

The Performance of Convertible Bonds versus Fixed Income Indices

Market Insights from:

Steve Wachtel, CFA, Portfolio Manager

Investing in the fixed income arena has been extremely challenging over the last few years. The Bloomberg US Aggregate Index, a broad-based benchmark for bonds, has lost -11.21% since the start of 2022 (through 4/30/24). During that time period, very few fixed income segments showed a positive return. However, one category of bonds, one that is often overlooked, did show positive returns. That is Investment Grade convertible bonds.

Convertible bonds are fixed income instruments that offer principal protection and return of investment at maturity. An investor holding a convertible bond from issuance to maturity will have a non-negative return, barring default. Convertibles consist of a bond with an embedded equity option and the bond value dominates the option value at issuance.

With the path of interest rates uncertain, Investment Grade converts make a lot of sense in a fixed income portfolio due to their low duration relative to Investment Grade and High Yield corporates. Converts also offer diversification as they have a different issuer composition and a low correlation to other fixed income securities. In addition, converts have a substantially lower default rate and superior liquidity relative to High Yield bonds.

For insurance companies, which are subject to capital reserve requirements and corresponding portfolio limits, another benefit from investing in Investment Grade convertibles is capital efficiency. This is because convertibles get the same favorable treatment as bonds for risk-based capital (RBC) charges due to their seniority in the capital structure and principal protection, while still benefitting from potential equity upside participation and exposure to the most dynamic sectors of the economy.

But the most compelling reason to consider Investment Grade convertibles is their significant outperformance over all other fixed income segments over multiple time periods. This can be seen below as the ICE BofA Investment Grade US Convertible Index (V0S1)¹ is compared to other bond categories. Investment Grade converts have the best 5, 10, and 15-year performance of the US fixed income indices².

Fixed Income Index ²	3 Year Total Return (%)	5 Year Total Return (%)	10 Year Total Return (%)	15 Year Total Return (%)
ICE BofA Investment Grade Convertible (V0S1)¹	0.21	5.60	9.08	10.04
Bloomberg US Corporate High Yield	1.51	3.72	4.28	7.96
Bloomberg US Long Corporate	-6.43	-0.20	2.36	5.79
Bloomberg US Credit	-3.02	0.78	2.11	4.22
Bloomberg US Long Govt/Credit	-8.38	-1.65	1.53	4.22
Bloomberg US Intermediate Credit	-1.20	1.41	2.10	3.78
Bloomberg US Municipal	-1.10	1.26	2.41	3.44
Bloomberg US TIPS	-1.55	2.07	1.90	3.12

Bloomberg ABS	0.24	1.58	1.72	3.08
Bloomberg US Govt/Credit	-3.41	0.13	1.37	2.63
Bloomberg US Aggregate	-3.54	-0.16	1.20	2.41
Bloomberg US Long Government	-10.60	-3.64	0.41	2.38
Bloomberg US Intermediate Govt/Credit	-1.67	0.78	1.42	2.33
Bloomberg US Intermediate Aggregate	-2.45	0.20	1.19	2.20
Bloomberg US STRIPS	-10.50	-3.55	0.27	2.09
Bloomberg US Mortgage Backed Securities	-4.00	-0.98	0.72	1.70
Bloomberg US Government	-3.67	-0.45	0.76	1.54

¹ICE BofA Investment Grade US Convertible Bond ex-Mandatory & Preferred Index (V0S1)

²Total Annualized Return as of 4/30/2024. Data in the table is sorted by the 15 Year period.

Notes/Sources:

SSI internal research, as of 04/30/2024. Past performance is not necessarily indicative of future results. The table is intended to show the asset class over long term periods. It is not intended to show or reflect SSI products.

eVestment Sourcing: eVestment Alliance, LLC and its affiliated entities (collectively "Nasdaq eVestment") collect information directly from investment management firms and other sources believed to be reliable, however, eVestment does not guarantee or warrant the accuracy, timeliness, or completeness of the information provided and is not responsible for any errors or omissions. Performance results may be provided with additional disclosures available on eVestment's systems and other important considerations such as fees that may be applicable. Not for general distribution and limited distribution may only be made pursuant to client's agreement terms. * All categories not necessarily included, Totals may not equal 100%. Copyright © Nasdaq. All Rights Reserved.

Bloomberg Sourcing: Bloomberg Index Services Limited. BLOOMBERG® is a trademark and service mark of Bloomberg Finance L.P. and its affiliates (collectively "Bloomberg"). Bloomberg or Bloomberg's licensors own all proprietary rights in the Bloomberg indices. Bloomberg does not approve or endorse this material or guarantee the accuracy or completeness of any information herein, nor does Bloomberg make any warranty, express or implied, as to the results to be obtained therefrom, and, to the maximum extent allowed by law, Bloomberg shall not have any liability or responsibility for injury or damages arising in connection therewith.

ICE BofA Sourcing: Merrill Lynch, Pierce, Fenner & Smith Incorporated ("BofAML"), used with permission. BofAML PERMITS USE OF THE BofAML INDICES AND RELATED DATA ON AN "AS IS" BASIS, MAKES NO WARRANTIES REGARDING SAME, DOES NOT GUARANTEE THE SUITABILITY, QUALITY, ACCURACY, TIMELINESS, AND/OR COMPLETENESS OF THE BofAML INDICES OR ANY DATA INCLUDED IN, RELATED TO, OR DERIVED THEREFROM, ASSUMES NO LIABILITY IN CONNECTION WITH THE USE OF THE FOREGOING, AND DOES NOT SPONSOR, ENDORSE, OR RECOMMEND SSI INVESTMENT MANAGEMENT LLC, OR ANY OF ITS PRODUCTS OR SERVICES. The index data referenced herein is the property of Merrill Lynch, Pierce, Fenner & Smith Incorporated ("BofAML") and/or its licensors and has been licensed for use by SSI Investment Management LLC. BofAML and its licensors accept no liability in connection with its use. See subscription agreement for a full copy of the Disclaimer.

SSI Investment Management LLC believes all the information contained in the report to be accurate, but we do not guarantee its accuracy. The analyst(s) principally responsible for the preparation of this research report certify that the views expressed in this research report accurately reflect his/her (their) personal views about the subject security (ies) or issuer(s) and that his/her (their) compensation was not, is not, or will not be directly or indirectly related to the specific recommendations or views contained in this research report. None of the information reported or opinions expressed constitute a solicitation of the purchase or sale of securities or any commodities.

SSI operated under the name of SSI Investment Management, Inc. (1/1/1973-4/30/2019) and as of 5/1/2019 operates as SSI Investment Management LLC

© 2024 SSI Investment Management LLC