COLUMBIA THREADNEEDLE INVESTMENTS

2023 high-yield midyear market review

U.S. high-yield total returns have stabilized following the second worst year on record in 2022. Despite the continuation of the most aggressive Fed tightening cycle in 40 years, heightened interest-rate volatility and the emergence of regional banking stress, the high-yield market has been resilient thus far in 2023. Spreads have tightened 63 basis points (bps) as macroeconomic data, particularly labor market data, has come in better than expected and corporate earnings have generally managed to meet reduced expectations, pushing out near-term recession risk. Technical factors also continued to support bond prices. We highlight the drivers and nuances of the first half of the year herein. All data herein references the ICE BofA U.S. HY Cash Pay Constrained (JUC0) Index as of 06/30/23 unless otherwise noted.

Index high-yield returns

Quarterly progress of high-yield returns (%)

	Q1	Q2	YTD 2023
BB	3.32	0.78	4.13
B	3.85	1.83	5.75
CCC	4.71	4.54	9.47
Total	3.67	1.61	5.34

Source: ICE (references the ICE BofA U.S. HY CP Constrained Index).

Index return details

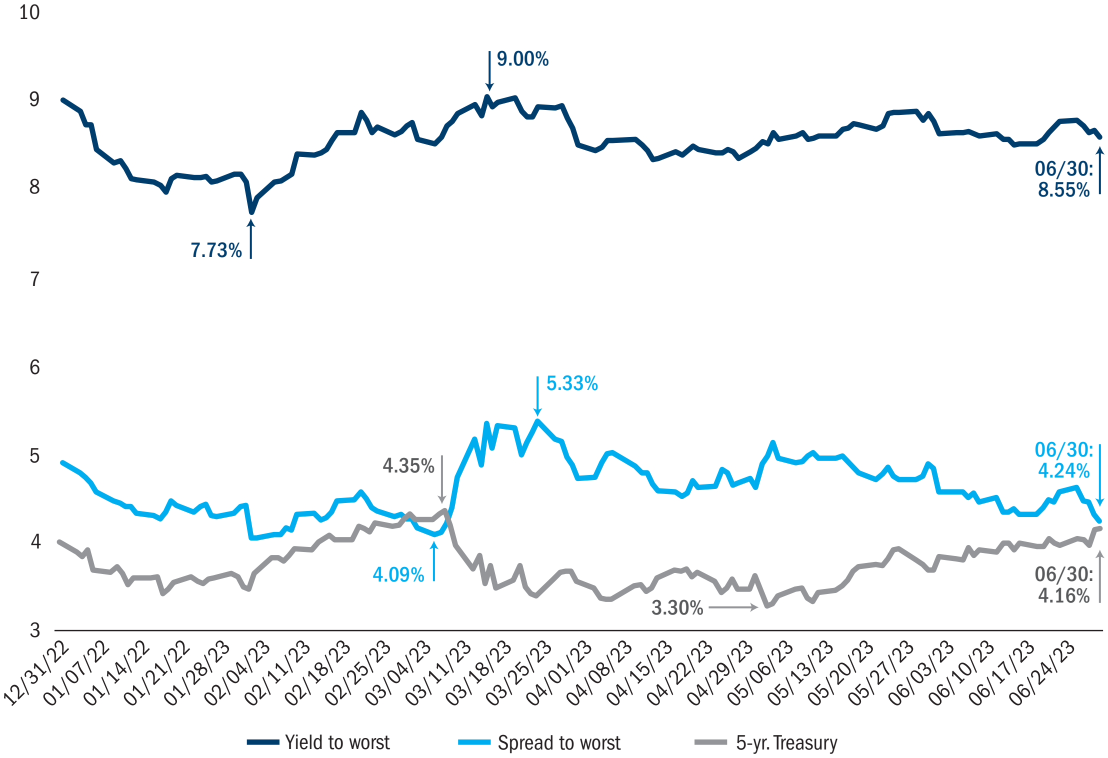
- Continuing the trend from 2022, the high-yield market has been characterized by elevated interest rate and spread volatility as well as heightened industry and issuer return dispersion over the first half of the year.
  - The first half return was driven by a 2.0% price increase, enhanced by a 3.3% coupon return.
  - Spreads began the year at +487bps. While tighter by 63bps through 06/30, spreads traded in a 128bps range, reaching as low as +405bps in early February and as high as +533bps during March's regional banking crisis. Following nine distinct spread moves of 75bps or more in 2022, there were four such instances over the first half of 2023.
  - Relative to spreads, the yield to worst (YTW) of the market was more stable, trading in 67bps range after rebounding from its early February low.
  - CCC rated securities outperformed materially with a 9.47% total return as overall fundamental concerns eased, and certain idiosyncratic credit stories boosted returns.
    - As is typical, and not unlike YTD equity market returns, the category's total return was skewed by its best performers. The top five contributors (representing 3% of all CCC issuers on an equal-weighted basis) contributed approximately one third of the rating category total return. These issuers averaged a 35% return over the period.
      - The top five CCC returners were Carvana (CVNA), Norwegian Cruise Lines (NCLH), Community Health (CYH), Transocean (RIG), Athena Health (ATHENA).
      - Further, the top contributor to CCC returns, auto retailer Carvana (CVNA), contributed approximately one fifth of the total CCC return with an average return of 76% across its five bonds.

High-yield return summary (%)

	High-yield	BB	B	CCC
YTD 2023 total return	5.34	4.13	5.75	9.47
Spread change	-63	-37	-75	-191
2023 YTD excess return	4.17	2.94	4.61	8.32

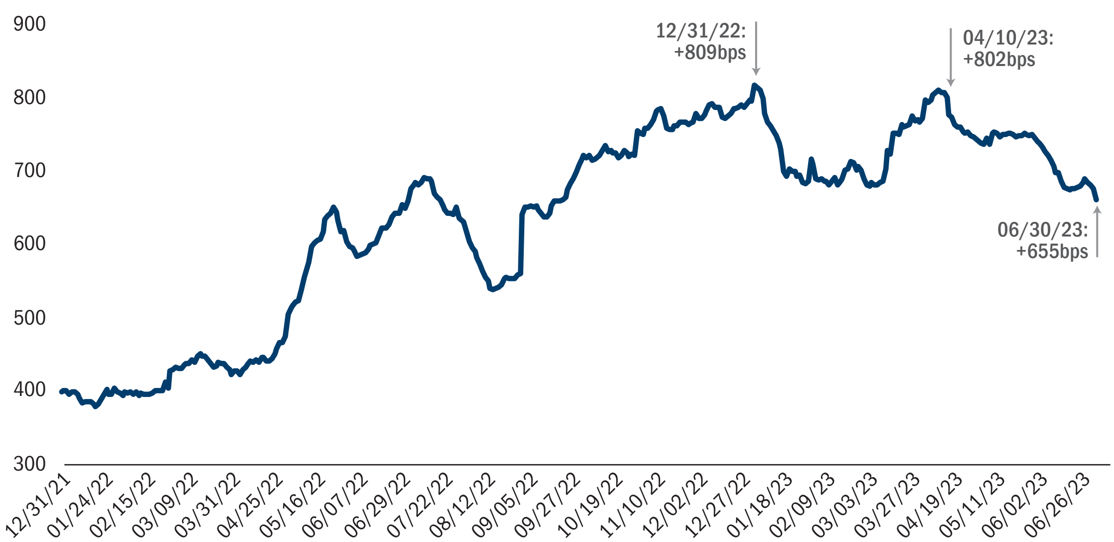
Source: ICE (references the ICE BofA U.S. HY CP Constrained Index).

U.S. high-yield spread to worst/yield to worst vs. 5-yr. Treasury



Source: ICE (references the ICE BofA U.S. HY CP Constrained Index).
Past performance is not a guarantee of future results.

Spread-to-worst differential: BBs vs. CCCs



Source: ICE (References the ICE BofA BB U.S. HY CP Constrained Index, ICE BofA CCC and Lower U.S. HY CP Constrained Index).
Past performance is not a guarantee of future results.

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By industry

- There was notable sector level return dispersion over the period with a greater than 11% gap between the best (leisure, 9.50%) and worst (banking, -1.55%) performing sectors.
- Leisure outperformance was primarily driven by the cruise line operators with theater chains also contributing.
- Strong retail performance was driven by auto retailer Carvana's (CVNA) outsized returns. Excluding this issuer from the sector's return results in market-like performance YTD.
- Unsurprisingly, banking was the worst performing sector, with First Republic Bank (FRC) briefly downgraded to high yield prior to its eventual failure. Legacy high-yield banking names, primarily composed of subordinated bonds of European banks, performed relatively well.
  - We would note that banking has only a small weight (<1%) within the U.S. high-yield market.
- Media underperformed as U.S. cable and satellite TV providers Dish Networks (DISH) and Altice U.S. (CSCHLD) underperformed. Content providers within media also struggled under the ongoing secular shift away from linear content.
- Similarly, legacy U.S. wireline providers Lumen Technologies (LUMN/LVLT) and Frontier Communications (FYBR) along with French cable and telecom issuer Alice France (SFRFP) drove telecommunications underperformance.

Quarterly progression of industry returns (%)

	Q1	Q2	YTD
Automotive	4.96	1.23	6.25
Banking	0.13	-1.68	-1.55
Basic industry	4.33	1.27	5.66
Capital goods	4.06	1.73	5.86
Consumer goods	4.97	0.19	5.16
Energy	3.96	1.50	5.52
Financial services	3.33	2.03	5.42
Healthcare	4.33	1.05	5.42
Insurance	2.88	2.53	5.49
Leisure	6.43	2.88	9.50

	Q1	Q2	YTD
Media	1.06	0.80	1.86
Real estate	2.46	2.74	5.28
Retail	3.15	4.62	7.92
Services	4.46	1.21	5.72
Technology and electronics	4.62	1.46	6.14
Telecommunications	0.40	1.28	1.69
Transportation	4.66	1.32	6.05
Utility	3.61	0.29	3.91
Total	**3.67**	**1.61**	**5.34**

Source: Columbia Threadneedle Investments based on ICE data. As of 06/30/23.
Past performance is not a guarantee of future results.

Notable items

Federal Reserve activity

- The Federal Reserve continued the most aggressive fed funds tightening cycle over the last 40 years with three additional 25bps hikes over the first half of 2023.
- Notably, the Fed paused in June following hikes at ten consecutive meetings, while still indicating the potential for hikes to resume in July if needed.
- Turmoil in U.S. regional and European banking sector drove volatility around Fed expectations and March saw the highest level of interest-rate volatility, as measured by the ICE BofA MOVE Index, since the global financial crisis of 2007–2009.
- After reaching a level not seen since mid-2007 (5.07%) on 03/08, the two-year Treasury rate declined 1.09% over the course of three trading days, marking its largest three-day decline since 1987's Black Monday stock market crash.
- The chart below illustrates the changes around Fed expectations thus far YTD. On March 8, prior to Silicon Valley Bank's (SVB) failure, the market was pricing in a 5.44% fed funds rate in January 2024. This was as low as 3.69% in the aftermath of SVB but has since rebounded as labor market and inflation data have showed little signs of cooling and hawkish Fed rhetoric have driven expectations higher.

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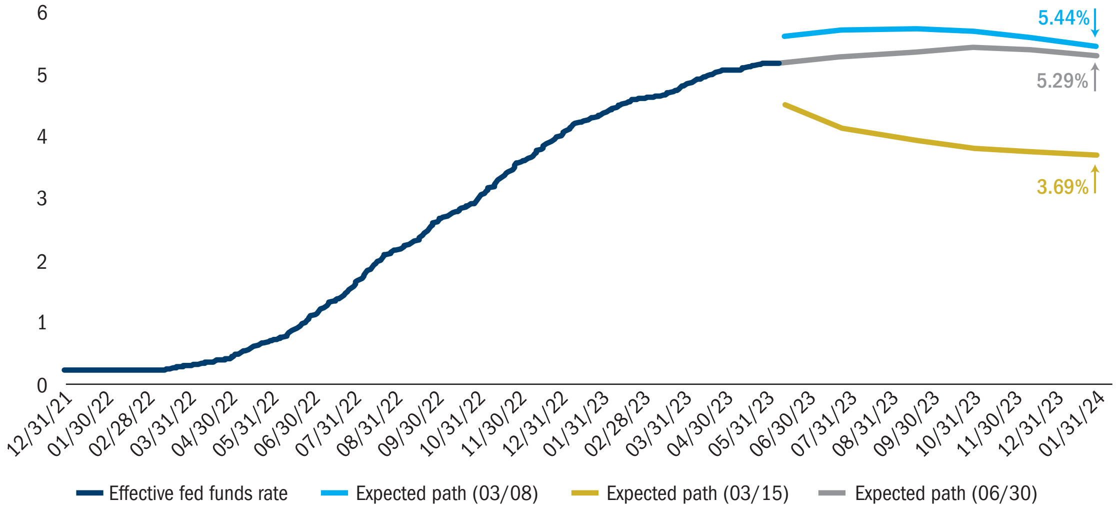
Fed funds rate projected path



Source: Bloomberg.
Past performance is not a guarantee of future results.

Rising stars/fallen angels

- Rising star activity continued to materially exceed fallen angels over the first half of 2023. There were $59.8b of rising stars vs. only $13.9b of fallen angels.
- Rising star activity was concentrated in energy and telecommunications. Three of four energy rising stars were issuers downgraded to high-yield during March–May 2020 (Occidental Petroleum, Western Gas Partners, Apache Corp).
- Also notable, the largest fallen angel of the period, Nissan Motor (NSANY), spent only two months in the high-yield asset class after receiving an investment-grade rating from Fitch after previously being unrated by the agency.

YTD 2023 rising stars

Ticker	Issuer	Par ($b)	Sector
OXY	OCCIDENTAL PETROLEUM	15,271	Energy
S	SPRINT CAPITAL CORP	9,973	Telecommunications
NSANY	NISSAN MOTOR	9,750	Autos
WES	WESTERN GAS PARTNERS	6,254	Energy
MSCI	MSCI INC	4,200	Financials
APA	APACHE CORP	3,874	Energy
MAT	MATTEL	2,350	Retail
LPLA	LPL HOLDINGS	1,700	Financials
LNG	CHENIERE ENERGY	1,500	Energy
BAH	BOOZ ALLEN HAMILTON	1,200	Capital goods
NOKIA	NOKIA CORP	1,000	Technology
ESGR	ENSTAR FINANCE	850	Financials
WEIRLN	WEIR GROUP PLC	800	Capital goods
GNW	GENWORTH MORTGAGE HLDING	750	Financials
AMETPR	AUTO METRO	364	Transportation

YTD 2023 fallen angels

Ticker	Issuer	Par ($b)	Sector
NSANY	NISSAN MOTOR	9,750	Autos
ENTG	ENTEGRIS	1,600	Chemicals
FRC	FIRST REPUBLIC BANK	800	Financials
RCICN	ROGERS COMMUNICATIONS	750	Media
WAL	WESTERN ALLIANCE BANCORP	600	Financials
CR	CRANE CO	350	Capital goods

Source: Bank of America.

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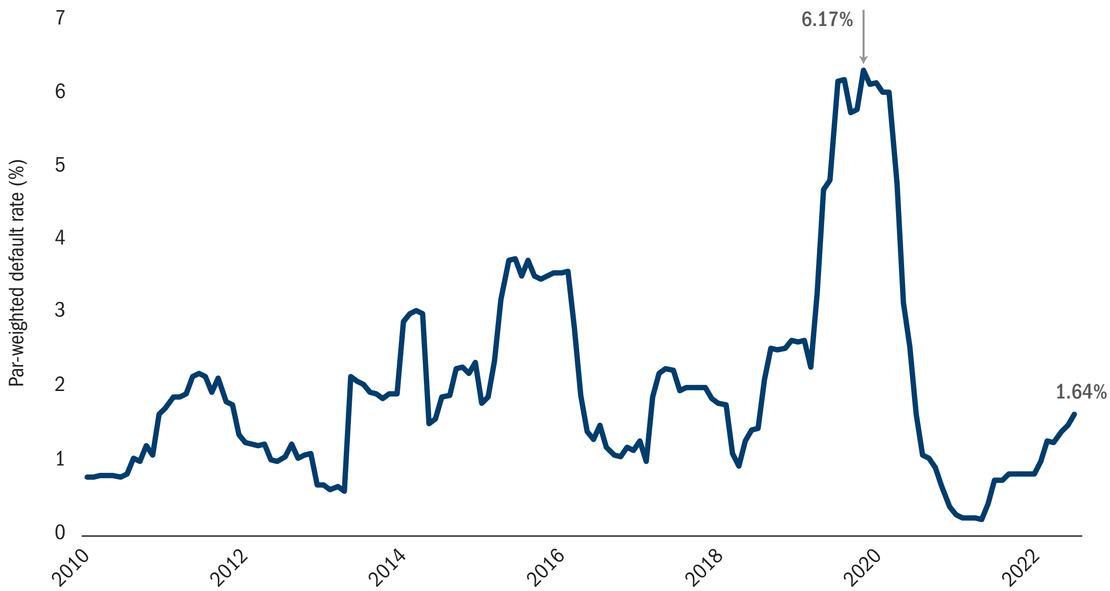
Defaults, recoveries and distressed exchanges

- Default and distressed exchange continued to increase with the J.P. Morgan trailing 12--month par-weighted default rate rising to 1.64% after beginning the year at 0.84%. Including distressed exchanges in the default rate increases it to 2.71%.
- Per J.P. Morgan data, there have been twelve defaults on $16.3b of par over the first half of the year. Already surpassing the seven defaults on $12.2b of par during all of 2022.
  - Annualizing default activity over the first half of the year results in annualized pace of 2.38%.
- Average recoveries declined to 17% driven by single-digit recoveries from Diamond Sports Group, Envision Healthcare, Bed Bath & Beyond and Lannett Co. This is well below the 25-year average of 40% and 2022's average rate of 55%.

J.P. Morgan par-weighted default rate (%)



Source: J.P. Morgan.

YTD 2023 high-yield defaults

Issuer	Ticker	Bonds (par, $b)	Sector	Date
Diamond Sports Group	DSPORT	4,785	Media	02/15/23
Wesco Aircraft Holdings	WESCO	3,025	Aerospace/defense	05/15/23
Diebold	DBD	1,100	Technology	06/01/23
Bed Bath & Beyond	BBBY	1,030	Retail	04/23/23
Party City	PRTY	1,025	Retail	01/17/23
Avaya	AVYA	1,000	Technology	02/14/23
Mallinckrodt	MNK	978	Healthcare	06/15/23
Envision Healthcare	EVHC	940	Healthcare	04/15/23
First Republic Bank	FRC	800	Banking	04/29/23
National Cinemedia	NATCIN	630	Media	02/15/23
Venator Materials	VNTR	600	Chemicals	05/14/23
Lannett Co	LCI	350	Healthcare	04/15/23

Source: J.P. Morgan.

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YTD 2023 high-yield distress exchanges

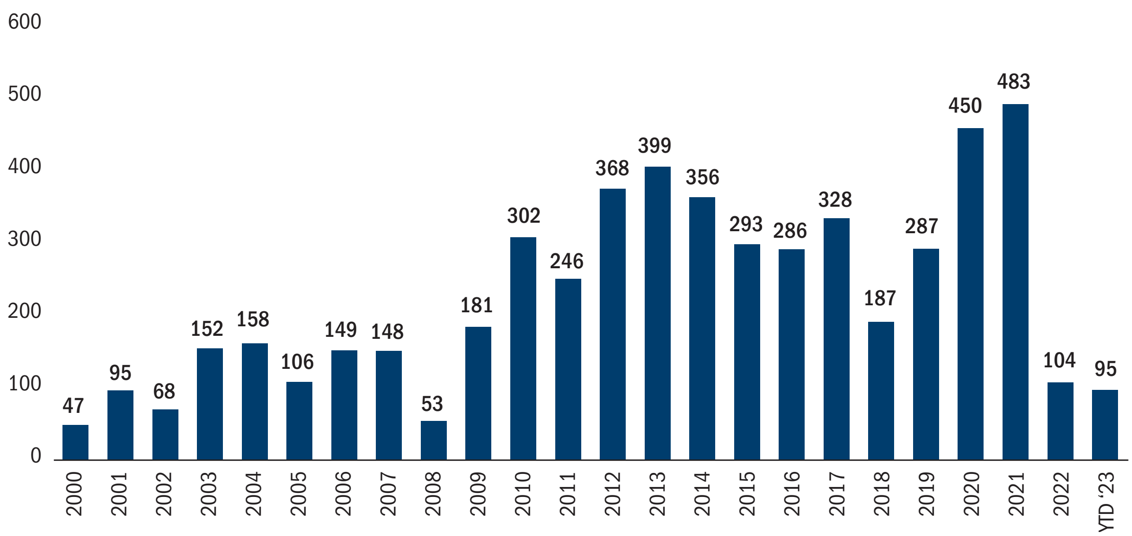
Issuer	Ticker	Bonds (par, $b)	Sector	Date
Lumen Technologies	LUMN	1,556	Telecommunications	04/17/23
Exela	EXLINT	1,270	Technology	06/29/23
WeWork	WEWORK	1,050	Real estate	05/05/23
Shutterfly	SFLY	735	Technology	06/15/23
Sabre GLBL	SABHLD	670	Technology	06/15/23
FXI Holdings	FXIHLD	500	Chemicals	04/28/23
At Home Group	HOME	450	Retail	05/12/23
Cooper Standard	CPS	350	Automotive	01/19/23
AMC Entertainment	AMCX	185	Media	02/17/23
Skillz	SKLZ	160	Gaming	04/19/23
Telesat Canada	TELSAT	105	Telecommunications	05/10/23

Source: J.P. Morgan.

New issues

- New issuance has rebounded following 2022's dearth of activity. Approximately $95b of face value was issued over the first half of the year, nearly matching full-year 2022's total of $104b.
- Issuance has been skewed towards refinancing (62% of proceeds) and higher quality issuers with approximately 85% raised by issuers with at least one BB rating. Conversely, only 1.2% of issuance has gone to issuers with CCC ratings from both Moody's and S&P.
- A notable feature of issuance thus far YTD is the amount secured issuance. Approximately 55% of YTD issuance has been secured, by far the highest pace on record. Elevated bond-for-loan issuance has driven the increase as issuers seek more accommodative capital market conditions in the high-yield market.

Annual high-yield bond new issue volume ($b)



Source: J.P. Morgan.

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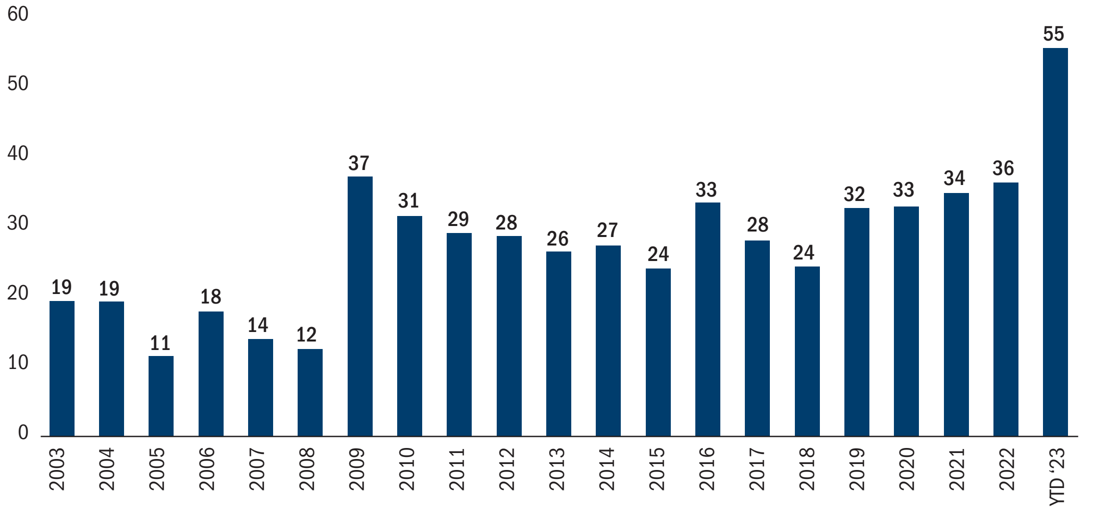
Secured issuance % of total

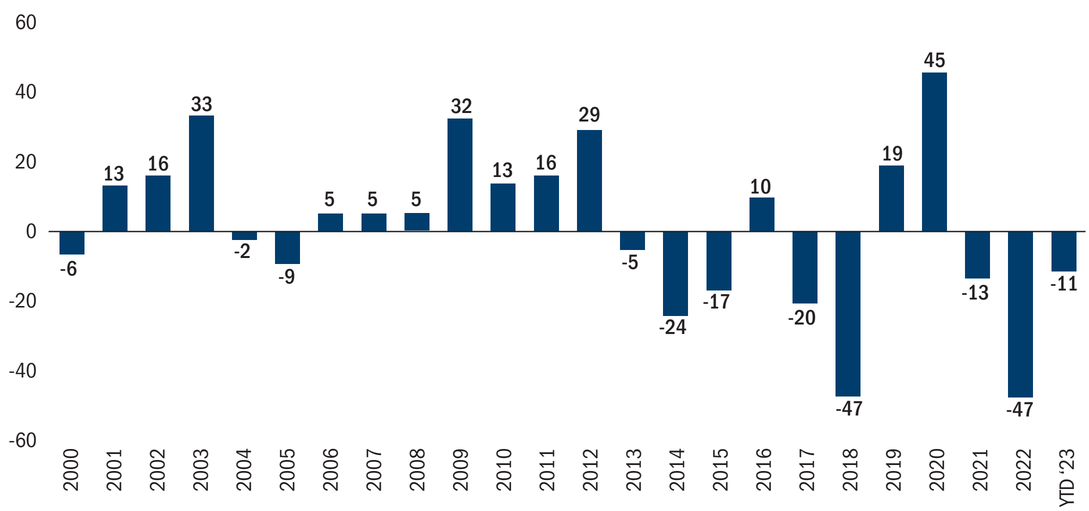


Source: Bank of America.

High-yield flows

- Retail fund flows have moderated over the first half of 2023 following record outflows in 2022.
- YTD outflows total $11.2b, split relatively evenly between active managers and passive ETFs.
- As detailed in the sources/uses table below, outflows were concentrated in the first quarter with a modest reversal seen in Q2.

Annual high-yield bond fund flows ($b)



Source: J.P. Morgan.

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U.S. high-yield market sources/uses of cash ($b)

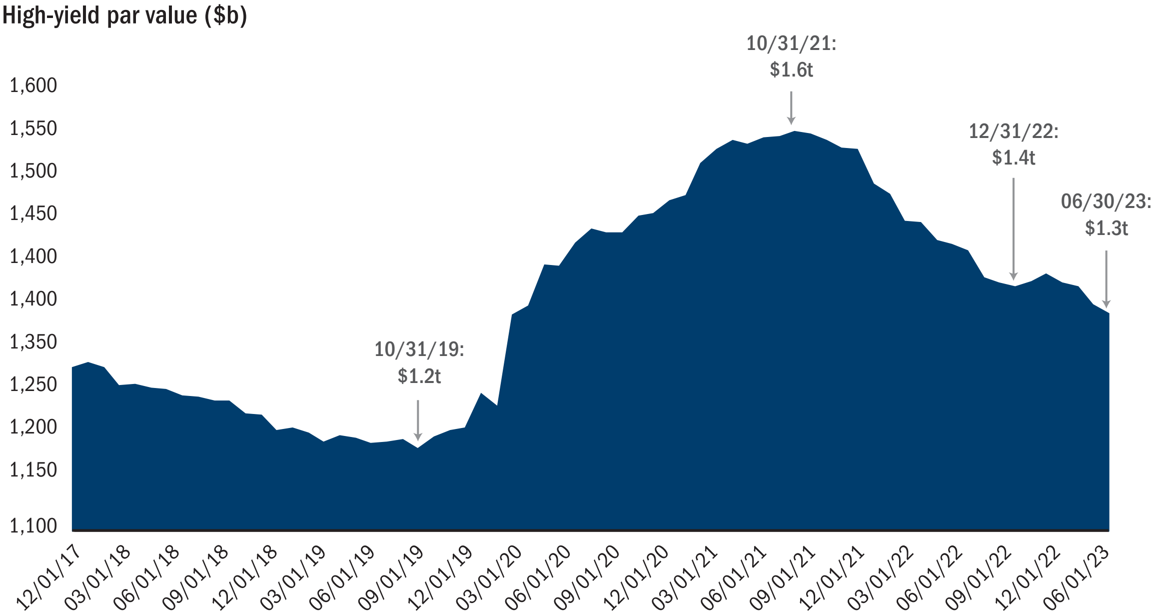
	Q1'23	Q2'23	YTD
Calls/tenders/maturities	39	31	70
Rising stars	15	45	60
Coupon payments	24	23	47
Retail fund flows	-15	4	-11
Total sources	**62**	**104**	**166**
	Q1'23	**Q2'23**	**YTD**
Gross issuance	41	55	95
Fallen angels	12	2	14
Total uses	**53**	**56**	**109**
Net sources/(uses) of cash	**10**	**47**	**57**

Source: Bank of America, J.P. Morgan.

Index changes

- The par value of the high-yield asset class continued to decrease over the first half of 2023, albeit at a more moderate pace than 2022. The par value of the market decreased from $1.37t to $1.34t, or just over 2%. This follows an 11% decrease in 2022.
- $46b of net rising star volume was the primary driver of the approximately $31b decrease in par value since the end of 2022.

High-yield par value ($b)



Source: ICE (References the ICE BofA U.S. HY Index).

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- There were a few notable industry weight changes over the first half of the year:
  - Telecommunications saw the largest change in weight, decreasing by approximately 108bps. The decline was driven largely by the upgrade of Sprint (S) to investment grade given its 91bps index weight to begin the year.
  - Similarly, energy also saw a large market value decline with several large capital structures upgraded to investment grade over the first half of the year. Occidental Petroleum (OXY), Western Gas Partners (WES) and Apace Corp (APA) began the year with weights of 126bps, 47bps and 28bps, respectively.
  - Conversely, weights within leisure and capital goods increased given net new issuance within these sectors.

Industry changes (%)

Industry	Weight %		
	12/31/22	06/30/23	Quintile change
Automotive	3.43	3.70	0.27
Banking	0.88	0.76	-0.12
Basic industry	7.93	7.97	0.04
Capital goods	6.45	7.06	0.61
Consumer goods	3.85	3.77	-0.08
Energy	12.32	11.40	-0.92
Financial services	4.99	4.82	-0.17
Healthcare	7.83	8.05	0.22
Insurance	1.57	1.86	0.28

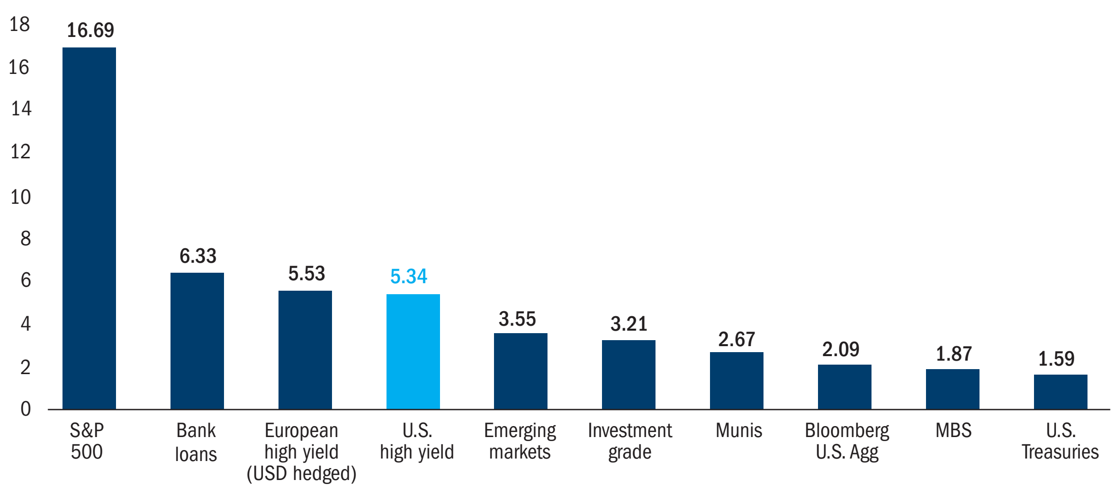
Industry	Weight %		
	12/31/22	06/30/23	Quintile change
Leisure	7.86	8.49	0.63
Media	9.25	9.07	-0.18
Real estate	4.04	4.11	0.07
Retail	5.38	5.64	0.25
Services	6.54	6.60	0.06
Technology and electronics	5.38	5.73	0.36
Telecommunications	6.56	5.48	-1.08
Transportation	2.29	2.28	-0.01
Utility	3.08	3.21	0.14

Source: ICE (references the ICE BofA U.S. HY CP Constrained Index).

Other asset class returns

- The risk-on tone over the first half of the year is evident in the chart below with equities materially outperforming fixed income.
- Within fixed income, bank loans outperformed high yield over the first half, benefiting from a coupon level approaching 9% and higher prices as macroeconomic data remained resilient and expectations for fed funds cuts were pushed further into the future.
- European currency high yield (referencing the ICE BofA European Currency HY Constrained Index, HPC0, in USD hedged terms) performed generally in line with its U.S. high-yield counterpart.

Other asset class total returns YTD 06/30/23 (%)



Source: ICE (References the ICE BofA U.S. HY Index). See following page for indices used.

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Indices used:

Equity S&P 500

Bank Loans Credit Suisse Leveraged Loan Index

European High Yield (USD Hedged) ICE BofA European Currency High Yield Constrained Index (USD Hedged)

U.S. High Yield ICB BofA US High Yield Cash Pay Constrained Index

Emerging Markets Bloomberg Emerging Market Hard Currency Aggregate

Investment Grade Bloomberg Corporate Index

Munis Bloomberg Municipal Bond Index

Bloomberg U.S. Agg Bloomberg U.S. Aggregate Index

MBS Bloomberg U.S. MBS Index

U.S. Treasuries Bloomberg U.S. Treasury Index

It is not possible to invest directly in an index.

Non-investment-grade (high-yield or junk) securities present greater price volatility and more risk to principal and income than higher rated securities.

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