

# Penn Capital Credit Month in Review

## Executive Summary

High yield (HY) bond returns narrowly outpaced returns for leveraged loans in April, snapping a six-month streak of loan outperformance. Bond performance was even stronger earlier in the month but a rallying 10 yr US Treasury rate and cost inflation fears tempered returns.

## Bonds

The HY bond asset class returned +0.54% in April as yields and spreads decreased 1 bp and 23 bp, respectively, to 6.54% and +387 bp. Returns were even stronger the first half of the month as yields/spreads touched 6.27%/+368 bp, but the rally faded during the last two weeks of April as US 10 yr Treasury yields climbed. Telecom (+2.65%), Retail (+1.87%), and Energy (+1.29%) were the best performing industries during the month while Automotive and Consumer Products were the largest underperformers, returning -1.83% and -0.29%, respectively. By rating, CCCs (+0.92%) were the top performers in April, beating the +0.87% and +0.13% returns posted by B-rated and BB-rated bonds during the month. Year-to-date (YTD), Telecom (+2.23%) is now the best performing industry while Automotive (-3.94%) remains the worst. CCC-rated bonds remain top performers YTD with +1.66% returns so far. This beats returns offered by B-rated (+0.73%) and BB-rated (-1.58%) bonds. Gross new issue activity totaled \$21b in April, down from March's ~\$28b but less skewed toward refinancing transactions. Refinancing transactions only accounted for 46% of April's issuance volume (~\$9bn) vs the 74% they represented throughout 1Q. YTD, gross HY new issue volume reached ~\$94b; this volume level is significantly below the gross issuance of ~\$118b we saw by this point last year. Including distressed exchanges, the US HY bond default rate increased 3 bp to 2.39%.

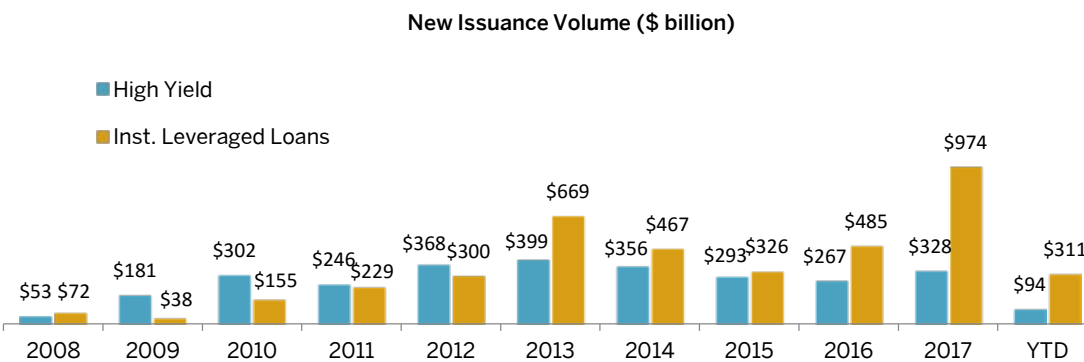
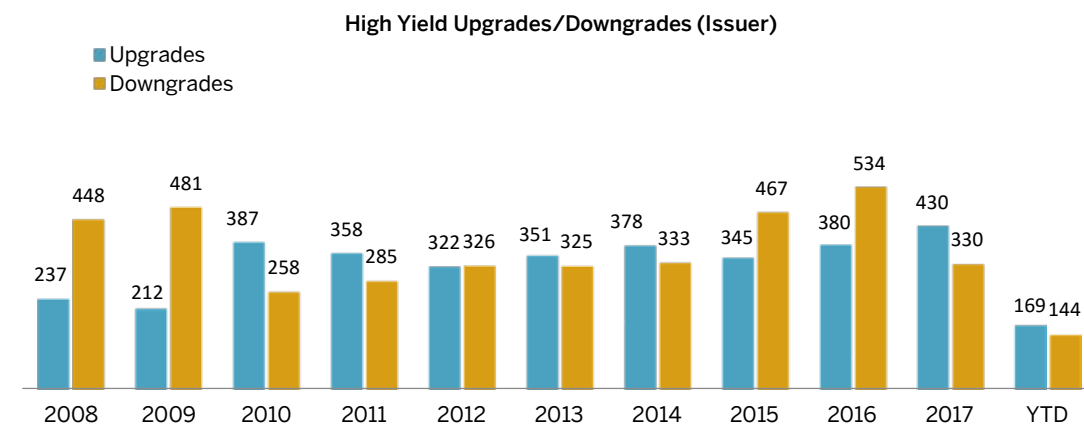
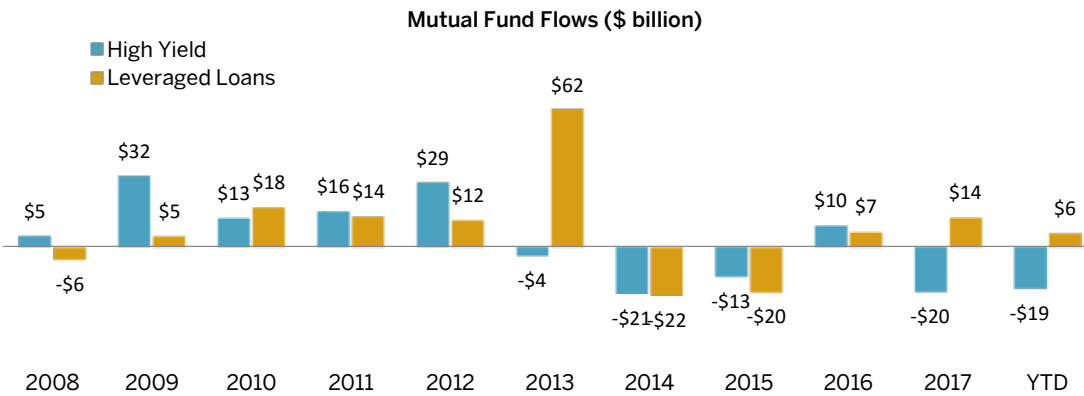
## Loans

Leveraged loans returned +0.44% in April, reversing the recent six-month trend of loan returns outpacing the returns of HY bonds. Metals & Mining (+1.17%) and Energy (+0.67%) were the best performing industries for the month while Automotive and Retail were the largest laggards returning -0.12% and +0.05%, respectively. During the month, B-rated loan returns of +0.48% bested the returns offered by BB-rated (+0.44) and CCC-rated (+0.16%) loans. Energy (+3.92%) is the best performing industry YTD while Media remains the worst performer through April with returns of +1.12%. CCC-rated loans (+4.66%) remain the top performers YTD as B-rated and BB-rated loans returned a lesser +2.08% and +1.67%, respectively. New issue activity totaled ~\$69b in April, -37% month-over-month and -21% year-over-year. Most of this volume, ~\$53b (or ~77%), continues to be related to refinancings/repricings. YTD, repricings and refinancings remain a significant ~70% of total new institutional loan volume, down modestly from the ~73% they represented in 2017. Gross US collateralized loan obligations (CLO) volume of \$30b in April was the fourth highest monthly total on record. This brings YTD US CLO volumes to ~\$92b. Of that total, ~\$40b or 43% of US CLO volume was used for refinancing/reset deals. The US leveraged loan default rate ended April down 17 bp to 2.35%.

Source: JP Morgan

As of April 30, 2018	Performance			Characteristics			
	Month	YTD	Spread	YTD Change	Average Price	YTW	YTM
10-Year Treasury	-1.40%	-3.76%	---	---	---	3.0%	3.0%
Bloomberg Barclays US Aggregate Bond Index	-0.74%	-2.19%	50 bp	1 bp	\$99.77	3.3%	3.3%
JP Morgan BB/B Loan Index	0.49%	1.74%	322 bp	-12 bp	\$99.88	6.1%	---
ICE BofA Merrill Lynch 1-3 Year BB-B Rated US Cash Pay High Yield Index	0.53%	0.95%	222 bp	3 bp	\$102.14	4.6%	5.0%
ICE BofA Merrill Lynch BB-B Rated Non-Distressed High Yield Index	0.53%	-0.66%	294 bp	10 bp	\$100.09	5.7%	5.9%
ICE BofA Merrill Lynch BB-B Rated US High Yield Constrained Index	0.55%	-0.57%	305 bp	8 bp	\$99.69	5.8%	6.0%
ICE BofA Merrill Lynch US High Yield Constrained Index	0.67%	-0.25%	357 bp	-16 bp	\$98.69	6.3%	6.5%

Sources: Barclays, BofA Merrill Lynch, JP Morgan. Past performance is no guarantee of future results.



Source for Charts: JP Morgan

### Specialists in capital structure investing

At Penn Capital, we believe that understanding a company's entire capital structure is the best way to identify investment opportunities with the most value. In fact, we've found that managing credit portfolios makes us better equity managers, and vice versa. Employing a fully integrated credit and equity research process, we focus on non-investment grade companies in the micro to mid-capitalization range, where we can take advantage of inefficient security pricing. We are an independent, employee-owned boutique investment management firm based in Philadelphia. We forge our own ideas, we respect hard work, and we are committed to our clients, our staff and our community.

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Historical Spreads / Default Rates	2009	2010	2011	2012	2013	2014	2015	2016	2017	YTD
ICE BofA Merrill Lynch US BB-B Rated High Yield Index	521 bp	485 bp	612 bp	443 bp	344 bp	434 bp	558 bp	348 bp	297 bp	305 bp
ICE BofA Merrill Lynch US BB Rated High Yield Index	445 bp	399 bp	503 bp	357 bp	281 bp	336 bp	427 bp	286 bp	228 bp	238 bp
ICE BofA Merrill Lynch US B Rated High Yield Index	613 bp	573 bp	736 bp	524 bp	417 bp	549 bp	722 bp	432 bp	381 bp	378 bp
ICE BofA Merrill Lynch US CCC Rated High Yield Index	980 bp	874 bp	1,262 bp	943 bp	766 bp	976 bp	1,648 bp	977 bp	843 bp	733 bp
J.P. Morgan's 12-Month Default Rate	10.3%	0.8%	1.7%	1.3%	0.7%	2.9%	1.8%	3.6%	1.3%	2.3%

Sources: BofA Merrill Lynch. J.P. Morgan. Past performance is no guarantee of future results.

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