



Finding Value in Corporate Bonds

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<https://www.bondsavvy.com/>

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Today's Agenda



- Corporate bonds 101



- How the recent banking crisis and rate hikes have impacted corporate bonds



- Where and how to find value in corporate bonds

- Overarching investment themes
- Issuer-level financial analysis
- Bond-level analysis
- Fundamental and technical analysis



- How to decide when to sell a bond before maturity



Corporate Bonds 101

Corporate Bond Example

Each corporate bond has fixed and variable factors that provide a framework for investment analysis most other investments do not have

LENNAR 5.875% 11/15/24

CUSIP: 526057CR3

Fixed "Security Master" Information

Variable Factors*

Issue date	May 10, 2018
Annual coupon for each bond	\$58.75
May 15 coupon payment	\$29.375
November 15 coupon payment	\$29.375
Annual interest for 10 bonds	\$587.50
Maturity date	November 15, 2024
Term	6.5 years
Principal repaid at maturity per bond	\$1,000

	<u>Oct 2, 2020</u>	<u>Apr 11, 2023</u>
Ask Price	113.40	100.65
Ask Yield to Maturity	2.01%	5.44%
Rating	Ba1 / BB+	Baa2 / BBB-
Credit Spread	1.79%	1.24%



* April 11, 2023 data provided by Fidelity.com. October 2, 2020 pricing data from FINRA. Credit spread based on US Treasury data and Bondsavvy calculations.

Price vs. Par Value Provides First Indicator of Value

Before doing any financial analysis, investors can look at a corporate bond's price and YTM and begin assessing its value and potential investment return

Illustrative Example: Target 3.90% 11/15/47

	← "Discount"		"Par"	→ "Premium"			
	<i>All-time low*</i> Oct 21 '22		Apr 4 '23			<i>All-time high*</i> Jul 24 '20	
Quoted as	75.34	80.00	87.70	100.00	110.00	120.00	137.74
Value per bond	\$753.40	\$800	\$877	\$1,000	\$1,100	\$1,200	\$1,377.40
Annual Coupon	\$39.00	\$39.00	\$39.00	\$39.00	\$39.00	\$39.00	\$39.00
Yield to Maturity (YTM)*	5.82%	5.40%	4.75%	3.90%	3.29%	2.76%	1.93%

* All-time high and low pricing data sourced from FINRA market data. YTM figures calculated on April 9, 2023.

Breaking Down Yield to Maturity for Corporate Bonds

Credit spreads reflect the amount a corporate bond's YTM exceeds a similarly dated US Treasury. Analyzing historical US Treasury yields and credit spreads can be a good indicator of value.

Moody's Baa Yield vs. 20-Year US Treasury Yields

April 6, 2007-April 6, 2023



Implied Credit Spread: Moody's Baa vs. 20-Year US Treasury

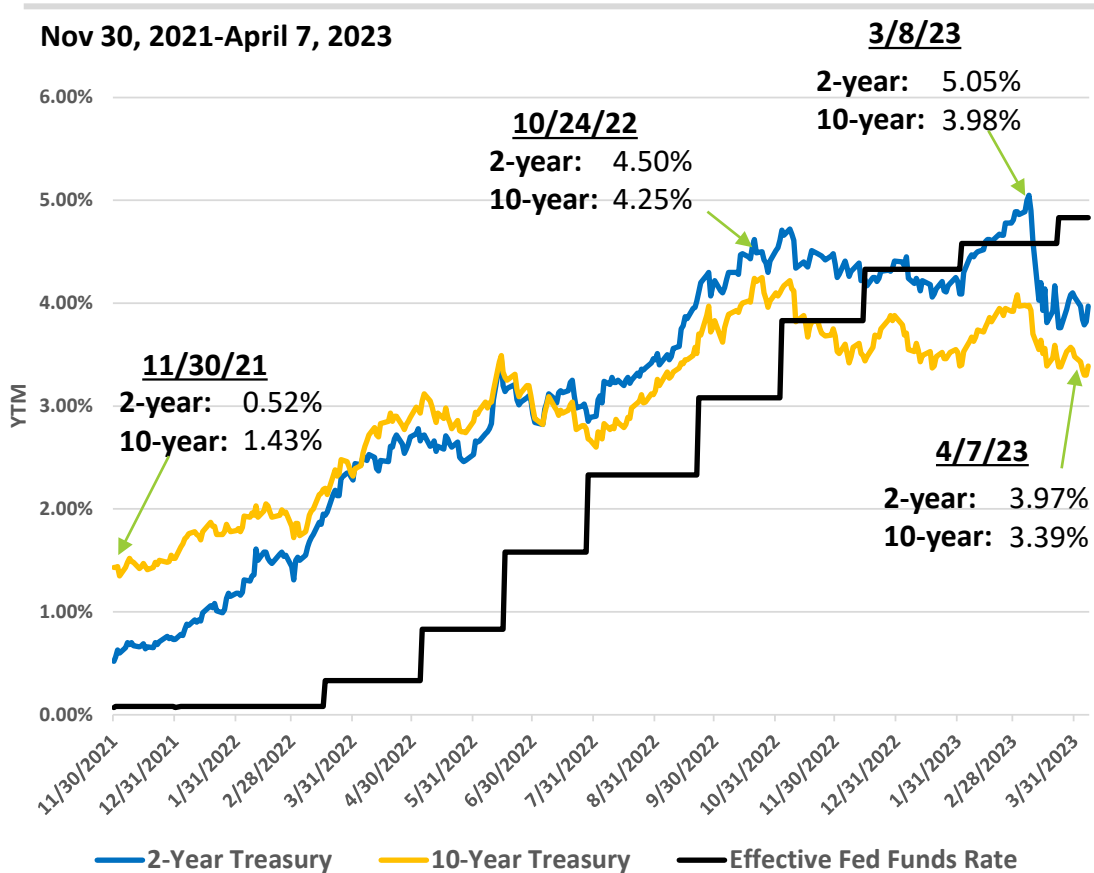
April 6, 2007-April 6, 2023



How the Banking Crisis and Rate Hikes Impacted Corporate Bonds

SVB-Induced Fall in US Treasury Yields Buoyed Many Corporate Bonds...

US Treasury Yields vs. Effective Fed Funds*

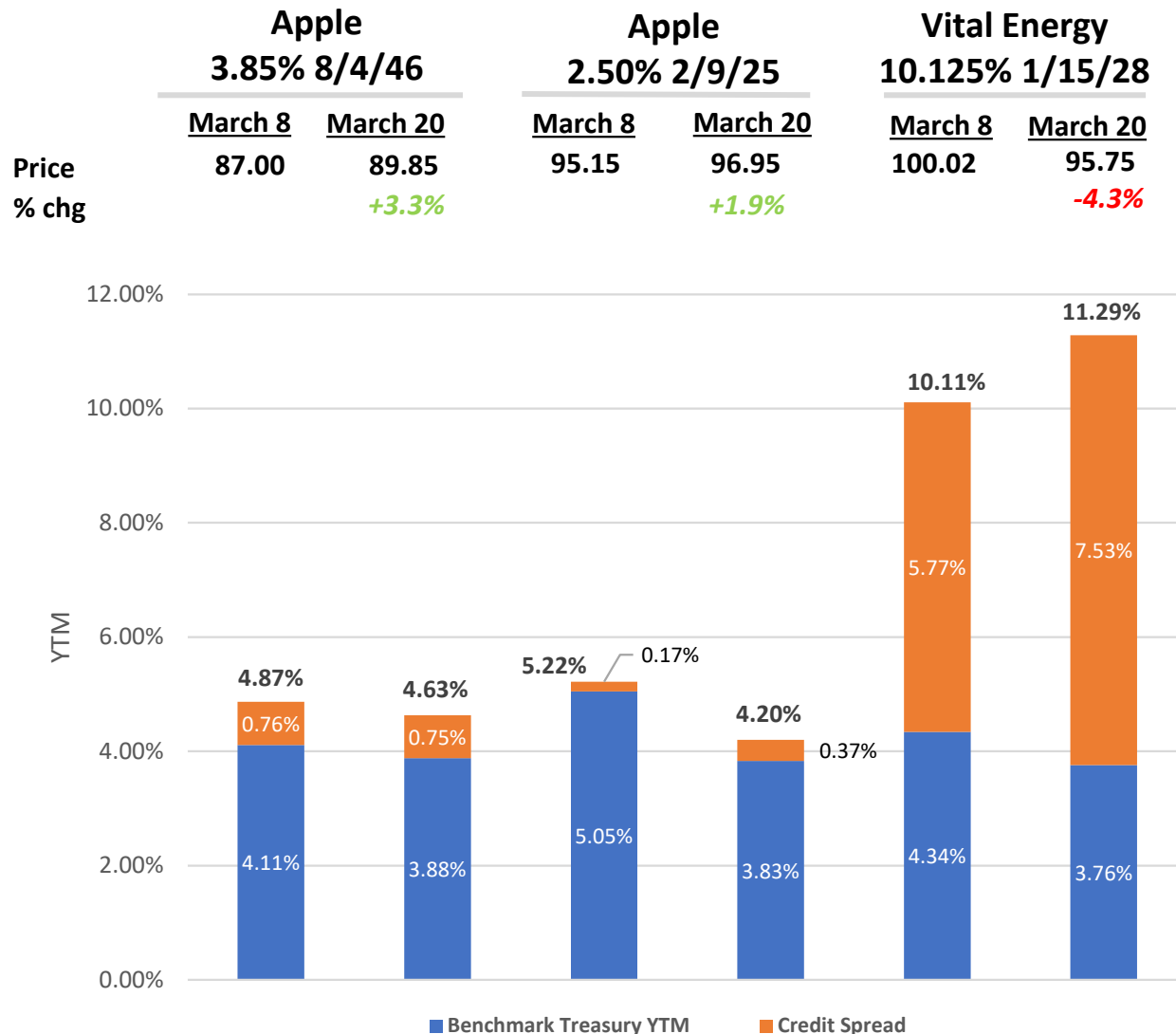


- US Treasury yields were trending up until March 8, anticipating continued interest rate hikes. Then:
- **March 9:** Silicon Valley Bank customers withdrew \$42 billion in deposits
- **March 10:** Regulators closed Silicon Valley Bank
- **March 12:** Signature Bank seized
 - Events caused ‘flight to safety’ into Treasuries, with the two-year YTM falling 1.24 percentage points from March 8 to March 17

The impact of the banking crisis on the bond market showed the importance of owning a variety of corporate bonds

...But Heightened Perceived Risk Drove Certain Credit Spreads Higher

Corporate Bond YTM Building Blocks: Mar 8 vs. March 20, 2023*



- The drop in short-term Treasury yields led the Apple '25 bond YTM down 102 bps (1.02 percentage points)
- The '25 bond's credit spread did increase 20 bps, slightly offsetting the drop in Treasury YTMs
 - However, the bond's near-term maturity limited the pricing impact
- Credit spreads of many high yield bonds widened, which drove certain high yield bond prices lower, such as Vital Energy '28

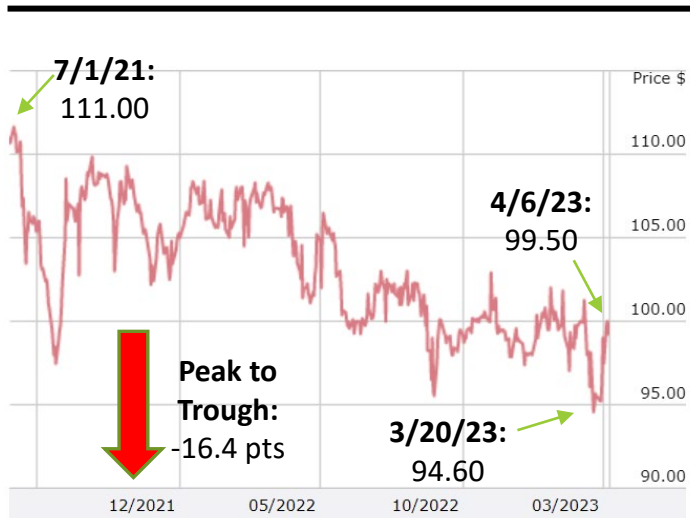


*Source: Bond price and YTM data are from FINRA TRACE data and Fidelity.com. March 20, 2023 credit spreads are from Fidelity.com. March 8, 2023 credit spreads were calculated by Bondsavvy based on 1) FINRA TRACE corporate bond YTM data and 2) Treasury yield data from the US Treasury.

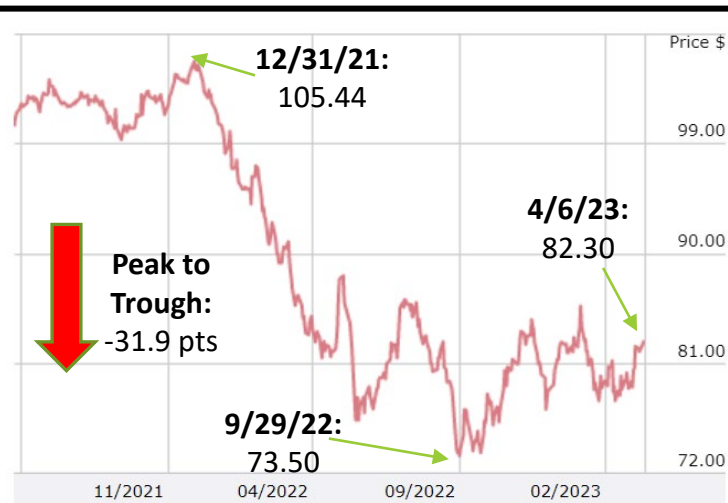
Select Corporate Bond Performance: July 1, 2021-April 6, 2023

Select High Yield Bonds

Vital Energy 10.125% 1/15/28 (B3/B+)



Ford 3.625% 6/17/31 (Ba2/BB+) "Fallen Angel"



Select Investment Grade Bonds

Exxon Mobil 2.440% 8/16/2029 (Aa2/AA-)

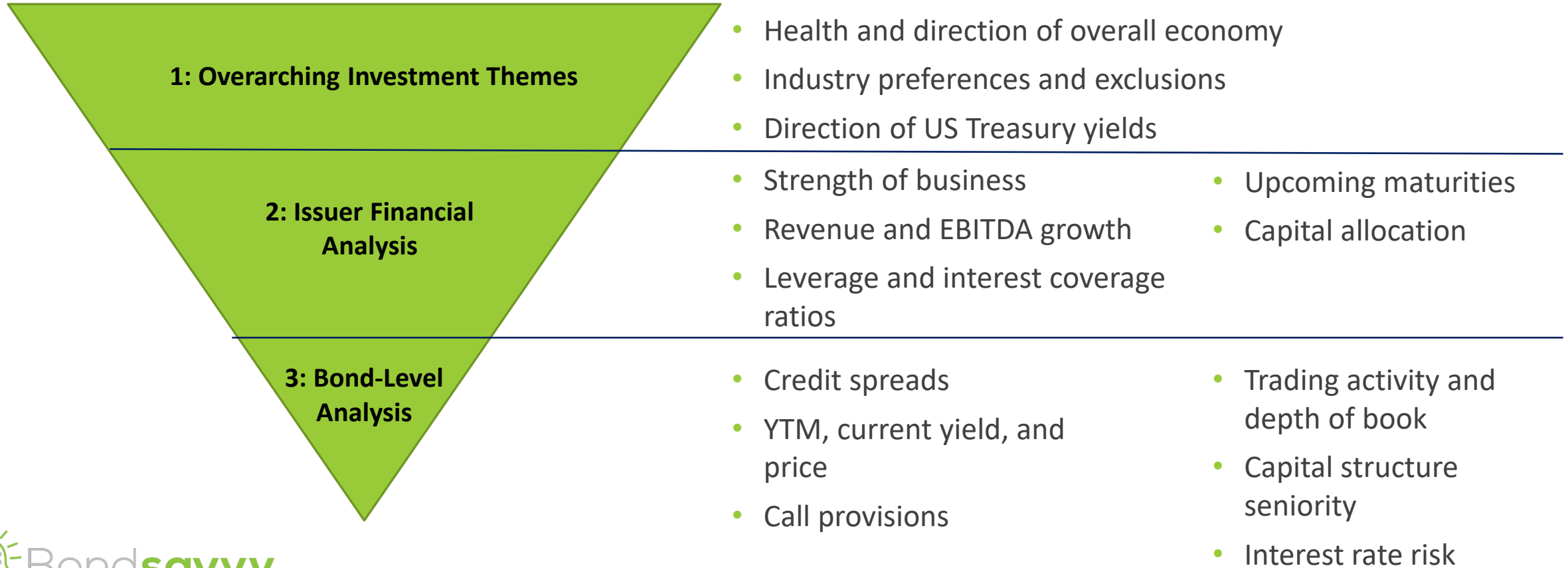


Johnson & Johnson 3.70% 3/1/46 (Aaa/AAA)



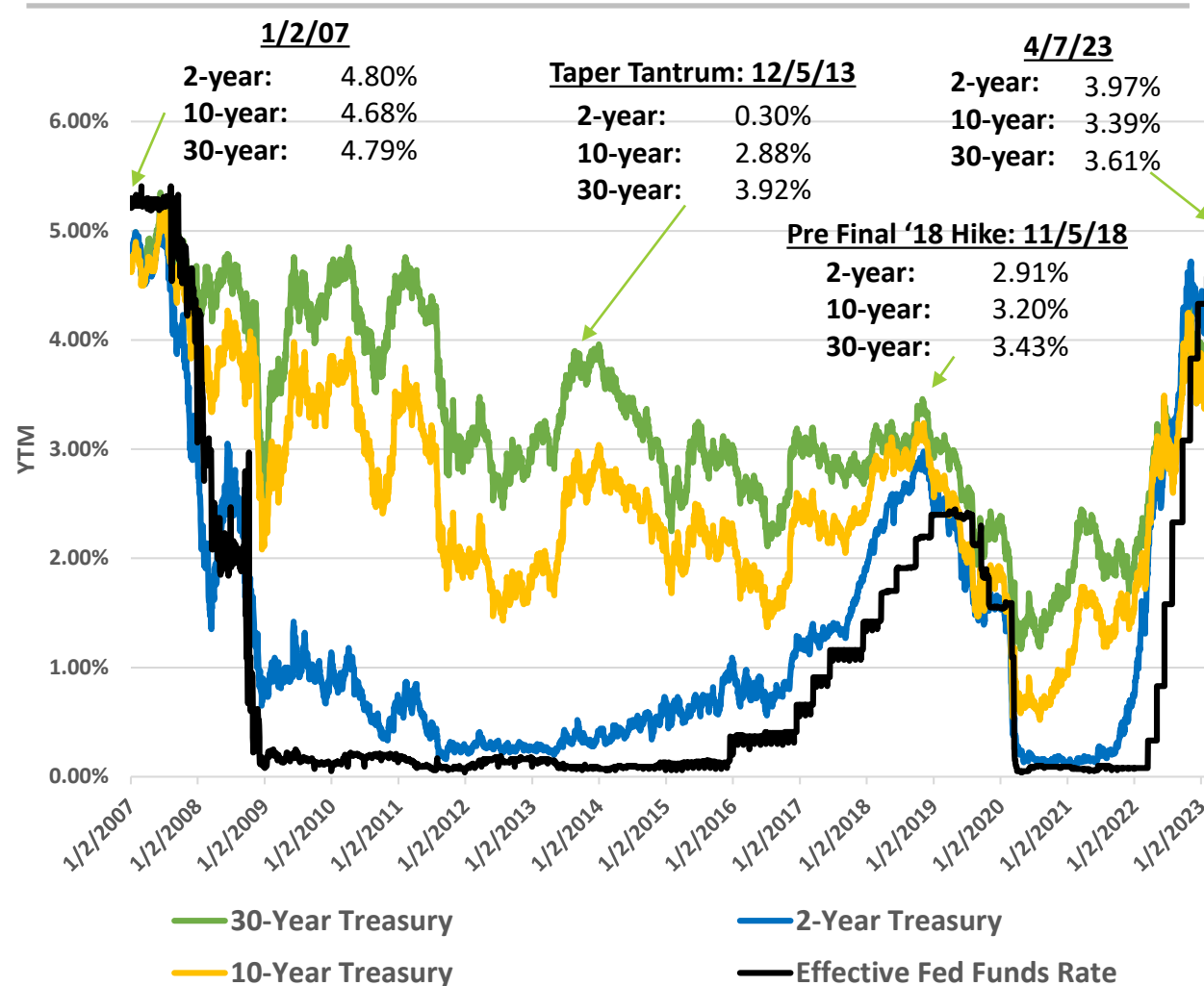
Identifying Value in Corporate Bonds

From 9,000 Available Corporate Bonds to 4-6 New Recommendations: Our Key Investment Considerations



Using US Treasury Yields To Determine Value

US Treasury Yields vs. Effective Fed Funds Rate: 2007-Apr 7 '23*



- Where are we historically?
- Are investors rewarded (or not rewarded) with longer maturities?
- **Investment Grade & Fallen Angels:** Often have many bonds that trade, offering investors various options on maturity dates
- **High Yield:** Typically, lower interest rate sensitivity and, generally, fewer CUSIPs outstanding can make other factors more important than a bond's maturity date

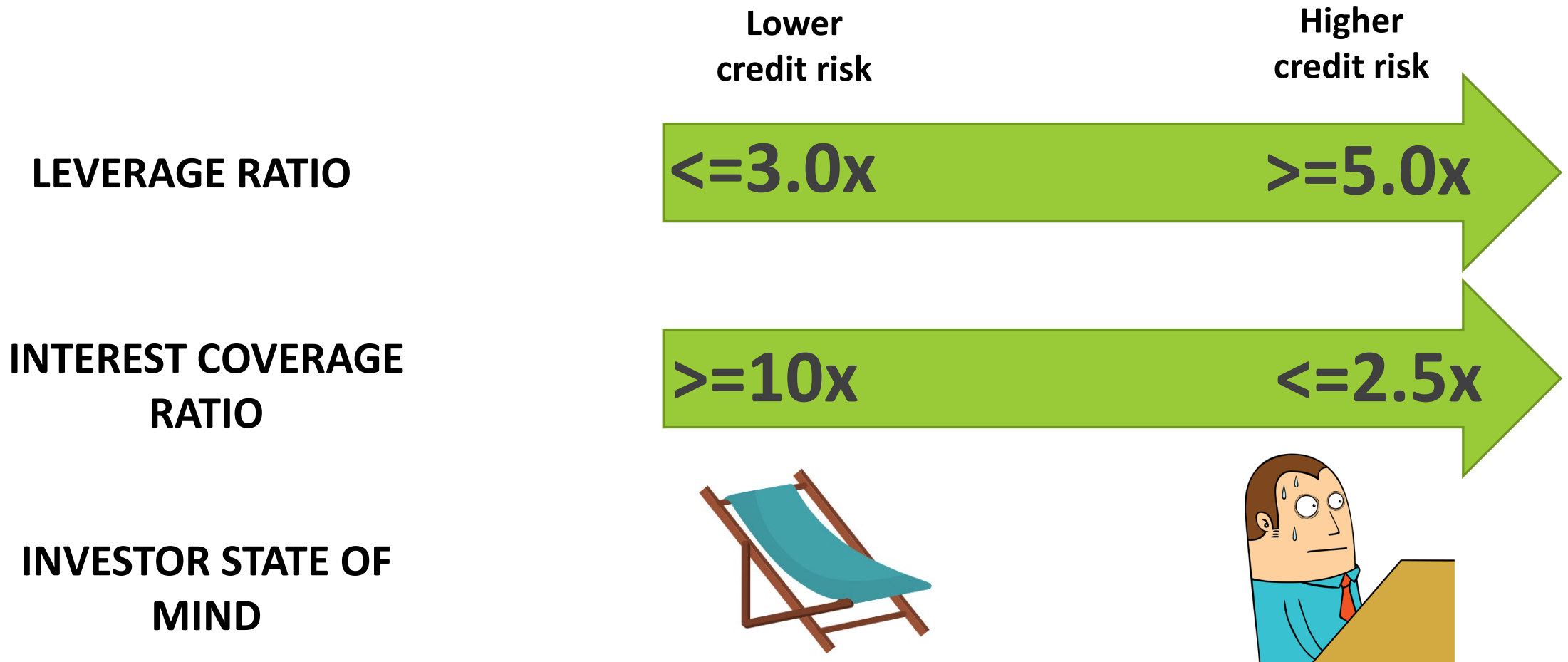


* Sources: Treasury yields from US Treasury. Effective Fed Funds Rate from the Federal Reserve Bank of New York.

Select Financial Metrics for Evaluating Corporate Bond Value

EBITDA	INTEREST COVERAGE RATIO	LEVERAGE RATIO
Earnings before interest, taxes, depreciation & amortization	$\frac{\text{EBITDA}}{\text{Interest Expense}}$	$\frac{\text{Total Debt}}{\text{EBITDA}}$
	<i>Higher = lower default risk</i>	<i>Lower = lower default risk</i> <div style="background-color: #cccccc; padding: 5px; text-align: center;">“Purer” of the two ratios</div>

Corporate Bond ‘Sweat Meter’

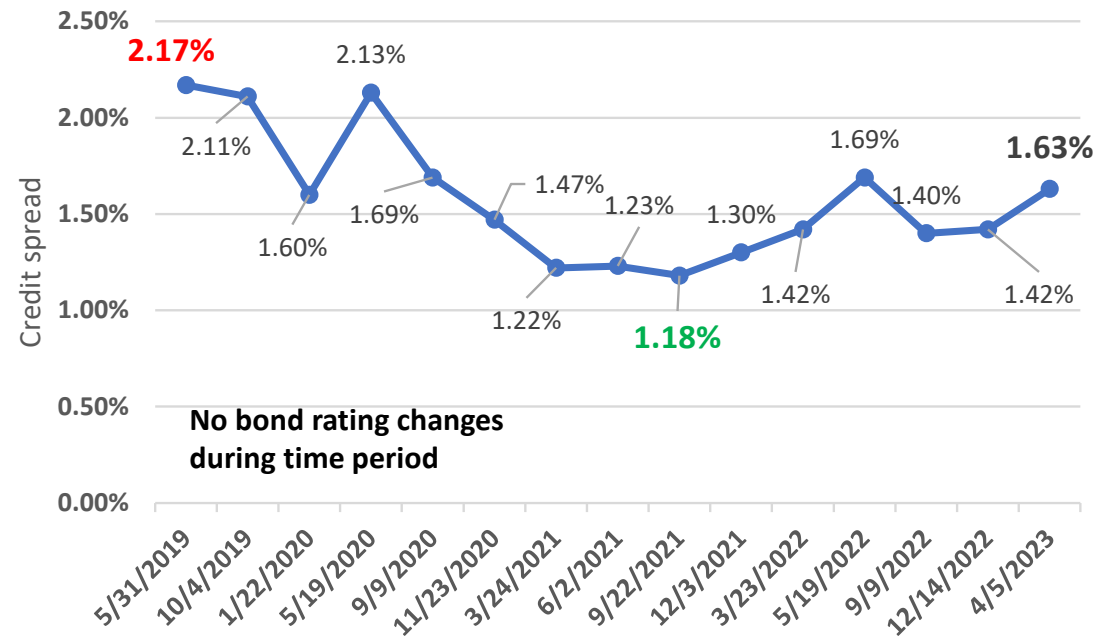


Overlaying Financial Ratios with Credit Spreads

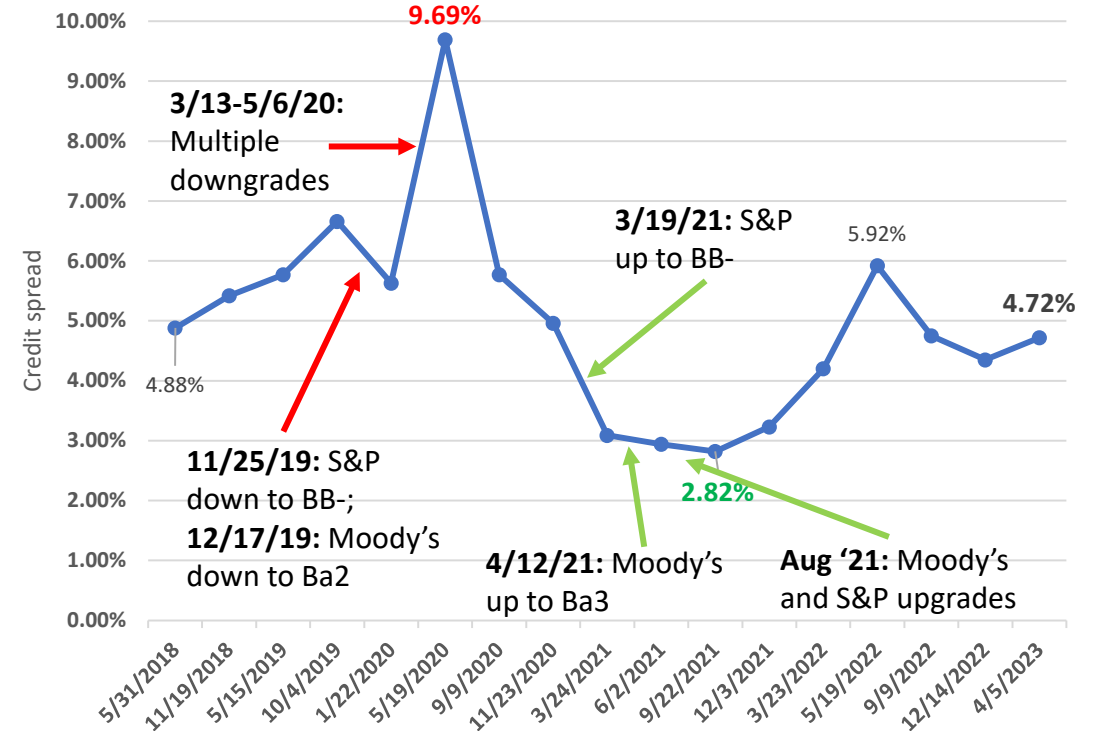
Comparing a bond's credit spread to its financial ratios enables investors to assess whether a bond is a compelling relative value. It can also be helpful for investors to evaluate credit spreads on a historical basis.

Historical Credit Spreads*

Investment Grade Grocer: 5/31/19-4/5/23



High Yield Retailer: 5/31/18-4/5/23



*Credit spreads are from Fidelity.com on each date shown. Bondsavvy records historical credit spreads, which are reflected on these charts. The first date shown in each chart is the date we initially recommended the bond. Each other data point was when Bondsavvy provided its quarterly recommendation updates to subscribers.

How We Identify Value in Corporate Bonds

Bondsavvy seeks to recommend bonds that have high credit spreads and yields and low prices relative to the bond issuer's financial strength. Below is a portion of the analysis we presented subscribers during a recent webcast reviewing new corporate bond recommendations.

Bond	Pricing & Liquidity Analysis						Credit Analysis			
	Quote ⁽¹⁾		Offer Price	Spread to	Bid/Offer	Amount Outstanding	Bond Rating	Credit Ratios		Interest Coverage ⁽³⁾
	Bid	Offer	Yield to Maturity ⁽¹⁾	Treasury ⁽¹⁾	# Quotes (# Bonds)			Leverage ⁽²⁾	Net	
							Gross			
Bond Recommendation 1	88.34	88.98	8.26%	4.44%	6 / 7 (600)	\$500	Ba2 / BB	3.4x	3.1x	5.0x
Bond Recommendation 2	82.81	83.54	8.76%	4.49%	9 / 7 (1,000)	\$1,000	Ba3 / B+	2.5x	1.8x	7.1x
Bond Recommendation 3	90.50	91.47	9.00%	4.80%	7 / 5 (500)	\$500	B2 / B	2.8x	2.3x	5.0x
Bond Recommendation 4	84.00	84.90	6.07%	1.82%	6 / 7 (1,500)	\$1,000	Ba3 / BB	1.2x	Negative	26.7x

\$ in millions, except quote values

⁽¹⁾ Quotes as shown on Fidelity.com from 12:15-12:30pm EST on March 8, 2023.

⁽²⁾ Most recent quarter's total debt divided by last twelve months' EBITDA.

⁽³⁾ Last twelve months' EBITDA divided by last quarter's annualized interest expense.



How We Identify Value in Corporate Bonds (Cont'd)

Apart from credit metrics such as leverage and interest coverage ratios, we need to understand a bond issuer's full picture, including recent growth, cash vs. debt, upcoming maturities, and the bond's interest rate risk

Credit Analysis											
<i>\$ in millions, except quote values</i>											
<u>Bond</u>	Spread to Treasury ⁽¹⁾	<u>YTD YOY Growth</u>		<u>Last 12 Months</u>					<u>Upcoming Maturities</u>		<u>Interest Rate Sensitivity</u>
		Revenue	EBITDA	Revenue	EBITDA	Margin	Debt	Cash	Amount	Date	
Bond Recommendation 1	4.44%	1%	-9%	\$4,169	\$956	23%	\$3,265	\$273	\$200 \$250	2025 2027	Medium
Bond Recommendation 2	4.49%	26%	12%	\$2,281	\$537	24%	\$1,316	\$354	\$275	2025	Low
Bond Recommendation 3	4.80%	-2%	-23%	\$2,308	\$356	15%	\$991	\$157	\$200	2028	Low
Bond Recommendation 4	1.82%	54%	71%	\$2,241	\$600	27%	\$750	\$2,710	\$500	2032	Medium

⁽¹⁾ As shown on Fidelity.com from 12:15-12:30pm EST on March 8, 2023.
All financial data are for company's most recently reported quarter.

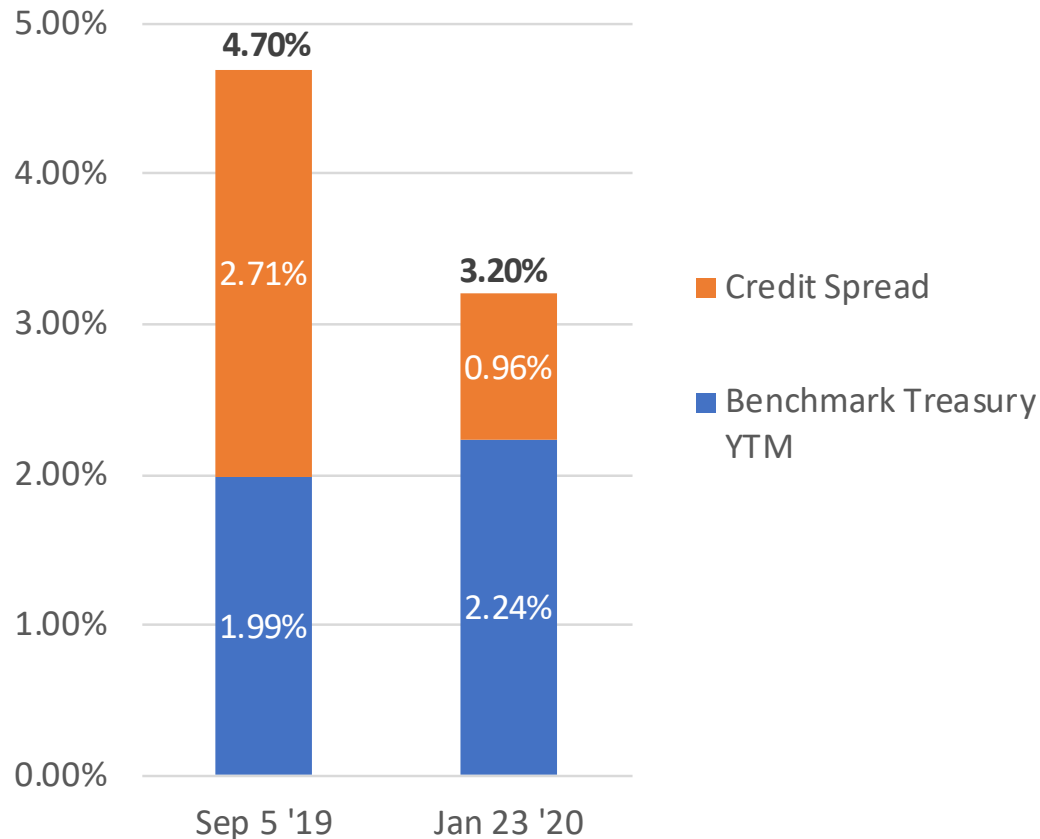


Deciding When To Sell Bonds Prior to Maturity

Deciding When To Sell a Bond – Tiffany ‘44



Tiffany 4.900% ‘44 Bond YTM Building Blocks



Price	103.01	128.00
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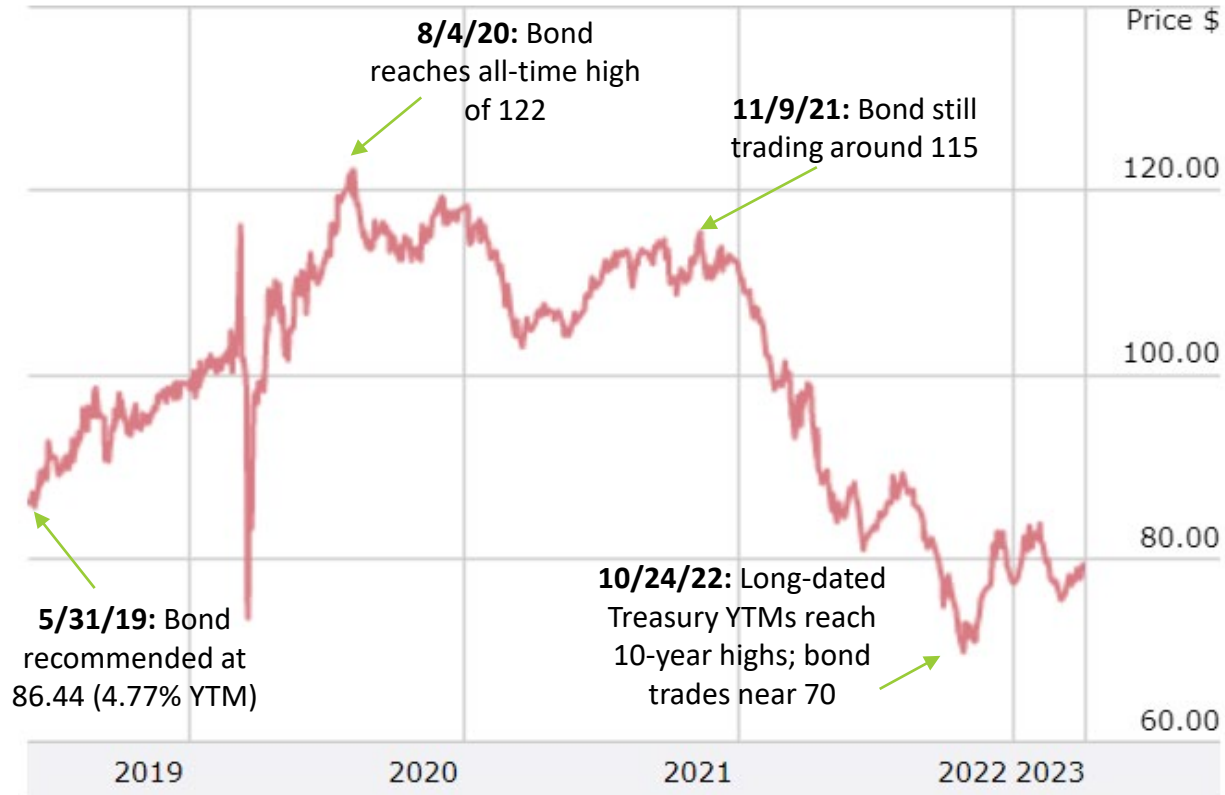
- Bondsavvy recommended a purchase of Tiffany ‘44 bonds on Sep 5 ‘19 at an offer price of 103.01
- Shortly after our recommendation, LVMH announced an agreement to purchase Tiffany
- LVMH was deemed a higher credit quality, and, since it would assume Tiffany’s debt, the Tiffany bonds surged to 128
- **Low credit spread and Treasury yields:** By January ‘20, the bond’s credit spread shrunk to 0.96%, and we didn’t see Treasury yields falling materially
- Due to limited remaining upside, we recommended selling the bond at 128, achieving a 26% return
- In late March ‘23, the bond traded in the high 90s

A Mistake Deciding *Not* To Sell a Bond

Especially for lower-coupon bonds, selling corporate bonds when they have increased significantly in price is a crucial part of maximizing total returns.

Long-Dated Investment Grade Recommendation

May 31, 2019-April 3, 2023

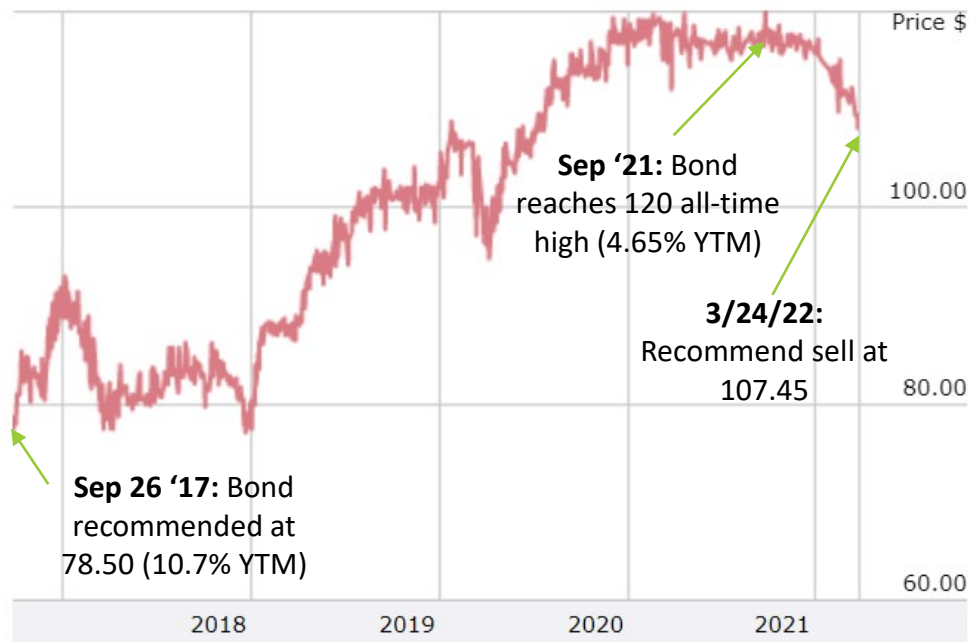


- Bondsavvy recommended subscribers purchase this bond at price of 86.44 on May 31, 2019
- US Treasury yields *and* the bond's credit spread fell, driving the price to 115-122 in 2020 and 2021
- Given limited other opportunities and the bond's pick date 4.77% YTM, we elected to hold the bond
- As long-term Treasury yields rose in '22, the bond fell to around 70 on Oct 24, 2022 before recovering to the high 70s on Mar 23

Deciding When To Sell a Bond – Albertsons '29

Albertsons 7.45% Price Performance

Sep 26, 2017 – Mar 24, 2022



- Bondsavvy recommended subscribers purchase the Albertsons 7.45% '29 bond at 78.50 on Sept 26, 2017
- The bond had fallen in the wake of Amazon's announced 2017 purchase of Whole Foods and Albertsons pulling its planned IPO
- At a 10.7% YTM and 4.2x leverage, we believed the bond was a good risk-reward (bond rated CCC+ on pick date)

Deciding to sell

- Albertsons' strong financial performance accelerated during Covid-19, with leverage falling below 2x
- Despite strong financials, rating failed to get above B+
- As bond prices began falling in Q1 '22, we elected to lock in nearly 30 points of capital appreciation and a 79.52% total return





Thank you

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Q&A

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