NCRAM
The Case for High Yield Bonds

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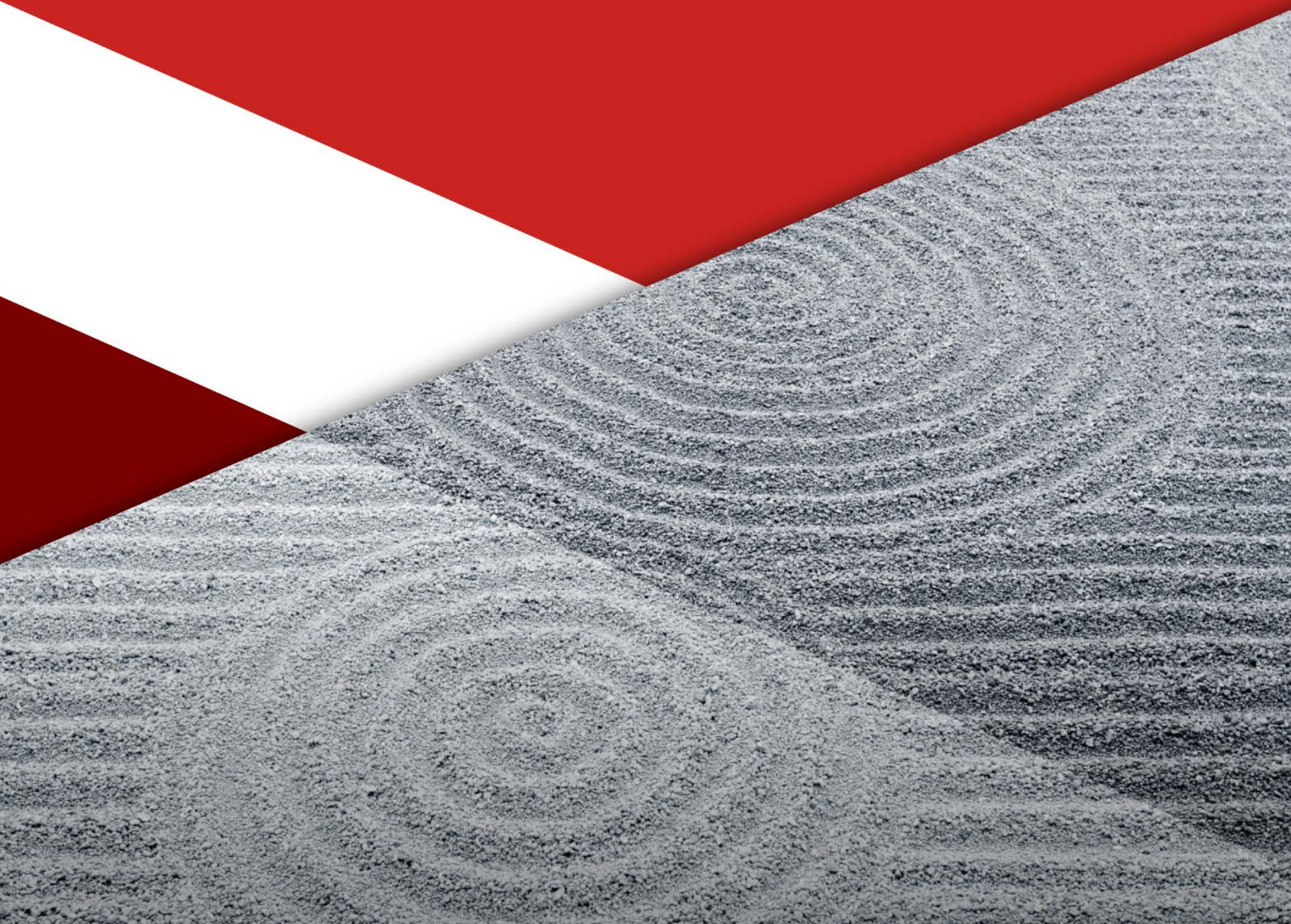

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The Case for High Yield Bonds

Over the last few decades, NCRAM has observed global investors increasingly embrace a strategic portfolio allocation to high yield bonds. We believe there are three key factors driving this interest:

- The asset class has delivered competitive absolute and risk-adjusted returns and attractive income
- High yield maintains limited correlation to other major asset classes and thus provides valuable portfolio diversification
- The high yield market offers opportunities for a skilled active manager to outperform passively managed alternatives

High yield has grown and matured as an asset class in recent years. In the post-Global Financial Crisis environment, the widely followed ICE BofA US High Yield Constrained Index has nearly doubled in size, with the face value of the index rising above $1.4tn (as of March 31, 2025). Over the same period, net leverage among high yield issuers declined from 5.0x to less than 4.0x[1]. As the market continues to evolve, investors across the world have incorporated high yield bond portfolio allocations, attracted to the favorable absolute and risk-adjusted returns, income, and diversification benefits. Asset owners have found the asset class is additive to a strategic allocation, augmented by alpha driven by manager selection. Wealth managers are similarly drawn to the asset class' carry and prospective return contribution to a client portfolio.

Solid Performance vs. Other Asset Classes

High yield bonds have generated competitive results vs. other risk or rates assets over the last 20 years. As seen in the table below, high yield returns have topped other public market fixed income options. While the absolute return in equities has been stronger, high yield's income provides downside cushioning, reducing volatility and generating superior risk-adjusted returns. High yield has also provided more consistent performance vs. most other fixed income or equity asset classes, as measured by batting average (percentage of months with a positive total return).

Returns and Risk

	Ann. TR	Std. Dev.	Risk/Return	Batting Avg.
High Yield	6.47%	9.02%	0.72	70.00%
Loans	4.98%	6.85%	0.73	76.25%
EM Sovereigns	5.55%	8.70%	0.64	65.00%
Inv Grade	4.18%	6.30%	0.66	62.50%
US Agg Bond	3.18%	4.25%	0.75	61.25%
10-Year UST	2.86%	7.33%	0.39	50.83%
US LC Equity	10.23%	15.02%	0.68	67.50%
US SC Equity	7.55%	20.24%	0.37	61.25%

Sources: NCRAM, Bloomberg, batting average calculated as the percentage of months with total returns greater than zero, data herein based on monthly returns from April 2005 through March 2025
High Yield as measured by the ICE BofA US High Yield Constrained Index (HUC0), Loans as measured by the Morningstar LSTA US Leveraged Loan Index, EM Sovereigns as measured by the JPMorgan Emerging Markets Bond Index Global (EMBIG), Investment Grade as measured by the ICE BofA US Corporate Index (C0A0), US Agg Bond as measured by the Bloomberg US Aggregate Bond Index, 10-Year UST as measured by the ICE BofA Current 10-Year US Treasury Index (GA10), US Large Cap (LC) Equity as measured by the S&P 500 Index, US Small Cap (SC) Equity as measured by the Russell 2000 Index

Diversification Benefits

High yield bonds enhance diversification in a fixed income or a multi-asset class portfolio. Somewhat surprisingly, high yield's long-term correlation vs. the 10-year US Treasury is slightly negative. Correlation vs. other rate-

[1] *JP Morgan Data, 4Q09 vs. 4Q24*

sensitive asset classes such as core bonds is also limited. This means an allocation to high yield is advantageous in a fixed income portfolio. High yield is a “risk asset,” thus correlations with equities are higher, but remain sufficiently low to provide meaningful diversification benefits. The connection with stock index returns also varies over time (rolling 36-month correlation to small cap equities has ranged as low as 0.4 over the last 20 years), further illustrating the important role played by high yield bonds in a multi-asset portfolio.

Asset Class Correlation

Correlation	High Yield	Loans	EM Sovereign	Inv Grade	US Agg Bond	10-Year UST	US LC Equity	US SC Equity
High Yield	1.00	0.84	0.79	0.68	0.36	-0.04	0.75	0.72
Loans	0.84	1.00	0.56	0.45	0.06	-0.32	0.58	0.57
EM Sovereigns	0.79	0.56	1.00	0.83	0.64	0.33	0.62	0.54
Inv Grade	0.68	0.45	0.83	1.00	0.86	0.59	0.47	0.39
US Agg Bond	0.36	0.06	0.64	0.86	1.00	0.88	0.24	0.16
10-Year UST	-0.04	-0.32	0.33	0.59	0.88	1.00	-0.09	-0.16
US LC Equity	0.75	0.58	0.62	0.47	0.24	-0.09	1.00	0.89
US SC Equity	0.72	0.57	0.54	0.39	0.16	-0.16	0.89	1.00

Sources: NCRAM, Bloomberg, batting average calculated as the percentage of months with total returns greater than zero, data herein based on monthly returns from April 2005 through March 2025
High Yield as measured by the ICE BofA US High Yield Constrained Index (HUC0), Loans as measured by the Morningstar LSTA US Leveraged Loan Index, EM Sovereigns as measured by the JPMorgan Emerging Markets Bond Index Global (EMBIG), Investment Grade as measured by the ICE BofA US Corporate Index (C0A0), US Agg Bond as measured by the Bloomberg US Aggregate Bond Index, 10-Year UST as measured by the ICE BofA Current 10-Year US Treasury Index (GA10), US Large Cap (LC) Equity as measured by the S&P 500 Index, US Small Cap (SC) Equity as measured by the Russell 2000 Index

Alpha Generation Possibilities

High yield is a less liquid public market asset class, featuring an array of bonds issued by companies lightly followed by Wall Street analysts. This creates alpha generation opportunities for a skilled active manager with sufficient research resources, a robust investment process, and the relationships necessary to gain access to trading liquidity, new issue allocations, and traditional and non-traditional sources of data and information.

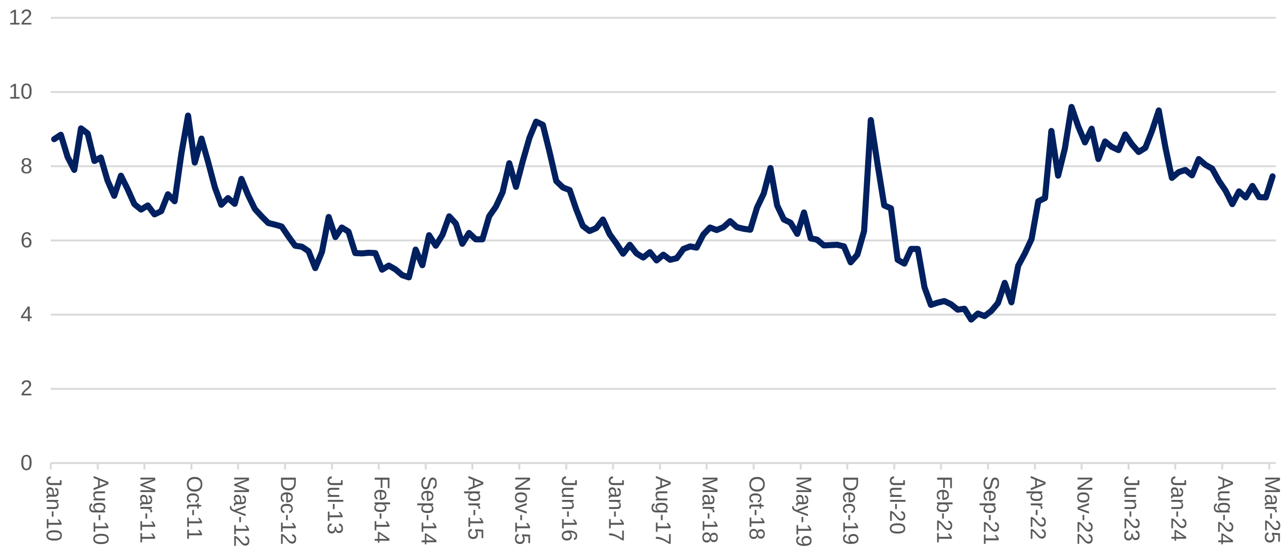
The $1.4tn market features over 1,900 bonds issued by nearly 900 companies, well-diversified across sectors and industries[2]. This breadth offers a wealth of investment opportunities. Furthermore, some investors and traders have structural biases, which can cause asset prices to stray from intrinsic value. Data from Morningstar typically shows active high yield managers outperform passive strategies with greater frequency relative to active managers in most other fixed income or equity asset classes.

Yields Self-Regulate High Yield Returns

Investors should note the high yield market also possesses an important self-correcting mechanism – the yield from bond coupons. In the post-Global Financial Crisis environment, the yield to worst on the ICE BofA US High Yield Constrained Index has ranged between 3.9% and 9.6% (see chart overleaf). When market forces move yields higher, all else equal, the carry increases, driving up prospective total return. Conversely, when yields decline, carry falls and expected forward total return shrinks. Price moves also impact equity valuations, but a catalyst is required to unlock that value. High yield features a built-in catalyst, as lower prices create higher current yield and superior prospective returns.

[2] *ICE BofA US High Yield Index as of March 31, 2025*

ICE BofA US High Yield Constrained Index Yield to Worst



Source: ICE BofA. Data shown from January 2010 through March 2025

In summary, NCRAM believes high yield bonds should be part of a strategic portfolio allocation for long term investors. High yield has delivered competitive absolute and risk-adjusted returns, maintains limited correlation to other major asset classes, and offers opportunities for a skilled active manager to outperform passively managed alternatives.

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