Mesirow

High Yield | Commentary

Market overview

High yield bonds and leveraged loans gained in November, as investors benefitted from tightening spreads and high coupon rates. The Bloomberg US Corporate High Yield Index rose +1.15% and the Credit Suisse Leveraged Loan Index increased +0.84% during the month. Year to date, the indices are up +8.66% and +8.41%, respectively.

Treasury rates ultimately fell, with 5-year and 10-year Treasuries down 11bps and 12bps, respectively. The Federal Funds target rate was also lowered by 25bps.

The Bloomberg US Corporate High Yield Index option-adjusted spread continued to decrease, falling 17bps to 265bps by month end. The Credit Suisse Leveraged Loan Index's 3-year discount margin, similarly, decreased 18 bps since last month to 461bps.

Loans continued to dominate defaults and distressed exchanges in November. Four actual defaults occurred, totaling $1.5B in bonds and $3.5B in loans. Three distressed exchanges also took place with $140M in bonds and $1.8B in loans.

When including distressed exchanges, the last twelve months (LTM) par-weighted default rates continued to highlight the stark difference between high yield and loan quality: the US high yield bond default rate decreased by 25 basis points to 1.14%, while loan default rates increased by 26 basis points to 4.04% month-over-month. Compared to year-end figures, these rates are down 174 basis points for bonds and up 77 basis points for loans. These rates compare to 25-year averages of 3.4% for high yield bonds and 3.0% for leveraged loans. (JP Morgan)

High yield market overview

The Bloomberg US Corporate High Yield Index returned +1.15%.

- **CCCs outperformed once again:** BB-rated bonds returned +1.10%, B-rated bonds returned +1.07% and CCC-rated bonds returned +1.41%.
- **Industries were positive:** Pharmaceuticals (+2.22%) and Transportation (+2.13%) were top performers, while Supermarkets (+0.32%) and Healthcare (0.44%) were the worst performers.
- **Issue size performance was consistent:** Large issue sizes ($1B+) were up +1.17%, mid-size issues ($500M–$1B) were up +1.13% and small issue bonds ($200–$500M) were up +1.15%.

Loan market overview

The Credit Suisse Leveraged Loan Index returned +0.84%.

- **CCC loans lagged:** BB-rated loans returned +0.96%, B-rated loans returned +0.95% and CCC-rated loans fell -0.38%.
- **Industries were mostly positive:** Metals/Minerals was the best performing sector returning +1.32%, while Food/Tobacco was only sector with negative performance with a -0.15% return.
- **Large loan issues outperformed:** Small issue size loans (less than $500M) rose +0.59%, mid-size issues ($500M–$1B) rose +0.77% and large issue sizes ($1B+) returned +0.89%.

Source: Bloomberg, JP Morgan. | Mesirow High Yield Management ("MHY") is a division of Mesirow Financial Investment Management, Inc., ("MFIM") an SEC-registered investment advisor. | Past performance is not indicative of future results. | Please see the disclosures at the end for additional, important information. Any performance mentioned above is supplemental; please see the GIPS Report that is included for complete performance and benchmark descriptions.

Performance review

The strategy outperformed the benchmark in November, with the outperformance almost exclusively due to strong security selection.

In terms of rating, and as is typical for our strategy, the bulk of the month's outperformance was concentrated in B-rated holdings, with BB-rated and CCC-rated positions minor contributors to November's excess return.

Sector-wise, the strategy's credit decisions in the Basic Industry and Consumer Cyclicals sectors were particularly impactful, with Technology and Transportation also delivering robust performances throughout the month. In contrast, individual credits in the Energy and Communication sectors underperformed.

Regarding bond issue sizes, the strategy's outperformance was split evenly between large and small issue bonds. Mid-sized issues, meanwhile, slightly detracted from overall performance during the month.

Outlook and positioning

Looking ahead to 2025, a consensus has formed between the largest banks and rating agencies that today's benign high yield default rate is likely to persist for the year and possibly through 2026. Among the reasons for continued moderation, firms are citing factors such as easing lending standards, declining distressed rates and relatively strong corporate fundamentals. Others, such as Barclays, still go so far as to cite the credit quality of 2025's approaching maturity wall as another reason for optimism, that is, these companies should be able to successfully refinance. This has all culminated in an expectation of a 1.25%-2% default rate for the high yield market in 2025, with some anticipating a 3% high yield default rate in 2026. (JP Morgan, Barclays, S&P).

Perhaps even more welcomed, however, are predictions of improvement in the leveraged loan market default rate in 2025. While there is seemingly universal agreement on the challenges to the market — higher interest rates today and weaker credit fundamentals for loan issuers, for example — there is equal mention of mitigating factors, such as potential rate cuts, refinancing activities and an improving economic backdrop that should help contain defaults. This has resulted in a projected loan default rate in the range of 2%–3% from those same institutions.

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About Mesirow

Mesirow is an independent, employee-owned financial services firm founded in 1937. Headquartered in Chicago, with locations around the world, we serve clients through a personal, custom approach to reaching financial goals and acting as a force for social good. With capabilities spanning Global Investment Management, Capital Markets & Investment Banking, and Advisory Services, we invest in what matters: our clients, our communities and our culture. To learn more, visit mesirow.com and follow us on LinkedIn.

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GIPS REPORT – HIGH YIELD COMPOSITE

Gross and Net of Fees Total Returns from January 1, 2014 – September 30, 2024

	Year end						Annual performance results				3-year annualized dispersion	
Year	No. of portfolios	Composite Asset at end of period ($MM)	MHY Assets at end of period ($MM)	Total Firm Assets ($MM)	Non paying fee (%)	Carve out (%)	MFIM (gross) Composite (%)	MFIM (net) Composite (%)	Bloomberg US Corp. High Yield Index (%)	Composite Dispersion [(1)] (%)	MFIM (gross) Composite[(2)] (%)	Bloomberg US Corp. High Yield Index[(2)] (%)
2014	8	593	797	–	1	0	3.14	2.68	2.45	0.7	4.01	4.50
2015	8	617	757	–	1	0	-1.02	-1.45	-4.47	0.7	4.26	5.26
2016	7	742	841	–	0	0	15.18	14.67	17.13	n/a	4.57	6.00
2017	5 or fewer	512	526	4,772	0	0	8.90	8.45	7.50	n/a	4.24	5.65
2018	5 or fewer	859	873	4,137	0	0	-1.02	-1.37	-2.08	n/a	3.76	4.59
2019	5 or fewer	1,124	1,199	3,895	0	0	13.02	12.58	14.32	n/a	3.74	4.02
2020	5 or fewer	1,338	1,407	6,706	0	0	9.00	8.55	7.11	n/a	12.23	9.24
2021	5 or fewer	1,301	1,421	6,168	0	0	12.12	11.67	5.28	n/a	12.08	9.00
2022	5 or fewer	717	898	3,616	0	0	-10.38	-10.76	-11.19	n/a	12.70	10.97
2023	5 or fewer	1,089	1,457	3,963	0	0	15.65	15.15	13.44	n/a	5.86	8.24
Current Performance Results												
2024	5 or fewer	1,402	2,615	5,203	0	0	8.15	7.80	8.00	n/a	5.76	8.40

Past performance is not necessarily indicative of future results.

Mesirow Financial Investment Management Institutional – Fixed Income claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Mesirow Financial Investment Management Institutional – Fixed Income has been independently verified for the periods 01.01.1996 through 12.31.2023. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards. Verification provides assurance on whether the firm's policies and procedures related to composite and pooled fund maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. The High Yield Composite has had a performance examination for the periods from 03.01.1999 to 12.31.2023. The verification and performance examination reports are available upon request.

*Creation date is 03.01.1999. * Performance and Composite inception are 03.01.1999.*
Benchmark returns are not covered by the report of independent verifiers.
All returns are calculated and presented in US dollars.

Mesirow Financial Investment Management, Inc. ("MFIM") is an investment adviser registered with the Securities and Exchange Commission under the Investment Advisers Act of 1940.ßor purposes of claiming GIPS compliance, as of 01.01.2010, the firm is defined as Mesirow Financial Investment Management - Fixed Income divisions. The Mesirow Financial Investment Management - Fixed Income groups specialize in managing portfolios for institutional clients adhering to an investment process geared towards institutional investors. The historical performance presented prior to the creation of the Mesirow Financial Investment Management - Fixed Income groups was managed by MFIM or its predecessor firms prior to 01.01.2005. MFIM provides investment management services to separately managed accounts, limited partnerships, public mutual funds/Registered Investment Companies (RICs) and Collective Investment Trusts (CITs).

The Mesirow Financial Investment Management - Fixed Income business unit includes the Mesirow Financial Investment Management - Strategic Fixed Income (formerly Core Fixed Income) group and the Mesirow Financial Investment Management - High Yield Fixed Income group and manages portfolios primarily for institutional investors adhering to an investment process incorporating fundamental analysis of security valuation factors and drivers. The composites within this business unit vary primarily by duration and the type of originator of the security.

Effective 10.23.2017, MFIM Fixed Income completed the lift-out of the High Yield team from a former and unaffiliated registered Investment Advisor.

Effective 05.29.2020, MFIM Fixed Income completed the lift out of the Analytic Fixed Income Team from a former and unaffiliated registered Investment Advisor, Chicago Equity Partners (CEP) which its team, became an integral part of MFIM Fixed Institutional Fixed Income. On 05.29.2020, MFIM acquired the asset management rights for a portion of the managed portfolios from an independent investment advisory firm and retained all the principals and employees related to such portfolios. Effective 11.30.2022, the MFIM Fixed Income - Analytic Fixed Income business discontinued operations. Accounts either transferred to the Strategic Fixed Income business unit or terminated its relationship with Mesirow.

The list of composite descriptions, the Firm's list of pooled fund descriptions for limited distribution pooled funds and the Firm's list of broad distribution pooled funds is available upon request. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. The Performance presented from 03.01.1999 to 4.30.2010 was generated while the Portfolio Managers were affiliated with a prior firm. Prior to 05.01.2010, the track record was reviewed for conformance with the portability requirements of GIPS standards. The predecessor firm was also verified, and the composite underwent a performance examination from inception in 03.01.1999 to 12.31.2009 by Ashland Partners & Company LLP. The High Yield Composite had been examined for the period of 05.01.2010 – 06.30.2016 while at Pacific Income Advisers (PIA). PIA had been verified for the period of 01.01.1994 – 06.30.2016.

The High Yield Composite consists of portfolios whose major concentration is in high yield bonds, both public and private. Equity-linked securities purchased in conjunction with debt securities, and equity securities obtained in exchange offers or insolvency proceedings, as well as leveraged corporate loans, and ETFs (in certain circumstances when onboarding a new account) may also be included. The portfolios are considered to be substantially fully invested, with minor cash holdings, at such time as the portfolio consists of at least 85% high yield bonds. This High Yield Composite definition was amended as of October 2019 to more fully reflect the intended strategy. On 01.01.2009, a substantially large equity position (comprising several securities) became non-discretionary and was transferred from the High Yield Composite portfolio when the client restricted the portfolio manager from selling the positions due to tax consequences.

Prior to 11.01.2010, the High Yield Composite was named the U.S. High Yield Composite. It is not for use with the general public and may not be redistributed. Please reference the last page of this presentation for important additional information.

Beginning 05.01.2010, composite policy requires the temporary removal of any portfolio incurring a client initiated significant cash inflow or outflow of 20% of portfolio assets or greater. Additional information regarding the treatment of significant cash flows is available upon request..

Prior to 01.01.2010, carve-outs reflect the capping of cash to 8% of Net Asset Value on an account which represents the personal holdings of one of the portfolio managers in order to align such cash amount to the level typical of an institutional account.

Calculation of Risk Measures: Annual / 3 Years Dispersion

(1). N/A = Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. Composite dispersion presented is the equal-weighted standard deviation of the gross annual returns of portfolios in the composite for the entire year.

(2). N/A = The 3-year Ex-post standard deviation isn't presented since there aren't 36 monthly returns available prior to this period. 1999 is a partial period from March 1 through December 31. The three- year annualized Ex-post standard deviation measures the variability of the composite gross returns, and the benchmark returns over the preceding 36-month period. It is not required to be presented for annual periods prior to 2011, or when a full three years of composite performance is not yet available.

Performance / Net of Fee Disclosure
Performance information that is provided gross of fees does not reflect the deduction of advisory fees. Client returns will be reduced by such fees and other expenses that may be incurred in the management of the account. Advisory fees are described in Form ADV Part 2 of MHY. As of 10.01.2013, net of fee performance was calculated using actual management fees. Prior to 10.01.2013, net of fee performance was calculated using the highest annual management fee applied to the gross results on a monthly basis. For the period 04.01.2011 through 09.30.2013, the highest management fee was 0.65%. Prior to 03.31.2011, the highest management fee was 0.50%. Actual investment advisory fees incurred by clients may vary. The management fee schedule is as follows:

High Yield Strategy (*described in MHY's Form ADV, Part 2*)
0.60% on the first $25 million
0.55% on the next $25 million
0.50% on the next $50 million
0.45% on the balance.

High Yield CIT
0.40% on all assets – Founder Class (First $100 million) [Closed]*
0.55% on all assets – Class A (under $25 million)**
0.48% on all assets – Class L ($25 million and above)**

*The Founders share class was closed to new investors 01.21.2022 after reaching $100 million in assets under management.
**Class A Units are available to Participating Plans investing less than $25 million and Class L Units are available to Participating Plans investing $25 million or more.
An actual fee charged to an individual portfolio may vary by size and type of portfolio. Fees are collected quarterly, which produces a compounding effect on the total rate of return net of management fees. As an example, the effect of investment management fees on the total value of a client's portfolio assuming (a) $1,000,000 investment, (b) portfolio return of 8% a year, and (c) 0.60% annual investment advisory fee would reduce the portfolio's value by $6,292 in the first year, by $36,614 over five years and $89,411 over 10 years. Actual investment advisory fees incurred by clients will vary.

Benchmark Definition
The primary benchmark was formerly the Credit Suisse High Yield Index. The benchmark was changed to the Barclays U.S. Corporate High Yield Index on 05.01.2010, since the Portfolio Management Team believes it is more commonly recognized as the industry standard index for the high yield asset class. The index was renamed the Bloomberg Barclays U.S. Corporate High Yield Index, following Bloomberg's acquisition of Barclays Risk Analytics and Index Solutions (BRAIS) in August of 2016. The Bloomberg Barclays fixed income benchmark indices have since been rebranded as the "Bloomberg Indices" as of 08.24.2021, further updating the benchmark name to the Bloomberg U.S Corporate High Yield Index. The Bloomberg U.S. Corporate High Yield Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on Bloomberg EM country definition, are excluded.
Mesirow Financial Investment Management, Inc. and its affiliated companies and/or individuals may, from time to time, own, have long or short positions in, or options on, or be a market maker in, any securities discussed herein and may also perform financial advisory or investment banking services for those companies.