TEAM INSIGHTS
JUNE 3, 2025

FULL DISCRETION TEAM

Extra Credit

Keep Your CHIN Up: A Helpful Insight for Understanding High Yield Risk Premia

Key Takeaways

- Loomis Sayles’ Applied IQ team created a proprietary tool called the Credit Health Index, or CHIN, that provides a forward-looking view of corporate health.
- The CHIN is a key input into the Full Discretion team’s top-down risk framework. By utilizing the CHIN’s output to calculate the estimated high yield risk premium, we can gauge whether investors are being compensated for their credit risk.
- We have seen greater compression and more volatility in the CHIN since the start of 2025, which has impacted our forecast for losses in high yield.

A Forward-Looking Common Language

When it comes to assessing value in the high yield market, we believe the big picture is essential. For the Full Discretion team, and other Loomis Sayles fixed income investors, the big picture means analyzing where we are in the credit cycle and calculating the current high yield risk premium, defined as the high yield market’s option-adjusted spread (OAS) less our forecasted one-year-forward downgrade and default loss. The combination of where we are in the credit cycle and how much high yield risk premium is available gives us a clear vision of how much risk we should be taking.

To better understand the potential for credit losses from downgrades and defaults, our Applied IQ team created a proprietary tool called the Credit Health Index, or CHIN. The CHIN is a macroeconomic research tool that gives us a forward-looking view of corporate health. The tool creates a foundation for our team to estimate the expected losses due to downgrades and defaults over the coming 12 months, which we then use to calculate the estimated current risk premium. It assists us in looking through a vast range of economic data points to focus primarily on what drives returns in the credit markets.

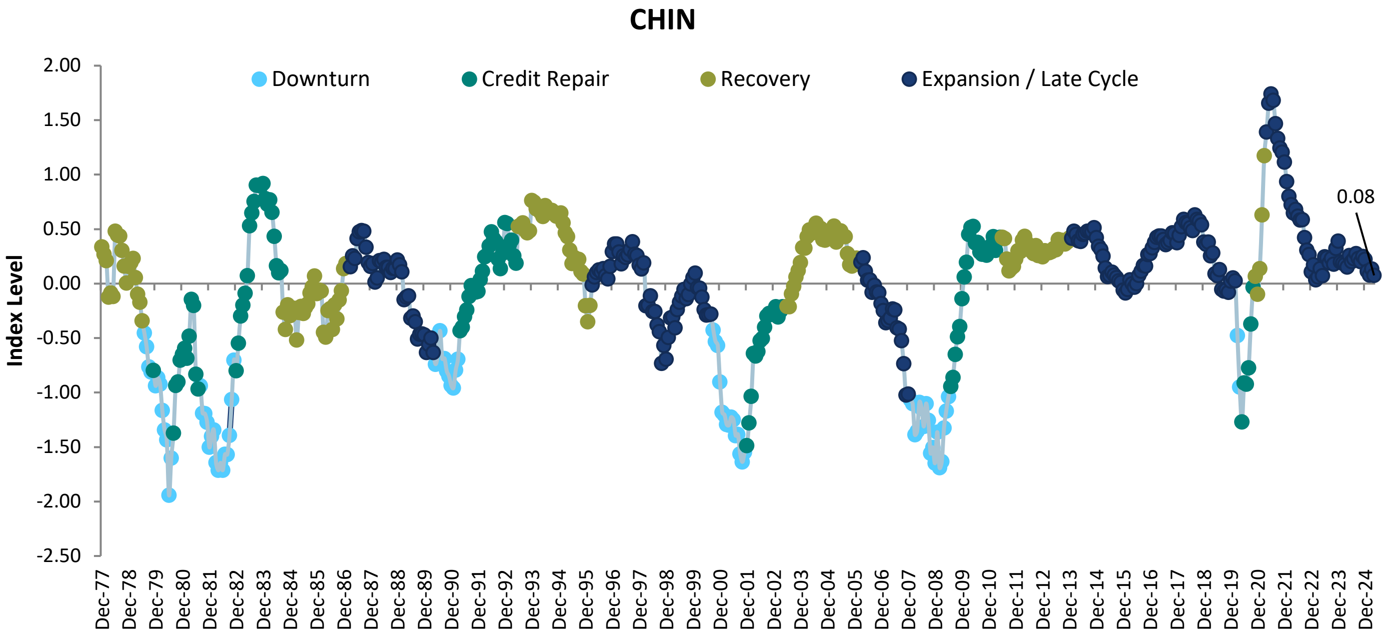
How it Works

The CHIN uses multi-faceted layers of data, covering macro fundamentals, policy and interest rates, as well as bottom-up credit fundamentals, such as leverage, profitability and interest coverage. The CHIN framework scales our view of the credit markets across a variety of indicators, informing our expectations for future losses from downgrades and defaults. When the CHIN is high, it indicates low expected future losses, and vice versa. We then compare the CHIN’s output with today’s spread levels to calculate the estimated high yield risk premium, which helps us gauge whether investors are currently being compensated for the risk of investing in credit versus US Treasury bonds.

Where is the CHIN Now?

As shown in the chart below, while the CHIN remained fairly consistent in 2024, we have seen greater compression and more volatility in the CHIN since the start of 2025. The scale of the recently announced tariffs has caused us to increase the odds of our stallflation scenario, and the impact of this shows up in our forecast for losses in high yield. We now expect the CHIN to hold between 0.0 and 0.3. This range of CHIN levels equates to losses over the next 12 months in the high yield market of 230-280bps.

One bright spot, in our view, has been bottom-up corporate fundamentals. Bottom-up fundamentals have remained very strong and are keeping the CHIN from getting too bearish on forward losses. This area of strength should help create a ceiling on how wide spreads can go in a market sell off.



Source: Loomis Sayles, data shown from of 12/1/1977 - 4/30/2025.
The Credit Health Index (CHIN) is a macro tool created by Loomis Sayles. The CHIN is currently managed by the Loomis Sayles Applied IQ team. It is proprietary framework that utilizes a combination of macro, financial market and policy variables to project US corporate health. A higher reading indicates stronger corporate health whereas a lower reading indicates weaker corporate health.

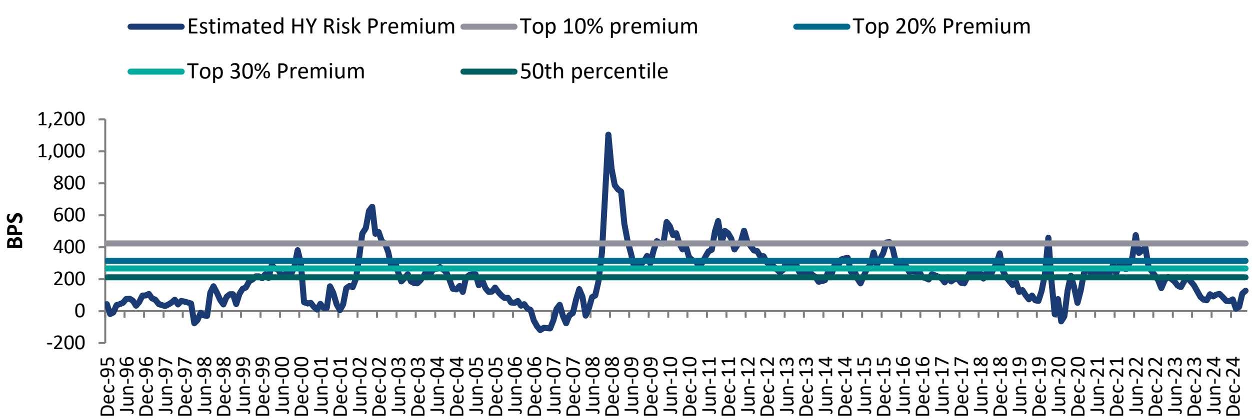
What Can the CHIN Tell Us About the High Yield Market?

Using the history of the CHIN and the implied estimated risk premium, we can look back at periods similar to today's market valuations to see how the high yield sector performed. As of April 30, 2025, we estimated the risk premium to be around 130bps (385bps of OAS minus 255bps of estimated losses due to downgrades and defaults). Looking at the data in the chart below, that level is below the median risk premium through the cycle of 200bps and well below the levels shown that have historically resulted in outsized forward returns in the high yield market.

However, managing market timing can be very challenging. Our models forecast a 48% chance of positive excess returns over the next six months. Opportunities for very strong returns like those in the chart below do not occur often., In our opinion, we believe investors should consider moderately leaning into credit risk for any potential extra carry pick-up, while also maintaining some extra liquidity to take advantage of spread widening events like what occurred in April.

ESTIMATED HY PREMIUM 12/31/1995 – 4/30/2025			BLOOMBERG US CORPORATE HIGH YIELD INDEX	
	BPS	% TIME ABOVE ESTIMATED PREMIUM	AVERAGE 12-MONTH FORWARD TOTAL RETURN	AVERAGE 12-MONTH FORWARD EXCESS RETURN*
Top 10% Premium	423	11%	22.43	19.39
Top 20% Premium	314	22%	15.58	12.47
Top 30% Premium	267	32%	13.01	9.84

HY Risk Premium Distribution

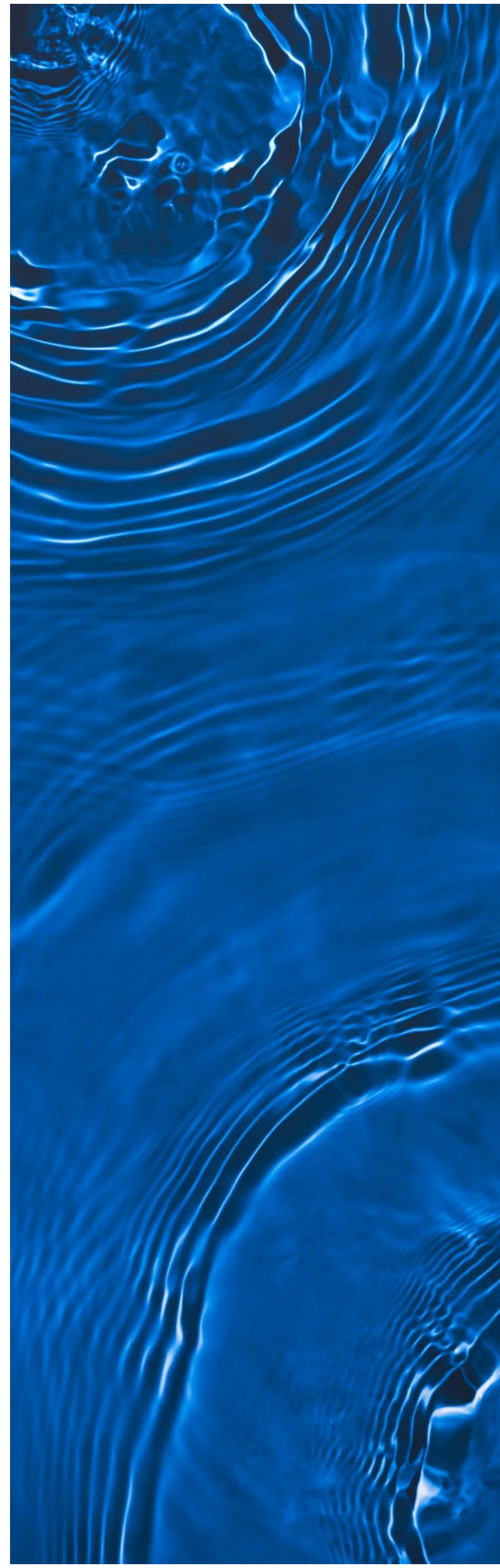


**Calculated as in excess of Treasurys.*
Source: Loomis Sayles, Bloomberg, as of 4/30/2025.
***The chart presented above is shown for illustrative purposes only**. Some or all of the information on this chart may be dated, and, therefore, should not be the basis to purchase or sell any securities. The information is not intended to represent any actual portfolio managed by Loomis Sayles.*
Indices are unmanaged and do not incur fees. It is not possible to invest directly in an index.
Markets may behave very differently than history suggests, it is not possible for any methodology to accurately identify and interpret all relevant market events.
Any investment that has the possibility for profits also has the possibility of losses, including the loss of principal.
Past performance is no guarantee of future results.

Tying It All Together: Full Discretion's View

The CHIN is a key input into the Full Discretion team's top-down risk framework. We also stress the variables that are inputs to the CHIN to see how the index may change over the next 6-12 months based on the team's forward-looking macroeconomic scenarios. With the potential for slower growth and higher inflation, we see the CHIN being pinned close to zero. However strong bottom-up fundamentals keep us from forecasting the CHIN to break below zero, which is what is what would be necessary to get spreads out to levels typically experienced in a downturn or recession.

It is important to note that markets may behave very differently than history suggests and it is not possible for any methodology to accurately identify and interpret all relevant market events. While we believe there is value in the high yield corporate market, we think investors should remain poised to take advantage of spread widening events given the wide range of outcomes on growth, inflation and the path of interest rates.



Meet the Team

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Investment Director

CHERYL STOBER
Investment Director

KRISTEN DOYLE
Associate Investment Director

About the Team

The Full Discretion team brings decades of expertise and collaboration to create tailored solutions for their clients.

28	Investment Professionals
23+	Avg. Years of Industry Experience (Portfolio Management Team)
$79.1	Team Assets Under Management (Billion USD)

Team Philosophy

We have a legacy of independent thinking and leaning into the market when others may be pulling away. We take a deep-value, equity-like approach to credit selection across global fixed income markets. Our disciplined process helps gives us confidence in seeking to identify macro trends, formulate a clear view on market sectors, and invest throughout the credit cycle.

For more than 40 years, we have been applying our distinctive style of bond picking to deliver portfolios designed to provide excess yield potential and have low correlations to traditional benchmark-focused fixed income strategies.

Source: Loomis Sayles, as of 3/31/2025
Average years of expertise reflected at portfolio management level

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