Reasons To Consider Insight's* GLOBAL SHORT-DATED HIGH YIELD BOND STRATEGY

January 2024

KEY STATS: DECEMBER 2023[1]

Average expected maturity: 1.86 years | **Average yield to expected redemption: 7.73%**

The value of investments can fall. Investors may not get back the amount invested. Income from investments may vary and is not guaranteed.

Strategy overview: focused on visible cashflows

Insight's global short-dated high yield bond strategy targets bond issues which will be repaid within a two-year time horizon. Ideally, these issuers are seeking to enhance their business in some way; this can take the form of selling an asset, buying a competitor, or undertaking capital investment such as building a factory or plant. This activity will lead to an increase in the amount of cash generated by the company, either via increased revenue streams or from the proceeds of a sale. This additional cash can be used by the company to repay its debt, or to refinance its debt on more attractive terms. This is how we get repaid in two years. In our view, this strategy can produce attractive levels of income while minimising earnings and default risk. Given that credit spreads are flat in high yield for shorter dated or long dated bonds, we believe we are being disproportionately paid for the credit risk we are taking.

In general, within our global universe, we also target short-dated debt issued by companies with defensive properties. For example:

- Telecoms companies tend to have consistent cashflows as consumers are reluctant to give up their mobile phones even during recession.
- Packaging companies can benefit during recessions as products are not discretionary.
- Some companies build cash piles well in advance of debt maturities, allowing opportunistic purchases given our short-dated focus.

Once we have identified a potential target for investment, regular contact with management is key to ensure that events are progressing as planned. We would normally identify four to five key stages over the two-year period which need to be met for us to be confident that we will be repaid on time. If it becomes clear that these stages are not being met, or that timelines are delayed we will seek to divest the issue. A sale in this situation is generally straightforward, as the original business plan is generally still in place, just delayed or not meeting our prudent timelines.

Minimising default risk

In addition to our focus on visible cashflows, we also avoid issuers with a rating in the CCC category other than the subordinated debt of higher rated issuers. For CCC-rated subordinated debt, the default risk is that of the higher rated BB or B rated company. Although CCC rated issuer paper offers a yield premium, in our view it is generally not sufficient to compensate for the higher default risk (see Figure 1). By taking this approach, we have experienced very few defaults since the inception of our strategy relative to the broader high yield universe (see Figure 2).

FIGURE 1: AVERAGE ANNUAL DEFAULT RATES BY RATING[2]

BB	1.2%
B	3.3%
CCC	9.1%
Aggregate high yield	3.7%

1 Source: Insight. Data as at 31 December 2023.
2 Source: Moody's and Insight as at 31 December 2023. Default data covers period 1920 to 2023.

*** Investment Managers are appointed by BNY Mellon Investment Management EMEA Limited (BNYMIM EMEA), BNY Mellon Fund Managers Limited (BNYMFM), BNY Mellon Fund Management (Luxembourg) S.A. (BNY MFML) or affiliated fund operating companies to undertake portfolio management activities in relation to contracts for products and services entered into by clients with BNYMIM EMEA, BNY MFML or the BNY Mellon funds.**

This paper was written by Insight Investment. As such, it is in its voice as opposed to that of BNY Mellon Investment Management.

BNY MELLON INVESTMENT MANAGEMENT | Insight INVESTMENT

FIGURE 2: DEFAULT RATES[3]

	Calendar year												
	2023	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011
BNY Mellon global short-dated high yield bond strategy	0	0	0	1	0	0	0	0	0	2	0	0	0
Global HY universe	159	90	54	219	98	73	116	145	105	64	73	72	45

How did the strategy perform in 2023?

2023 saw periods of extreme volatility as market participants tried to gauge the peak in the hiking cycle and determine when central banks may start to ease policy. With economic data proving broadly more resilient than expected, hopes of a soft landing grew, but fears that economies could tip into recession were ever present. Against this backdrop the 10-year US Treasury yield rose to a high of 4.99%, before ending the year back at 3.88%, virtually exactly where it started. A combination of heightened volatility and macro uncertainty resulted in limited issuance, and the global high yield market ended the year at $6.5 trillion, unchanged over the year. A combination of high income and spread tightening drove a strong positive performance in 2023, with the strategy generating a gross 14.71% performance in US dollars, and a gross 12.36% in euros (see Figure 3). This outperformed the broader high yield market and investment grade credit.

FIGURE 3: PERFORMANCE OF THE BNY MELLON GLOBAL SHORT-DATED HIGH YIELD BOND COMPOSITE VERSUS HIGH YIELD BOND BENCHMARKS IN 2023[4]

	2021	2022	2023
BNYM Global Short Dated High Yield Bond	USD 5.63% EUR 4.69% GBP 5.41%	USD -3.14% EUR -5.11% GBP -3.68%	USD 14.71% EUR 12.36% GBP 14.05%
Euro HY	3.35%	-11.48%	12.00%
US HY	5.36%	-11.22%	13.45%
Euro IG	-1.02%	-13.94%	8.02%
US IG	-0.95%	-15.44%	8.39%

[3] Source: Insight. Data as at 31 December 2023. The strategy adheres to the same investment approach as Insight's global short-dated high yield bond strategy. The global HY universe constitutes of global issuers rated by Moody's based on their rating at the beginning of the year.

[4] Source: Insight. Performance calculated as total return, income reinvested, gross of fees, in GBP, USD and EUR. Fees and charges apply and can have a material effect on the performance of your investment. Insight claims compliance with the Global Investment Performance Standards (GIPS). A GIPS compliant presentation is available upon request via your BNY Mellon Investment Management EMEA contact. The market indices have been shown against the short duration high yield bond composite to provide an analysis of the impact of the sell-off on the strategy versus the high yield indices of different maturities in the wider market. Bank of America Merrill Lynch indices total returns to 31 December 2023: ICE BofA US High Yield Index Effective Yield 'H0A0', ICE BofA Euro High Yield Index Effective Yield 'HE00', ICE BofA European Investment Grade Index 'ER00', ICE BofA US Investment Grade Index 'C0A0'.

Past performance is not a guide to future performance.

Performance

TEN-YEAR PERFORMANCE RECORD TO 31 DECEMBER 2023

	Calendar year returns									
	2023	2022	2021	2020	2019	2018	2017	2016	2015	2014
BNY Mellon global short-dated high yield bond composite (GBP)	14.05	-3.68	5.41	0.43	6.93	-0.41	5.23	7.95	4.06	1.54
Benchmark (GBP)	4.34	1.03	-0.03	0.17	0.68	0.60	0.23	0.38	0.45	0.42
BNY Mellon global short-dated high yield bond composite (EUR)	12.36	-5.11	4.69	0.06	5.59	-1.65	4.36	–	–	–
Benchmark (EUR)	3.27	0.35	-0.65	-0.54	-0.49	-0.47	-0.47	–	–	–
BNY Mellon global short-dated high yield bond composite (USD)	14.71	-3.14	5.63	1.87	8.84	1.24	6.47	–	–	1.20
SOFR (90-day compounded)	4.90	1.17	0.06	0.56	2.28	2.28	1.19	0.66	0.22	0.14

Returns may increase or decrease as a result of currency fluctuations.

Source: Insight. Performance calculated as total return, income reinvested, gross of fees, in USD, GBP and EUR. Fees and charges apply and can have a material effect on the performance of your investment. Insight's short-dated high yield bond strategy (USD) composite inception date: 31 July 2013. No components within composite during July 2015 to November 2016 hence returns beyond this period cannot be calculated. Effective 1 November 2021, the comparator benchmark changed from the 3-Month USD LIBOR to the SOFR (Secured Overnight Financing Rate) (90-day compounded). All benchmark past performance prior to this date was calculated against 3-Month USD LIBOR. Insight's short-dated high yield bond strategy (GBP) composite inception date: 31 January 2009. Effective 1 November 2021, the comparator benchmark changed from 3-Month GBP LIBID to SONIA. All benchmark past performance prior to this date was calculated against 3-Month GBP LIBID. Insight's short-dated high yield bond strategy (EUR) composite inception date: 31 January 2016. Effective 1 January 2022, the comparator benchmark changed from the EURIBOR to 3-Month EURIBOR. All benchmark past performance prior to this date was calculated against EURIBOR. Insight claims compliance with the Global Investment Performance Standards (GIPS). A GIPS compliant presentation is available upon request via your BNY Mellon Investment Management EMEA contact.

Strategy outlook

The strategy ended 2023 with an average coupon of just under 6%. As more companies come to the market to refinance, we expected the average coupon to increase through the year. We are currently observing issuers that have bonds maturing in 2025 and 2026 with coupons sub 3% come to markets to refinance with coupons of around 6% to 7%. This should allow us to gradually raise our average coupon.

In addition, the average price of the bonds we hold within the strategy is around 95, a level well below the price issuers would have to pay to call the bonds early. We hold a large percentage of these issues in 2025 and 2026 maturities and expect around 60bn euros of 2025 maturities to be refinanced in 2024. Historically we have seen around 4% of our holdings called each month, and we see no reason for this to change in the current environment. This would result in around 50% of our holdings being called in 2024; we would benefit from this capital appreciation if this proved to be correct.

As bonds get called, we are able to invest these proceeds into new issues, locking in higher coupons and income for a further two years or more. In our view, this environment is one in which it should be possible to generate another strong positive annual return. If central banks do start to reduce rates, it should benefit the prices of newer issues we have purchased, where call dates remain distant, while at the same time being a positive for corporate refunding rates and the market as a whole.

RISK DISCLOSURES

- **Objective/Performance Risk:** There is no guarantee that the Strategy will achieve its objectives.
- **Currency Risk:** This Strategy invests in international markets which means it is exposed to changes in currency rates which could affect the value of the Strategy.
- **Derivatives Risk:** Derivatives are highly sensitive to changes in the value of the asset from which their value is derived. A small movement in the value of the underlying asset can cause a large movement in the value of the derivative. This can increase the sizes of losses and gains, causing the value of your investment to fluctuate. When using derivatives, the Strategy can lose significantly more than the amount it has invested in derivatives.
- **Changes in Interest Rates & Inflation Risk:** Investments in bonds/money market securities are affected by interest rates and inflation trends which may negatively affect the value of the Strategy.
- **Credit Ratings and Unrated Securities Risk:** Bonds with a low credit rating or unrated bonds have a greater risk of default. These investments may negatively affect the value of the Strategy.
- **Credit Risk:** The issuer of a security held by the Strategy may not pay income or repay capital to the Strategy when due.
- **Emerging Markets Risk:** Emerging Markets have additional risks due to less-developed market practices.
- **Liquidity Risk:** The Strategy may not always find another party willing to purchase an asset that the Strategy wants to sell which could impact the Strategy's ability to sell the asset or to sell the asset at its current value.
- **Share Class Hedging Risk:** The hedging strategy is used to reduce the impact of exchange rate movements between the share class currency and the base currency. It may not completely achieve this due to factors such as interest rate differentials.
- **Counterparty Risk:** The insolvency of any institutions providing services such as custody of assets or acting as a counterparty to derivatives or other contractual arrangements, may expose the Strategy to financial loss.

For a full list of risks applicable to this fund, please refer to the Prospectus or other offering documents.