



T.RowePrice

Global High Yield Diversified source of income and growth

June 2025

Why High Yield Bonds?

While we would always state the long-term case for a strategic portfolio allocation to high yield, the decision by the Australian Prudential Regulation Authority (APRA) to phase out hybrid securities has certainly brought the asset class to the forefront of many adviser's minds.

Global high yield provides investors with some of the key benefits of hybrids like regular income and diversification and less of the potential issues regarding liquidity or equity market exposure. Both investments come with risks, including credit risks and market risks.

With this in mind, advisers will need to navigate individual investors goals and risk profiles before making an investment decision.

The paper highlights the strategic case for high yield bonds.

Familiar companies

Firstly, it is important to recognise that some of the world's most iconic brands

are issuers of high yield bonds. These companies span various industries and regions globally, offering investors the opportunity to invest in familiar and reputable names.

Investing in high yield bonds allows investors to participate in the financial journeys well-known companies such as Hilton (Hotels and Resorts), Land Rover (Luxury Automobiles), Goodyear (Tire and Rubber Manufacturing), KFC (Renowned for Fried Chicken), and Samsonite (Luggage and Travel Bags)¹.

The dynamic nature of the high yield market ensures a continuous influx of quality companies entering and exiting the asset class, such as Netflix (subscription streaming service), Ford Motor (American automobile manufacturer), Tesla (automotive and clean energy company) who all in recent years have all moved into the global investment grade index), providing investors with diverse opportunities to enhance their portfolios.



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¹ As at 31 March 2025. High yield issuers example in the ICE BofA Global High Yield Index.

Durable returns over time

High yield bonds have broadly performed favorably across different market cycles. Since 1980, the high yield market has only experienced seven calendar years of negative returns. Perhaps even more impressive is that there have never been two consecutive years of negative returns in the asset class covering 40 years (Fig. 1). Following years of negative returns, the asset class usually experiences years of either outsized gains or several years of modest returns. This resilient return pattern is simply due to “bond math.” The high yield market may experience bouts of weakness, resulting in lower dollar prices, however, it still generates (high) coupons and eventually bonds are pulled to par as they near maturity, fortifying the returns recovery.

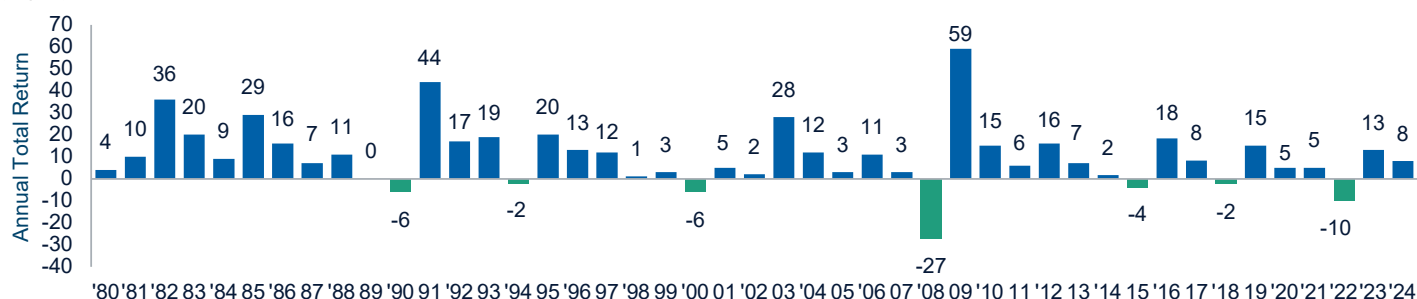
Leveraged credit has generated compelling risk-adjusted returns

While return is certainly an important consideration when evaluating an asset class, volatility must also be evaluated. The Sharpe Ratio, which measures return in excess of the risk-free rate, per unit of standard deviation, can be a useful metric to compare risk-adjusted returns across asset classes. Over the last ten years, high yield bonds have had the second highest risk-adjusted returns, trailing only below-investment grade bank loans (Fig. 2). Consequently, we believe that investors have been fairly compensated for the additional performance risk when moving to below investment grade credits.

“We believe high yield bonds deserve a strategic allocation and could offer attractive investment opportunities in the current environment.”

High yield bond annual returns

(Fig. 1)



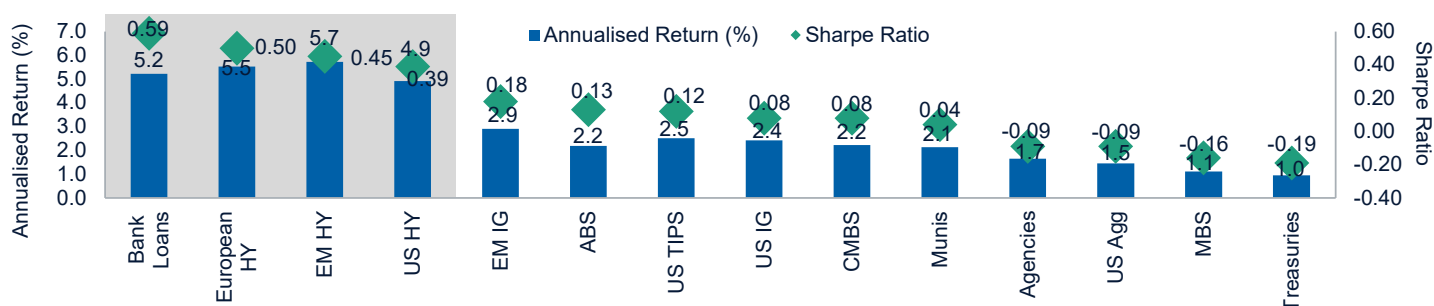
1980 Through 31 December 2024. Figures are Calculated in U.S. Dollars.

Past performance is not a guarantee or a reliable indicator of future results.

High yield bond annual returns are represented by the Bloomberg U.S. High Yield 2% Issuer Capped Bond index beginning in 2024 due to limited data availability. Historical returns are represented by the J.P. Morgan Global High Yield Index. Please see the Additional Disclosures.

High yield has generated leading risk-adjusted returns

(Fig. 2)



From 31 March 2015 Through 31 March 2025.

Past performance is not a guarantee or a reliable indicator of future results.

Sources: ICE BofA, Bloomberg, J.P. Morgan, and Morningstar. Bank Loans: Morningstar LSTA Performing Loan Index; European HY: ICE BofA European Currency High Yield Constrained Excluding Subordinated Financials Index Hedged to USD; US HY: ICE BofA US High Yield Index; EM HY: J.P. Morgan Corporate Emerging Market Bond Index Broad Diversified High Yield; Munis: Bloomberg Municipal Bond Index; EM IG: J.P. Morgan Corporate Emerging Market Bond Index Broad Diversified Investment Grade; ABS: Bloomberg Asset Backed Securities Index; US IG: Bloomberg U.S. Corporate Investment Grade Bond Index; US TIPS: Bloomberg U.S. TIPS Index; CMBS: Bloomberg CMBS ERISA-Eligible Index; US Agg: Bloomberg U.S. Aggregate Bond Index; Agencies: Bloomberg U.S. Agency Bond Index; MBS: Bloomberg U.S. Mortgage Backed Securities Index; US Treasuries: Bloomberg U.S. Treasury Bond Index; Risk Free Rate (for Sharpe Ratio): FTSE 3-Month Treasury Bill. Please see the Additional Disclosures.

Low default rate profile

Although the macro backdrop remains challenging for risk assets, high yield fundamentals continue to be resilient. Since the Global Financial Crisis (GFC), high yield market new issuance has been dominated by refinancings as issuers capitalised on low global rate environment. Additionally, record capital markets activity in 2020 and 2021 (post-COVID drawdown) at cheap financing rates strengthened balance sheet liquidity and increased interest coverage metrics to peak levels. The US high yield

default rate is 1.3% in March 2025 and remains well below its long-term average of 3% (Fig. 3).

Why High Yield Bonds Now?

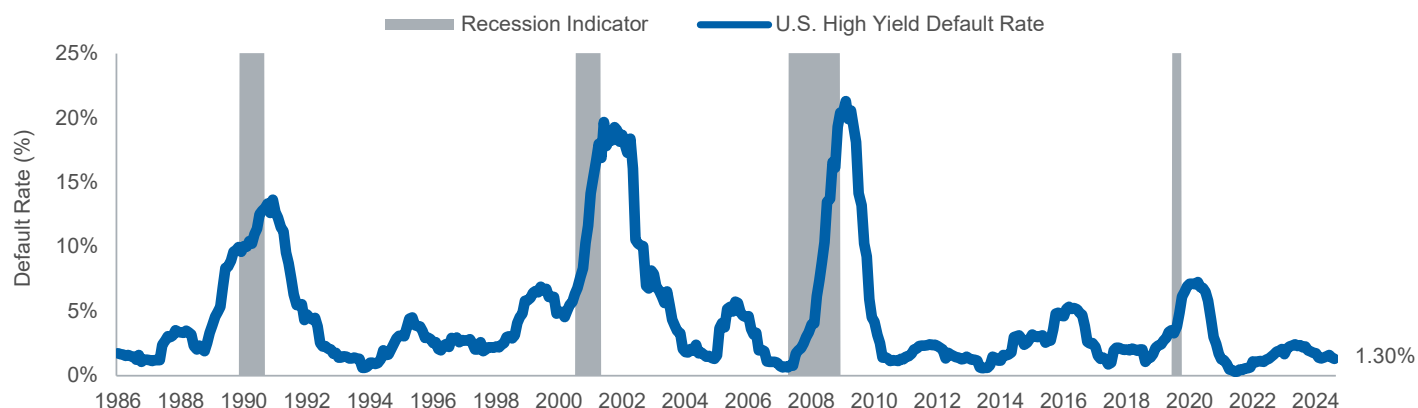
Evolution to a higher credit quality market

The current high yield market is drastically improved compared to the GFC in terms of credit quality. Using the ICE BofA Global

High Yield Index as a proxy, the high yield market has migrated up considerably in credit quality since the GFC. In 2007, only 37% of the index had at least one BB rating, today that figure is roughly 60% (Fig. 4). Partially the result of record Fallen Angel volume (US\$240 billion) entering high yield in 2020, the average company in the high yield market has a larger market cap and generates more free cash flow today than prior to the GFC. Therefore, we feel the asset class is in a position of strength should the economic outlook weaken.

High yield market default rates

(Fig. 3)

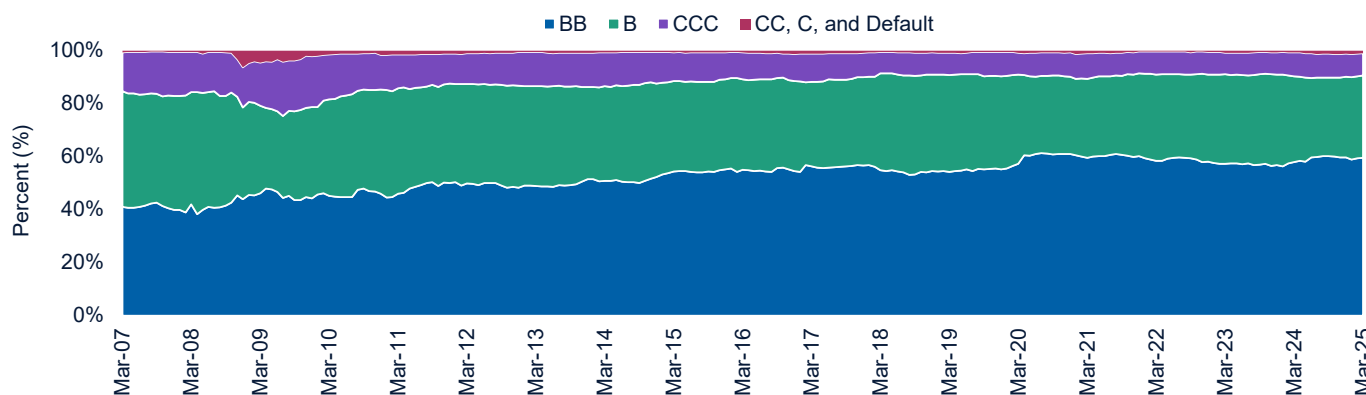


As of 31 March 2025.

Source: BofA Global Research. Par-weighted and issuer-weighted default rates, trailing-12m, including bankruptcies, missed payments, and liability-management exercises (LMEs).

High yield market ratings quality “migrates up”

(Fig. 4)



As of 31 March 2025.

Credit ratings do not remove market risk and are subject to change.

Source: ICE BofA.

High Yield Market represented by the ICE BofA Global High Yield Index.

Date used for Pre-Global Financial Crisis is 30 June 2007.

See the Additional Disclosures.

Today's yields have rarely been observed over the last ten years

As of 31 March 2025, the yield to worst on the ICE BofA Global High Yield Index was almost 7.5%. This is well above the average level of 6.54% observed over the last ten years (Fig. 5). Considering the credit quality of the market is much higher today, the absolute yield on the asset class screens attractive, especially compared to similar dislocation levels during the Energy Crisis (2015-2016) and the Pandemic selloff

where both the quality and fundamentals of the market were lower than levels observed today. Despite the uncertainty introduced by Trump's tariffs, global high yield continues to offer a healthy yield.

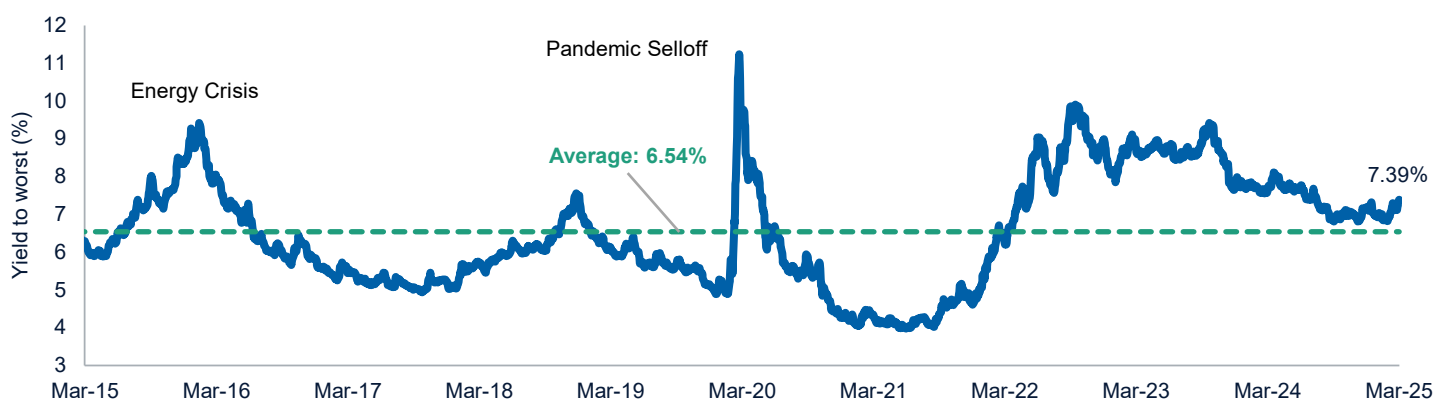
Yields indicate attractive valuation

While we cannot predict future returns from current yields, we can use history as a baseline for when the high yield market

had similar yield levels and what forward returns looked like. Since the GFC, the high yield market has crossed the 9% yield threshold five times. In each instance, the one year forward return picture has been in the mid-double digits range (Fig. 6). Since 2012, the median 12-month forward returns have been in double digits when yields in the market have exceeded 8%.

Yield to worst of the global high yield market

(Fig. 5)



From 31 March 2015 to 31 March 2025.

Past performance is not a guarantee or a reliable indicator of future results.

Source: ICE BofA.

Global High Yield Market represented by the ICE BofA Global High Yield Index.

Please see Additional Disclosures.

Historical global high yield returns once yields reached various thresholds

(Fig. 6)



From 1 January 2012 to 31 March 2025.

Past performance is not a guarantee or a reliable indicator of future results.

Returns since 1 January 2012. Performance periods shown once index yields moved through the yield threshold and had not been at that level for the preceding 30 business days.

Global High Yield Market represented by the ICE BofA Global High Yield Index.

Please see Additional Disclosures.

Adding value in your asset allocation

High yield bonds are uniquely positioned as both defensive and growth assets due to their mixed characteristics (Fig 7). As fixed income instruments, they provide income-driven returns, which can act as a buffer during market downturns, offering a defensive characteristic. Their sensitivity to economic growth and corporate fundamentals, rather than interest rate changes, aligns them more closely with equities, providing growth potential.

Defensive characteristics: High yield bonds offer a historical downside buffer relative to stocks, primarily due to their income-driven return profile. This makes them attractive in volatile markets, as they can provide steady income through regular coupon payments, helping to preserve capital during market drawdowns.

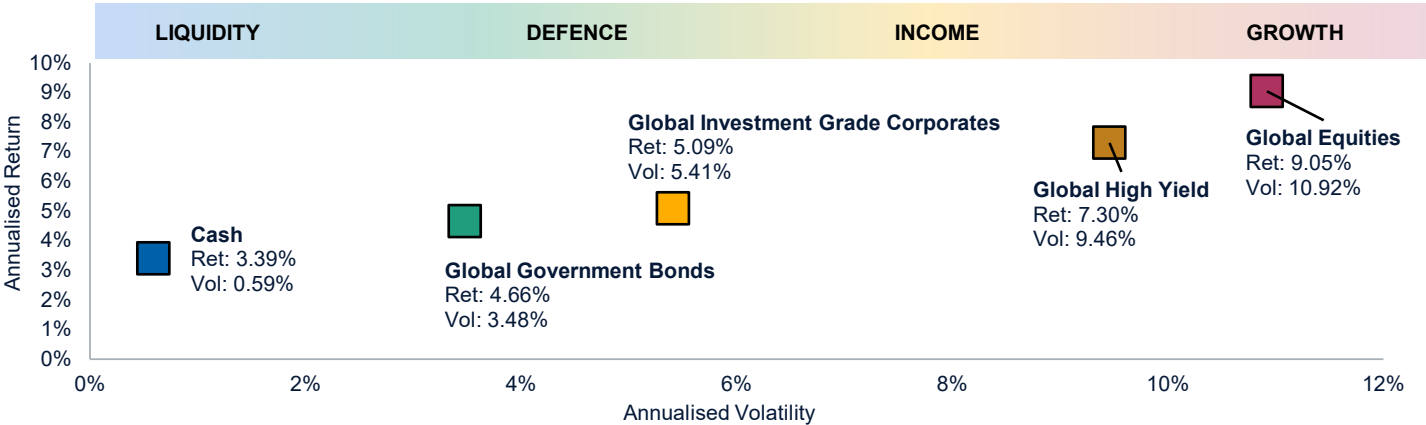
Growth potential: High yield bonds are considered mid-risk assets that mainly provide income but also have growth traits similar to equities. They offer compelling yields and total return potential, making

them attractive for investors seeking higher returns with less volatility compared to equities. Their sensitivity to economic growth means they can benefit from pro-growth policies and economic optimism.

Overall, high yield bonds can serve as a strategic long-term investment and a mainstay allocation in diversified portfolios, offering both defensive and growth benefits.

High yield as a strategic allocation

(Fig. 7)



20 years data ending on 28 February 2025.
Past performance is not a guarantee or a reliable indicator of future results.
Source: Analysis by T. Rowe Price.
Indices used: Cash: Bloomberg AusBond Bank Bill Index (BAUBIL Index); Global Treasury: Bloomberg Global Agg Treasuries TR Index Hedged AUD (H03432AU Index); Global IG: Bloomberg Global Agg Corporate Index Hedged AUD (LGCPTRAH Index); Global High Yield: ICE BofA Global High Yield Index Hedged AUD (HW00 Index hedged to AUD); Global Equity: MSCI ACWI Index Unhedged AUD (MGWD Index).
See Additional Disclosures.

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