# HYI Quarterly Commentary

## Horizons Active High Yield Bond ETF

Q1 2023

### Market Overview

Government bonds continued to be volatile in the first quarter (Q1) of 2023, with the U.S. 10-year Treasury note trading as low as 3.32% in January and as high as 4.08% at the beginning of March. Yields then dropped sharply to 3.28% on March 24, 2023, as a result of the collapse of two regional banks in the U.S. and the pressure exerted on the financial system. The future actions of central banks remain a focus. The U.S. Federal Reserve (Fed) is being closely watched for hints as to when this rate-hike cycle will end, and how long rates will stay at elevated levels.

### Quarter in Review

High-yield credit spreads were also volatile, trading as wide as +516 basis points (bps) and as tight as +386 bps (Bloomberg U.S. High Yield Index) before ending the quarter at +455 bps. The theme of spread compression continued this quarter as lower-rated (B and CCC) bonds again outperformed higher-rated (BB) bonds.

The JP Morgan High Yield Index shows high-yield bonds declining by 42 bps over the quarter to 8.76%. New issuance has recovered from the anemic levels of the fourth quarter of 2022 as a total of US $40.5 billion came to market. It is worth noting that issuance came to a halt in the second half of March due to the regional banking crisis.

While the manufacturing sector of the economy appears to be slowing, the service sector continues to expand. Employment also continues to be strong and upward pressure on wages continues to pose a challenge to monetary policy. While central banks (led by the Fed) are now expected to end rate-hiking campaigns in the second quarter, sticky inflation, and the need to keep rates higher for longer may derail current market expectations for rate cuts later this year or early in 2024.

Geopolitical events remain wild cards. The Ukraine/Russia war and a potential default by the United States this summer are adding to the uncertainty. Conversely, economic stimulus from the U.S. infrastructure program and the end of COVID-19 restrictions in China and Japan may increase global economic activity.

### Outlook and Positioning

HYI continues to maintain below-average duration exposure as market conditions are expected to remain volatile throughout the balance of the year. Market expectations for a “soft landing” may be optimistic as indications suggest the manufacturing sector is slowing rapidly and that consumers, especially in the U.S., have rapidly increased their debt load, which could lead to a sharp slowdown in spending. Default rates are expected to begin rising from cyclical lows this year and profit margins may come under additional pressure, impacting corporate earnings. As a result, HYI will remain allocated to better-rated credits and maintain a lower duration profile for the next several months.

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