Steinberg High Yield Fund Quarterly Commentary

Lorne Steinberg Wealth Management

A High Income Opportunity

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Environment

The high yield market enjoyed another quarter of positive performance in Q1'2024 as investors embraced risk while tempering rate cut expectations as strong economic data continued to support the FED stance of holding rates. January was the weakest month as markets slowed and digested the rally that occurred in December. As the quarter progressed, February and March data caused the market to revise expectations from five cuts (1.25%) this year down to three (.75%). March was the strongest month in the quarter as investors continued to embrace risk and were spurred by economic data that reinforced views of a soft landing. The FED remained on hold during the quarter while reiterating their outlook of expected rate cuts of about 75 bps for the year, but stressing that it is still data driven and subject to adjustment. This view was reinforced by resilient economic data and persistent inflationary pressures that warranted a longer hold before beginning the rate cut cycle. With central banks remaining idle, the US 10-year bond yield moved higher, ending the quarter at 4.20% compared to 3.88% seen at the end of Q4'2023. On the commodity side, oil prices were higher during the quarter as OPEC production cuts and rising tensions in the middle east firmed oil prices during the quarter. WTI Crude ended the month of March at $83.17, up from the previous quarter closing of $71.65 at the end of December, but still at levels supportive of lower inflationary pressures.

Performance

The Steinberg High Yield Series-O Fund outperformed relative to the market, with a positive return of 1.57% for the quarter. Within the High Yield market, BB bonds underperformed CCC bonds during the quarter as the riskiest bonds enjoyed the most upside. March was the strongest month in the quarter in terms of performance, as January and February returns were positive and consecutively moving higher with anticipated rate cuts getting ever closer. Much of our outperformance was due to our Canadian holdings that had a strong rally and our positioning being more defensive with shorter duration names that were less impacted as the US 10-year yields moved higher during the quarter.

Portfolio Highlights

During the quarter, the Fund added new positions in Canadian government bonds, buying 3-year and 5-year paper (governments), while adding to our existing holdings of Brookfield Property Finance (real estate). We had the bonds of Univision Communications Inc. (media) and Rakuten Group (retail) called from the portfolio. The fund also sold its positions in Finance of America Funding (financials) and Frontier Communications Holdings (telecom).

New issuance activity continued to pick-up pace during the quarter as companies took advantage of demand in the market to refinance existing holdings. We maintained adequate liquidity throughout the quarter with cash averaging roughly 4.5% over the first quarter. We continue to prefer higher quality names to add to our holdings and will look to extend duration as the right opportunities materialize. Our U.S. dollar holdings will remain hedged as we look for favorable opportunities to deploy capital and add to our existing holdings.

Outlook

The outlook for high yield bonds remains attractive as we look out into the rest of 2024. While there are many uncertainties, markets remain stable and expected rate cuts should drive strong performance in fixed income this year. While resilient economic and consumer data have pushed out the start to the rate cut cycle, the anticipation of rate cuts and the actual rate cuts themselves should provide a strong driving force for fixed income performance. While we expect inflationary pressures to remain a key concern, we may see a wider tolerable inflation band be adopted by the FED and other central banks in order to better accommodate a soft landing and steer the economy.

Our new issuance expectations for 2024 have been revised higher as we see additional market opportunities for potential borrowers to access liquidity. We are still expecting the primary market to provide good buying opportunities later this year. So far defaults are trending below expectations, a good sign of corporate resilience and a positive for high yield returns. We continue to view high yield as an attractive asset class within fixed income and more likely to outperform investment grade bonds this year and in a rising rate environment.

As always, we are committed to the disciplined investment approach and long-term perspective that defines Lorne Steinberg Wealth Management.

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