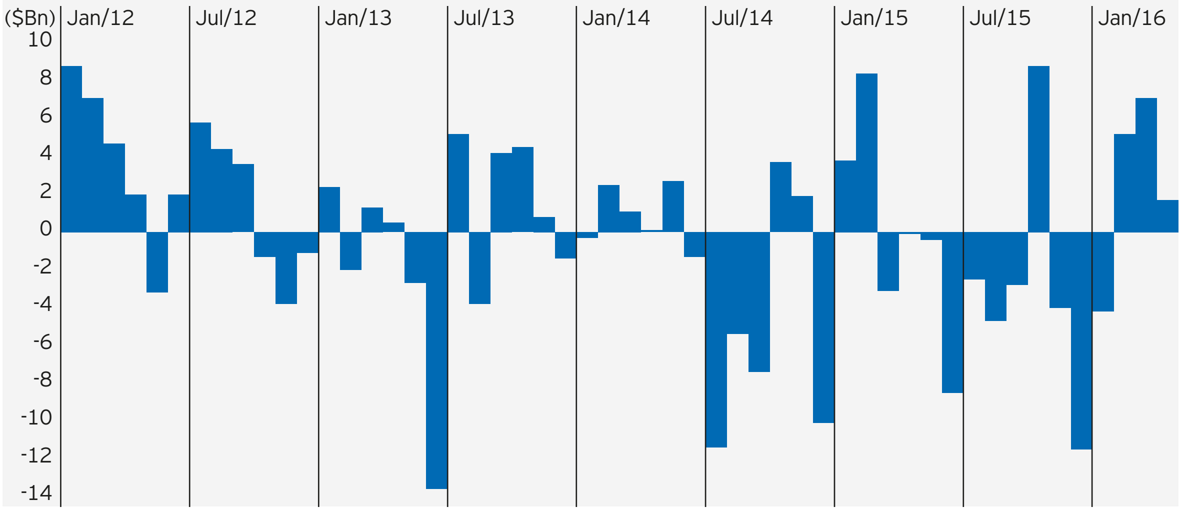
Fundamentals

- The Barclays U.S. Corporate High Yield 2% Issuer Capped Index finished the month with a yield-to-worst of 7.37%, a modified duration of 4.18, an option-adjusted spread of 577 bps, and an average price of 94.70.
- There were seven defaults in April in the high yield market, increasing the par-weighted default rate to 3.68% from 3.22%. Excluding energy and metals and mining, the default rate is 0.42%.[2]
- Credit metrics for the overall market continue to reside in a healthy zone, in our opinion.
- Recent leverage statistics continue to increase, driven by poor earnings within the metals and mining and energy sectors. We don't see this trend reversing in the near-term.

Technicals

- High yield mutual funds reported $1.7 billion of inflows during April, which marks the third consecutive month of positive flows. In contrast, 2015 saw full-year outflows totaling $16.6 billion even after a record $23.8 billion of outflows in 2014.
- New issuance for April came in at $32.3 billion, increasing for the fourth consecutive month. Deal volume exceeded $30 billion for the first time since 2015. However, overall deal volume remains down year-over-year.
- New issuance was led by refinancing activity with 61% followed by 27% being used for acquisition/LBO activity. 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.[2]

High yield has posted three consecutive months of positive inflows
Monthly high yield fund flows



Source: JP Morgan, as of April 29, 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 (%)

	2015	1/16	2/16	3/16	4/16	YTD 2016
Barclays U.S. HY 2% Issuer Cap Index	-4.43	-1.61	0.57	4.44	3.92	7.40
Barclays U.S. Aggregate Bond Index	0.55	1.38	0.71	0.92	0.38	3.43
Barclays U.S. Treasury 5-10 Year Index	1.84	2.85	1.10	0.09	-0.08	4.00
JPM EMBI Global Diversified Index	1.18	-0.18	1.91	3.27	1.77	6.90
S&P 500 Index	1.38	-4.96	-0.13	6.60	0.39	1.74
S&P/LSTA Leveraged Loan Index	-0.69	-0.65	-0.53	2.64	1.99	3.56

Source: Morningstar, as of April 29, 2016

1 Barclays
2 JP Morgan

About risk

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

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