

Chartwell Investment Partners

Institutional and Private Asset Management



High Yield Market Outlook

Chartwell Investment Partners

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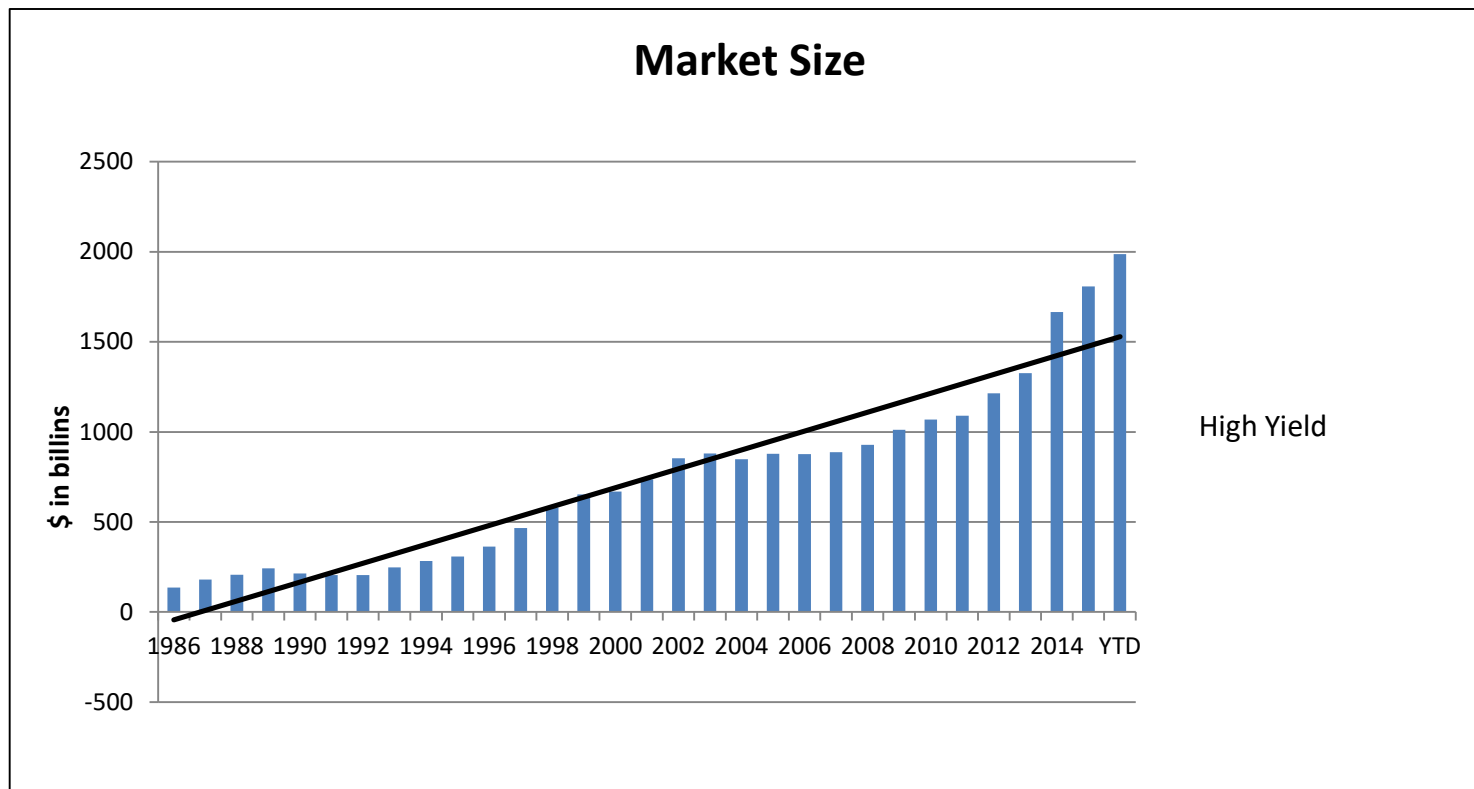
December 2, 2016

Pacific Region Investment Conference

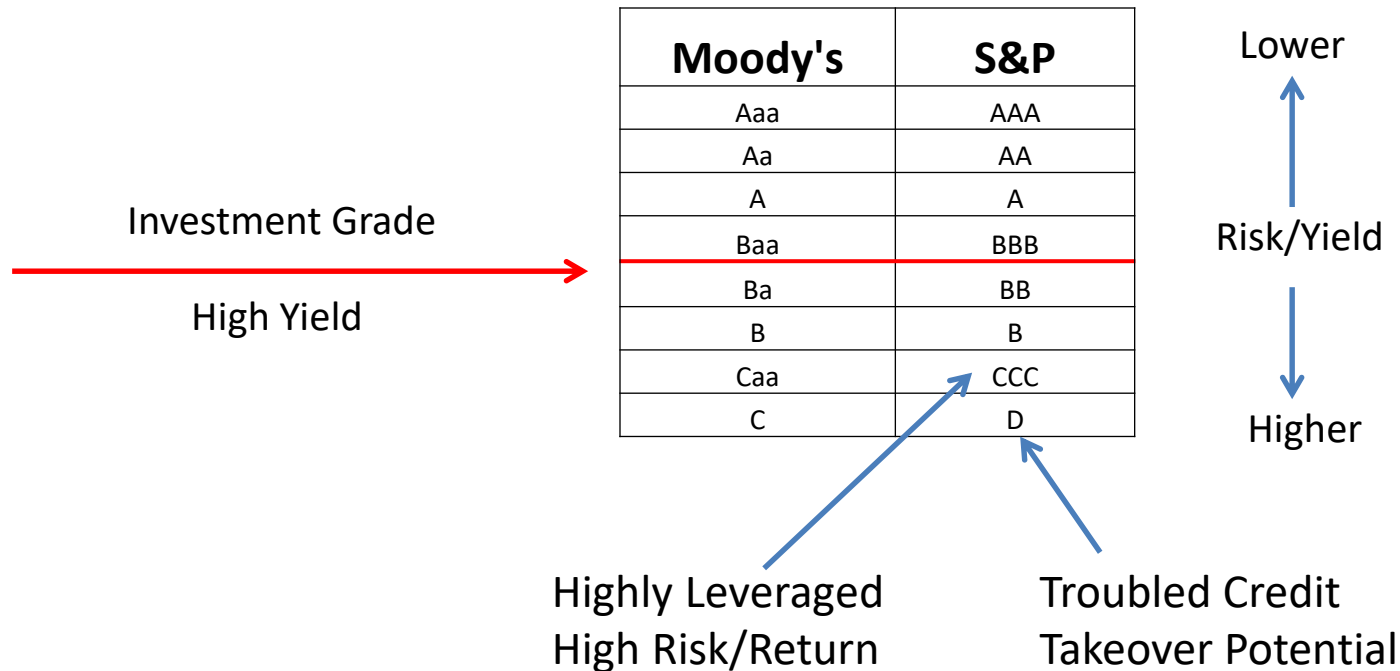
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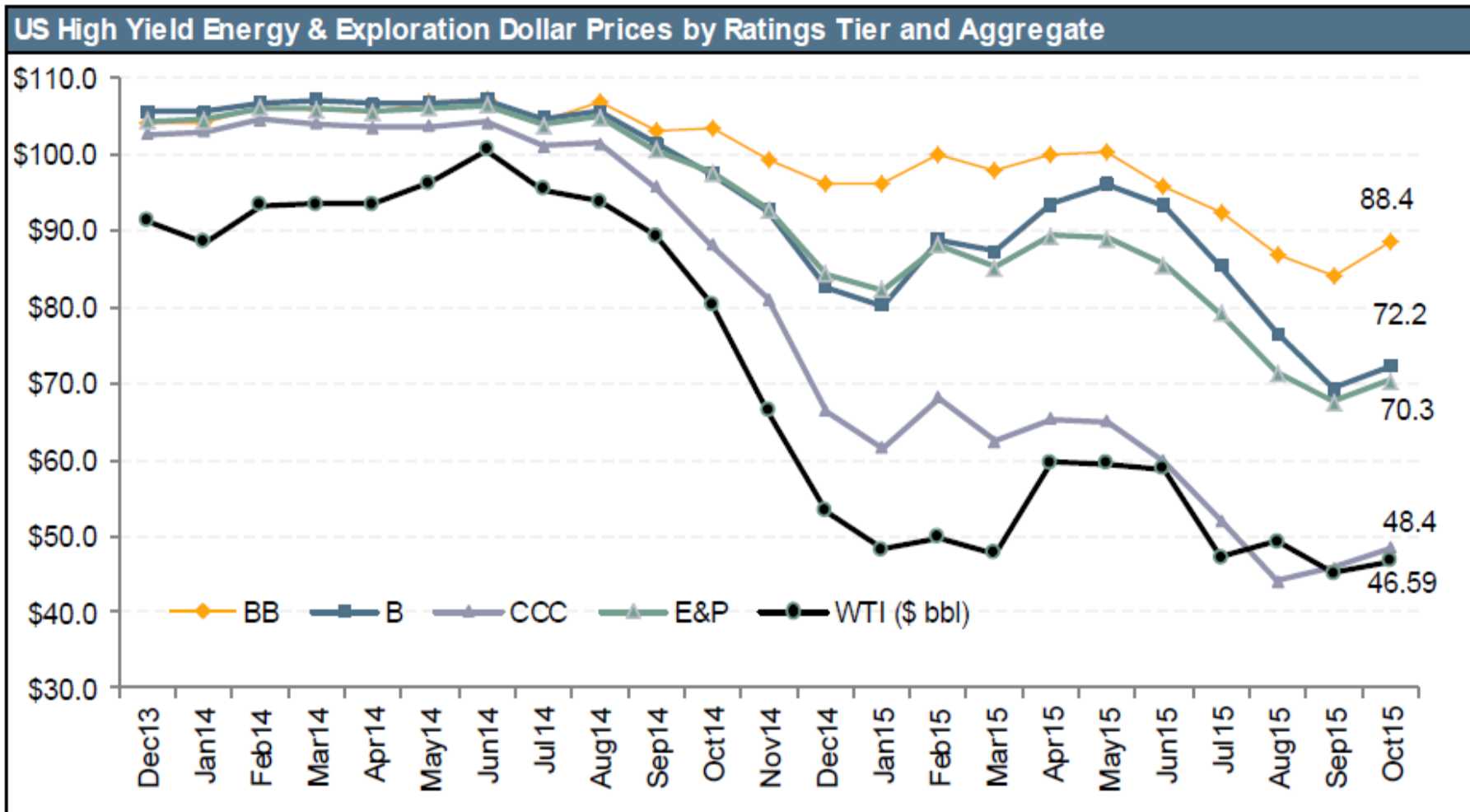
- High Yield bonds are issued by companies that do not qualify for “investment grade” ratings by one or more of the major ratings agencies (Moody’s, S&P, and Fitch)
- These issuers must pay a **higher interest rate** in order to attract investors to compensate them for the **risk** associated with investing in organizations of lower credit quality
- Low correlation with other parts of the bond market
- Often perform well in a rising interest rate environment
 - Investment Grade bonds trade on interest rates and rate expectations. HY tends to trade on credit and economic sensitivity.



Source: J.P. Morgan



High Yield – Where We Were Last Year – Oil Prices Falling



Source: CreditSights, BofA/ML indices data presented is on a monthly basis
data through 10/31/2015



- “Fallen Angels” – formerly investment grade
- “Rising Stars” – small or newer companies
- High Debt Companies – refinancing debt, takeovers
- Capital Intensive Companies (cable TV, telecom, hotels)
- Foreign Governments and Corporations

Source: SIFMA

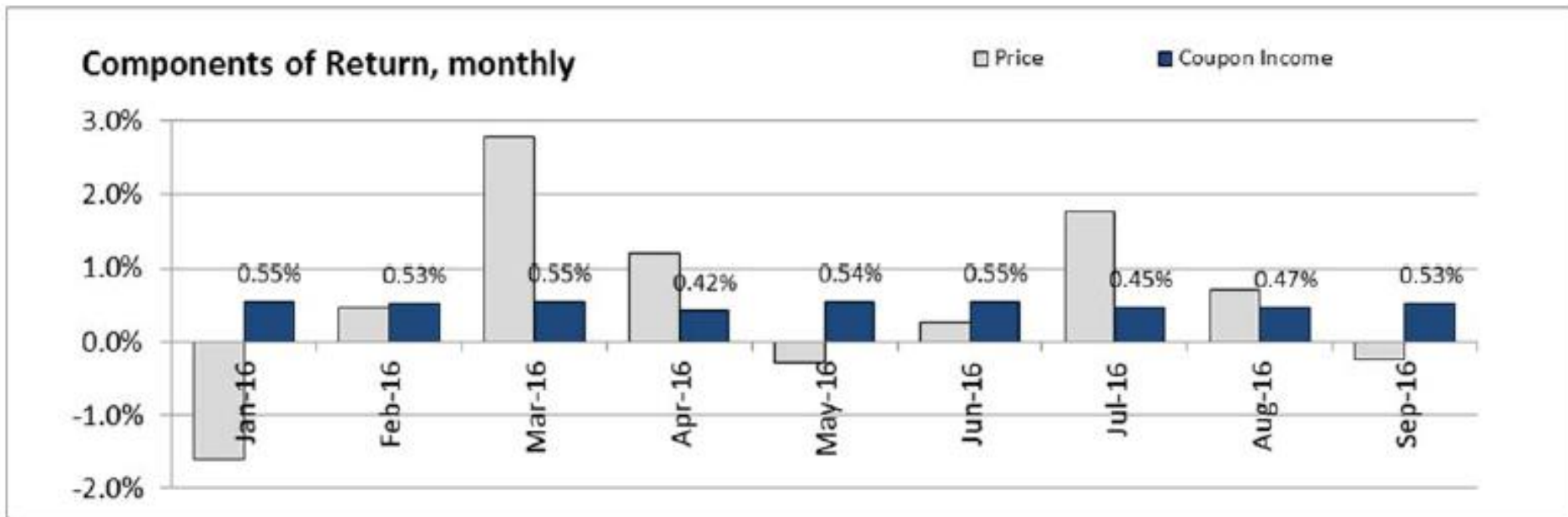
Sample Fallen Angels 2016 – Energy & Materials



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		Coupon	Maturity	Current Ratings	Downgrade Date	Price at Downgrade	10/31/16 Price	Return
AALLN	Anglo American	4.875%	05/14/25	Ba2/BB	02/15/16	60.94	102.37	75%
CVECN	Cenovus	3.800%	09/15/23	Ba2/BBB	02/18/16	80.99	99.06	26%
CLR	Continental Resources	3.800%	06/01/24	Ba3/BB+	02/18/16	63.25	91.66	50%
DVN	Devon Energy	3.250%	05/15/22	Ba2/BBB	02/25/16	76.61	100.17	34%
DO	Diamond Offshore	3.450%	11/01/23	Ba2/BB+	02/29/16	72.29	89.05	27%
ECACN	Encana	3.900%	11/15/21	Ba2/BBB	02/18/16	63.18	101.64	66%
ENLK	EnLink Midstream	4.150%	06/01/25	Ba2/BBB-	02/25/16	62.60	97.87	62%
ESV	EnSCO	4.500%	10/01/24	B1/BBB-	02/29/16	50.92	80.30	65%
FCX	Freeport-McMoRan	4.550%	11/14/24	B1/BB-	01/27/16	43.49	91.77	120%
MRO	Marathon Oil Corp.	3.850%	06/01/25	Ba1/BBB-	02/25/16	67.25	96.53	48%
NBR	Nabors Industries	5.100%	09/15/23	Ba2/BBB-	03/03/16	66.18	99.49	57%
NE	Noble Corp.	5.950%	04/01/25	B1/BB+	02/29/16	50.88	81.38	70%
RDC	Rowan Companies	4.750%	01/15/24	B1/BB	02/29/16	60.14	83.91	46%
SWN	Southwestern Energy	4.950%	01/23/25	B1/BB-	02/18/16	59.29	95.60	68%
SPN	Superior Energy Services	7.125%	12/15/21	B2/BB	03/14/16	72.33	98.06	44%
<u>VALEBZ</u>	<u>Vale</u>	<u>3.750%</u>	<u>01/10/23</u>	<u>Ba3/BBB-</u>	<u>02/26/16</u>	<u>73.15</u>	<u>105.67</u>	<u>49%</u>
Avg:						63.97	94.66	54%

Sample Monthly High Yield Performance in 2016





Private foreign investor net flows to U.S. fixed income

Cumulative foreign private net flows into USTs and Corporates, \$ billion



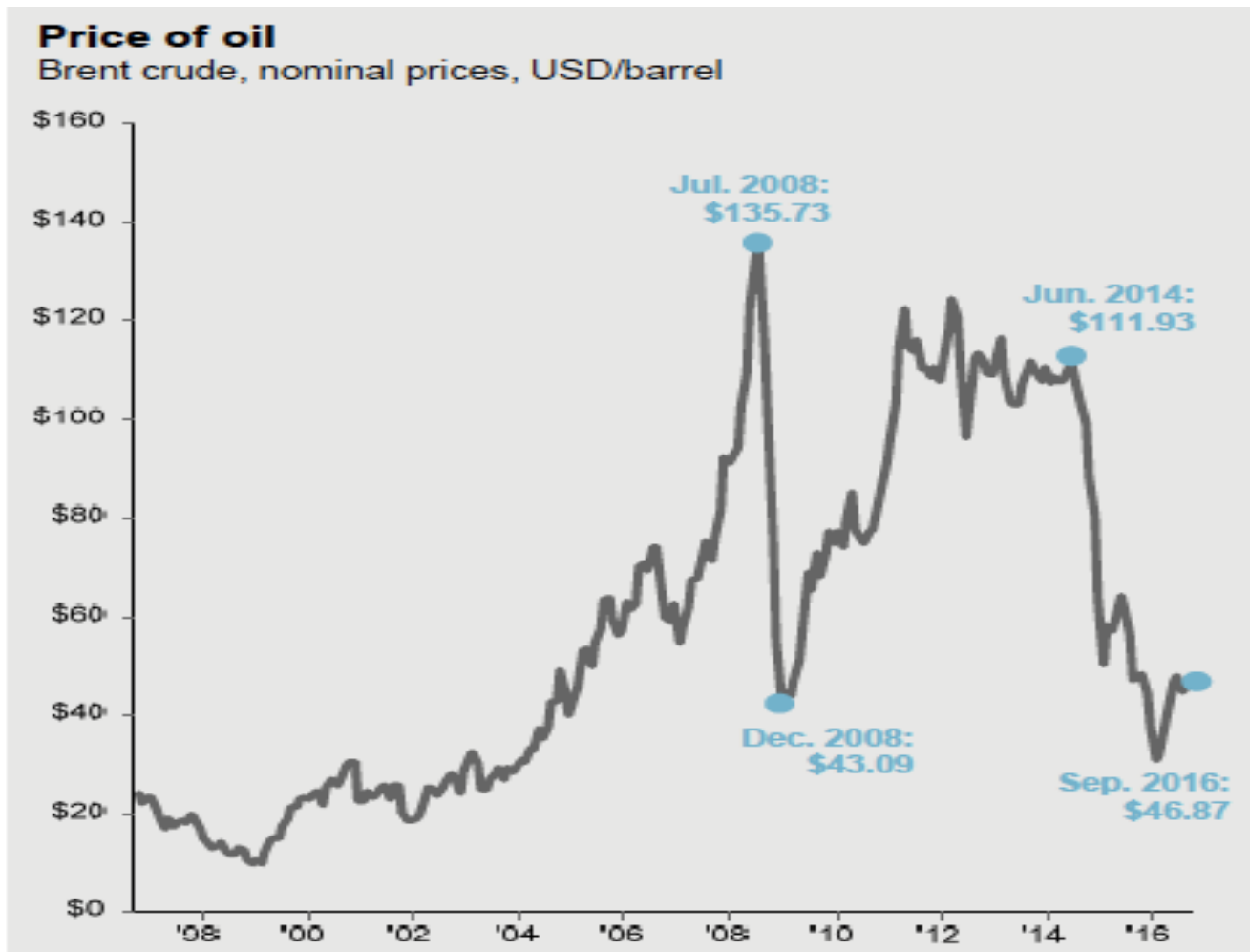
Source: FactSet, J.P. Morgan Asset Management; (Bottom left) U.S. Treasury.

High Yield - Correlations Remain Low



U.S. Treasuries	Correlation to 10-year	Avg. Maturity	Yield		Return
			9/30/2016	6/30/2016	2016 YTD
2-Year	0.62	2 years	0.77%	0.58%	1.20%
5-Year	0.91	5	1.14%	1.01%	3.96%
10-Year	1.00	10	1.60%	1.49%	7.14%
30-Year	0.92	30	2.32%	2.30%	16.96%
TIPS	0.57	10	0.00%	0.09%	7.27%
Sector					
Broad Market	0.85	7.8 years	1.96%	1.91%	5.80%
MBS	0.79	5.1	2.06%	2.07%	3.72%
Municipals	0.44	10.0	1.72%	1.57%	4.35%
Corporates	0.43	10.9	2.84%	2.88%	9.20%
High Yield	-0.26	6.3	6.17%	7.27%	15.11%
Floating Rate	-0.21	2.3	1.75%	1.65%	1.93%
Convertibles	-0.31	--	0.99%	0.92%	8.94%
ABS	-0.02	5.4	1.97%	1.94%	5.68%

Source: JP Morgan Guide to the Markets 9/30/16



Source: JP Morgan Guide to the Markets 9/30/16

What is the “New Normal” for oil prices?

Stability is good for the High Yield market

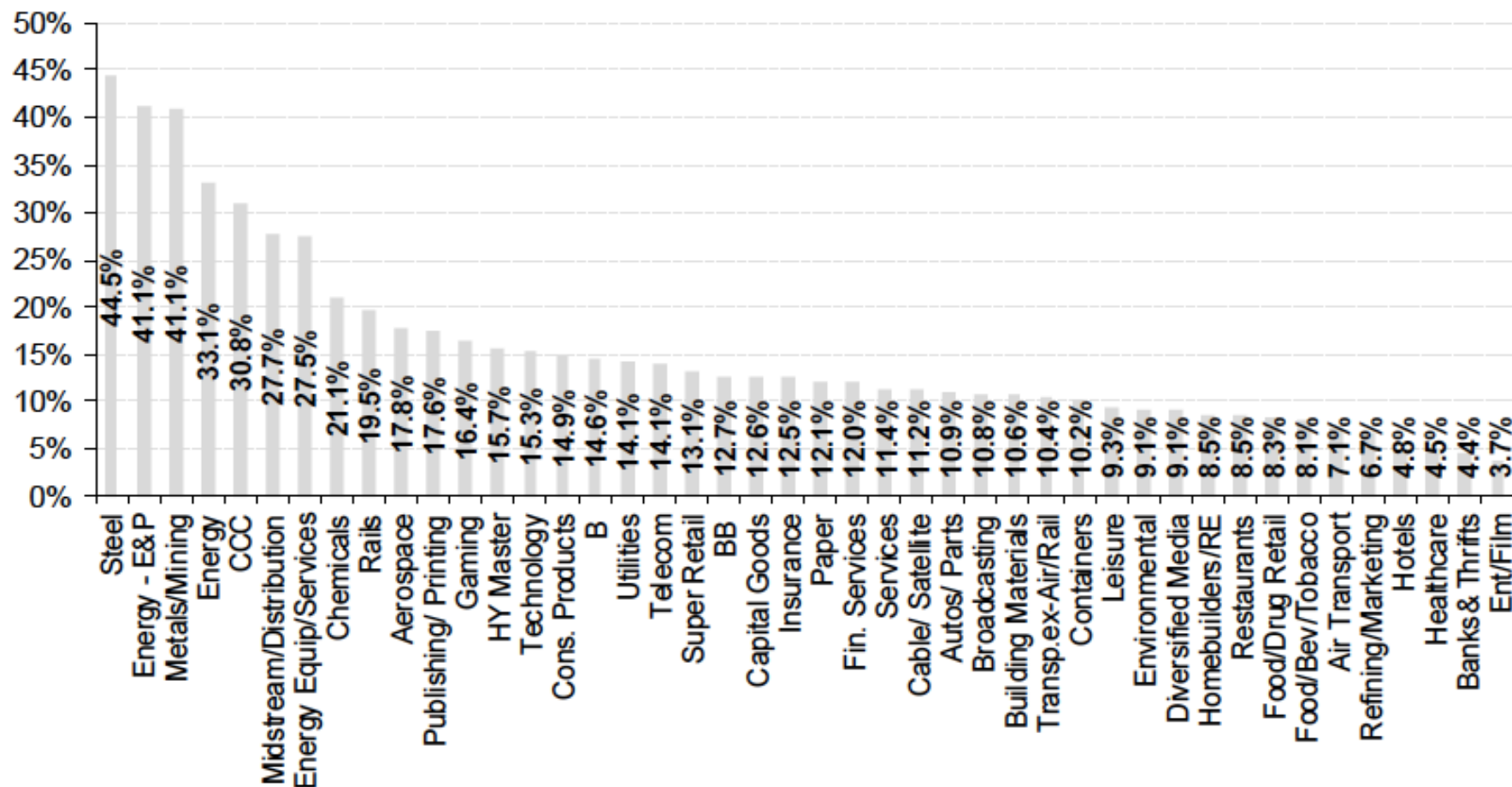
OPEC Agreement?

YTD Sector Performance Illustrates Energy Rebound



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US HY Industry and Rating Tier Indexes Total Returns Year to Date



Source: CreditSights, BofA/ML Indices data through 10/31/2016



FRED 

— Civilian Unemployment Rate



Source: US Bureau of Labor Statistics
fred.stlouisfed.org

myf.red/g/79wx

Absent a recession
High Yield should
generate consistent
returns in line with
the portfolio's coupon

We don't believe the
U.S. enters a recession
in 2017

The data suggests
modest economic
growth and low
inflation

Unemployment at 4.9%



Average Hourly Earnings growing at 2.4%

Low gas prices help consumers and businesses



U.S. Auto Sales
17 million+



Housing starts
1.1 million +



- Potential Stimulus from new President
 - Infrastructure spending
 - Decreased energy regulations
 - Tax cuts for businesses who employ in U.S.
- Inflation? Higher interest rates? Have oil prices come back as far as they will?
- Portfolio Construction
 - Spreads tightened significantly in 2016
 - Higher quality positioning prudent at this time
 - Shorter duration prudent at this time



The US High Yield Bond Market Offers:

- A large opportunity set
- High current income
- Low correlation to other bonds
- Historical performance when interest rates rise
- Portfolio diversification benefits
- Attractive total return potential
 - Absolute and risk adjusted (Sharpe Ratio)
- Compelling returns with manageable risk
 - Credit research, duration management, quality constraints, sector diversification, active management