# Rebound and Recovery

**November 2020 Commentary**

**Corporate bond markets continued to perform well in November, helped by positive news on the vaccine front.** At the start of the month, attention was focused on the US Presidential election. While the outcome of that contest was received favorably by markets, it was positive news from three drug companies on vaccine treatments that drove market sentiment through the balance of November. While the number of COVID-19 cases continues to escalate across the globe, investors are focusing on the "light at the end of the tunnel." Consequently, sectors and industries that were hit hardest earlier in the year have been the best performers recently – for example, Travel, Leisure, and Real Estate. We believe opportunity persists in the large valuation gaps that still exist in the market following the "K-shaped" recovery that markets have seen since March.

**It was a surprise not to see the US Primary and Secondary Market Corporate Credit Facilities extended beyond December 31st.** These two support mechanisms were put in place by the Federal Reserve ("Fed") following the liquidity crisis in March. The Primary Program provided a funding backstop for eligible corporations to enable them to access debt markets. The Secondary Program aimed to support market liquidity and involved the Fed purchasing corporate bonds in the market. In July, the expiration date of the programs was extended from September 30th to December 31st. Most market participants, including us, anticipated a further extension this month. However, the Treasury Secretary, Steven Mnuchin, decided not to extend these facilities beyond year-end. Mnuchin also asked the Fed to return the $455bn in taxpayer money that the Treasury provided to fund these and other programs. The funds can then be re-allocated by Congress for COVID-related fiscal relief.

**Market reaction was muted given the programs have been little used since the summer and credit spreads were relatively stable on the news.** We believe this is because to this point, actual central bank purchases have been largely symbolic. The purchases total less than $15bn and the majority of these occurred during the summer. Originally, the Fed and the financial media had talked about a potential $750bn in purchases of corporate bonds. This huge number had the desired effect, and the announcement was sufficient to give investors the confidence needed to buy corporate bonds. The Fed therefore did not need to act aggressively. As things stand, the Fed will have less ammunition going forward, although recent statements have reaffirmed that policy will remain very accommodative. In addition, we may see this decision reversed by the new Treasury Secretary (Janet Yellen) in the new year. We also point to the quick reinstatement of 2008 facilities during March of this year. We believe the bar to reinstate Fed purchases is low.

**We have been selectively adding positions with strong fundamentals but upside to the economy re-opening.** In general, we reduced risk in our portfolios during November as certain positions in the portfolios started to approach fair value. We continue to invest in defensive sectors and businesses with ample liquidity. Complementing this core focus, our credit research team has identified specific companies with strong fundamentals but more upward sensitivity to vaccine news. This has resulted in some of our mandates adding to sectors such as Aircraft Leasing and Real Estate. However, our approach has been highly selective and focused on issuers with strong balance sheets that are well-positioned to withstand shorter-term risks arising from lockdowns. We continue to closely follow the public health data and vaccine developments where consensus is forming around extensive inoculation by Q2 2021 and a rebound in economic activity in Q3. As this plays out, we expect to see performance in bonds issued by these companies.

**Given current valuations we are cautious and the focus in 2021 will be on credit selection within deleveraging companies and sectors.** We believe that with ultra-low yields and credit spreads where they are, the key to success in the new year will be a very selective approach. With wide dispersion in credit spreads and divergent company fundamentals, the real opportunity lies in identifying relative value opportunities in the marketplace. A key component of this is the credit research team identifying ratings migrations before they occur and investing to benefit. With a large amount of cash on their balance sheets, but also high leverage, a constructive backdrop in 2021 will provide the opportunity for issuers to decrease leverage and improve fundamentals. Although the market consensus is positive, there can always be volatility in the markets. As we close the year, our strategies are positioned to withstand volatility if it arises and capitalize on opportunities presented by the ongoing recovery.

### Important Information

Data as of November 30th, 2020. Source: Bloomberg.

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