2200 Ross Avenue, 31st Floor • Dallas, TX 75219 • 214-665-1900

November 2020 Leveraged Finance Update

High Yield And Loan Market Recap

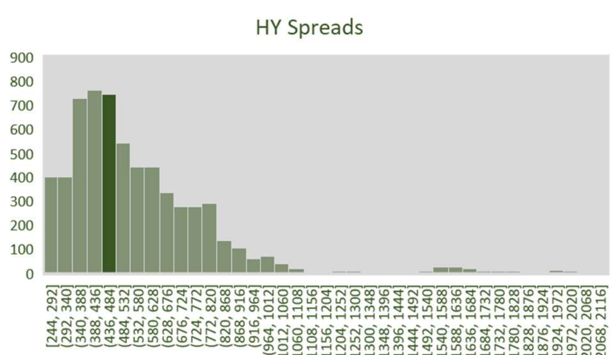
Multiple vaccine announcements and the completion of this election cycle propelled both High Yield (HY) and Leveraged Loans (LL) to strong performance in November. Equity markets also performed well: the S&P 500 was +10.95%; small cap equities were +18.4%; and the Credit Suisse Leveraged Equity Index was +20.8%. The HY market was +4% as CCCs outperformed (+7.47%) in a strong risk-on environment. Spreads for the index compressed 100bps, pushing the YTW down to a historic low of 4.72%. Spreads for CCCs compressed 200bps as this lowest-rated HY segment finished at its highest price level for the year ($91.62). While the HY market has reached new lows in yields, spreads remain near historical median levels and still offer value relative to other fixed income alternatives.

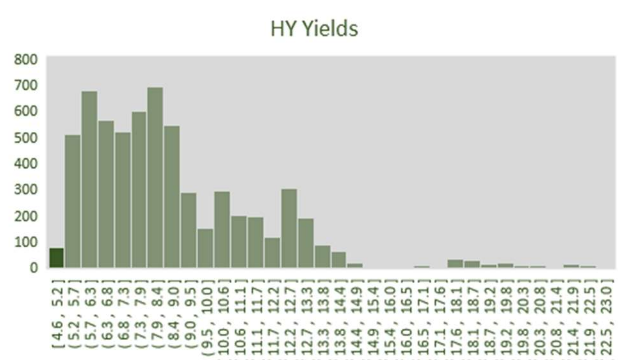
LL performance (+2.13%) lagged HY due more to subdued volatility and continued low nominal interest rates. Like HY, CCCs were very strong (+6.65%). Three-year yields for loans are currently 5.47% with a spread of +522bps. While yields for LL remain low relative to history, spreads remain roughly 50bps wider than the historical median.

Relative Valuation in High Yield

Although yields for the HY market are touching all-time lows, there are still reasons to be constructive. The Fed has strongly signaled that it does not plan to raise interest rates for several years because unemployment remains elevated and near-term inflation risks are low. HY issuers should enjoy natural deleveraging as economic growth returns in 2021, helping heal stretched balance sheets. The relative value of HY versus other fixed income alternatives remains attractive, particularly since spreads are near median levels.

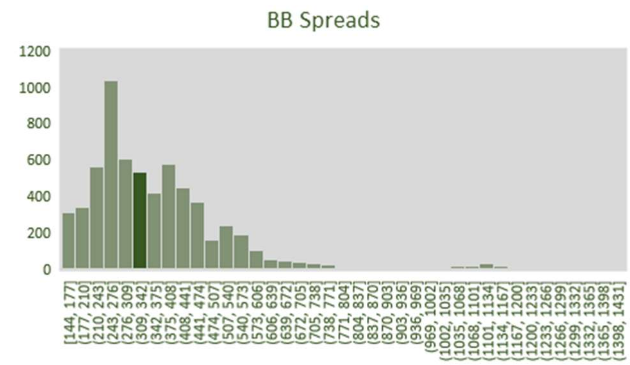
We have constructed this histogram to highlight where HY is currently on the distribution. Spreads compensate investors for the incremental risk versus risk-free rates. As seen in this histogram, HY spreads continue to offer better compensation based on historical perspective. Additionally, the BB-rated segment within HY has increased to 55.4% of the overall index as more Fallen Angels have entered the market. With the higher percentage of BBs, the quality of the HY index has increased.

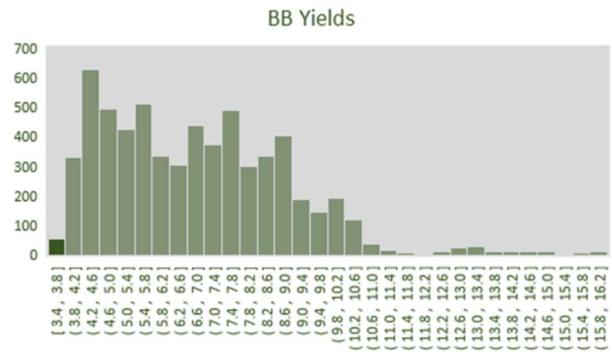




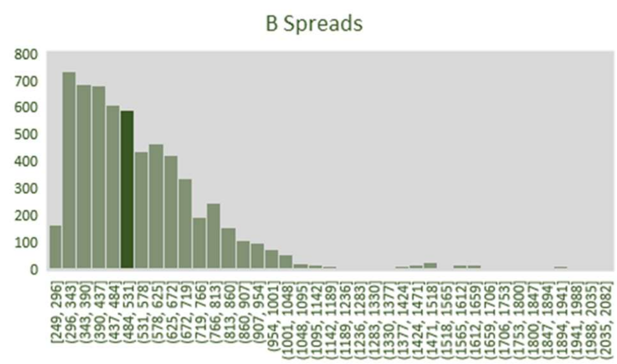
Source: Barrow Hanley and ICE/BAML Indices

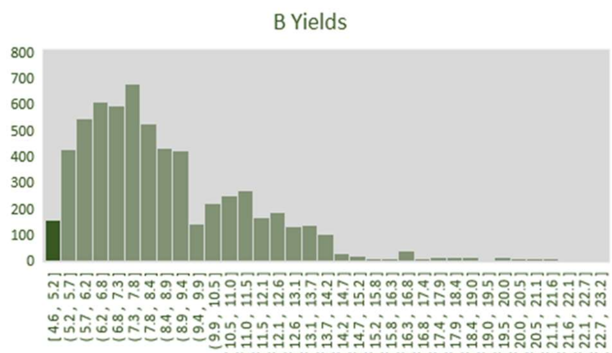
Spreads within BBs remain more compelling relative to history than other segments within HY.





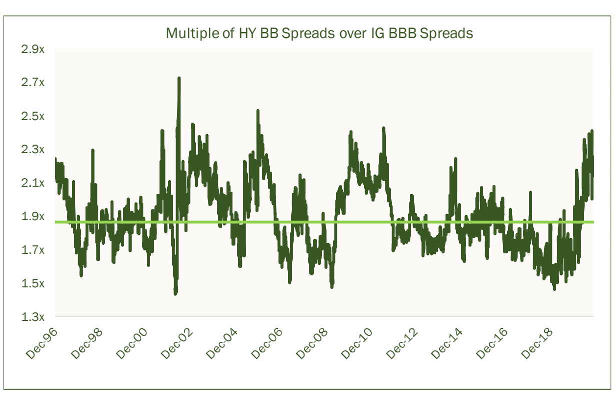
Source: Barrow Hanley and ICE/BAML Indices

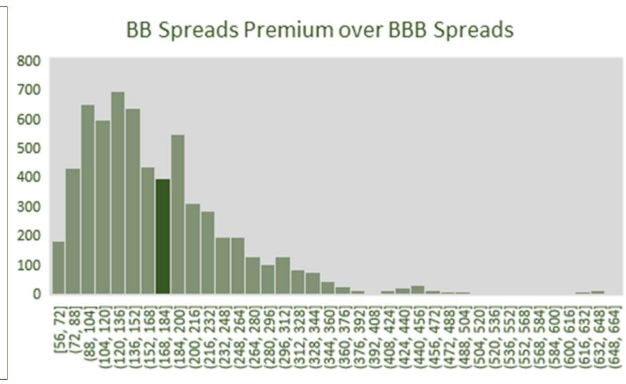




Source: Barrow Hanley and ICE/BAML Indices

When examining BB spreads relative to BBB spreads, the multiple between the two ratings has historically traded at 1.86x. Currently, BBs trade at 2.25x versus the historic 1.86x multiple. The absolute spread premium has historically been +150bps compared to the current level of +175bps. Meanwhile, the ICE/BAML IG index yields 1.84% with a spread of +107bps. Within IG, BBBs yield 2.14% and trade at a spread of +137bps.





Source: Barrow Hanley and ICE/BAML Indices

The BB segment of the HY index contains a large portion of attractive Fallen Angels, which are formerly investment grade credits that have been downgraded to HY. Historically, Fallen Angels underperform while IG-rated and outperform once they enter HY. These Fallen Angel credits often have more balance sheet flexibility than traditional HY issuers due to better credit metrics, more flexible covenants, and longer duration debt. Fallen Angels also often have greater discretion to allocate cash flow away from share buybacks, dividends, and capital expenditures to increased debt reduction. Fallen Angels comprise nearly 30% of BBs and carry a more attractive spread of +345bps compared to the BB index at +312bps. There is more positive convexity in Fallen Angels compared to other BBs due to a higher percentage of this debt having non-call features.

CLO MARKET UPDATE

LL continue to exhibit increased investor interest as the risk-on sentiment spreads across capital markets. CLOs, the largest buyer of bank loans, continue to experience a reduction in their costs of capital, allowing their equity tranches to potentially generate more attractive returns. CLO equity returns materially benefit from a lower cost of capital for the AAA tranche, and these spreads have now tightened to the low L+120s. At the same time, lower parts of the CLO capital structure such as the BB tranche have recently priced deals in the primary market 160bps tighter than those priced just one week prior. Unsurprisingly, returns in secondary CLO tranches strongly improved during November in lockstep with their ratings. BBB tranches were +3.63% and BB tranches were +8.46% in the month, providing more rationale for tightening primary spreads.

While COVID hampered the pace of CLO issuance in 2020 compared to 2019, the past three months have helped close the gap. It was a notably slower month for issuance in November, breaking the prior two-month trend of greater than $10B/month. The shortfall is understandable because of the uncertainty around the elections and the Thanksgiving holiday. The slower month also coincided with lower corporate loan new issuance, more closely matching supply with demand from CLOs.

Confidence in the CLO market has shifted markedly positive for other reasons beyond just a lower cost of capital. The market has once again embraced longer reinvestment periods as 11 deals have priced for longer tenors versus the three-year deals that were more common during the early stages of the COVID crisis. The pace accelerated as three of the 11 deals recently priced with a five-year reinvestment. Single-B tranches are becoming more frequent in recent deals. These two dynamics, among other factors, show an increasing level of comfort that markets are approaching a healthy post COVID-environment.

BHMS Strategy Returns	Mo	QTD	YTD	Index
High Yield Composite Gross	3.60%	3.54%	6.35%	BHMS
High Yield Composite Net	3.58%	3.50%	6.13%	BHMS
Bank Loan Composite Gross	1.98%	2.21%	1.54%	BHMS
Bank Loan Composite Net	1.98%	2.18%	1.43%	BHMS
Asset Class	**Mo**	**QTD**	**YTD**	**Index**
HY Return	4.00%	4.49%	4.18%	ICE BAML HY Index
HY BB Return	3.61%	4.12%	6.96%	ICE BAML BB HY Index
HY B Return	3.45%	3.94%	1.92%	ICE BAML B HY Index
HY CCC Return	7.47%	7.77%	-1.21%	ICE BAML CCC HY Index
Leveraged Loan Return	2.13%	2.31%	1.46%	CS Leveraged Loan Index
LL BB Return	1.54%	1.35%	-0.75%	CS Leveraged Loan BB Index
LL B Return	1.84%	1.99%	1.84%	CS Leveraged Loan B Index
LL CCC Return	6.65%	7.15%	3.16%	CS Leveraged Loan CCC Index
HYG	3.35%	3.77%	2.47%	Ishares Iboxx High Yield
BKLN	2.67%	1.81%	-0.19%	Invesco Senior Loan ETF
S&P 500 Return	10.95%	8.00%	14.02%	S&P 500
Russell 2000 Return	18.43%	20.91%	10.41%	Russell 2000 Index
CS Leveraged Equity Index	20.77%	17.56%	14.45%	CS Leveraged Equity Index
10yr Beg	0.88%	0.69%	1.92%	10yr Treasury
10yr End	0.84%	0.84%	0.84%	10yr Treasury
10yr Return	0.31%	-1.33%	11.23%	10yr Treasury
	Beg Mo	**Beg Qtr**	**Beg Year**	**Ending YTW/STW**
HY YTW	5.75%	5.76%	5.41%	4.72%
HY BB YTW	4.34%	4.40%	3.85%	3.54%
HY B YTW	6.08%	6.00%	5.38%	4.98%
HY CCC YTW	11.59%	11.77%	11.80%	9.47%
HY STW	535	545	372	437
HY BB STW	388	403	213	312
HY B STW	575	574	370	472
HY CCC STW	1,126	1,154	1,012	918
LL YT3Y	6.08%	6.02%	6.27%	5.47%
LL BB YT3Y	3.99%	3.93%	4.29%	3.59%
LL B YT3Y	5.80%	5.70%	6.36%	5.26%
LL CCC YT3Y	14.27%	13.94%	15.29%	12.37%
LL ST3Y	583	579	461	522
LL BB ST3Y	372	369	262	333
LL B ST3Y	555	547	470	501
LL CCC ST3Y	1,403	1,371	1,365	1,213

Source: Barrow Hanley

CONTACT INFORMATION

FOR ANY INQUIRIES PLEASE REACH OUT TO:

ALEX GRAUSE, AGRAUSE@BARROWHANLEY.COM. 617-759-1110 OR MARKETING@BARROWHANLEY.COM

General Disclosures:
All opinions included in this report constitute Barrow Hanley's judgment as of the time of issuance of this report and are subject to change without notice. This report was prepared by Barrow Hanley with information it believes to be reliable. This report is for informational purposes only and is not intended to be an offer, solicitation, or recommendation with respect to the purchase or sale of any security, nor a recommendation of services supplied by any money management organization. Past performance is not indicative of future results. Barrow, Hanley, Mewhinney & Strauss, LLC is a value-oriented investment manager, providing services to institutional clients.

These investment summaries are provided for informational purposes only and should not be viewed as representative of all investments by the firm. This report includes certain "forward-looking statements" including, but not limited to, BHMS's plans, projections, objectives, expectations, and intentions and other statements contained herein that are not historical facts as well as statements identified by words such as "expects", "anticipates", "intends", "plans", "believes", "seeks", "estimates", "projects", or words of similar meaning. Such statements and opinions contained are based on BHMS's current beliefs or expectations and are subject to significant uncertainties and changes in circumstances, many beyond BHMS's control. Actual results may differ materially from these expectations due to changes in global, political, economic, business, competitive, market, and regulatory factors. Additional information regarding the strategy is available upon request.

Index Disclosures:
Bloomberg Index Services Limited. BLOOMBERG® is a trademark and service mark of Bloomberg Finance L.P. and its affiliates (collectively "Bloomberg"). BARCLAYS® is a trademark and service mark of Barclays Bank Plc (collectively with its affiliates, "Barclays"), used under license. Bloomberg or Bloomberg's licensors, including Barclays, own all proprietary rights in the Bloomberg Barclays Indices. Neither Bloomberg nor Barclays approves or endorses this material, or guarantees the accuracy or completeness of any information herein, or makes any warranty, express or implied, as to the results to be obtained therefrom and, to the maximum extent allowed by law, neither shall have any liability or responsibility for injury or damages arising in connection therewith.

Credit Suisse Index data is permissible for use by Barrow Hanley for client reporting and marketing purposes. This data is not permitted to be re-distributed.

Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. Russell® is a trademark of Frank Russell Company. The presentation may contain confidential information and unauthorized use, disclosure, copying, dissemination or redistribution is strictly prohibited. This is a presentation of BHMS. Russell Investment Group is not responsible for the formatting or configuration of this material or for any inaccuracy in BHMS' presentation thereof.

Standard and Poor's and S&P are registered trademarks of Standard & Poor's Financial Services LLC ("S&P"); Dow Jones is a registered trademark of Dow Jones Trademark Holdings LLC, and these trademarks have been licensed for use by S&P and Dow Jones Indices LLC and S&P Dow Jones Indices LLC. The presentation may contain confidential information and unauthorized use, disclosure, copying, dissemination or redistribution is strictly prohibited. This is a presentation of Barrow Hanley. S&P Dow Jones Indices LLC is not responsible for the formatting or configuration of this material or for any inaccuracy in Barrow Hanley's presentation thereof.