



U.S. Credit Update – August 31, 2021

- Sector Performance Recap
- Industry Total Returns and Spread Performance
- Reported Data and Real Time Indicators
- Scenario Analysis
- Weekly Feature – Investor Flows
- Issuance Recap



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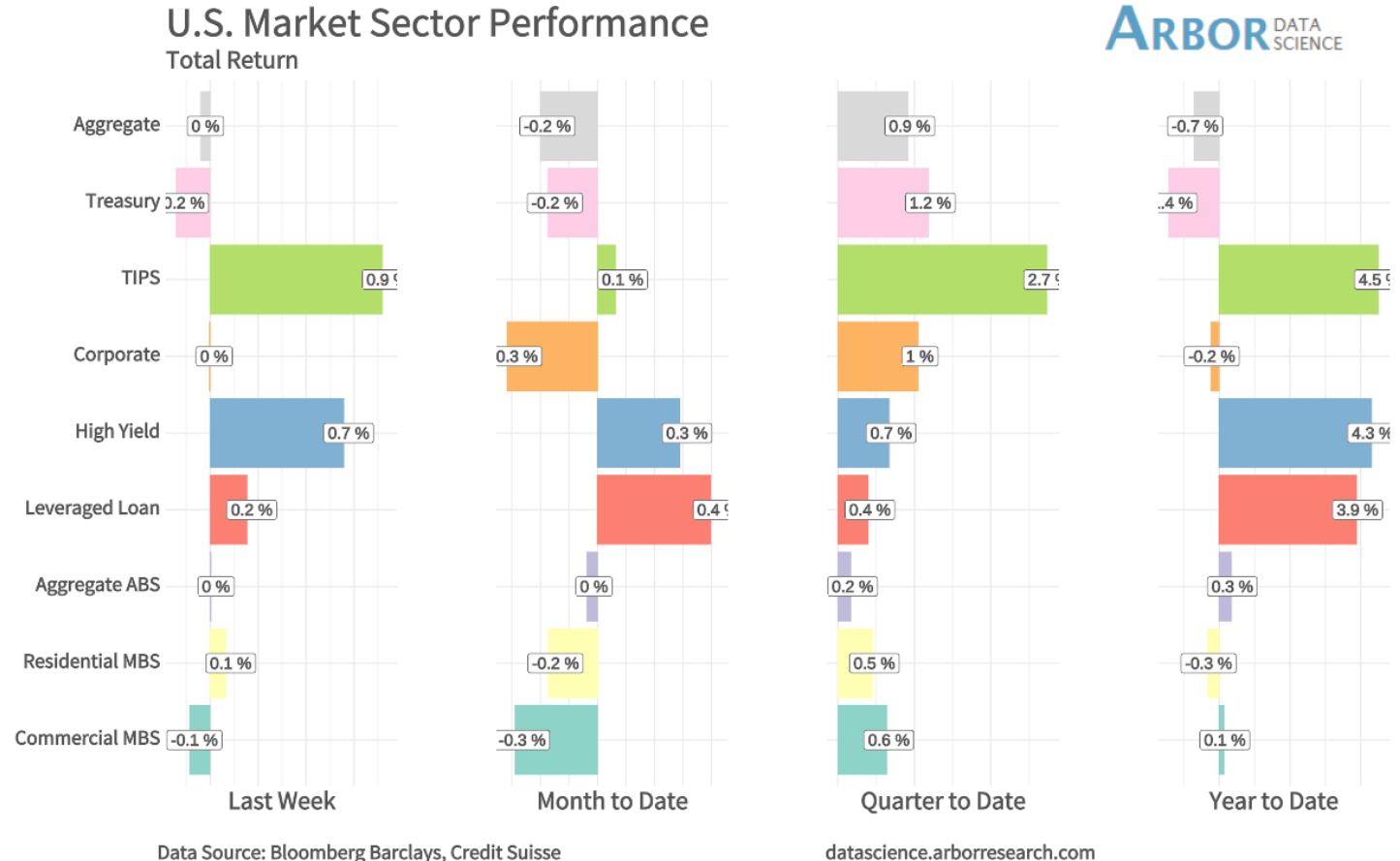
Sector Total Returns

Bond Performance Mixed Last Week

TIPS performed the best last week returning 0.9% followed by HY Corporates which returned 0.7%.

Safer assets remain in the hole for the year. Investment grade corporates are -0.2% and USTs are down -1.4% for the year. TIPS have fared better with a total return of 4.5%.

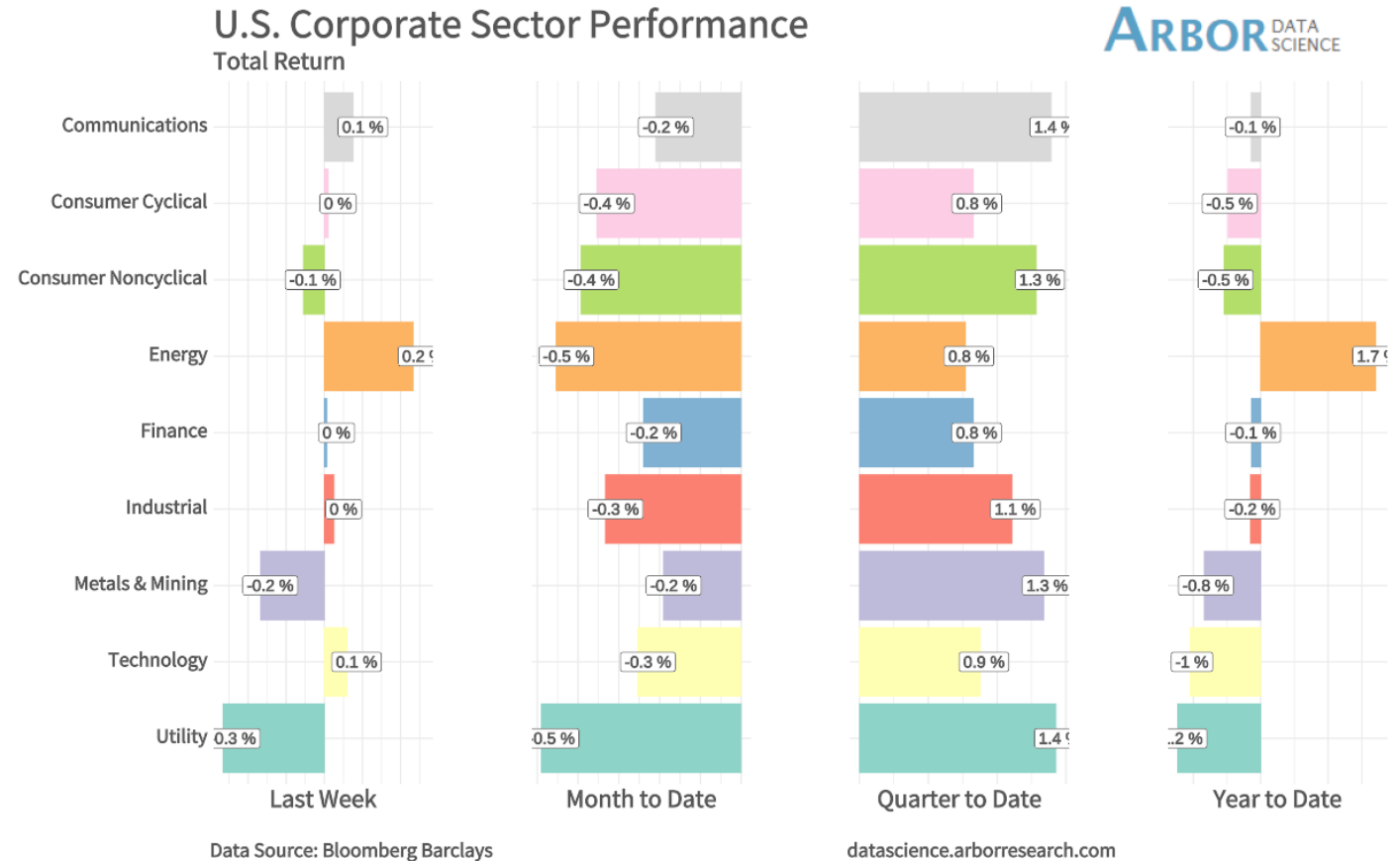
Riskier Assets have performed well for the year. High Yield Corporates and Leveraged Loans have returned +4.3% and +3.9% YTD, respectively.



Sector Total Returns

Energy Outperforms

Corporates mostly fared poorly last week. Energy performed the best with a total return of 0.2%. Energy is also still the best performing sector year to date.

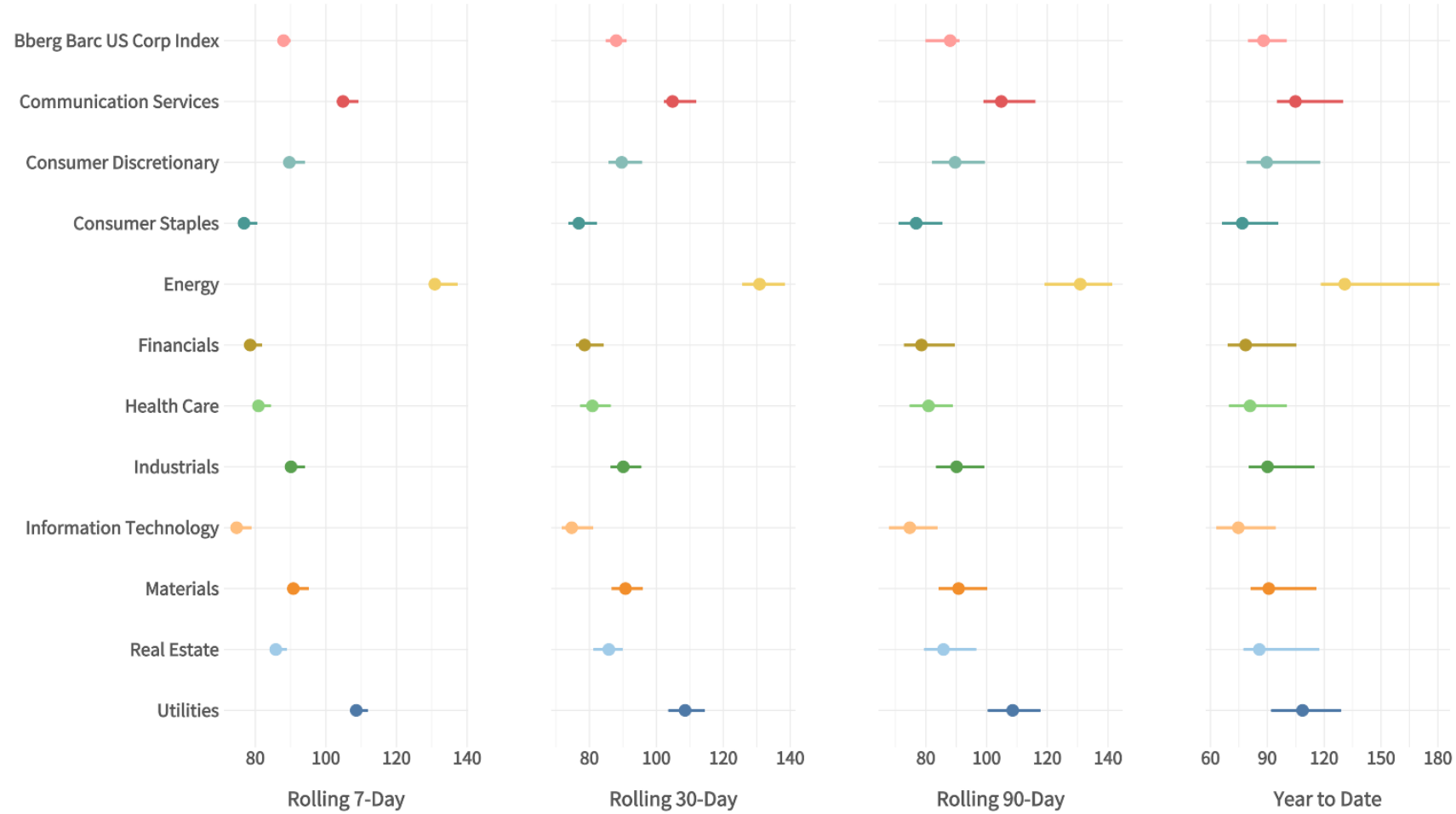


Sector OAS

U.S. Investment Grade Credit Options-Adjusted Spread

Range of OAS over Period

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Data Source: Bloomberg, LP

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Industry Excess Returns – Spreads remain stable

Brokerage and banking reversed the previous week’s trend, tightening by a basis point or two last week. Clients were better buyers of the sector by a 1.2:1 margin, though volumes remained subdued.

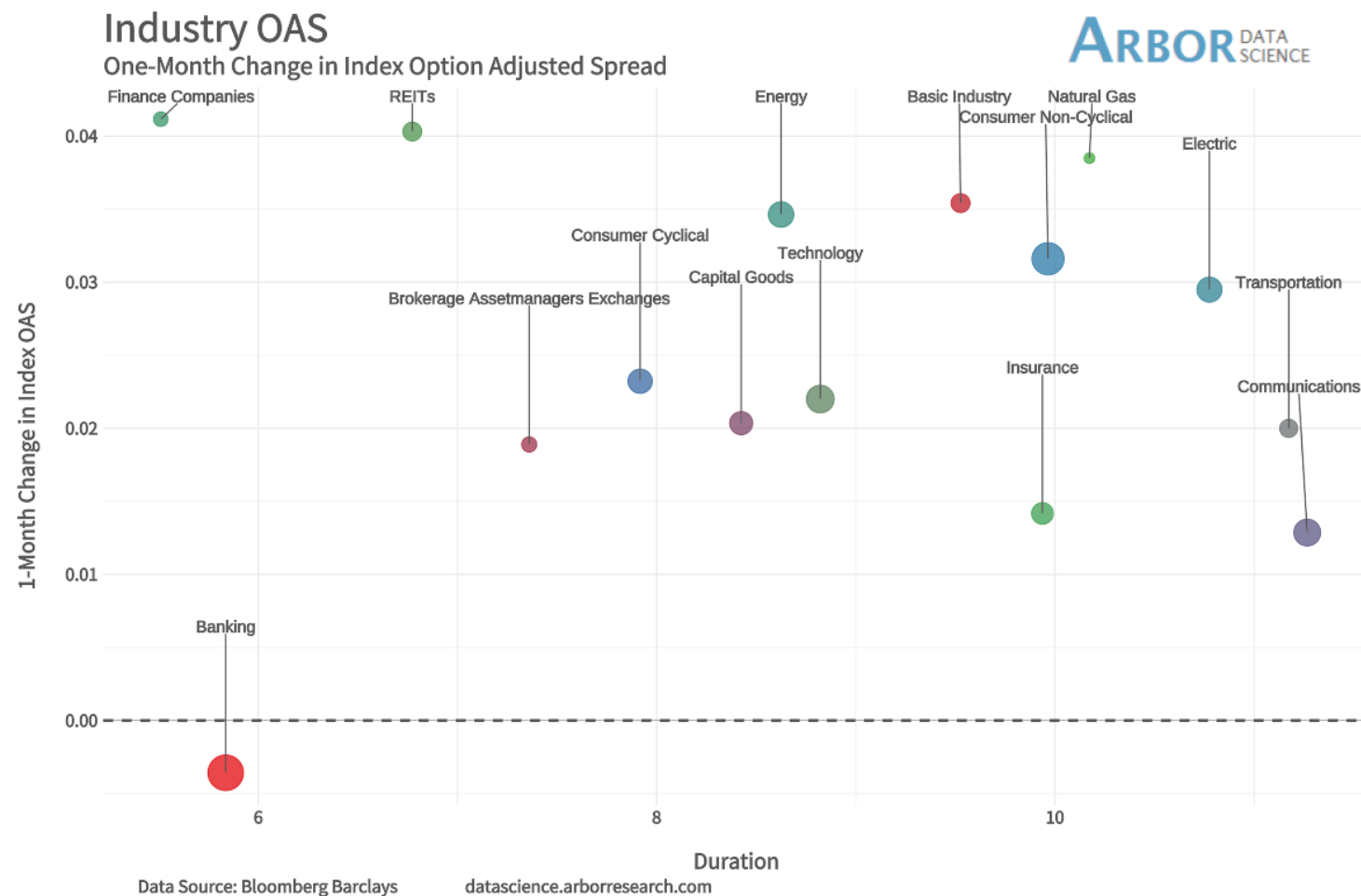
This chart shows three-month excess returns over benchmark Treasuries versus weighted average duration for Bloomberg Barclays investment grade indices.



Industry Spread Performance – Volatility Limited

It was a good week for the basic industry spreads. The sector saw better buying by 1.2:1 margin, led in large part by a very small new issue calendar.

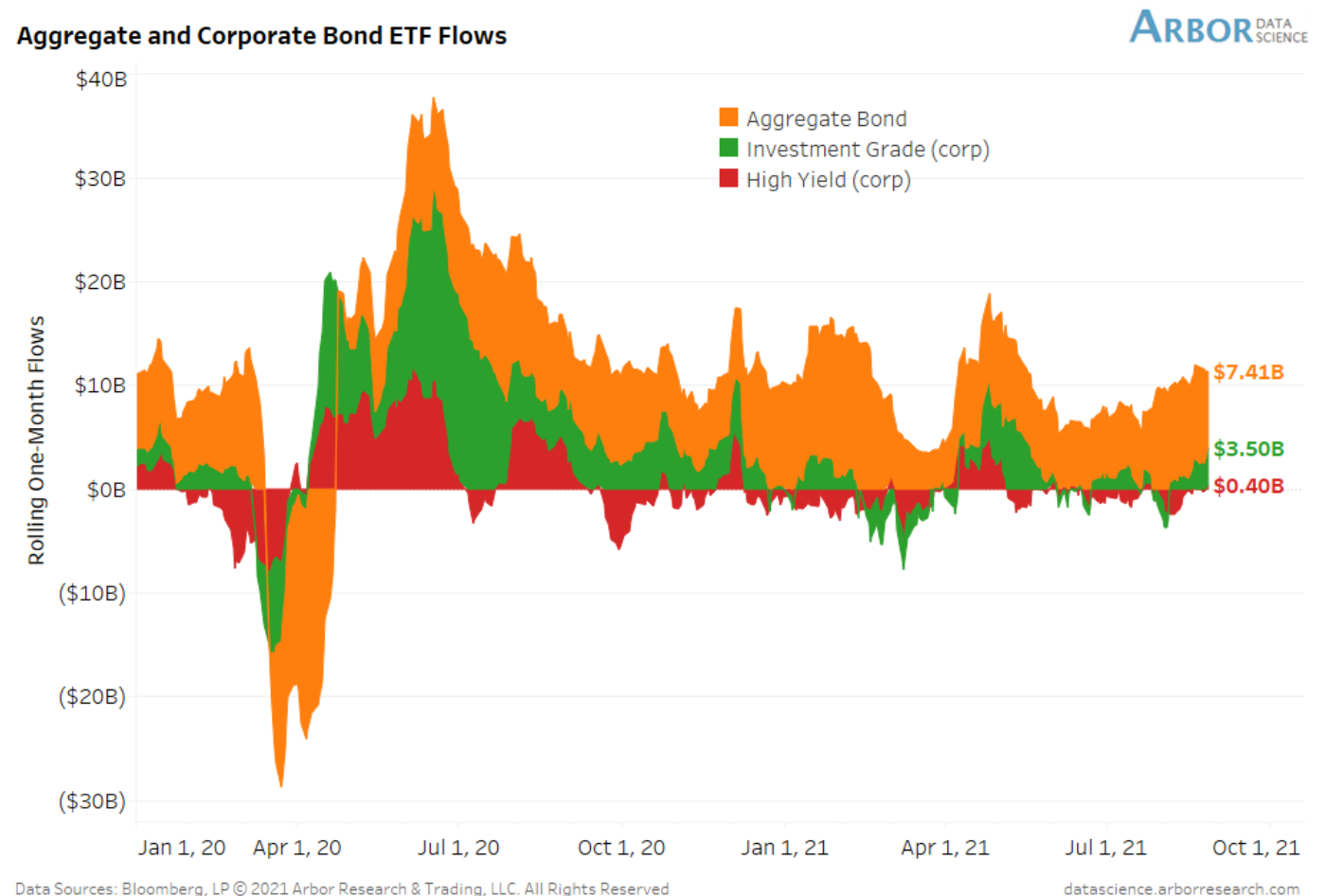
This chart shows one-month changes in index option-adjusted spread (OAS) versus weighted average duration for Bloomberg Barclays investment grade indices.



Reported Economic Data – Aggregate and Corporate Bond ETF Flows

Aggregate bond funds remain the top dog among fixed-income funds, taking in \$7.4 billion over the past month. Investment grade corporates are finally seeing steadily improving demand at a pace of \$3.5 billion. High yield corporates have yet to see strong flows either way.

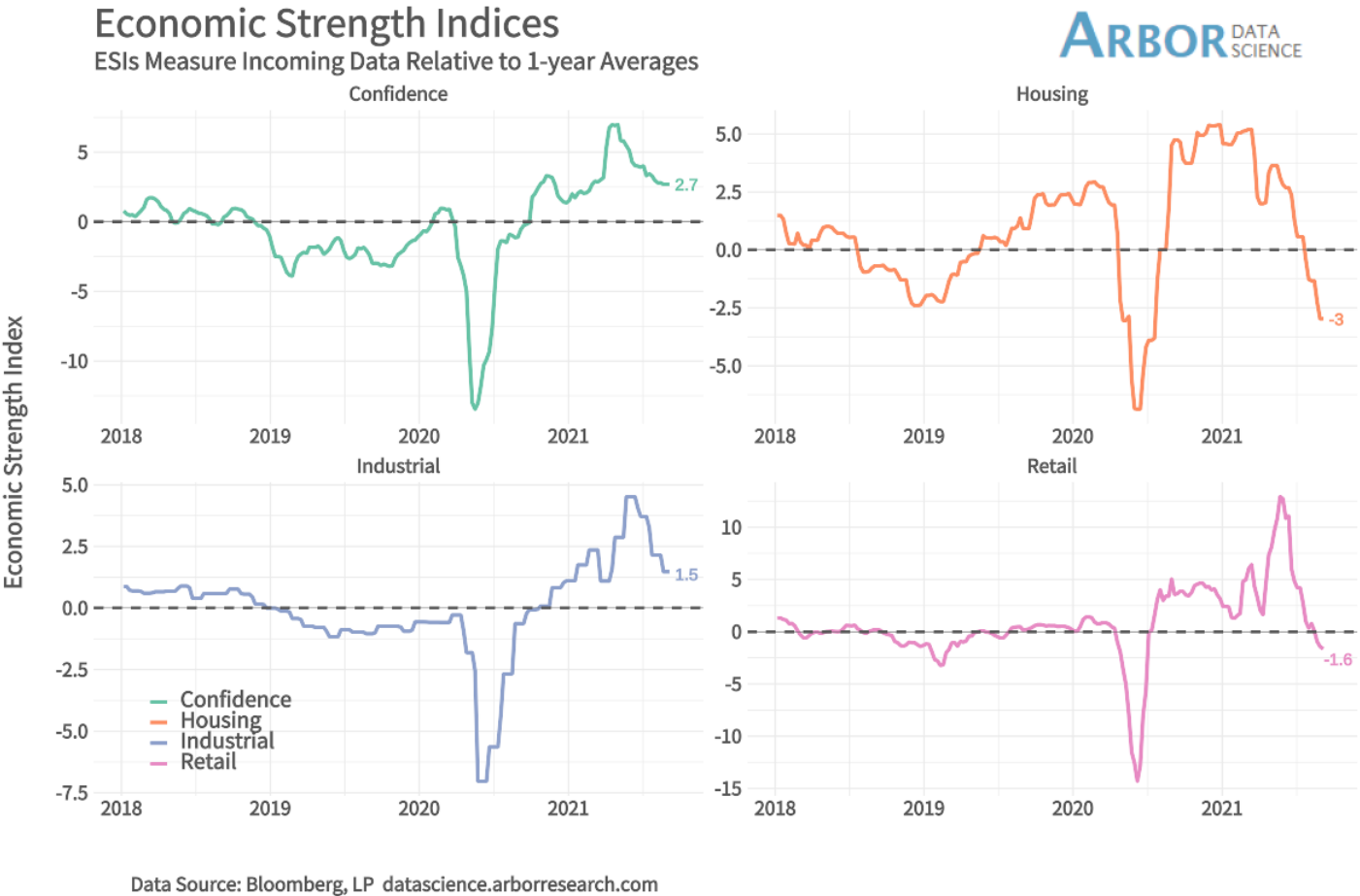
The chart shows stacked rolling one-month flows into bond ETFs.



Reported Economic Data - Economic Strength Indices

Economic strength in retail and housing continue to decline with housing strength at its lowest since early in the pandemic. Whether transitory or not, consumers are experiencing higher prices in their day-to-day outings which certainly has impacted the retail and housing sector as well as consumer confidence.

The chart shows our Economic Strength Indices for global industrial activity by region. ESIs measure incoming data relative to one-year averages.

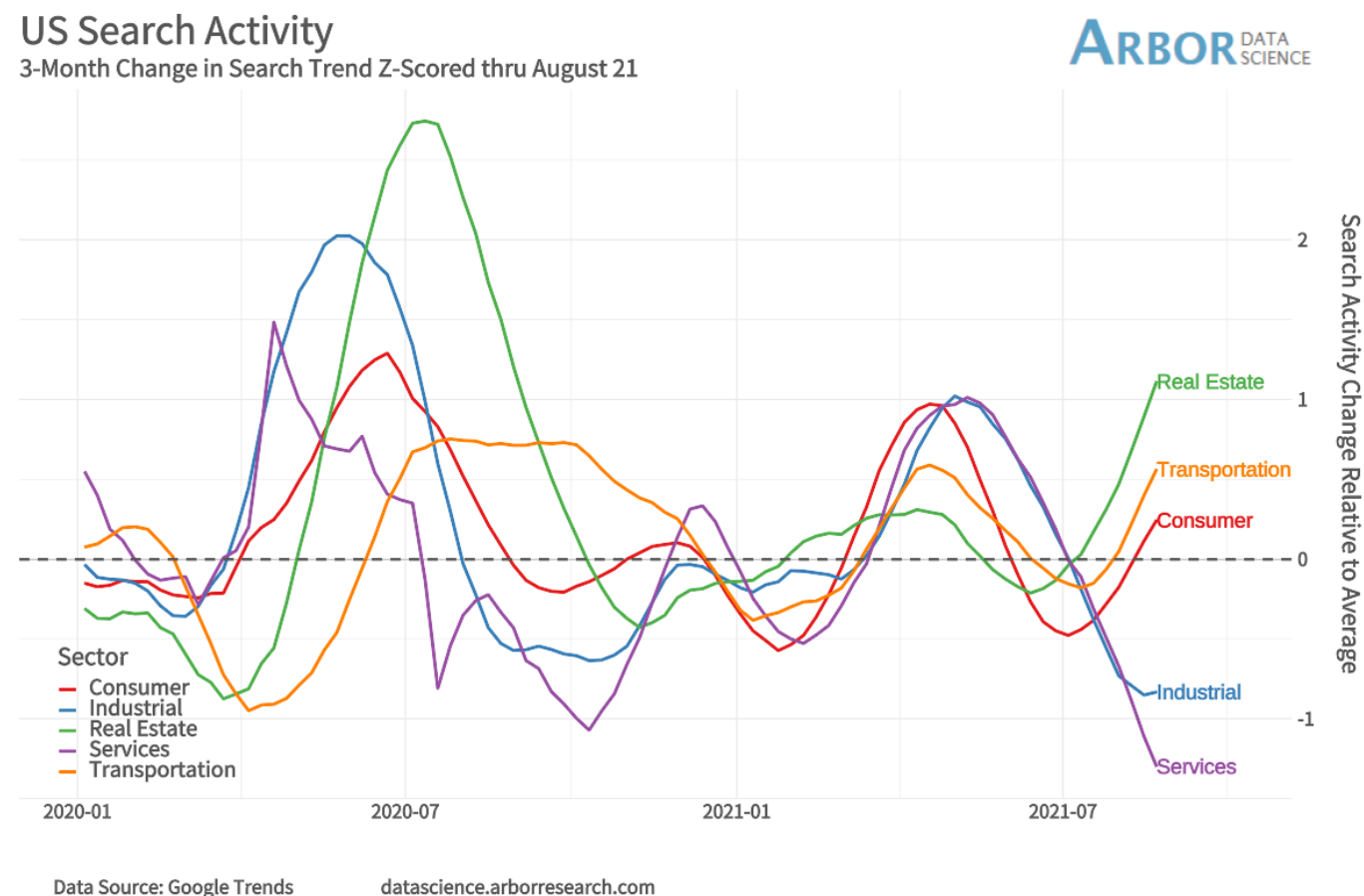


Real Time Indicators – Google Search Activity

US Google search activity has been less unified since the reopening burst that increased searches across the board. Real Estate searches have seen a massive second wind with Transportation and Consumer Sector search trends not far behind. Services and Industrial searches, on the other hand, have plummeted.

The Delta variant among other supply chain constraints continue to threaten U.S. economic stability.

The chart aggregates Google searches across several dozen topics, showing the three-month change in search activity relative to historical average in five key sectors.

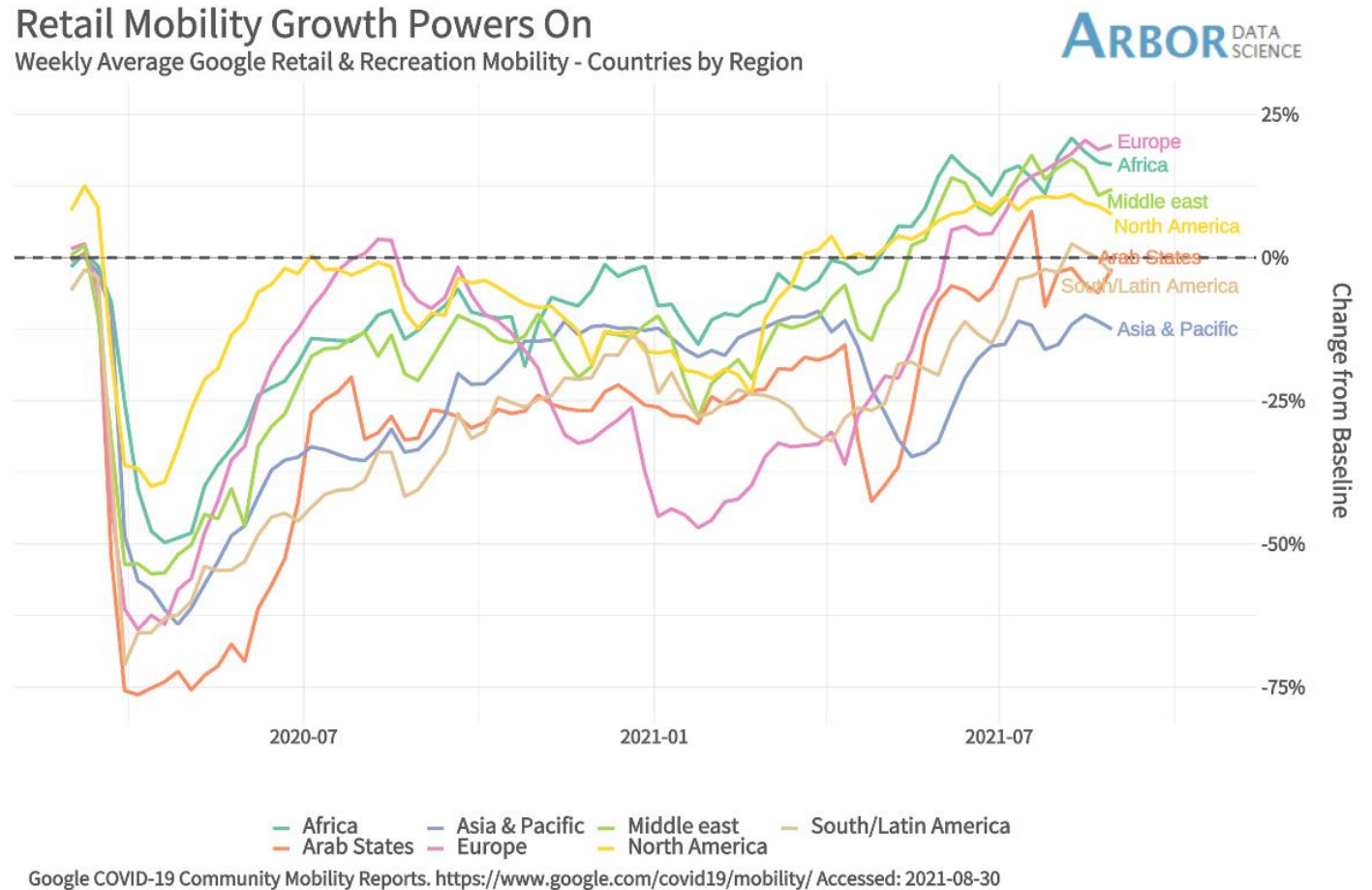


Real Time Indicators – Mobility

Google's retail & recreation mobility has stagnated across the world. North America has seen a distinct decline in mobility along with Africa, the Middle East, and South/Latin America. Europe has maintained its momentum for the most part.

Asia's mobility remains below baseline and has begun to decline again.

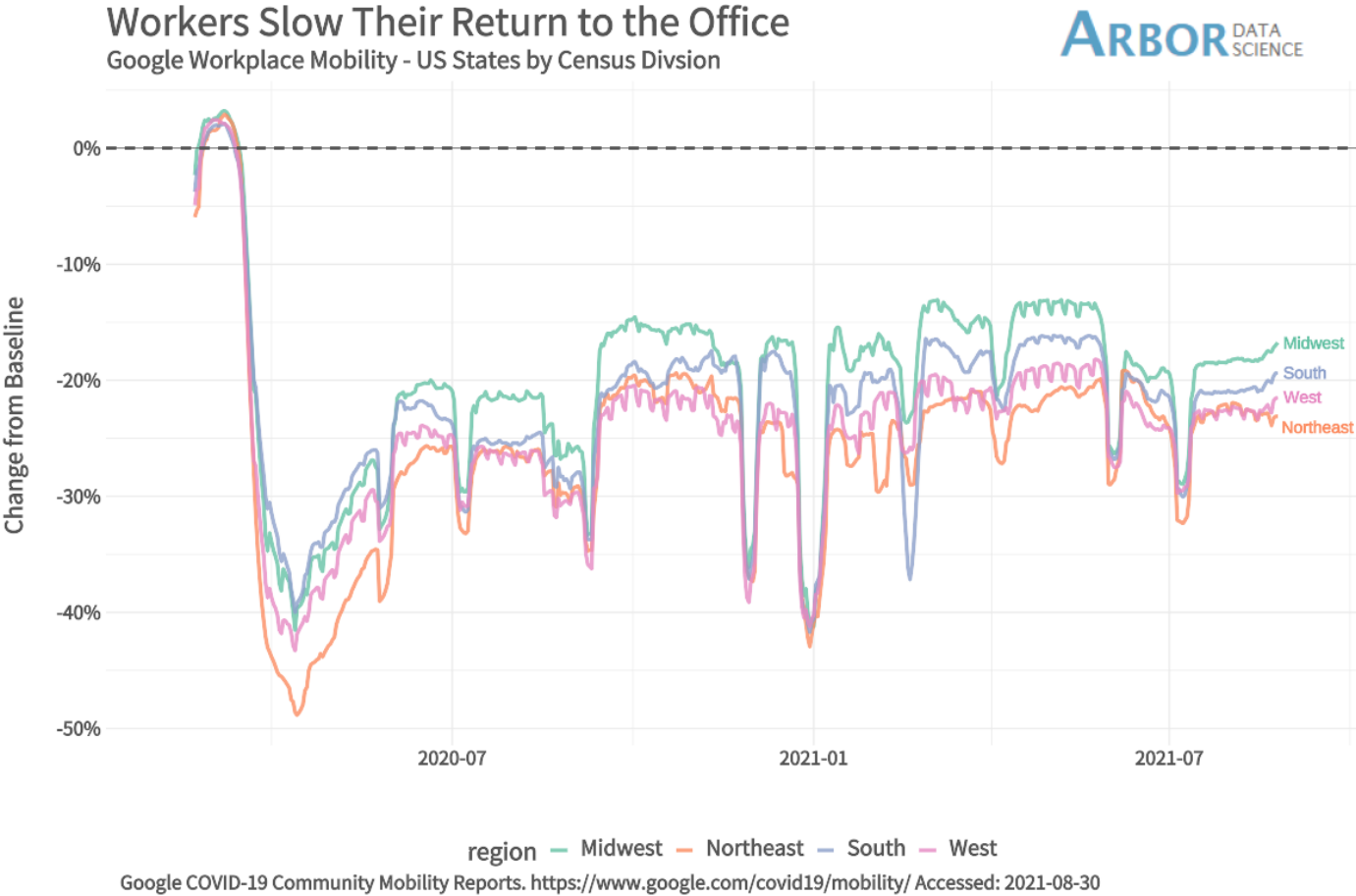
The chart shows global 7-day averages of Google's retail & recreation mobility relative to the pre-lockdown baseline by census region.



Real Time Indicators – Mobility

Workers are finally beginning to show signs of a return to the office despite many major companies pushing off the return for several more months due to rising Covid-19 cases. It's probable that this can be attributed to school starting up again and parents not needing to be home to care for children all day.

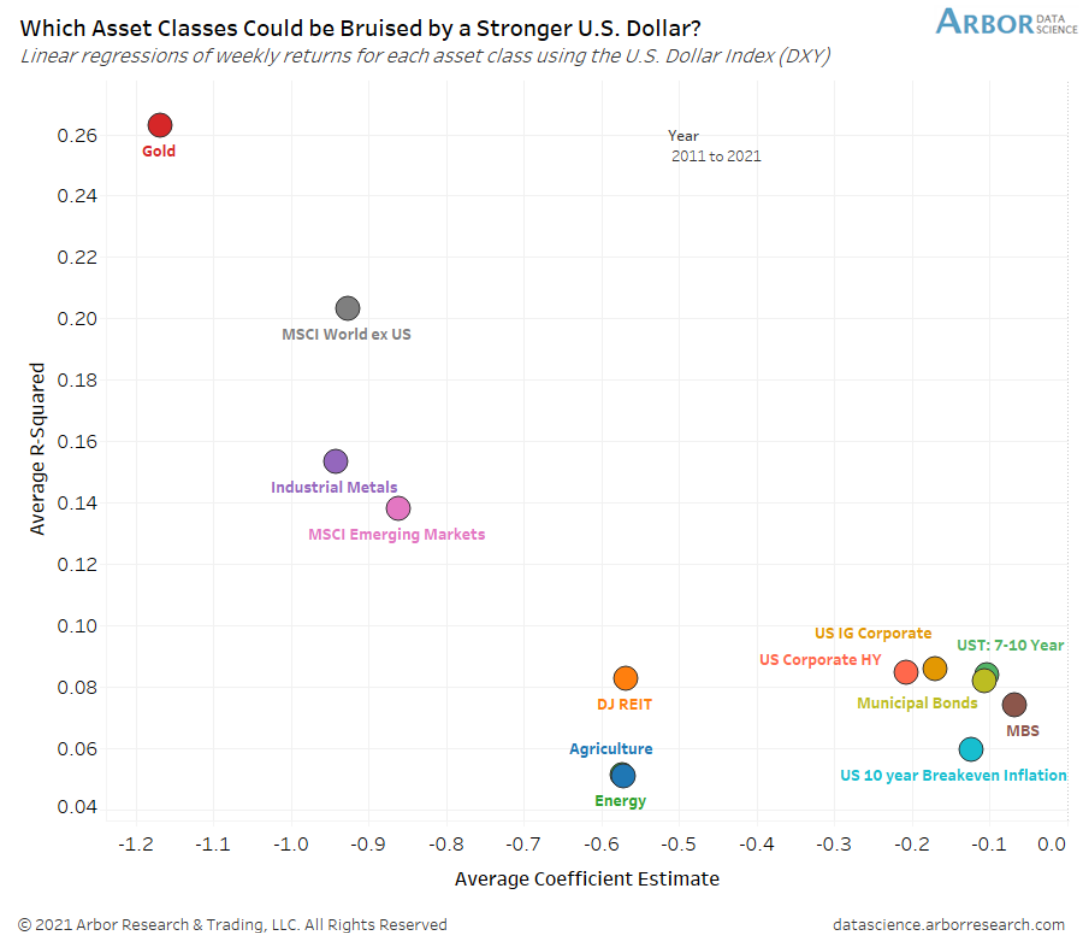
The chart shows select Google US Workplace Mobility by region.



Scenario Analysis – Rising Real Yields and USD

The next set of analysis focuses on the impact of a rising US dollar and US 10-year real yields (TIPS) on major asset classes.

The relationship since 2011 between weekly returns for each asset class and the US dollar is the most negative (and significant) for gold, global ex-US equities, and industrial metals. We just saw how quickly gold dropped (-2.3%) in response to the non-farm payrolls beat sending the US dollar higher and emboldening taper expectations.



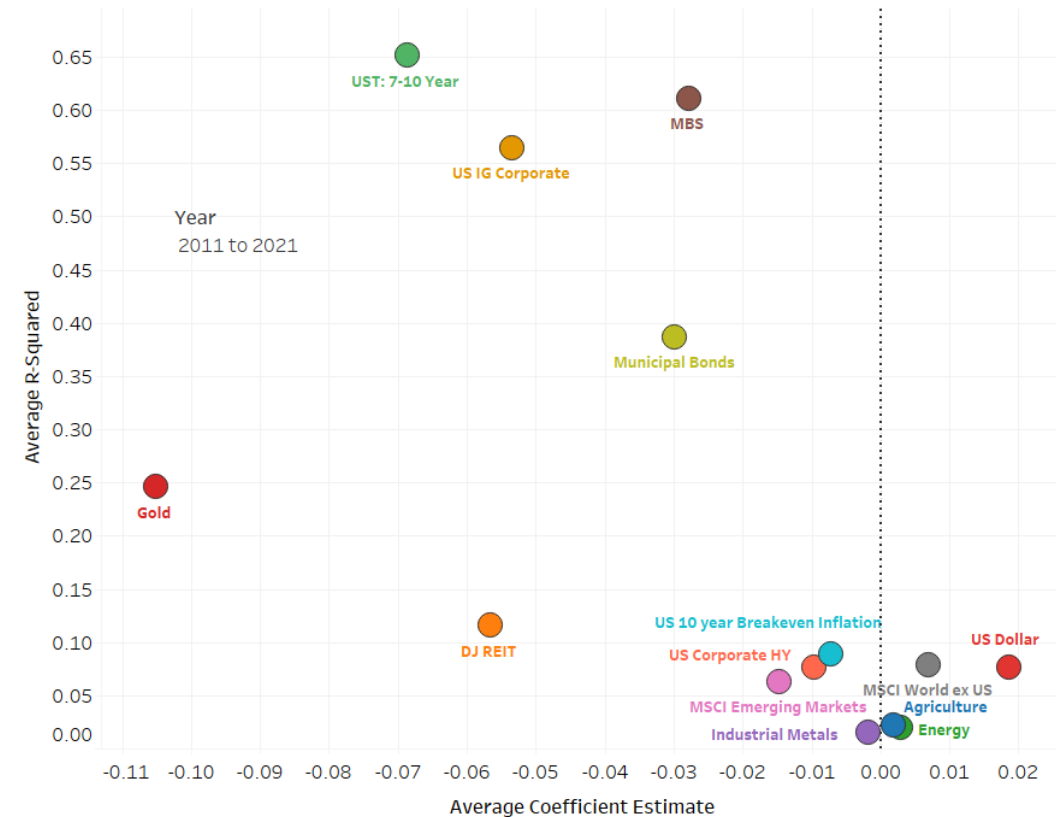
Scenario Analysis – Rising Real Yields and USD

The US dollar would benefit from rising real yields, which would also be a negative for gold. Additionally, US Treasuries, investment grade corporates, and REITs would face headwinds.

Which Asset Classes Could be Bruised by Higher Real Yields?

Linear regressions of weekly returns for each asset class using U.S. 10-year real (TIPS) yields

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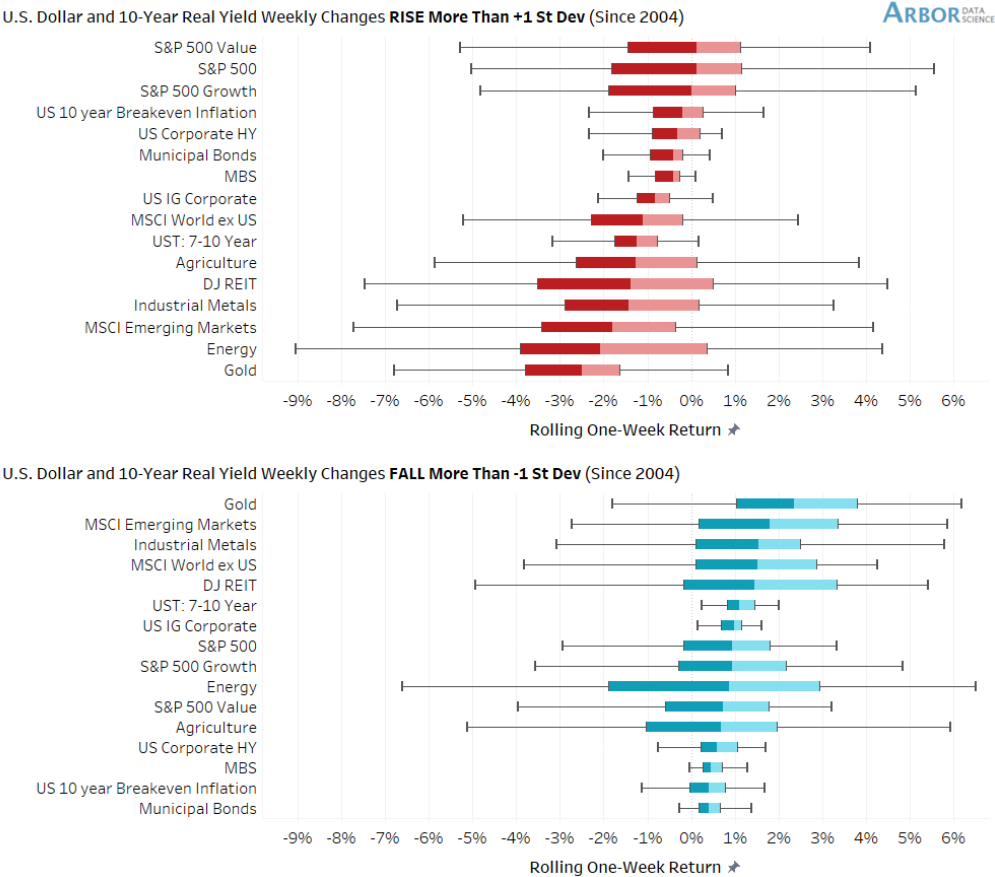
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Scenario Analysis – Rising Real Yields and USD

For a different perspective the final set of charts show the returns by each asset class when the US dollar and real yields rise in unison greater than one standard deviation above average.

Unfortunately, this scenario is not favorable for investors with median weekly returns negative across risk and safe assets.

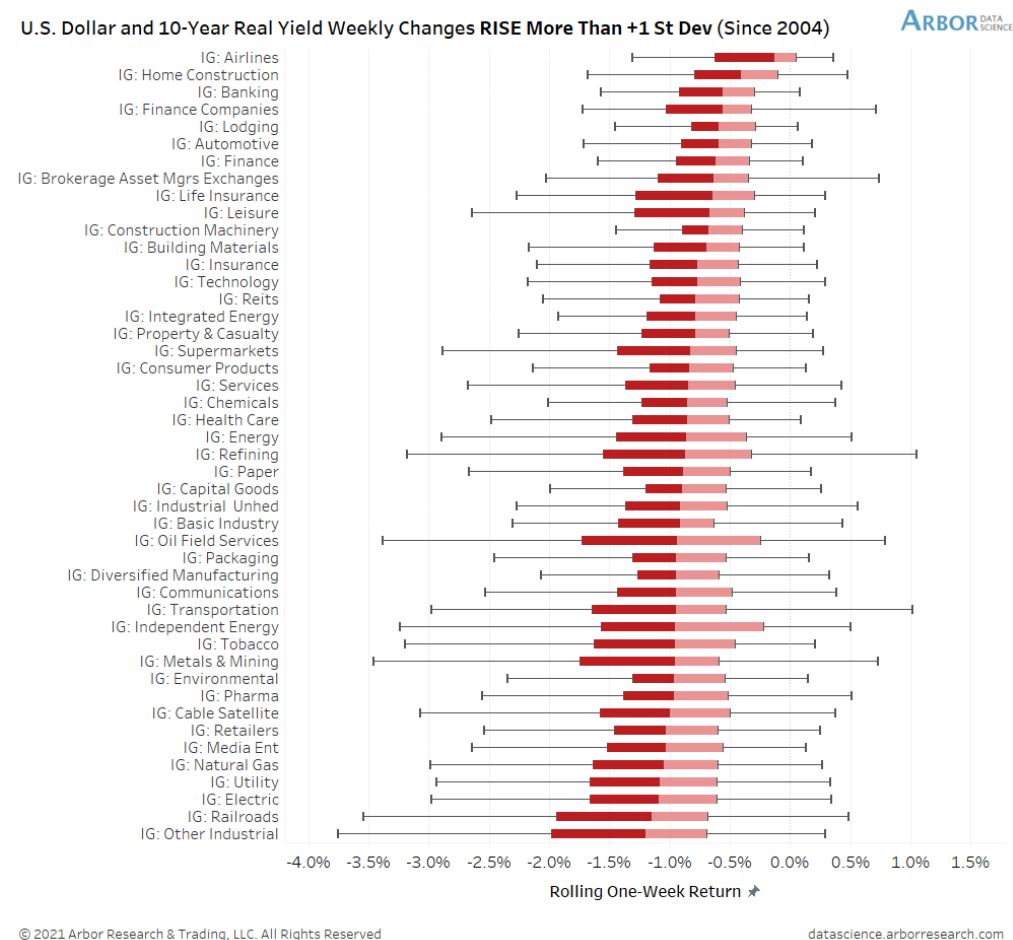
Again, gold suffers the most followed by emerging markets and major commodities.



Scenario Analysis – Rising Real Yields and USD

As for investment grade industries, returns tend to stay in line with average duration. Higher duration industries like railroads and utilities suffer the heftiest losses, while shorter duration industries like airlines remain most insulated.

In this event, investors would benefit from shortening duration into the global shift toward hawkish policy.



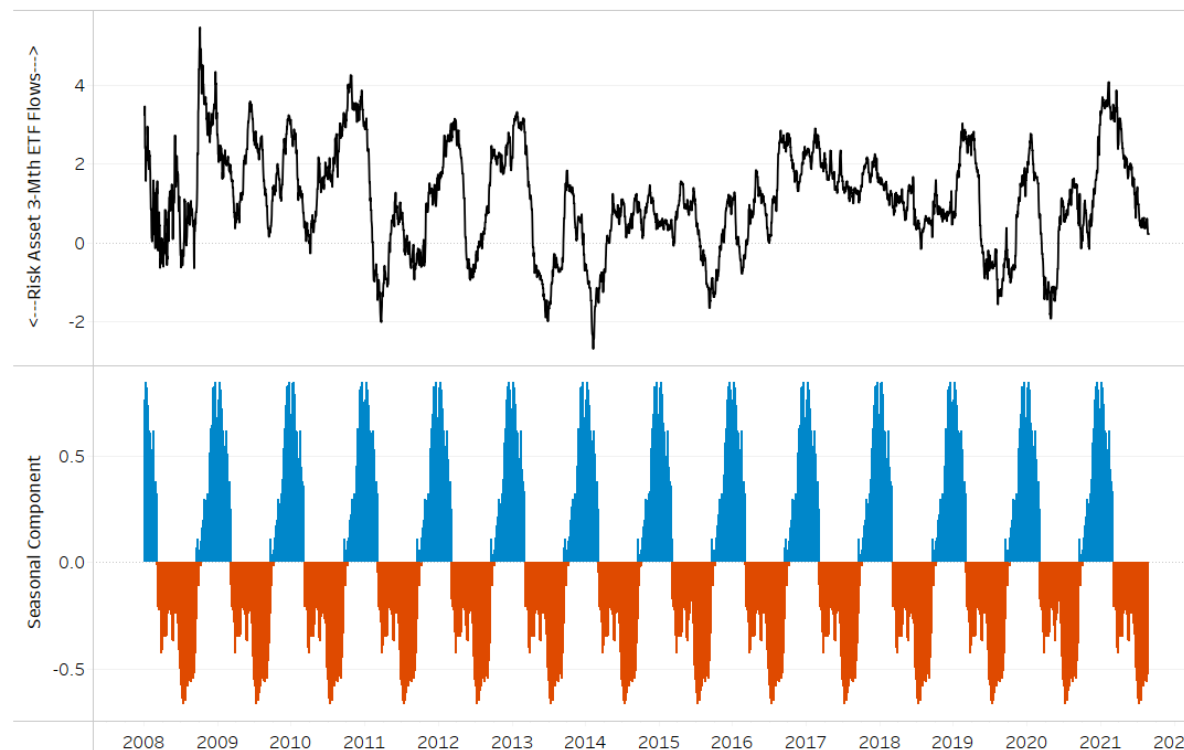
Weekly Feature – Investor Flows

Investors habitually revert flows back into riskier investments including emerging markets, high yield corporates, and small caps from September into year-end. Could a similar cycle be underway in 2021?

Risk Asset Flows Enter Favorable Seasonal Period by Mid-September

Risk asset flows as z-scores = emerging mkts, high yield corps, and small caps

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Weekly Feature – Investor Flows

Bigger picture, investors could really do no wrong with nearly all asset classes producing very favorable risk-adjusted returns. In fact, the average Sharpe ratio across the range of assets has persisted above 1-to-1 for a record 270 trading days!

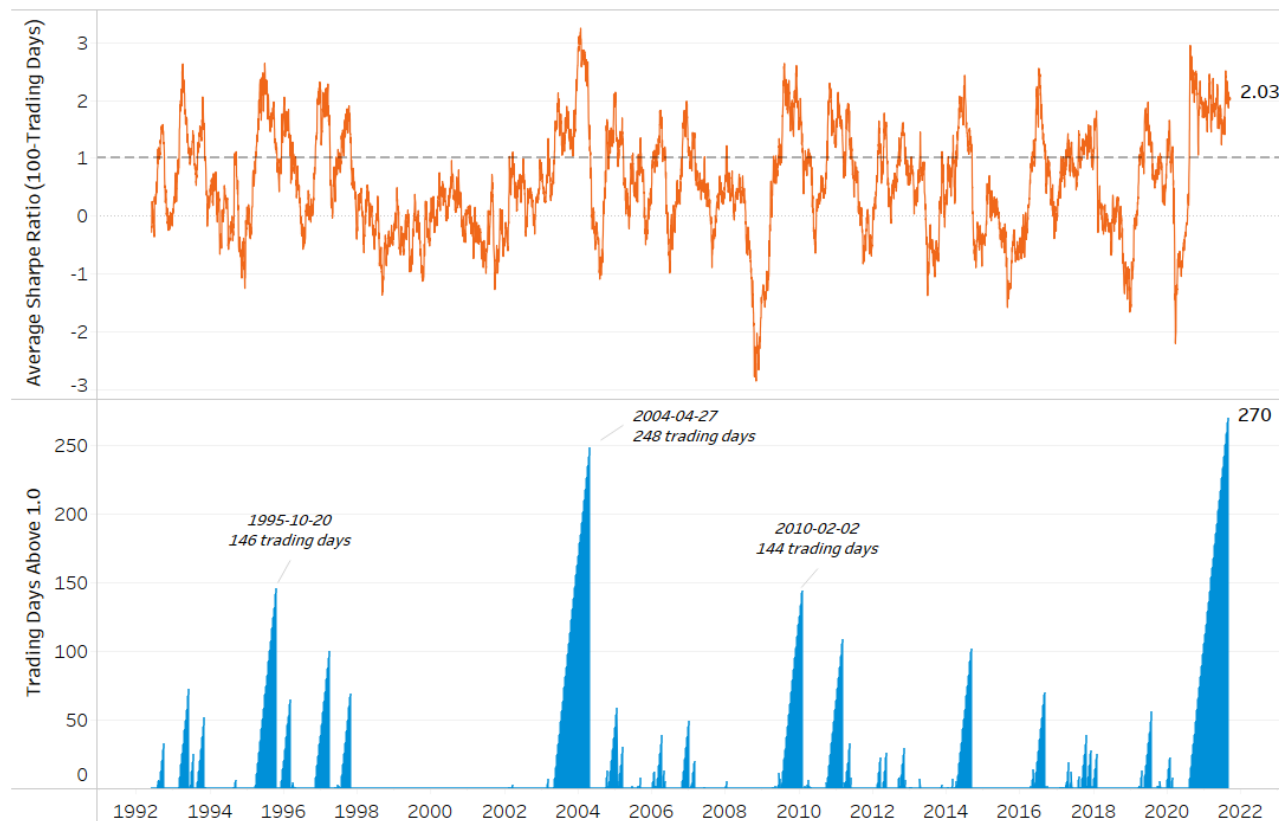
[A favorite chart of ours over the past two weeks](#) has been of tightly huddled together Sharpe ratios. Their range is on par with only two periods in history, which both occurred ahead of tightening cycles.

Read the full post here: [Investor Flows: The Everything Rally Becomes the Longest on Record](#)

The Everything Rally of 2020/2021 the Longest on Record

Average Sharpe ratio across agriculture, industrial metals, US inv grade corps, USTs, TIPS breakevens, S&P 500, MSCI World ex-US, and REITs

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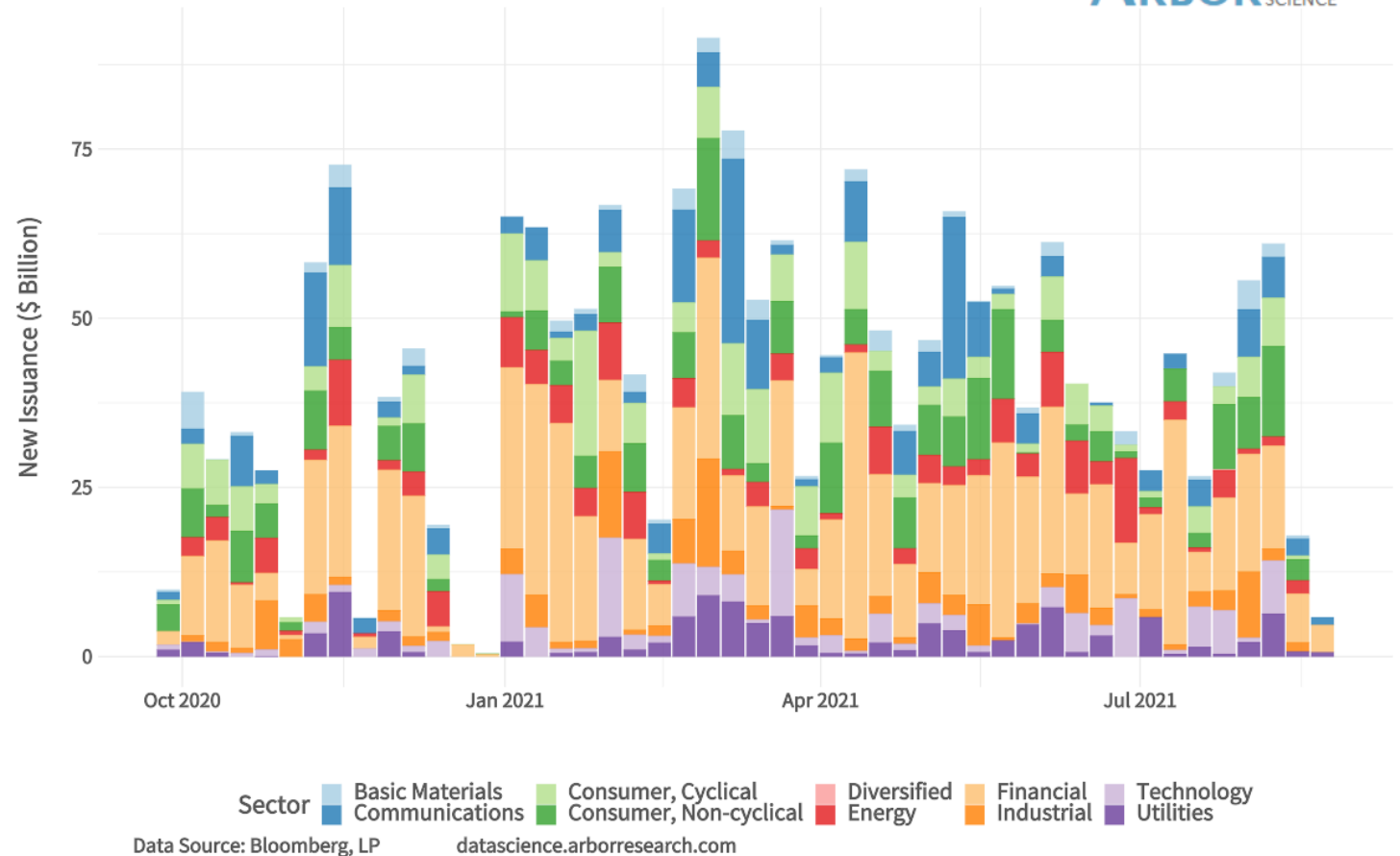
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Issuance Recap

Primary issuance was negligible last week, registering as the lightest week of the year. This week expected to be very soft as well, before we see heavy issuance pick up after the Labor Day holiday.

Weekly U.S. Corporate Issuance - Last 11 Months

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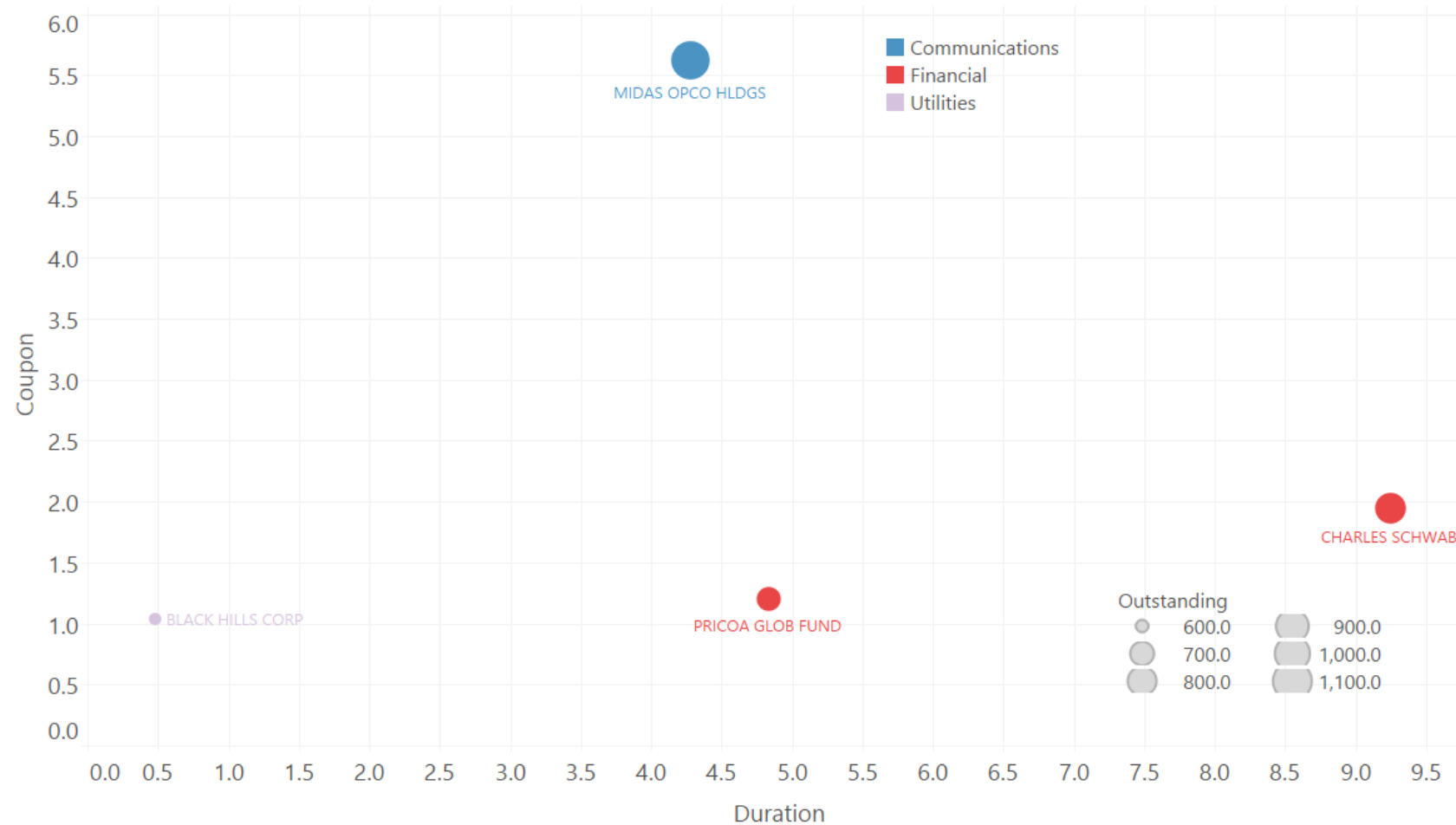


Issuance Recap

New Credit Issuance - Last Week

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Coupon vs. Duration



Data Source: Bloomberg LP

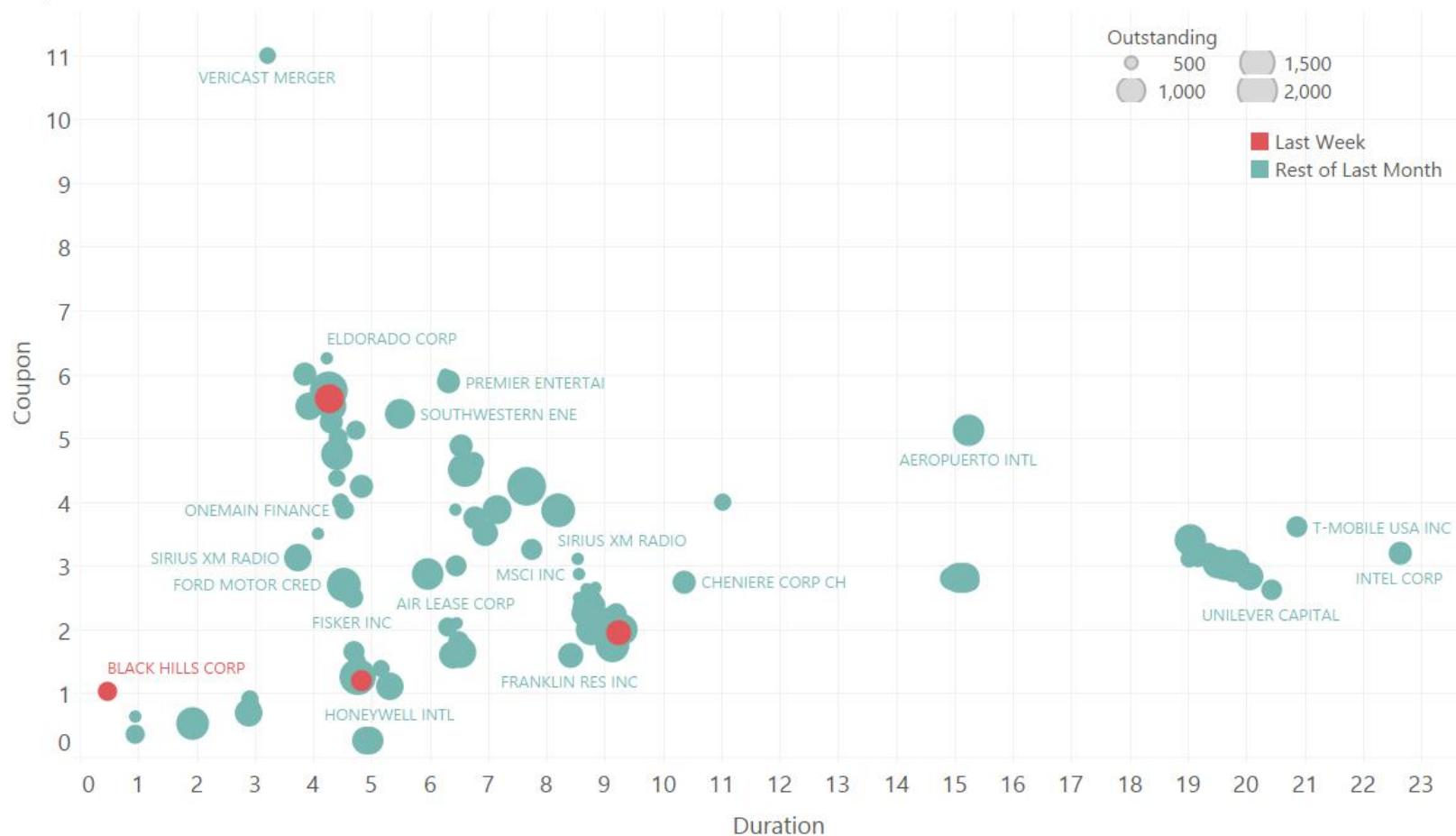
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Issuance Recap

New Credit Issuance - Last Calendar Month

Coupon vs. Duration

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Data Source: Bloomberg LP

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