Flash update

Reaching the end of the hiking cycle: Time to consider high yield again

3-minute read

Marketing communication

For Professional Investors in Switzerland or Professional Investors as defined by the relevant laws The classification of the funds as per the Sustainable Finance Disclosure Regulation (SFDR) is 8

In a nutshell (Data as of 31.10.2023 unless otherwise stated.)

- *Significant communication shift from central banks lately, indicating that we have passed peak hawkishness. Central bankers hinted that they may be **done with rate hikes***
- *Technical set-up for fixed income and valuations are currently very favourable with large cash volumes waiting to be put to work. **Yields at 11.3%*** are above both equity and high yield annualised returns since 1998*
- *UBP's global high yield strategy is an attractive way to take advantage of this backdrop before year-end, with a **track record of outperformance** and liquidity*

* UBAM - Global High Yield Solution ($)

Dear all,

A significant communication shift from central banks suggests we have passed peak hawkishness and potentially peak rates. The discussion is moving away from how many more hikes are needed, towards how long policy should stay restrictive for. This was clearly observed at the Fed meeting this week. Fed Chair Powell said that:

"given how far we have come, […], the Committee is proceeding carefully"

Most importantly on inflation – Powell said that they had seen *"pretty significant progress"* and that

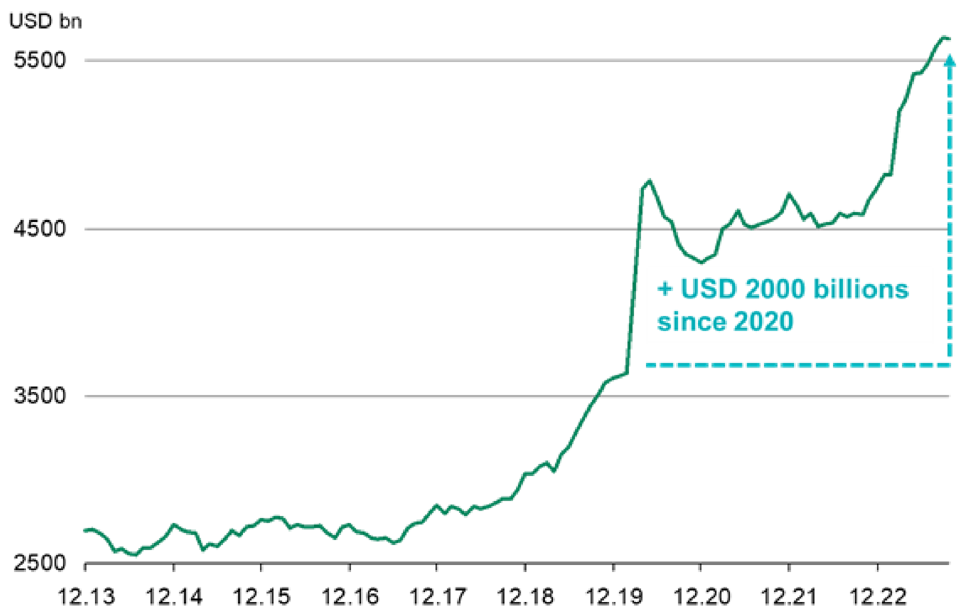
[wage inflation has] "come down significantly", "I feel good about that".

The statement also mentioned for the first time the tightening in financial conditions which Powell and several Fed members have recently said that if persistent, could replace the need for any further rate hikes.

The ECB shift in communication has been even clearer. One of the most hawkish members of the board, Klaas Knot, said this week that current policy is at a *"good cruising altitude"*. This week's inflation release surprised to the downside, with headline CPI breaking through 3%, at 2.9% YoY for the first time since mid-2021, which is very encouraging from the ECB's perspective.

The technical set-up for fixed income is currently very favourable. Positioning is clean. Over the past few years we have seen a surge of flows into cash like products such as money market funds and out of fixed income given elevated uncertainty with regards to the central banking outlook, as shown in Figure 1 below. As this uncertainty fades and investors gain confidence that peak hawkishness is in, we expect for these flows to reverse out of cash and into fixed income products.

Figure 1. Assets in US money market funds since the pandemic increased USD +2000 Bn



Source(s): UBP, Bloomberg Finance L.P. As of 31.10.2023. ICI Money Market Funds Assets (ticker: MMFA).

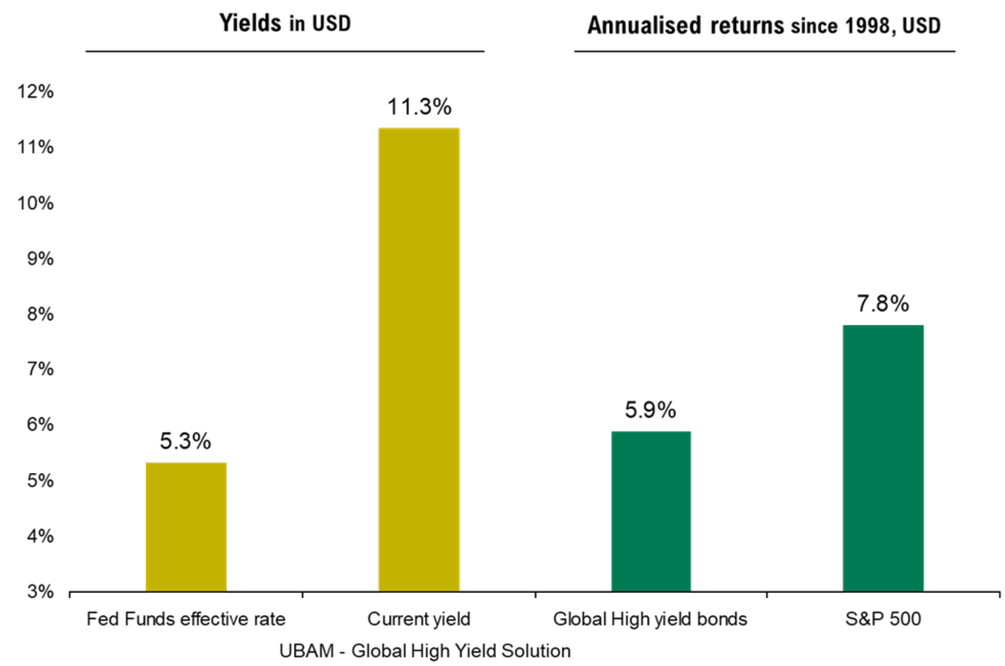
Past performance is not a guide for current or future results

Supportive flows could drive a year-end rally. Whilst many investors will likely wait for the beginning of next year to allocate, there could be a first mover advantage for those that allocate before year-end. Given the central banking communication shift described above, as well as the current disinflation trend, we anticipate that the shift in flows could start sooner rather than later and provide support for the asset class into year-end.

Valuations. The market is currently pricing the Fed to cut rates to a trough of 4% over the next five years. This indicates that a lot of hawkishness is in the price given the Fed's neutral rate estimate of just 2.5%. Valuations within High Yield are also attractive where all-in yields of around 11% means that one is being well compensated for taking high yield risk, where the power of accrual is significant at such elevated yields.

Current yield levels for UBP's global high yield strategy means i) there is a 6% yield pick-up over cash deposit rates, ii) yields are above past returns for global high yield markets and iii) yields are above past returns for equities (since 1998).

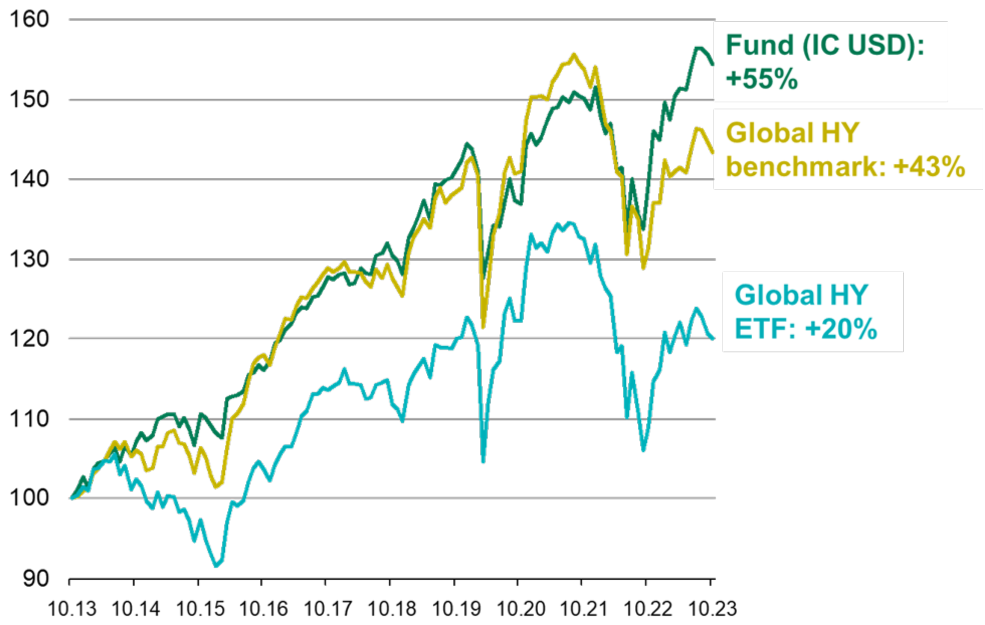
Figure 2. Current yield of UBAM - Global High Yield Solution: yield pickup of 6% vs. cash deposit and above past return for equities and high yield



Source(s): UBP, Bloomberg Finance L.P. As of 31.10.2023 and since 31.12.1997. Global high yield represented by ICE BofA Global High Yield Index hedged USD (HW00). Past performance is not a guide for current or future results.

UBP's global high yield flagship strategy is outperforming. UBP's Global & Absolute Return Fixed Income team has been managing since 2010 a best-in-class global high yield strategy outperforming peers, ETF and high yield benchmarks, as illustrated in Figure 3 below.

Figure 3. UBAM - Global High Yield Solution (IC USD) is outperforming – over 10 years



Source(s): UBP, Bloomberg Finance L.P. As of 31.10.2023 since 31.10.2013. Fund: UBAM - Global High Yield Solution, IC USD (net of fees). Global HY benchmark represented by The Bloomberg Global High Yield Index hedged USD (LG30TRUH). Global HY ETF represented by iShares Global High Yield Corp Bond (ticker: HYLD). Past performance is not a guide for current or future results.

Finally, according to Bloomberg Finance L.P., UBAM - Global High Yield Solution is outperforming 93% of peers over 3 years and 92% of peers over 5 years.

The strategy is available via two sub-funds:

UBAM - Global High Yield Solution: ▪ Size: USD 3.7 bn ▪ Yield in USD: 11.3% ▪ Interest rate duration: 1.7 years	UBAM - Global High Yield Solution Extended Duration: ▪ Size: USD 516 mio ▪ Yield in USD: 10.9% ▪ Interest rate duration: 4.0 years

Best regards

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