JUNE 2023

REPLACING EQUITIES WITH HIGH YIELD

THE ERA OF ULTRA-LOW RATES AND AN IMPLICIT "FED PUT" HAS POTENTIALLY COME TO A CLOSE, MAKING THE RELATIVE CERTAINTY OF CONTRACTUAL FIXED INCOME (INCLUDING HIGH YIELD) INCREASINGLY COMPELLING WITHIN A GROWTH ALLOCATION.

SUMMARY

- High yield returns have matched equities this century
- Default rates are lower than you may think
- Investors can achieve exceptional liquidity in high yield, essentially earning a "free" illiquidity premium

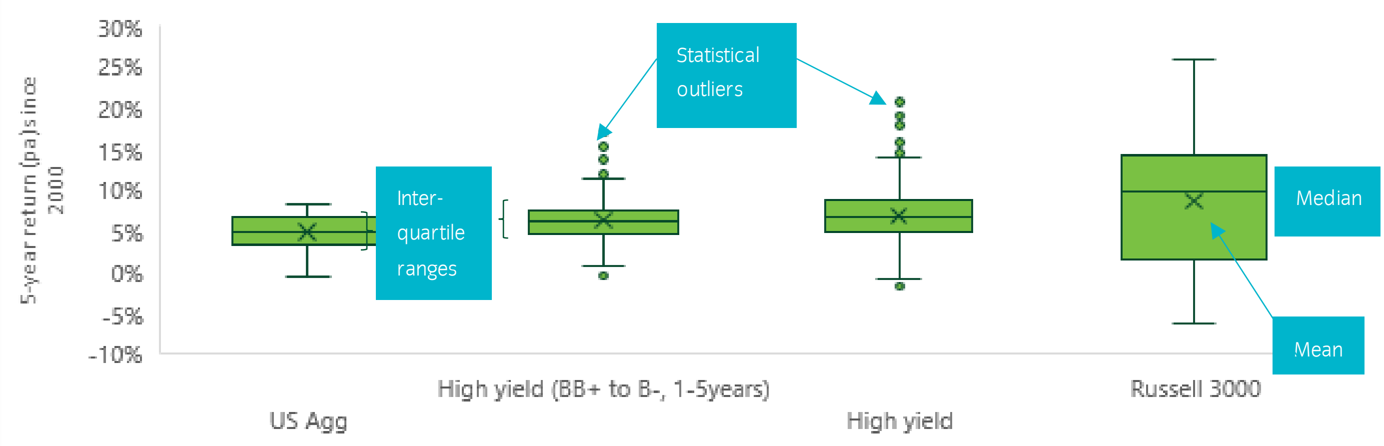
A POTENTIALLY LOWER RISK GROWTH BUCKET, WITHOUT SACRIFICING EXPECTED RETURNS

With the "Fed put" now in the rear-view mirror, we have seen asset allocators shift long-term equity return expectations down to a 6% to 8% pa range, similar to high yield (which currently yields 8% to 9%)[1].

This is more consistent with history. It may surprise you that this century (i.e. since 2000), equities have returned 6.7% pa, and high yield has returned a very close 6.2% pa. Despite this, high yield has been far less volatile, with a 9% annualized standard deviation, versus equities at 16%[2].

The dispersion of outcomes (a better measure of risk in our view) has been narrower for high yield. This is even more pronounced when limiting the high yield universe to bonds rated B- or higher with maturities of less than five years (Figure 1).

Figure 1: Over 5-year investment horizons, high yield has delivered near-equity returns with lower dispersion[3]



[1] Bloomberg, June 2023

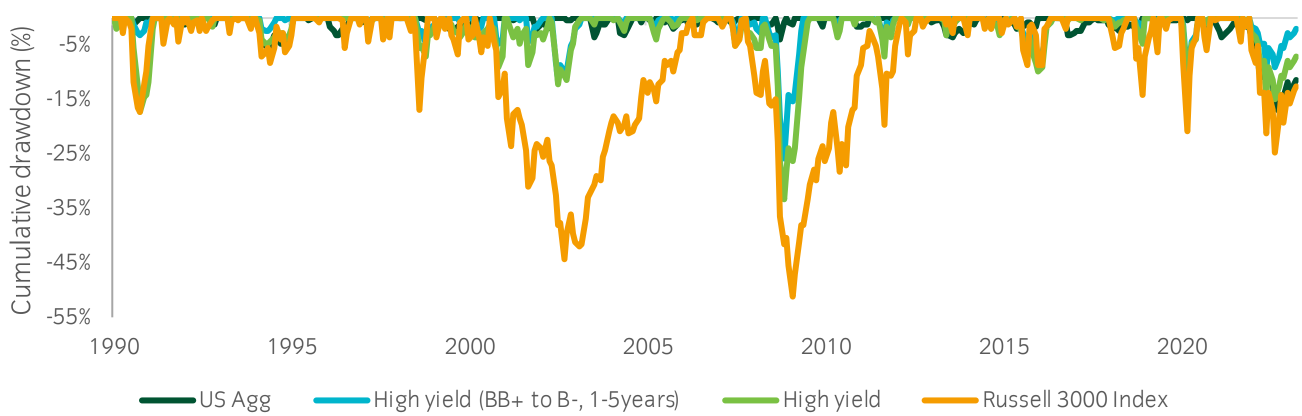
[2] Bloomberg, May 2023. Russell 3000 index, Bloomberg US Corporate High Yield Index. Please see index descriptions at the back of the document. Based on monthly returns. The "whiskers" extend 1.5x the interquartile range either side of the box.

[3] Bloomberg, Insight calculations, March 2023. **Past performance is not indicative of future results. Investment in any strategy involves a risk of loss which may partly be due to exchange rate fluctuations.**

The (maximum-minimum) range for equity was ~30%, about twice the HY range of ~15%. The Inter-Quartile-Range (IQR) of equity is more than three times as large as that of high yield.

Historically, high yield has also tended to benefit from more benign drawdowns during risk market sell-offs (Figure 2). This is partly because high yield bonds are senior to equity in the capital structure and generally have defined maturity structures, resulting in the "pull-to-par" effect: a maturing bond not in default will return principal. In equities there is no such guarantee, which can result in depressed valuations for extended periods.

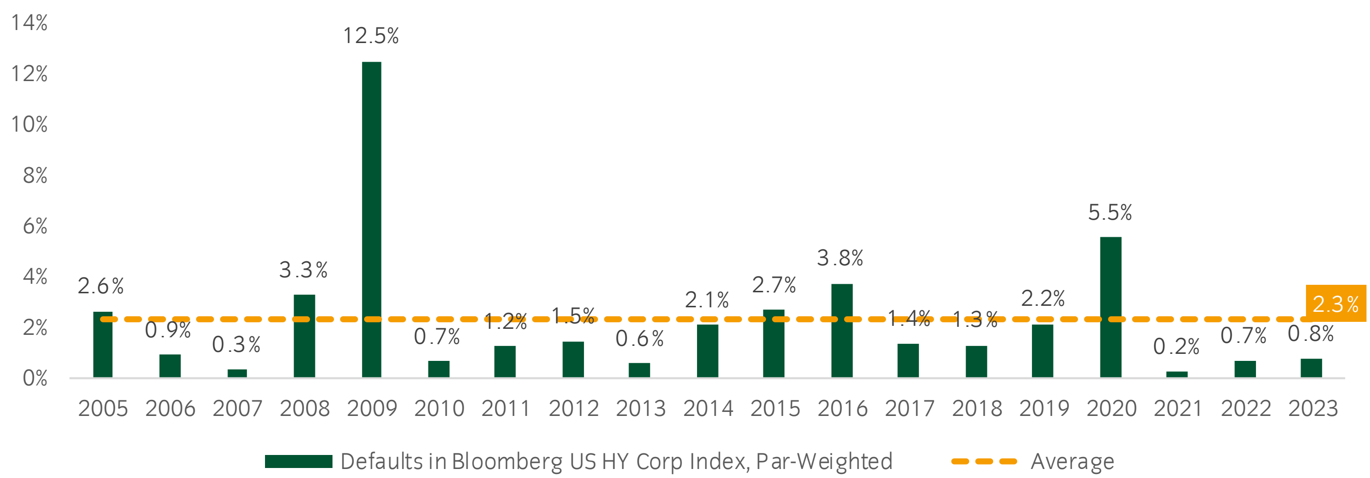
Figure 2: High yield has historically recovered faster from drawdowns[4]



HIGH YIELD DEFAULT RATES HAVE BEEN LOWER THAN YOU MAY THINK

Defaults are the main risk for high yield investors, as they threaten permanent losses of capital. However, consensus default predictions consistently exceed realized defaults in high yield indices. Ratings agency default expectations are typically in the range of 3% to 5% pa. But broad high yield index defaults since 2004 have averaged ~2.3% pa on a par-weighted[5] basis (Figure 3). This is because Moody's and S&P default metrics cover all speculative grade investments they provide ratings for. But these universes are wider ranging than what is included in the most indices, and thus unrepresentative of most institutional high yield portfolios.

Figure 3: High yield defaults in broad high yield indices have been contained[6]



[4] Bloomberg, Insight calculations, March 2023, Russell 3000 index, Bloomberg US Corporate High Yield Index and Bloomberg BB+ to B- US Corporate High Yield Index. **Past performance is not indicative of future results. Investment in any strategy involves a risk of loss which may partly be due to exchange rate fluctuations.**

[5] We believe calculating defaults in par ($100) terms provides the most conservative metric, as bonds may already trade at deep discounts when they default.

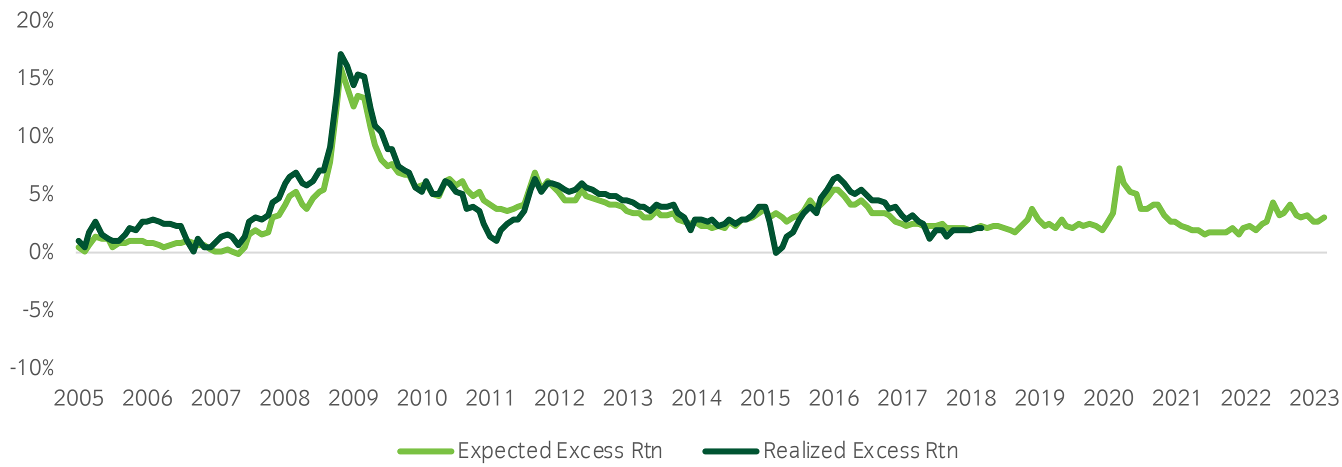
[6] Bloomberg, Insight calculations, March 2023

Further, recovery rates are often forgotten. ***Loss-given-default*** (LGD) is a more important metric than default. High yield recovery rates have been ~45% on average, resulting in a realized average LGD of ~1.5%[7].

When adjusting for average LGD, historically we have seen strong predictive power from initial option-adjusted spreads (OAS) and realized returns, indicative of the contractual nature of bond market returns.

This is demonstrable using the definition *Expected Excess Return = Starting OAS–Expected LGD* (Figure 4).

Figure 4: Adjusting for LGD, spreads have strongly predicted returns[8]



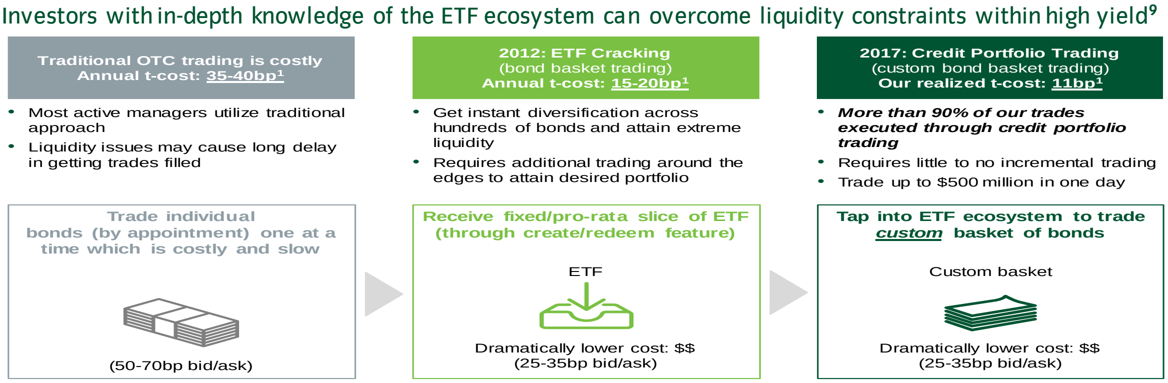
A "FREE" LIQUIDITY PREMIUM

The high yield market is infamous for its poor liquidity. This is certainly true when trading bonds over-the-counter (which is how almost all managers operate – Figure 5). The high transaction costs incorporating the additional illiquidity premium is a key factor behind the median high yield fund underperforming the broad index by ~50bp pa, net of fees.

However, innovations in portfolio construction and implementation technology that leverage the ETF infrastructure can allow investors to trade large, customized baskets of high yield bonds seamlessly to build a diversified and highly liquid high yield portfolio. We recognized this hidden pool of liquidity early on in 2012 and catered our investment process to benefit from this trend.

For years, we worked side-by-side with the sell-side community to improve their understanding as well to grow the "credit portfolio trading" market overall. As long as there is a vibrant ETF ecosystem, we are able to tap into this source of liquidity at a fraction of prevailing market bid/ask spreads.

Figure 5: Investors with in-depth knowledge of the ETF ecosystem can overcome liquidity constraints within high yield[9]



---

[7] Moody's, December 2023

[8] Bloomberg, Insight calculations. Using long-term average 1.5% for expected LGD after March 2023.

[9] For illustrative purposes only. Process presented represents that of predecessor firm Mellon Investments Corporation. Hypothetical trade example: actual trading may reflect prices from banks, bids and offers that are materially different than what is shown herein.

Importantly, investors that are able to leverage these innovations can essentially earn the asset class's illiquidity premium for free.

IT COULD BE TIME TO CONSIDER PIVOTING YOUR GROWTH BUCKET TO HIGH YIELD

During the quantitative easing era, equity allocations were well rewarded. However, in a post-QE world of normalized rates and the disappearance of the Fed put, the equity market is becoming a wilder ride. TINA (there is no alternative to equities) is dead.

We believe high yield – which for the first time in years lives up to its name with a current yield of ~8-9% – can play a particularly useful role in a pension plan's portfolio. It can help grow the portfolio, add a measure of duration exposure and provide sizable and predictable cash flows to help meet obligations as they fall due.

FIND OUT MORE

Insight Investment
200 Park Avenue, 7th Floor
New York, NY 10166
212-527-1800

inquiries@insightinvestment.com
company/insight-investment-north-america
@InsightInvestUS
www.insightinvestment.com

IMPORTANT INFORMATION

IMPORTANT DISCLOSURES

Each account is individually managed, and could differ from what is presented herein. The quoted benchmark does not reflect deductions for fees, expenses or taxes. The benchmark is unmanaged and does not reflect actual trading. There could be material factors relevant to any such comparison such as differences in the volatility, and regulatory and legal restrictions between the index shown and the strategy. Investors cannot invest directly in any index. [1]Represents typical range and subject to change. Insight makes no assurances that the bp represented on this slide will be within the range. Actual bp could be higher or lower than what is shown.

Past performance is not a guide to future performance, which will vary. The value of investments and any income from them will fluctuate and is not guaranteed (this may partly be due to exchange rate changes). Future returns are not guaranteed and a loss of principal may occur.

Targeted returns intend to demonstrate that the strategy is managed in such a manner as to seek to achieve the target return over a normal market cycle based on what Insight has observed in the market, generally, over the course of an investment cycle. In no circumstances should the targeted returns be regarded as a representation, warranty or prediction that the specific deal will reflect any particular performance or that it will achieve or is likely to achieve any particular result or that investors will be able to avoid losses, including total losses of their investment.

The information shown is derived from a representative account deemed to appropriately represent the management styles herein. Each investor's portfolio is individually managed and may vary from the information shown. The mention of a specific security is not a recommendation to buy or sell such security. The specific securities identified are not representative of all the securities purchased, sold or recommended for advisory clients. It should not be assumed that an investment in the securities identified will be profitable. Actual holdings will vary for each client and there is no guarantee that a particular client's account will hold any or all of the securities listed.

The quoted benchmarks within this document do not reflect deductions for fees, expenses or taxes. These benchmarks are unmanaged and cannot be purchased directly by investors. Benchmark performance is shown for illustrative purposes only and does not predict or depict the performance of any investment. There may be material factors relevant to any such comparison such as differences in volatility, and regulatory and legal restrictions between the indices shown and the strategy.

Transactions in foreign securities may be executed and settled in local markets. Performance comparisons will be affected by changes in interest rates. Investment returns fluctuate due to changes in market conditions. Investment involves risk, including the possible loss of principal. No assurance can be given that the performance objectives of a given strategy will be achieved.

Insight does not provide tax or legal advice to its clients and all investors are strongly urged to consult their tax and legal advisors regarding any potential strategy or investment.

Information herein may contain, include or is based upon forward-looking statements within the meaning of the federal securities laws, specifically Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements include all statements, other than statements of historical fact, that address future activities, events or developments, including without limitation, business or investment strategy or measures to implement strategy, competitive strengths, goals expansion and growth of our business, plans, prospects and references to future or success. You can identify these statements by the fact that they do not relate strictly to historical or current facts. Words such as 'anticipate', 'estimate', 'expect', 'project', 'intend', 'plan', 'believe', and other similar words are intended to identify these forward-looking statements. Forward-looking statements can be affected by inaccurate assumptions or by known or unknown risks and uncertainties. Many such factors will be important in determining our actual future results or outcomes. Consequently, no forward-looking statement can be guaranteed. Our actual results or outcomes may vary materially. Given these uncertainties, you should not place undue reliance on these forward-looking statements.

Insight and BNY Mellon Securities Corporation are subsidiaries of BNY Mellon. BNYMSC is a registered broker and FINRA member. BNY Mellon is the corporate brand of the Bank of New York Mellon Corporation and may also be used as a generic term to reference the Corporation as a whole or its various subsidiaries generally. Products and services may be provided under various brand names and in various countries by subsidiaries, affiliates and joint ventures of the Bank of New York Mellon Corporation where authorized and regulated as required within each jurisdiction. Unless you are notified to the contrary, the products and services mentioned are not insured by the FDIC (or by any government entity) and are not guaranteed by or obligations of the Bank of New York Mellon Corporation or any of its affiliates. The Bank of New York Mellon Corporation assumes no responsibility for the accuracy or completeness of the above data and disclaims all expressed or implied warranties in connection there with. Personnel of certain of our BNY Mellon affiliates may act as: (i) registered representatives of BNY Mellon Securities Corporation (in its capacity as a registered broker-dealer) to offer securities, (ii) officers of the Bank of New York Mellon (a New York chartered bank) to offer bank-maintained collective investment funds and (iii) associated persons of BNY Mellon Securities Corporation (in its capacity as a registered investment adviser) to offer separately managed accounts managed by BNY Mellon Investment Management firms.

Disclaimer for Non-US Clients: Prospective clients should inform themselves as to the legal requirements and tax consequences within the countries of their citizenship, residence, domicile and place of business with respect to the purchase and ongoing provision of advisory services. No regulator or government authority has reviewed this document or the merits of the products and services referenced herein.

This document is directed and intended for 'institutional investors' (as such term is defined in various jurisdictions). By accepting this document, you agree (a) to keep all information contained herein (the 'Information') confidential, (b) not use the Information for any purpose other than to evaluate a potential investment in any product described herein, and (c) not to distribute the Information to any person other than persons within your organization or to your client that has engaged you to evaluate an investment in such product.

Telephone conversations may be recorded in accordance with applicable laws.

INDEX DEFINITIONS

Information about the indices shown here is provided to allow for comparison of the performance of the strategy to that of certain well-known and widely recognized indices. There is no representation that such index is an appropriate benchmark for such comparison.

You cannot invest directly in an index and the indices represented do not take into account trading commissions and/or other brokerage or custodial costs. The volatility of the indices may be materially different from that of the strategy. In addition, the strategy's holdings may differ substantially from the securities that comprise the indices shown.

The Russell 3000 index is composed of 3000 large U.S. companies, as determined by market capitalization. This portfolio of Securities represents approximately 98% of the investable U.S. equity market. The Russell 3000 Index is comprised of stocks within the Russell 1000 and the Russell 2000 Indices. The index was developed with a base value of 140.00 as of December 31, 1986.

The Bloomberg US Corporate High Yield Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on Bloomberg EM country definition, are excluded

The Bloomberg BB+ to B- US Corporate High Yield Index measures the USD-denominated, high yield, fixed-rate corporate bond market with a rating between Moody's, Fitch and S&P is Ba1/BB+/BB+ and B3/B-/B-. Bonds from issuers with an emerging markets country of risk, based on Bloomberg EM country definition, are excluded