Steinberg High Yield Fund Quarterly Commentary

LorneSteinberg Wealth Management

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Environment

The high yield market performed well in Q3'2024 as investors enjoyed another positive quarter. All months in the quarter had positive returns with July returns being the highest, followed by September and August respectively. This was the 8th straight quarter of positive returns in the high yield market and was the second highest quarterly return during this two-year period. During the quarter, BB credit underperformed with returns being slightly below single B bonds while riskier credit drove the quarterly performance. While BB bonds benefited from the rally in the US treasury market, lower rated bonds far outperformed as investors embraced risk and the FED began the highly anticipated easing cycle. The US 10-year bond yield moved lower during the quarter, ending the third quarter at 3.78% compared to 4.40% seen at the end of Q2'2024. The FED lowered rates once during the quarter, moving 0.50% in September while remaining on hold in the prior months. The Bank of Canada cut rates throughout the quarter at each of its scheduled meetings, cutting rates by 0.25% in both July and September. Weaker Canadian economic numbers supported the rate cuts while a mix of economic news on the US side kept market participants on tenterhooks while awaiting the FED move. On the commodity side, oil prices were lower during the quarter as WTI Crude ended September at $68.17, down significantly from the previous quarter closing of $81.54, despite oil prices being supported by OPEC production cuts.

Performance

The Steinberg High Yield Series-O Fund lagged relative to the market, with a positive return of 3.55% for the quarter. Within the High Yield market, BB bonds underperformed both single B and CCC bonds during the quarter as the riskiest bonds enjoyed the most upside and benefitted the most in this risk on environment. July was the strongest month in the quarter with all months having strong positive returns. Much of our lagging performance was due to being more defensively positioned with shorter duration names that did not rally as much as the market as well as our higher quality portfolio that had less exposure to CCC credit names that enjoyed a strong rally during the quarter.

Portfolio Highlights

During the quarter, the Fund had bonds of Manitowoc Company (capital goods) and PRA Group (financials) called from the portfolio. We had the bonds of Brookfield Property REIT (real estate) partially called from the portfolio. We maintained adequate liquidity throughout the quarter with cash averaging roughly 5.0% over the third quarter. We continue to prefer lower duration, higher quality names to add to our holdings as we remain cautious in this environment and patiently wait to see if a soft landing can be achieved by the FED and other central banks. 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 encouraging as we look out into the last quarter of 2024. While there are many uncertainties, markets remain resilient and we are encouraged by the FED and other central banks starting the easing cycle. We are seeing continued strength in economic activity in the US which may weigh on the timing of interest rate cuts going forward but the direction of the moves are now set and should support fixed income returns in the near term. We are also encouraged by receding inflationary pressures across the world and supportive of the FED view that inflation will gradually fall to their target rate. With the easing cycle already started, we are maintaining our view that the remainder of the year should be positive for fixed income and high yield in particular as investors continue to embrace risk and lock in attractive yields in the market.

We expect new issuance to accelerate as companies take advantage of market opportunities to refinance their bonds. We are slowly seeing default rates rising and future default expectations also drifting higher but still remaining below long-term averages. 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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