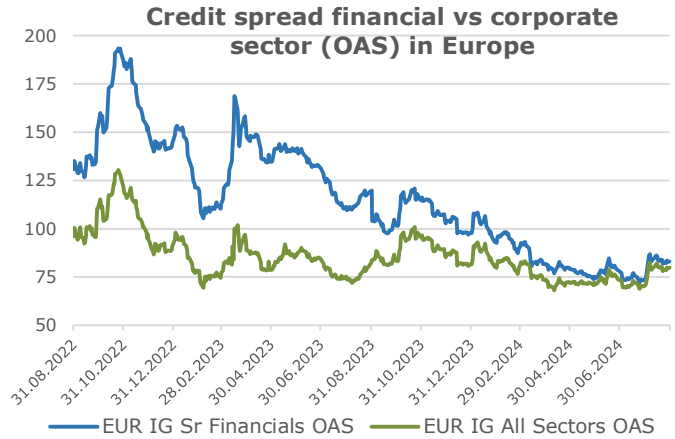


Monthly Spotlight

Banking sector reflects credit quality improvements

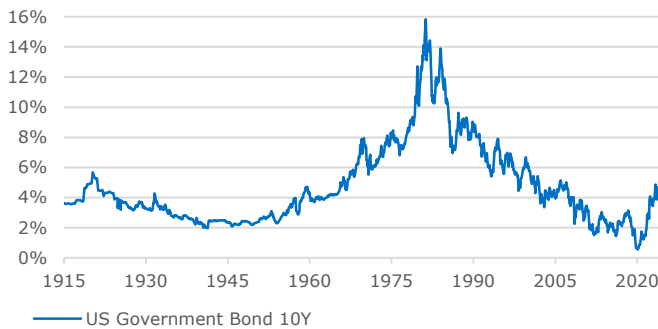
Historically, bank spreads have typically traded wider than those in the broader corporate market. However, this gap has almost disappeared, driven by the positive dynamics and performance within the banking sector since the European Central Bank started the hiking rate cycle in 2022.

EUR IG Sr Financial spreads (see blue line in graph) are now at their lowest point in two years vs the Eur IG All Sectors OAS Index (green line). Banks are benefiting from higher net interest margins, which have significantly boosted net income and return on equity following years of underperformance and sluggish growth. Additionally, capital ratios have remained robust, with evolving capital requirements enhancing the sector's credit quality. However, the potential for spread widening cannot be dismissed, as margins can shrink, and non-performing loans may increase in a weakening economic environment.

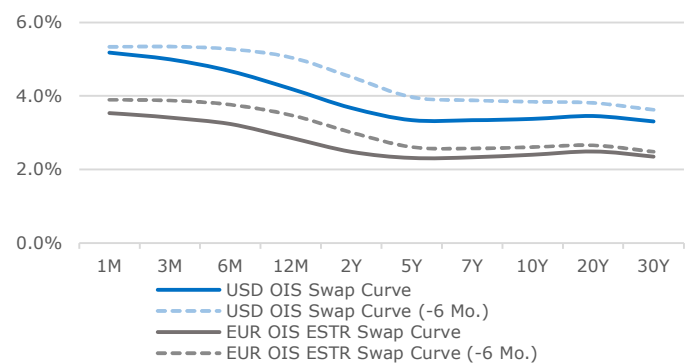


Rates Perspective

1) Historical US Treasury Yield: 10-year US government bond yield reached its 100-year low in 2020.

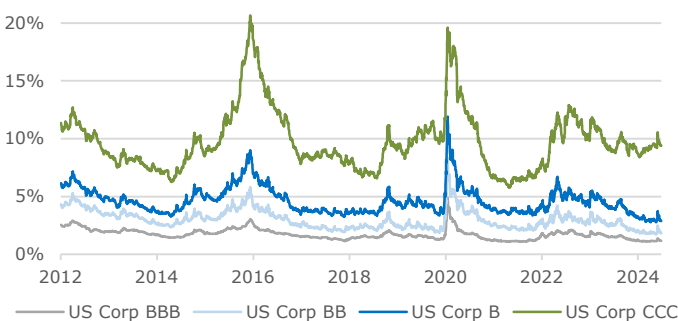


2) Interest Swap Curve: The USD and EUR curves remain inverted with shorter tenors continuously higher.



Corporate Perspective

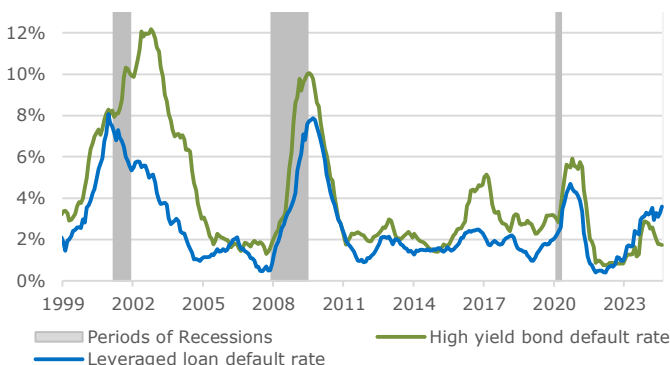
3) US Corp. Rating: Credit spreads (OAS) of lower rated high-yield bonds widened disproportionately.



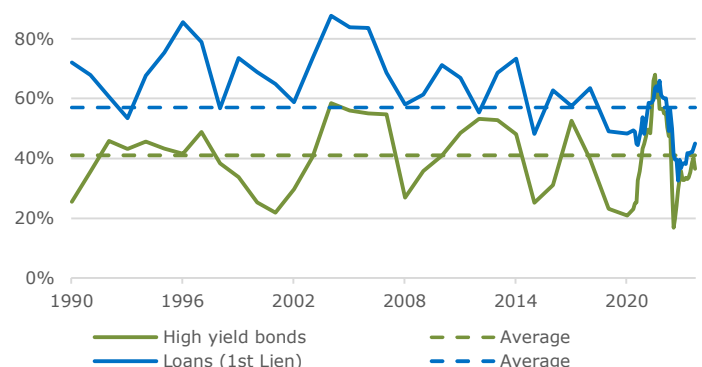
4) EU vs US: Since 2022 EU credit spreads (OAS) have remained wider than in the US.



5) Default Rates: HY bond default rates are structurally higher (Ø4.1%) vs. loans (Ø2.7%).



6) Recovery Rates: Recovery rates of leveraged loans are higher (Ø57%) vs. high yield bonds (Ø41%) due to lower severity.



OAS spread change overview across major credit asset classes - as of month end

US corporates by rating (bps)

| | curr | Δ month |
|-----|------|---------|
| AAA | 38 | +2 |
| AA | 53 | +3 |
| A | 81 | +2 |
| BBB | 119 | +1 |
| BB | 183 | -11 |
| B | 289 | -12 |
| CCC | 937 | +5 |

Global high yield (bps)

| | curr | Δ month |
|---------|------|---------|
| US HY | 315 | -10 |
| EU HY | 350 | +6 |
| Asia HY | 434 | +13 |
| EM HY | 522 | -10 |

■ spread tightening (positive price action)
■ spread widening (negative price action)

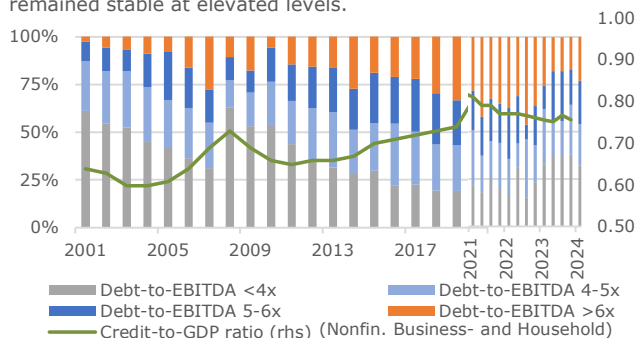
CDS spreads (bps)

| | curr | Δ month |
|----------------|------|---------|
| CDX IG - US | 49 | +3 |
| iTraxx IG - EU | 53 | +2 |
| CDX HY - US | 322 | +9 |
| iTraxx XO - EU | 288 | +6 |

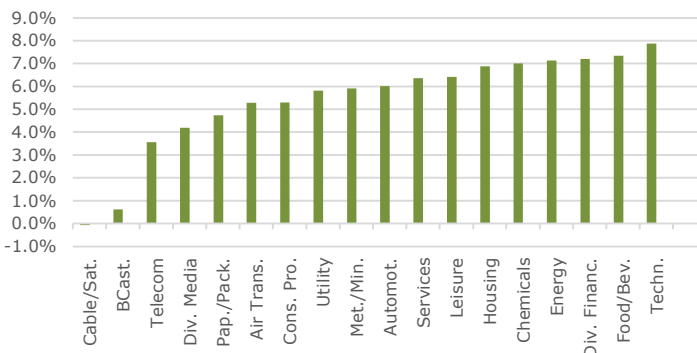
Loans and CLOs (yld, bps)

| | curr | Δ month |
|---------|------|---------|
| US Loan | 920 | +0 |
| CLO AAA | 659 | +1 |
| CLO BBB | 907 | +1 |
| CLO BB | 1229 | +1 |

7) US Leverage: Debt-to-EBITDA ratio of US companies remained stable at elevated levels.

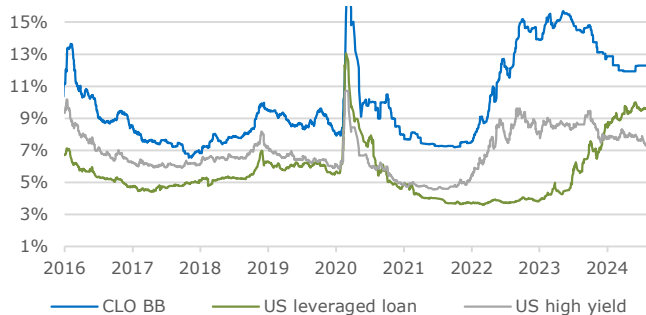


8) YTD Sector High-Yield Returns: Positive YTD results across most of the sectors, with leisure outperforming significantly.

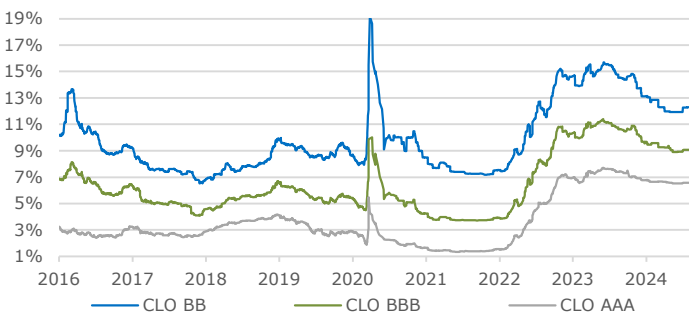


Alternative Perspective

9) Loans vs. CLO vs. HY: CLO BB yields are wider vs Loans and HY bonds.



10) CLO Yields: CLOs offer an attractive yield premium over bonds and Loans.



11) Asia vs. US: Asian IG spreads have tightened thanks to gradual post-COVID recovery and US inflation easing.



12) Capital vs IG: Capital Securities structurally earn a premium vs. US IG bonds. Capital Securities are dominated by the financial sector.



Education Corner - Series: AIM Credit Analysis (7)

Bondholder Protection: Covenant package

Companies have a fiduciary duty to their shareholders, while their obligations to debtholders are merely contractual. This matter is particularly significant in the leveraged finance market, where covenants play a crucial role in aligning the interests of all stakeholders.

IG issues generally feature covenant-lite structures due to their higher perceived credit quality. In contrast, high-yield issuers face more restrictive covenant packages. For instance, covenants in investment-grade bonds are often "incurrence covenants," meaning they are triggered by specific events like M&A, issuing additional debt, or paying dividends. On the other hand, in the HY and leveraged loan markets, it is common to find "maintenance covenants," which are tested regularly, typically on a quarterly basis, and require companies to maintain certain financial ratios continuously.

Covenants can safeguard against various management decisions, such as limiting leverage, preventing value leakage, and or changes in ownership.

| | Covenants |
|-----------------------------------|--|
| Additional Debt Limitation | <ul style="list-style-type: none"> - Limitations on debt incurrence - Limitations on secured debt incurrence - Leverage maintenance covenants - Limitations on liens |
| Value Transfer out of the company | <ul style="list-style-type: none"> - Limitations on restricted payments - Permitted investments language |
| Selling the company | <ul style="list-style-type: none"> - Change of Control - Limitations on Asset sale |

US Loan Index Total Return - Attractive Long Term Yield Generation



List of Abbreviations

Capital Securities (Or preferred securities): Are fixed income securities combining features of bonds and preferred stocks.

CDS: Credit default swaps transfer credit event risk to another party in exchange of a periodically paid premium. CDX index covers the US IG-, iTraxx the EU IG- and iTraxx crossover (XO) the EU HY market.

CLOs: Collateralized loan obligations are structured finance securities collateralized predominantly by a large pool of different loans.

Default Rate: Number of defaulted corporate issuers of leveraged loans and high yield bonds.

Loans: Are syndicated, public tradable loans. Synonyms are «syndicated loans», «loans», «leveraged loans» and «bank loans».

OAS: Option-adjusted spread is the yield difference of an interest paying security to the risk free rate considering embedded options.

TIPS: Treasury Inflation-Protected Securities are US government linked to the US CPI Urban Non-Seasonally Adjusted.

Up-/ downgrades: Rating actions of Moody's and S&P of up-or downgrades of US high yield bond issuers denominated in USD.

Up-/ downgrade ratio: Number of upgrades of total rating actions.

Recovery Rates: Bond issuer-weighted recovery rates express the principal and accrued interest on defaulted debt that can be recovered in percentage of face value. Example:

Expected loss rate if US HY defaults were 10%: 10% ./ Estimated average recovery rate of ~30% = -7%;

Expected loss rate if US Loan defaults were 10%: 10% ./ Estimated average recovery rate of ~65% = -3.5%;

Data and Price Sources

Alpium Investment Management

Bank of America Merrill Lynch indices

Bloomberg

The Federal Reserve

US Census Bureau

Federal Reserve Bank of St. Louis

Markit CDS indices

Moody's Investors Service

J.P. Morgan

Palmer Square indices

Preqin

S&P

Federal Housing Finance Agency

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