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Global high yield starts 2017 on the up

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January lifted high yield bonds to a good start to 2017, with both economic reports and earnings releases across regions being supportive.

In the run up to Donald Trump's inauguration, US high yield performed very well on the anticipation of a growth spurt. As a result, the materials sector globally outperformed, factoring in a boost from US manufacturing, and energy also continued to perform well helped by OPEC keeping supply subdued for now.

There were detractors, however, including speculation regarding a 'hard' Brexit, which impacted sterling high yield, and European Central Bank (ECB) policy talk regarding tapering of their quantitative easing programmes. Inflation prospects led to low to negative returns in US Treasury bonds and other rates markets such as German Bunds.

Credit news

The big credit story for January was Fiat being the next name to be drawn into the diesel emissions scandal with talk of a possible fine in the US. Fiat bonds initially sold-off sharply and subsequently retraced to a large extent as the story is still unfolding. Bonds of packaging company Ardagh rallied on an S&P rating upgrade. In a similar fashion, Mexican building materials company Cemex benefited from a credit rating upgrade from B+ to BB-. Anglo American followed the trend of other materials sector names by reporting decent results, as well as an improving outlook.

An active new issue market

The new issue market was very active in investment grade credit at the start of the year, propelled by merger and acquisition (M&A) activity and potential tax reforms in the US. The primary market for high yield bonds was more muted, but a window did open and quite a few sterling issuers seized the opportunity.

Fluctuating sentiment but a positive outlook

The high yield bond market is likely to remain sensitive to fluctuations in sentiment caused by a number of factors including Brexit, Trump's policies and rhetoric and the potential impact on global economic growth, volatile commodity prices, expectations with regards to US interest rate hikes and ECB tapering.

High yield bonds still appear attractively valued from a spread perspective, which still prices in relatively high defaults and recession risk. Their appeal going forward lies predominantly in the income generated and the relatively low interest rate sensitivity. We believe that the major central banks will continue to adopt a broadly accommodative stance, providing general support for capital markets and continuing demand for the high yield asset class.

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