

Fixed Income Perspectives

As investors grapple with a new era of macroeconomic uncertainty, liquidity is king in the near term.

Bond Market Outlook

Global Rates: 10-year U.S. Treasury yield back to pre-pandemic levels, but we see some resistance to a further move higher

Global Currencies: U.S. dollar continues to move higher in a flight to quality

Investment Grade: Strong corporate earnings continue, creating a robust fundamental backdrop for the sector; spreads more attractive but waiting for better entry point

High Yield: Solid fundamental backdrop allows for tactical positioning through volatility, selling on strength and resetting risk on weakness

Senior Loans: The U.S. loan market continues to exhibit resilience amid ongoing broad market weakness

Securitized Credit: Continue to prefer mortgage credit and CMBS with strong fundamentals, as well as higher-quality ABS, as consumer fundamentals remain strong

Emerging Markets: We remain cautious on the asset class given the potential slowdown in Chinese growth, along with the impact of rising food and energy prices on EM consumers



Matt Toms, CFA
CIO Fixed Income

Voya Investment Management's fixed-income strategies cover a broad range of maturities, sectors and instruments, giving investors wide latitude to create a new portfolio structure or complement an existing one. We offer investment strategies across the yield curve and credit spectrum, as well as in specialized disciplines that focus on individual market sectors. We build portfolios one bond at a time, with a critical review of each security by experienced fixed income managers.

Is This What “Unprecedented and Extraordinary” Actually Feels Like?

Unprecedented and extraordinary. For more than a decade, this was the description for actions taken by the Federal Reserve to keep the economy—and by extension, risk assets—on track. If you wanted to evaluate macroeconomic risk, Fed policy was your measuring stick. Interpreting Fed minutes became a full-time job for some market participants and media pundits.

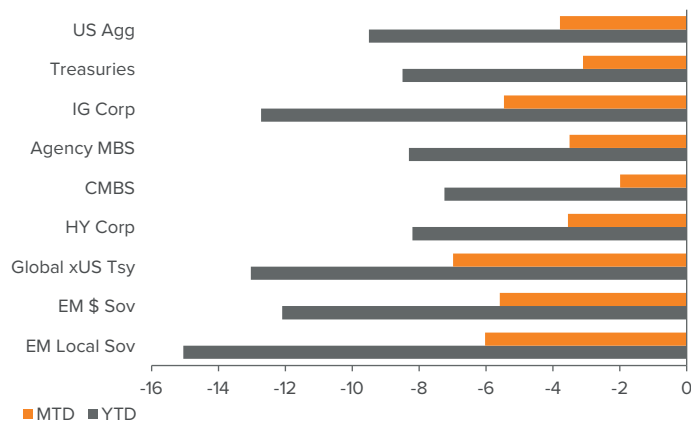
There is nothing markets hate more than uncertainty, and for a very long time, the Fed mitigated investors' fear of the unknown by answering every shock to the system with more “unprecedented and extraordinary” measures. Over time, these measures felt more like the norm than the exception. That era is over. The new measuring stick of macroeconomic risk is inflation. We expect the Fed will do everything in its power to avoid surprises. But the ball isn't in its court. The market knows that the Fed must control inflation. What it doesn't know is whether the Fed will be successful.

As investors grapple with this new source of uncertainty, we expect the recent episodes of spread and rate volatility to continue. In this environment, liquidity is king. Across our portfolios, we are increasing the liquidity of our holdings to manage risk more effectively. In addition, we are keeping dry powder on hand to take advantage of opportunities created by market dislocation.

Over the long term, we believe this period of volatility will prove to be fertile ground to pick up fundamentally strong assets that become oversold. But in the short term, it's all eyes on inflation.

Rates, Spreads and Yields

Fixed Income Sector Total Returns



	30-Apr	31-Mar	1Y Low	1Y High	
Yields	US 2 Yr	2.72	2.32	0.14	2.72
	US 10 Yr	2.94	2.34	1.17	2.94
	GER 10 Yr	0.94	0.55	-0.50	0.97
	JPN 10 Yr	0.23	0.22	0.01	0.25
	EM Local Sov	6.77	6.23	4.89	7.47
Spreads	IG Corp	135	116	80	145
	Agency MBS	40	24	7	48
	CMBS	132	129	92	136
	HY Corp	379	325	262	411
	HY x-Egy Corp	385	328	252	416
	EM \$ Sov	439	400	330	526

As of 04/30/22. Source: Bloomberg, Bloomberg/Barclays, JPMorgan and Voya. Past performance is no guarantee of future results.

Sector Outlooks

Global Rates and Currencies

Amid the ongoing volatility, it's important to step back and take stock of the longer-term picture: the recent uptick in the 10-year Treasury yield (while swift and severe) has only brought us back to pre-pandemic levels. Zoom out even further, and yields remain near their lowest levels of the past 40 years.

The move higher in rates was not limited to the U.S., as German and Japanese government bond yields also continued to climb. However, the euro and yen continued to weaken against the dollar. The ECB has also found a hawkish tone to combat rising inflation in the euro area. The market is now pricing in 80 basis points of hikes by the ECB through year-end.

Investment Grade (IG) Corporates

Earnings remain strong on average. With 86% of S&P 500 companies reporting 1Q22 results (as of May 6, 2022), 79% exceeded earnings expectations and 74% beat revenue expectations. Profit margins continue to come under some pressure, but they still look healthy overall as companies pass along higher prices to end users. Valuations are more attractive, with spreads having widened out further, but we are waiting for a better entry point given the continued macro-driven volatility. At the sector level, we continue to like utilities and financials, maintaining a defensive posture given broader macroeconomic uncertainty. In addition, financials provide a hedge against higher rates.

High Yield Corporates

High yield sold off with other risk assets in April, with CCC and BB rated bonds underperforming. B-rated bonds were the best house in a bad neighborhood. At the issuer level, we continue to see increased dispersion in financial results, as investors are

punishing companies that miss earnings. High yield looks cheaper as spreads are now pricing in a material slowdown and some defaults, but spreads are still not indicating recession risk. From a positioning standpoint, we are overweight building products, independent energy, and media and entertainment. We are underweight financials and consumer cyclicals. Overall, we are seeking yield with duration roughly below index; given the heightened uncertainty, we are trying to be surgical about where we take on duration risk.

Senior Loans

The U.S. loan market continued to exhibit resilience amid ongoing broad market weakness, as the Index registered a gain of 22 bps in April. The asset class has fared considerably better than both bonds and equities, which have experienced sharp losses in 2022.

Performance among rating cohorts continued to reflect a risk-off tone. BB rated loans were on top of the leaderboard for a second consecutive month. From a market technicals perspective, new-issue activity increased relative to the muted levels experienced in the last two months. In April, total issuance was \$35.5 billion, more than double March's tally of just \$17.3 billion and well ahead of February's \$23.9 billion. Arrangers syndicated a healthy slate of M&A-related deals, which represented approximately 51% of all transaction volume.

Securitized Credit

Collateralized loan obligations (CLOs) outperformed in April, and we see room for this to continue due to reduced issuance, attractive yields and investors' healthy appetite for floating-rate/low-duration assets. We favor tier-1 managers and clean collateral pools with shorter spread duration, especially for positions with lower credit quality.

In asset-backed securities (ABS), we maintain our positive outlook in the near term. After a successful cycle of transactions to open the quarter (spreads 5–15 bps tighter), we expect a reasonable new-issue pipeline to be well received and lead to additional spread tightening. New issue volume dropped by \$4 billion in April to \$23 billion. However, volume is up 48% relative to the comparable period in 2021.

In commercial mortgage-backed securities (CMBS), we maintain our neutral position in the near term. While issuance receded in April (and helped drive outperformance), the space has picked up correlation to broader risk markets since February and is expected to continue to do so until new-issuance volume further recedes. Fundamentals continue to improve, with delinquencies down 21 of the last 22 months to 3.5%. We continue to favor seasoned subordinate credit to on-the-run issuance with the exception of select single asset/single borrower securities and retain our long-standing bias against hotel and class B enclosed malls.

In residential mortgage-backed securities, we remain positive. The housing market remains in expansion mode, as the space has been a clear beneficiary of the pandemic, catching up a decade of lost growth even after a historic run-up in house prices. Mortgage credit, after lagging growth in the broader economy on a secular basis, is also increasing in availability—a positive at this early stage. In addition, a paradigm shift in the residential mortgage prepayment market presents an interesting entry point; given that recent rate hikes have greatly improved the prepayment outlook, which was a thorn in the residential mortgage market's side for much of 2021.

Emerging Market (EM) Debt

The global backdrop remains challenging for EM assets as continued inflation pressures, declining growth expectations, a hawkish Fed and a tightening of financial conditions are clear headwinds.

The potential for a slowdown in Chinese economic growth introduces risk of further downside despite the government's pledge to provide more stimulus. As the conflict in Ukraine continues, commodity prices are likely to remain at elevated levels (even if China slows).

Higher prices are an overall positive for EM markets particularly for external balances, but they will also put further pressure on domestic demand in Europe and Latin America where inflation is already running hot and the weight of food and energy in local CPI baskets is significant. An increasing number of governments have proposed subsidies to shield consumers from rising prices as social unrest is evident in some countries. Issues of food insecurity are growing but the risk currently predominates in frontier countries. Against this backdrop, we remain cautious on the asset class.

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Past performance does not guarantee future results.

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