PPMAMERICA

US High Yield

KEY TAKEAWAY

> A risk-off quarter in high yield provided an opportunity to selectively add credit risk while avoiding stressed parts of the market

High yield saw a risk off quarter (-1.82%), driven by a September decline of -2.49%, the worst monthly return since September 2022.[1] Yields increased 115 bps in Q3 2026 to end at 8.30%, above the symbolic 8% threshold. Treasuries did most of the work, as the 10-year yield rose 85 bps as higher energy prices buffeted inflation fears alongside a more hawkish Fed.[2] High yield spreads also widened 31 bps during the quarter with heavy supply and the higher Treasury rates stoking negative sentiment. Single B and BB bonds returned similar levels around the index return with CCCs lagging (-3.57%) due to distressed returns of -8.23%, continuing the year-long trend of declines in this small but influential part of the market.

Technicals deteriorated in September.[3] Net issuance totaled a record of $36B last month ($283B YTD, $130B ex. refinancings) and included both the fourth- and fifth-largest individual transactions on record. High yield experienced a monthly outflow during September ($5B), which followed $12B of inflows over the prior five months.

Fundamentals remained supportive in Q3 2026.[4] The high yield distress ratio increased 91 bps over the quarter to 5.37%. The default rate ended at 2.95%, stable over the quarter and low by historical standards.[5] Additionally, upgrades exceeded downgrades (+$3B) for the fourth consecutive quarter

With risk-off sentiment and yields exceeding 8%, the strategy increased overall risk in September after reducing risk in July and August, leaving positioning close to unchanged over Q3 2026. We added core credits in the 200-400 bps spread bucket and reduced the 500-700 bps spread bucket, remaining overweight the former and underweight both the 100-200 bps spread bucket and distressed credit.

We view the high yield market as trading in a few buckets: AI, Software, distressed and "everything else." We targeted our risk additions in the "everything else" bucket. Within sectors, the strategy added to Capital Goods, Services and Energy and reduced Technology, Automotive and Financial



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Head of Leveraged Credit

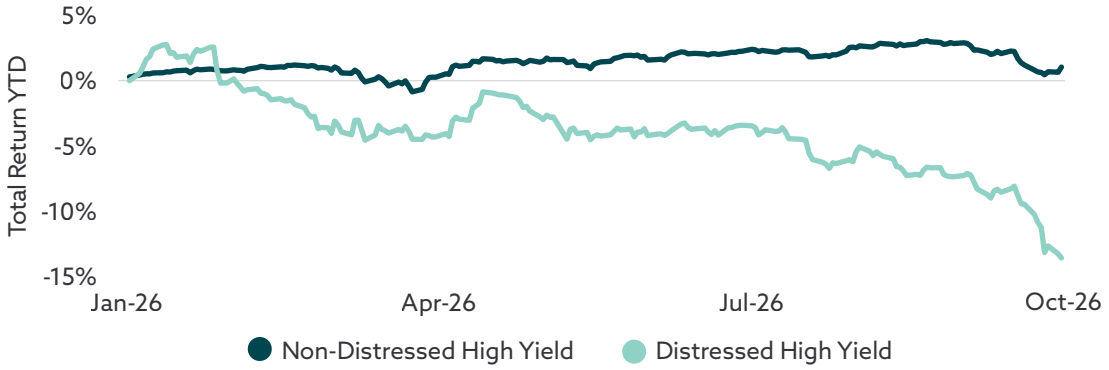


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DISTRESSED CREDIT RETURNS DETERIORATED FURTHER IN SEPTEMBER[1]



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Services. As an example, we established two new 50-bp core positions in the Packaging sub-sector of Capital Goods, one name through a new issue and the other in the secondary market. For these names, we observed improving underlying trends and attractive valuations.

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The **ICE BofA US High Yield Constrained Index** provides a measure of below investment grade bonds, is constructed based on the ICE BofA US High Yield Index and imposes a 2% issuer cap.

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