

Global High Yield

Available in: IMA, SMA, UCITS fund^(*)

AUGUST 2025

Market review

The high yield market posted a strong return in August, marking its fourth consecutive monthly gain. The month opened with a weaker-than-anticipated United States jobs report, causing markets to price in an additional rate cut this year and lifting 2025's expected total number of cuts to above two between the Federal Reserve's (Fed) final three policy meetings of the year. Dovish messaging from the Fed at the Jackson Hole symposium, and throughout the month, further solidified expectations for a cut in September, which would be the first since November 2024. The high yield rally was further supported by a stronger-than-expected earnings season and sustained fund inflows. Treasuries, particularly at the front end, rallied sharply on the softer labor market outlook on August 1st. Subsequently, short-term Treasury yields fell further as the month progressed, intermediate yields ended mostly unchanged, and long-end yields finished August higher. High yield spreads initially rose to their widest level since late June in tandem with the Treasury rally, before tightening modestly by month-end. Yields trended lower during August and ultimately reached their lowest level since April 2022 on the back of lower rates and a dovish Fed outlook.

The high yield market posted its fourth straight month of lower-quality outperformance. CCCs outpaced BBs and Bs by roughly 60 and 75 basis points, respectively, and now hold the top spot as the best-performing quality in 2025. BBs follow, outperforming the overall index, while Bs still lag the index year-to-date.

All but two industries posted gains in August. Pharmaceuticals led with a strong return, extending its position as this year's top-performing industry. Oil field services and building materials followed with solid returns. In contrast, packaging was the underperformer in August after posting a modest decline, while wireless followed with a slightly negative return after having solid performance in July.

The primary market continued to defy its typically slower seasonal trend in August before activity eased in the second half of the month. According to J.P. Morgan, issuance, largely front loaded during the month, totaled \$25.7 billion, with notably only 62% used for refinancings. Year-to-date supply reached \$208.7 billion, surpassing the same period in 2024 by more than \$5 billion, after trailing last year's pace over the first half of 2025.

Moody's reported a decline in corporate defaults, with eight last month versus a revised eleven previously. The trailing twelve-month global high yield default rate edged up slightly to 4.5%. Assuming a gradual easing in monetary policy over the next year, Moody's kept its year-end default forecast at 3.6% and lowered its twelve-month projection to 2.6%.

High yield funds recorded their fourth straight month of inflows, drawing +\$1.1 billion in August, according to J.P. Morgan. Strong demand over the past four months has brought year-to-date net flows to +\$13.2 billion, compared to an inflow of +\$16.3 billion for all of 2024.

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Strategy review

The majority of the underperformance on a gross basis was driven by negative security selection and the remainder attributable to sector allocation. Negative security selection came from overweight positions in Kronos Acquisition Holdings Inc, LABL Inc, Vibrantz Technologies Inc, Sigma Holdco BV, and LCPR Senior Secured Financing, and was partially offset by positive contributions from overweight positions in Park River Holdings Inc, B&G Foods Inc, and ZipRecruiter Inc, as well as zero exposure in Ardagh Packaging Finance PLC and Kelopatra Finco Sarl. Sector allocation modestly detracted from performance on a gross basis, with an underweight allocation to the energy sector and overweight allocation to the leisure sector contributing to most to the drag. Partially offsetting this was a positive impact from an underweight allocation to the utility sector. By quality, nearly all of the underperformance came from negative security selection within B-rated and CCC-rated credits, partially offset by positive security selection within BB-rated and BBB-rated credits. Cash was a slight drag on performance during the period..

Strategy and outlook

The Fed is currently facing a softening labor market, rising unemployment, and weak job growth, while inflation remains above their 2% target due to recent tariff effects that are slowly beginning to materialize in some prices. However, due to labor market concerns, markets fully expect a cut at the September policy meeting and at least one more by year-end. Economic growth indicators are mixed, with consumer spending holding up but showing some signs of softness. Political pressures and new dovish members potentially joining the Federal Open Market Committee could alter future policy decisions. Upcoming labor and inflation data will shape a cautious rate-cutting approach over the remainder of 2025, as the Fed weighs risks from tariffs and broader economic uncertainty.

High yield fundamentals remain healthy, with leverage at just under 4.1 times and interest coverage at 4.7 times. Both credit metrics are better than their long-term

averages, according to J.P. Morgan. The second quarter earnings season delivered impressive results, with nearly three times as many high yield companies beating earnings expectations than missing. Positive forward guidance also outpaced negative guidance by almost two-to-one. With virtually no 2025 maturities left and only a minimal amount due in 2026, focus will soon shift to 2027 as the forthcoming maturities to address. The majority of outstanding debt has been extended to at least 2029, and year-end default rates are projected to decline below historical averages.

The technical backdrop for high yield remains constructive, underpinned by steady fund inflows, an active primary market, and limited net supply, all of which continue to support robust demand for the asset class. On the valuation front, spreads have tightened further and sit well below their one-year average, while yields closed the month at their lowest level since April 2022 as front-end rates fell meaningfully lower. Although valuations are less compelling, high yield continues to offer a relatively attractive investment opportunity over other fixed income sectors, many of which ended August at historically tight valuation levels.

Strategically, we aim to maintain a flexible portfolio positioning, recognizing that markets have priced in a rate cut in September and at least one more by year-end amid a softening U.S. labor market. We continue to prioritize preserving dry powder given the active primary market and supportive technical environment, while also favoring higher quality issuers. With valuations tight and spreads below their one-year average, we anticipate a mostly rangebound environment in the near-term, though spreads could face widening pressure if tariff effects start showing up in price growth, which may keep inflation above the Fed's target. Overall, our focus remains on disciplined credit selection to drive outperformance.

In terms of sector positioning, we look to maintain overweight positions in the leisure, health care, and services sectors, while maintaining underweight positions in the energy, utility, and banking sectors.

Risk consideration

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