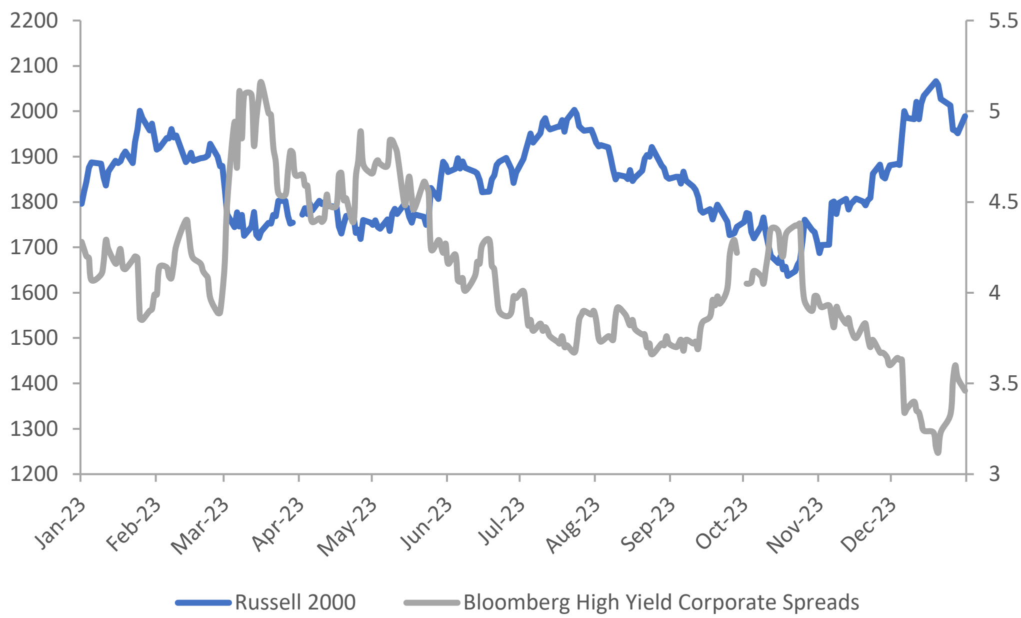
January 2024 High Yield Market Insights

- High yield credit spreads and the Russell 2000 index traditionally move inversely to one another
- Credit spreads are at historically tight levels and the Russell 2000 index is near a 52-week high
- The cyclical tights in credit spreads should eventually widen and the Russell 2000 index can then effectively be used as a hedge to reduce price volatility due to the widening of credit spreads

Credit spreads are the incremental yield that high-yield bonds offer versus same-duration government bonds. Over the past decade, high yield credit spreads and the Russell 2000 index have exhibited a strong inverse correlation of -0.73. High-yield bonds, like equities, are strongly linked to the business results and performance of the companies that issue them.

Russell 2000 and Bloomberg High Yield Corporate Spreads



Source: Bloomberg, Concise Capital as of 1/8/24

We believe credit spreads between Treasuries and high yield bonds are at unsustainably low levels. There comes a point where investor risk appetite will moderate with spreads as tight as they are currently. While spreads could technically move even lower if positive news emerges, they will likely widen back out over time.

Shorting the Russell 2000, for example via futures or ETF, can hedge a tail risk by providing a positive return in a severe market dislocation, such as a sudden widening of credit spreads.

1111 Brickell Avenue, Suite 1525 ● Miami, FL 33131 ● Office: +1 (305) 371-4578 Ext. 1014 ● Email: ir@concisecapital.com

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The Russell 2000 Index refers to a stock market index that measures the performance of the 2,000 smaller companies included in the Russell 3000 Index. The Russell 2000 is managed by London's FTSE Russell Group and is widely regarded as a bellwether of the U.S. economy because of its focus on smaller companies that focus on the U.S. market.