

# Bond Bargains Are Here

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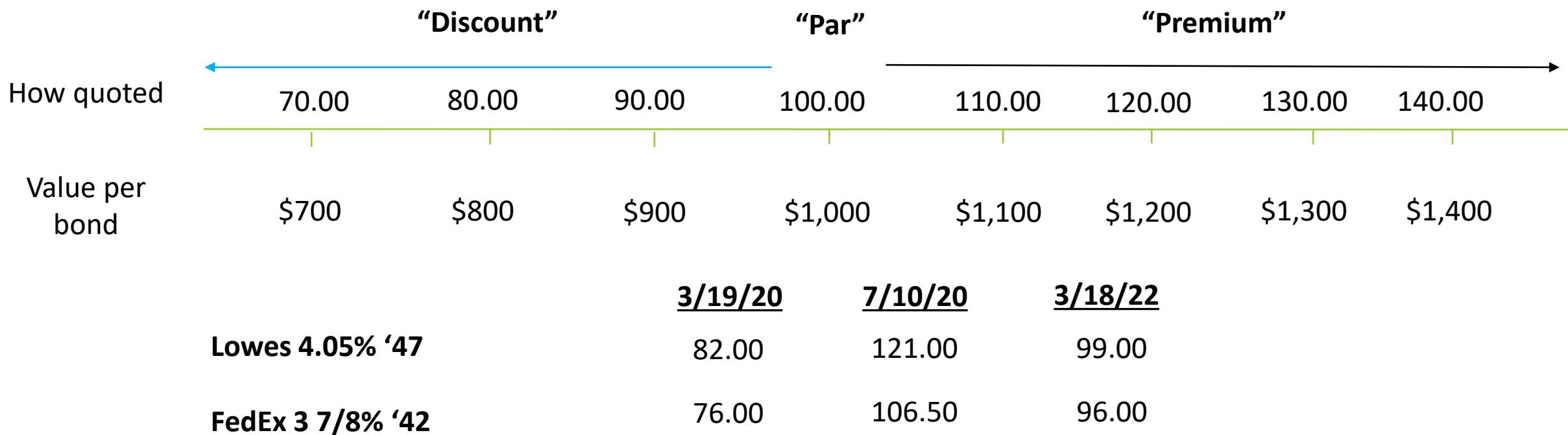
March 19, 2022



# How Do We Know When Bonds Are a Good Value?

# Individual Bonds Are Quoted Relative to Par Value

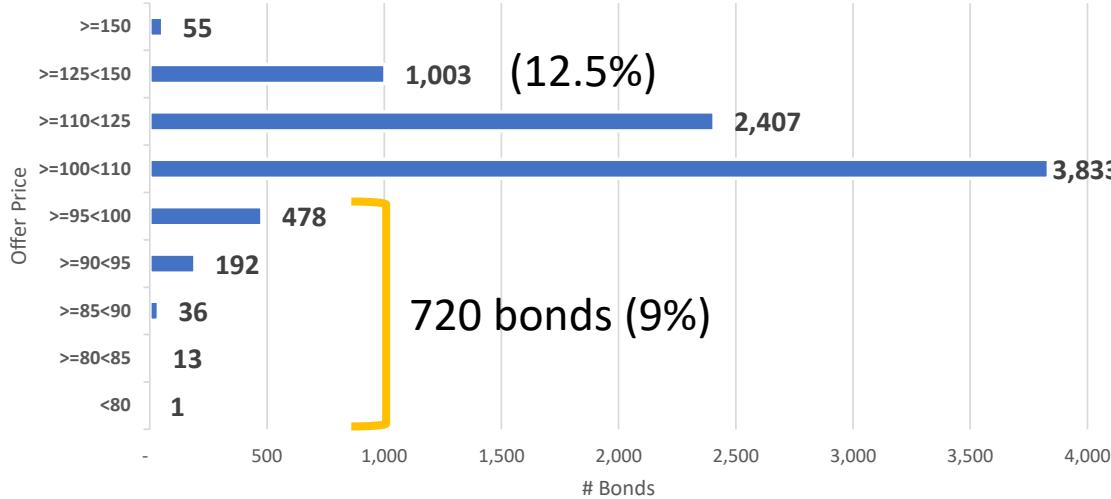
Since individual corporate bonds are quoted as a percentage of their face value, investors can begin assessing a bond's relative value



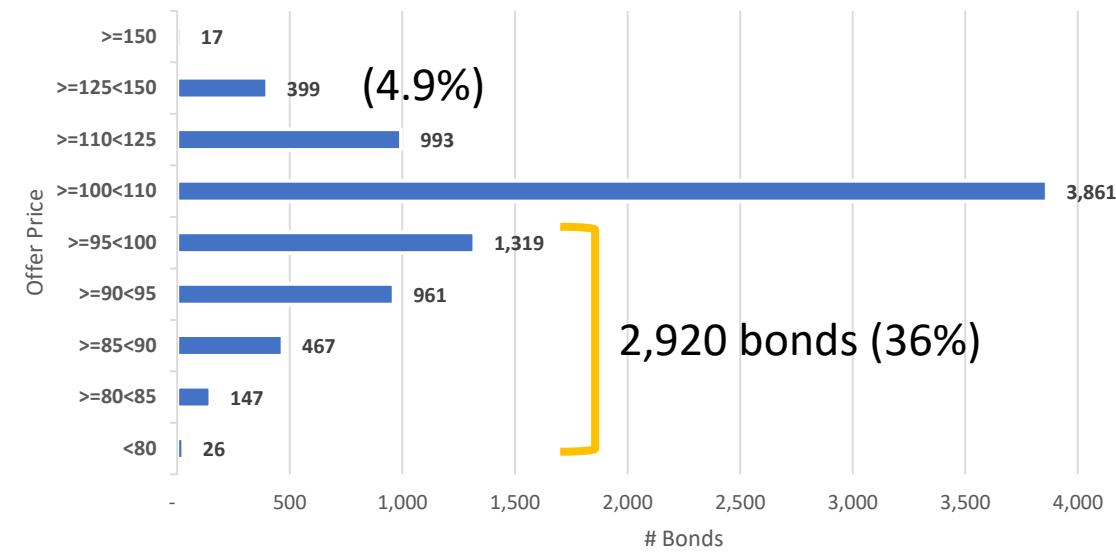
# Investment Grade Corporate Bond Prices: May '21 vs. March '22

- Higher US Treasury yields have driven many investment grade corporate bond prices lower, creating buying opportunities not seen in years

**8,018 Investment Grade Bonds – May 14, 2021\***



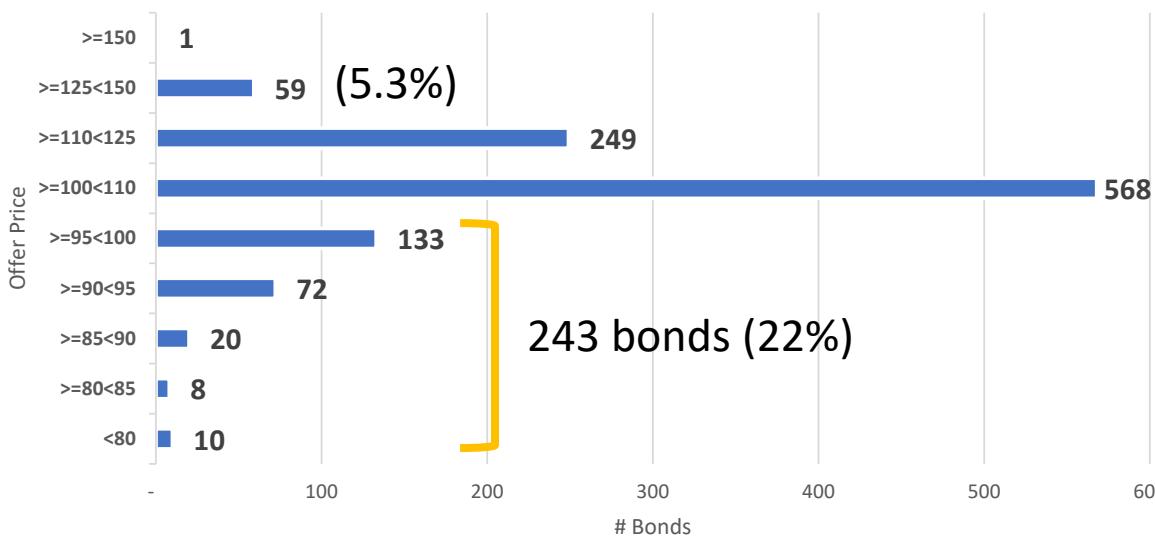
**8,190 Investment Grade Bonds – March 17, 2022\***



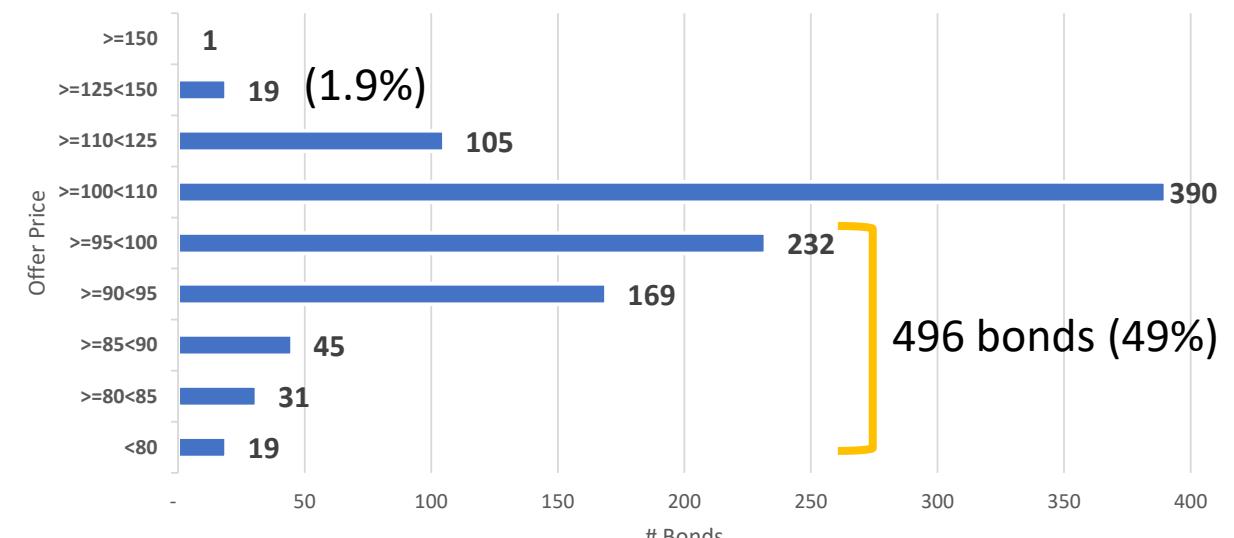
# High Yield Corporate Bond Prices: May '21 vs. March '22

On March 17, 49% of high yield corporate bonds trading on Fidelity.com were trading at less than par

**1,120 HY Bonds – May 14, 2021\***



**1,011 HY Bonds – March 17, 2022\***

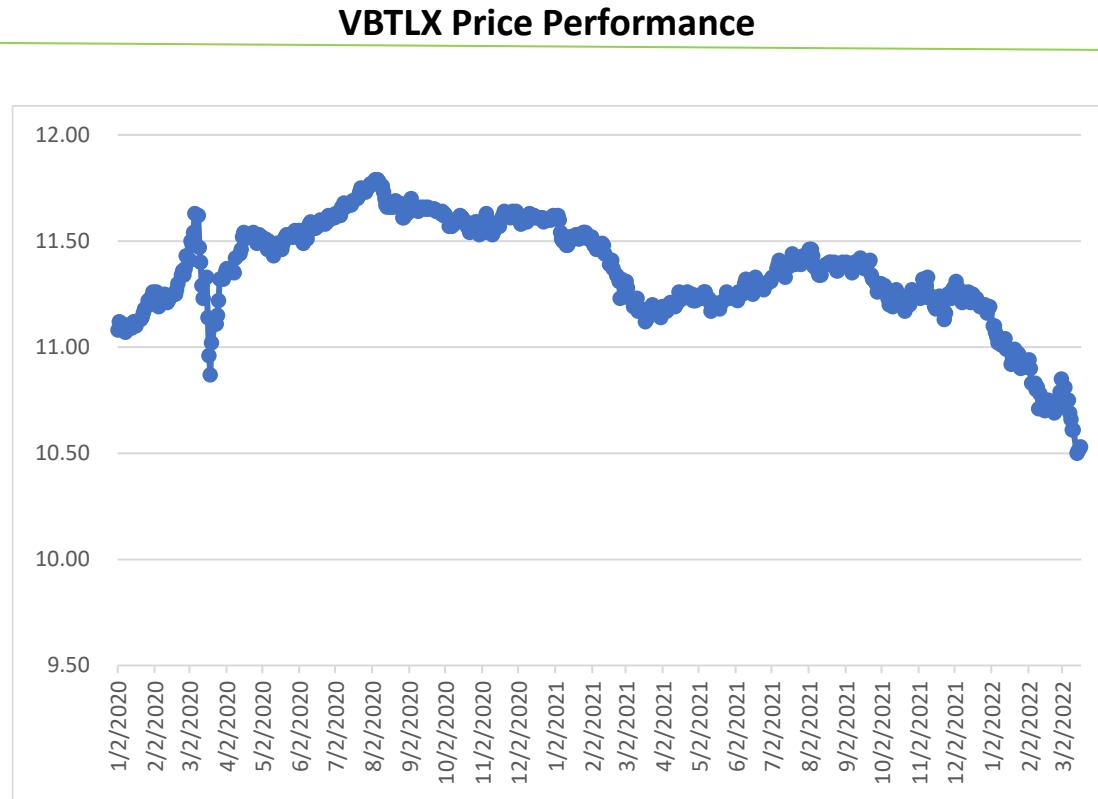


# Bond Funds: Impossible-to-assess prices and high turnover

Bond Fund	Net Assets \$BB*	# Bonds	3/18/22 Price	Turnover*
<b>Vanguard Total Bond Market Index Fund (VBTLX)</b>	\$305	10,127	10.53	69%
<b>iShares AGG</b>	\$85	10,149	108.48	179%
<b>PIMCO Total Return</b>	\$67	~2,500	9.66	133%
<b>MetWest Total Return</b>	\$78	1,916	10.27	474%

# Cannot Identify Value with Bond Funds

Bond fund investors lack the tools of individual bond investors to assess value and potential upside



Source: Nasdaq market data

- Bond funds are priced off NAV / share rather than as a percentage of par value
- Bond funds lack financials similar to bond issuers, so investors cannot compare financial metrics to prices
- Bond funds don't have credit spreads
- When assessing upside, a bond fund does not have to return to "par value" like a bond does and can stay at or below the current pricing level long term

# Value Investing: Individual Corporate Bonds vs. Funds and Stocks

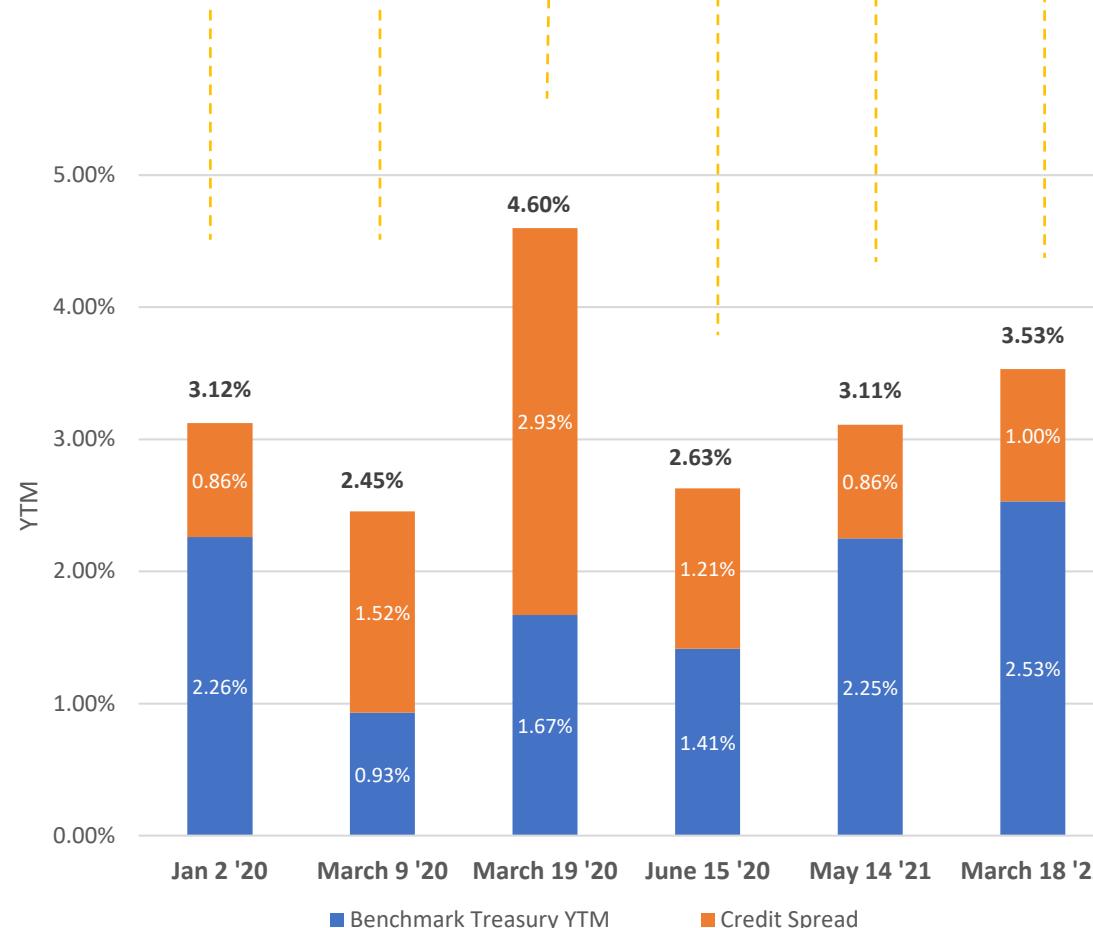
	Individual Corporate Bonds	Bond Funds	Stocks
Quantifiable Downside			
Can Compare Financial Metrics to Prices			
Contract with Issuer to Pay Face Value			
Higher Upside			

## Drivers of Recent Bond Price Movements

# Drivers of Changes in Apple '45 Bond Price

## Building Blocks of Apple 4.375% '45 Bond Price: 2020-Mar 18 '22

Price: **121.83 135.91 96.69 131.78 121.67 113.42**



## Apple 4.375% '45 Daily Bond Price: 2020-Mar 18 '22



# For More on Understanding Credit Spreads....

bondsavvy.com/corporate-bonds

 **BondSavvy**  
Making You a Better Bond Investor.

Why Returns Sample About Learn Reviews 4.9 ★ (33) Get Started 

## Corporate Bond Investing Tips and Resources

Blog Corporate Bond FAQ

How To Invest in Corporate Bonds 

Crash Course Video (\$ 



**How To Calculate and Use Leverage Ratios**

We calculate leverage ratios to assess default risk and relative value of corporate bond investments. Leverage ratios tell us how much... [Read more](#)



**Where Can I Buy Corporate Bonds Online?**

Corporate bond investors can buy bonds online from a number of online brokers, including Fidelity Investments, E\*TRADE Financial, Charles Schwab, and... [Read more](#)



**How BondSavvy Is Better Than Institutional Credit Research**

BondSavvy makes CUSIP-level **corporate bond investment recommendations** whereas most credit research provides issuer-level... [Read more](#)



**What Are Credit Spreads and How Do They Work?**

Credit spreads, also known as Treasury spreads, are the difference between a corporate bond's yield to maturity ("YTM")



**What Corporate Bond Returns Does BondSavvy Seek To Achieve?**

Many bond investors believe a bond's yield is the only return you can achieve. Further, many media outlets such as CNBC... [Read more](#)



**What Role Do Individual Corporate Bonds Play in Income Investing?**

Individual corporate bonds are a crucial component of income investing as they provide yields generally higher than

# Rising Treasury Yields Don't Impact All Bonds the Same Way

- The 0.76-0.79 percentage point increase in long-dated US Treasury yields has impacted some corporate bonds more than others

## Corporate Bond Price Charts: December 3, 2020-March 18, 2022\*

**Natural Gas Operator**



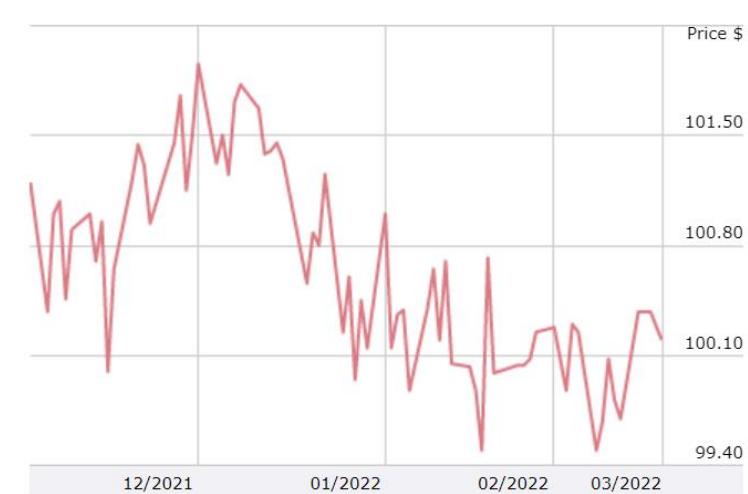
**Callable @ 102 in May '22**  
**Matures 2025**

**Leading Tech Company**



**Make-Whole Call**  
**30+ Year Maturity**

**Quad / Graphics 7.00% 5/1/22**



## How Do We Identify Value in Corporate Bonds?

# Rule #1: Don't Rely on Bond Ratings

	Moody's	S&P
Investment Grade	Aaa	AAA
	Aa1	AA+
	Aa2	AA
	Aa3	AA-
	A1	A+
	A2	A
	A3	A-
	Baa1	BBB+
	Baa2	BBB
	Baa3	BBB-
	Ba1	BB+
	Ba2	BB
	Ba3	BB-
	B1	B+
	B2	B
Non-Investment Grade or "High Yield"	B3	B-
	Caa1	CCC+
	Caa2	CCC
	Caa3	CCC-

**Bond ratings impact how bonds trade:**



Investment-grade bonds can be sensitive to changes in Treasury yields

Upgrades and downgrades can impact corporate bond prices



**But....they have many shortcomings:**



Can often go years without changing



Don't speak to the value of a bond

"Fuzzy metrics" often weighted more heavily than traditional credit ratios

# Good BBB vs. Bad BBB

Many market gurus have warned about lurking trouble in BBB-rated corporate bonds, but not all BBB bonds are created equal

- Kroger and AB InBev have similar ratings, but Kroger has much stronger financials
- Kroger is what an investment-grade issuer should be: a strong business with low leverage
- Investors doing their homework can find opportunities where a bond issuer's credit risk is not aligned with its bond rating

## Kroger vs. AB InBev Financials \*

	\$ in millions	Kroger	Anheuser-Busch InBev
June 15 '20 Rating		Baa1 / BBB	Baa1 / BBB+
Cash		\$2,726	\$7,169
Total Debt		<b>\$12,603</b>	<b>\$100,949</b>
Revenue (Last 12 Months)		\$126,584	\$51,108
EBITDA (Last 12 Months)		<b>\$6,028</b>	<b>\$19,903</b>
Leverage Ratio		2.1x	5.1x
<b>Q1 '20 Growth</b>			
Revenue		11.5%	-10.0%
EBITDA		25.2%	-17.7%

\* AB InBev balance sheet data are as of 12/31/19 while its income statement figures are through 3/31/20. Kroger's financials are for the period ending 5/23/20

# Why Kroger and AB InBev Have Similar Ratings

- Based on industry, Moody's and S&P weigh different factors to determine a corporate bond's rating
- Since “Leverage and Coverage” only comprise 30% of AB InBev’s rating, the other factors inflate its rating, which results, in our view, an undeserving Baa1 Moody’s rating for the company

## Moody's Weightings: Retail Industry

Factor	Factor Weighting	Sub-Factor	Sub-Factor Weighting
Scale	10%	Revenue	10%
Business Profile	30%	Stability of Product	10%
		Execution and Competitive Position	20%
<b>Leverage and Coverage</b>	<b>45%</b>	EBIT / Interest Expense	15%
		Retained Cash Flow / Net Debt	15%
		Debt/EBITDA	15%
Financial Policy	15%	Financial Policy	15%
<b>Total</b>	<b>100%</b>	<b>Total</b>	<b>100%</b>

## Moody's Weightings: Alcoholic Beverage Industry

Factor	Factor Weighting	Sub-factor	Sub-factor Weighting
Scale	15%	Revenue (USD Billion)	15%
Business Profile	32.5%	Diversification and Exposure to Riskier Markets	10%
		Category / Brand Strength and Diversification	7.5%
		Global Industry Position	7.5%
		Innovation, Distribution and Infrastructure	7.5%
Profitability	7.5%	EBITA Margin	7.5%
<b>Leverage and Coverage</b>	<b>30%</b>	RCF / Net Debt	10%
		Debt / EBITDA	12.5%
		EBIT / Interest Expense	7.5%
Financial Policy	15%	--*	15%
<b>Total</b>	<b>100%</b>		<b>100%</b>

\*This factor has no sub-factors.

Source: Moody's Investors Service

# How We Identify Value

\$ in millions, except quote values Bond	Quote <sup>(1)</sup>		Offer Price		Credit Ratings	# Quotes (# Bonds)	Amount Outstanding	Credit Ratios		
			Yield to Maturity <sup>(1)</sup>	Spread to Treasury <sup>(1)</sup>				Leverage <sup>(2)</sup>		Interest Coverage <sup>(3)</sup>
	Bid	Offer						Gross	Net	
	93.70	94.61	10.08%	8.83%	B3 / B	11 / 9 (2,500)	\$350	4.1x	3.6x	3.4x
	97.27	98.00	4.07%	2.48%	Ba3 / BB-	8 / 10 (2,215)	\$500	0.9x	0.8x	25.8x
	91.59	92.50	6.42%	4.84%	B3 / B-	4 / 6 (1,500)	\$1,500	2.9x	2.2x	5.4x
	84.70	85.56	3.28%	1.20%	Baa1 / A-	7 / 7 (1,800)	\$1,500	0.9x	Negative	38.1x

*Subscribe to learn  
recommended bonds*

(1) Quotes as shown on Fidelity.com from 1-1:15pm EST on January 12, 2022

(2) Most recent quarter's total debt divided by last twelve months' EBITDA

(3) Last 12 months' EBITDA divided by last quarter's annualized interest expense

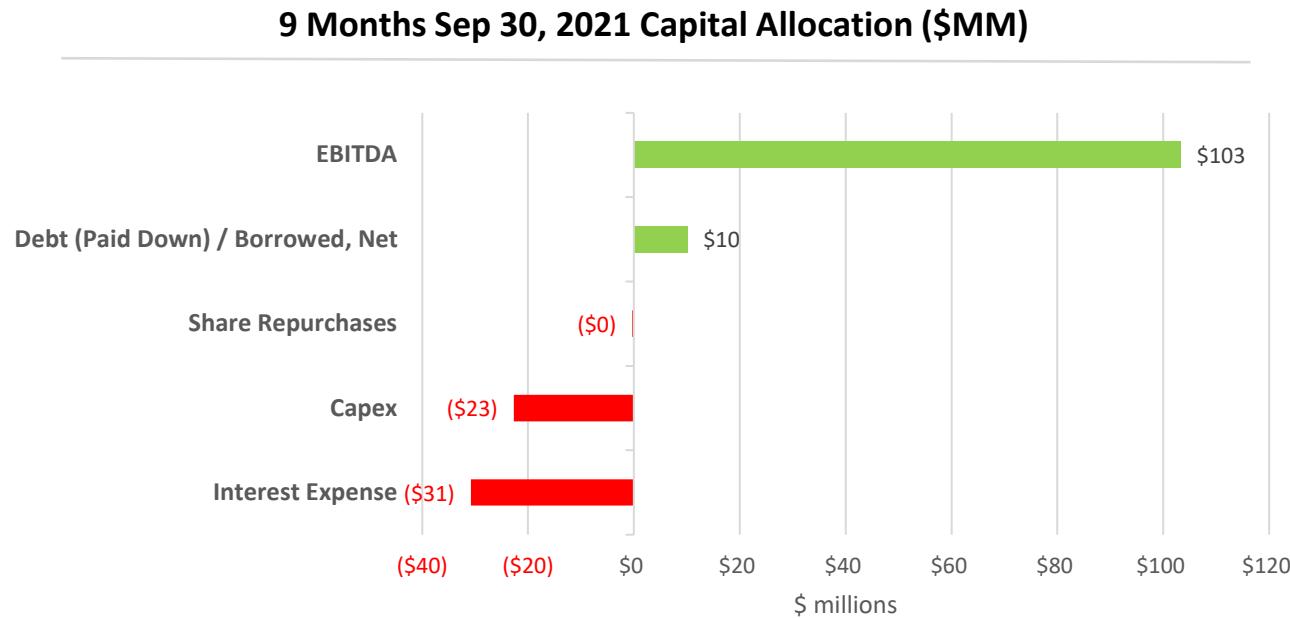
# Recommended Bonds: Size, Balance Sheet, and Duration Risk

Financials as of, or for date ending on, September 30, 2021

\$ in millions, except quote values		Spread to Treasury <sup>(1)</sup>	YTD YOY Growth		Last 12 Months			Debt	Cash	Interest Rate	Upcoming Maturities	
Bond			Revenue	EBITDA	Revenue	EBITDA	Margin				Amount	Date
	<i>Subscribe to learn recommended bonds</i>	8.83%	-4%	9%	\$595	\$142	24%	\$577	\$60	Low	\$226 \$350	Oct '23 May '25
		2.48%	32%	117%	\$25,071	\$1,671	7%	\$1,436	\$119	Low	\$550	Sep '25
		4.84%	1%	9%	\$12,811	\$3,478	27%	\$10,024	\$2,445	Low	\$2,000 \$1,500	Jul '22 Mar '23
		1.20%	17%	24%	\$9,052	\$4,110	45%	\$3,650	\$9,718	High	\$850 \$400	Sep '26 Jun '27

(1) Quotes as shown on Fidelity.com from 1-1:15pm EST on January 12, 2022

# Understanding Capital Allocation



- Comparing leverage ratios and growth to a bond's credit spread is the first step to identifying value

BUT...

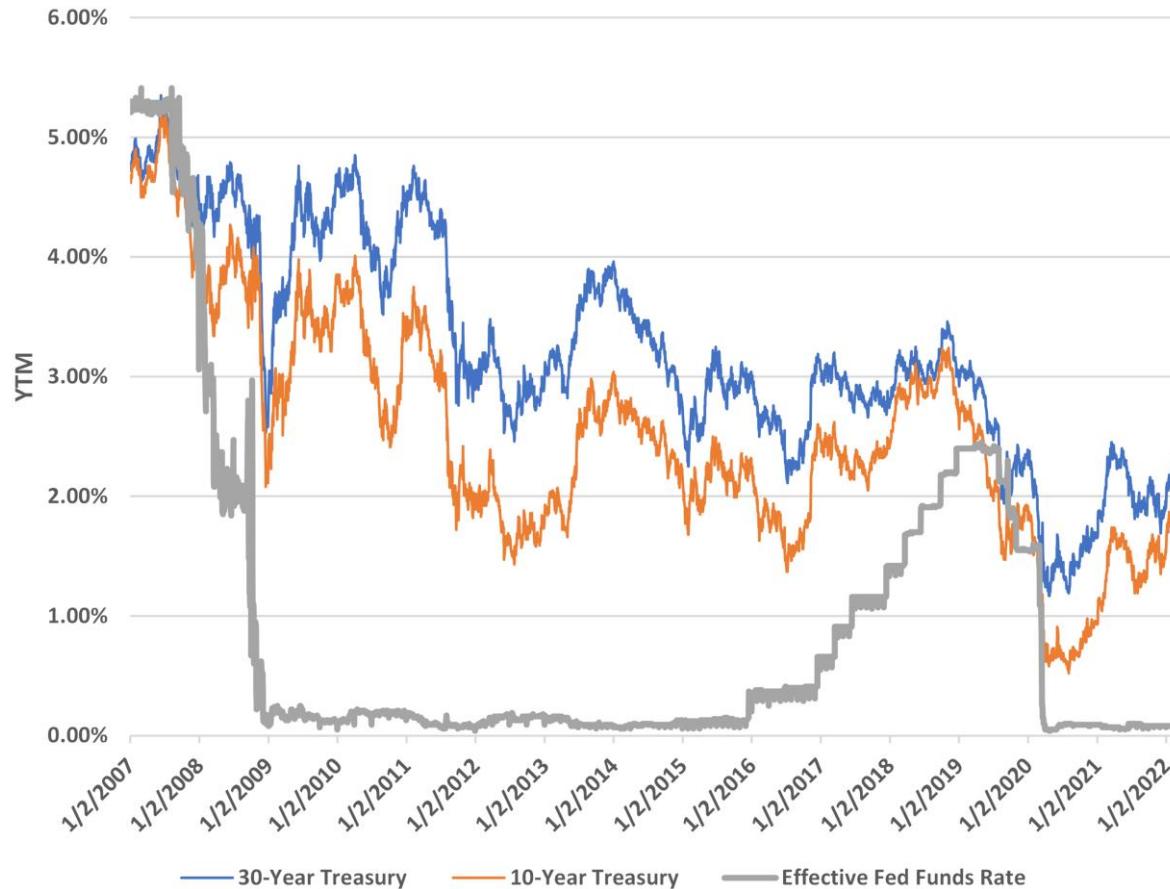
- The next key question is what a bond issuer does with its profits
- Many companies allocate significant portions of profits to share buybacks and dividends, which do not improve the lot of bondholders
- Issuers with 'value-enhancing' capital allocation can improve their credit profiles over time

## How Have We Been Approaching the Current Market?

- **Focus on high-yield bonds:** Of our four bond recommendations made January 12, three were high yield bonds, which are generally less sensitive to changes in US Treasury yields
- **Value in investment grade:** We continue to identify values in investment-grade corporate bonds that have fallen to the 70s and 80s
- **Moving bonds back to buy:** A number of previously recommended bonds remain holds; however, we intend to move certain of them back to BUY as market conditions improve
- **Strong issuer financials:** Of 40+ bonds recommended buy or hold, all but 6 were issued by companies with leverage ratios of 3.5x or less

# The Fed Holds Some but not All of the Cards

## US Treasury Yields vs. Effective Fed Funds Rate: 2007-Feb '22



- Short-term Treasury yields can move in lockstep with the federal funds rate, but the same is not true with longer-dated Treasurys
- As shown, US Treasury yields can be highly volatile even when the fed funds rate isn't changing
- US Treasurys are a \$20+ trillion market that is driven by many factors other than Fed activity

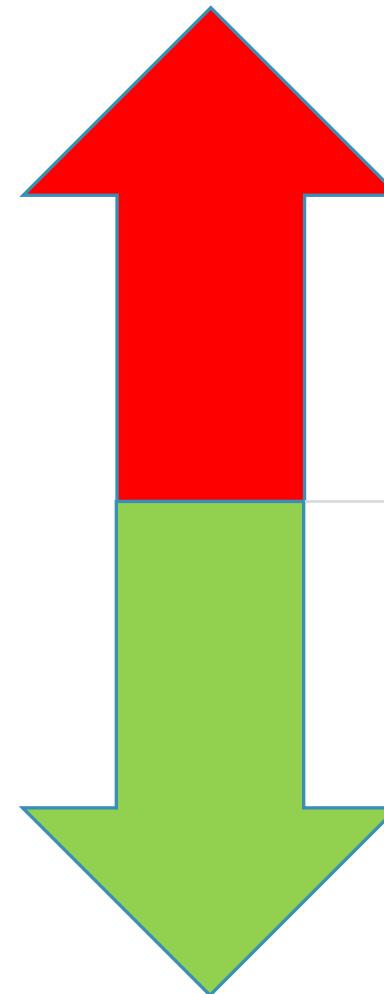
# Doesn't inflation erode the value of bonds?

## Key Recent Drivers of Long-Term US Treasury Bond Yields

- Believing “if inflation goes up, bond prices go down” oversimplifies how the bond market works
- Inflation is one of many factors that impacts US Treasury yields, as shown in the chart
- If rampant inflation ensues, it could hurt long-term investment grade bonds

**BUT...**

- Higher commodity prices have driven high yield bonds issued by oil & gas and other commodity-based issuers higher



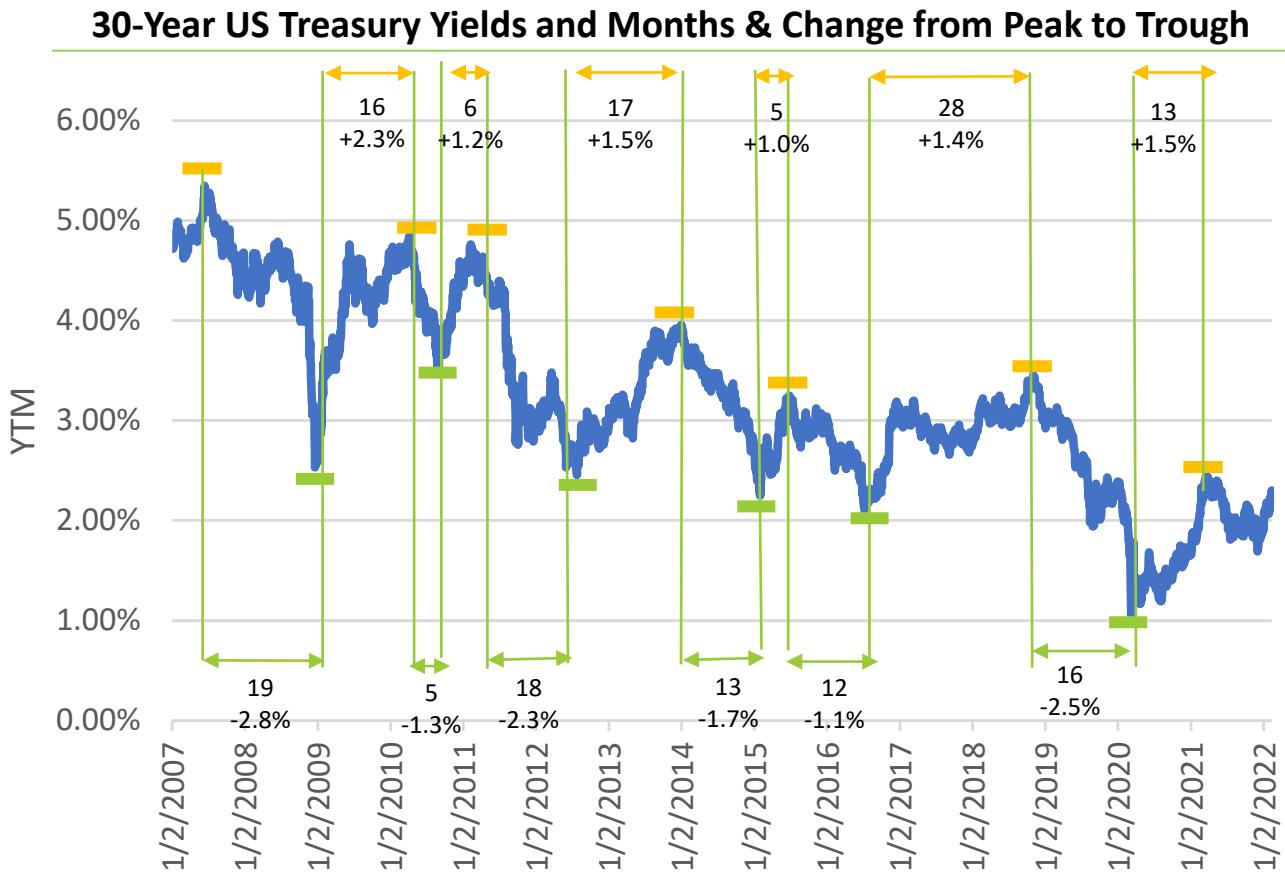
### Factors driving Treasury yields higher

- Record levels of US Treasury issuance
- *Higher inflation expectations*
- Increased appetite for riskier investments as economy recovers
- Reduced Treasury purchases by foreign investors

### Factors driving Treasury yields lower

- Treasury yields still high vs. Germany and Japan
- Fed purchases of Treasurys
- Global growth outlook still mixed
- Taxable bond fund inflows
- *Technology and globalization have kept inflation low for decades*

# US Treasury Yield Volatility Can Be a Long-Term Investor's Friend



Source: US Treasury data and BondSavvy calculations

- Treasury yields are volatile, and peaks and troughs regularly occur
- Going back to 2018, many investors stayed away from bonds due to the 'rising rate environment'
- Investing in bonds over time limits investors' risk of buying at inopportune times
- Upward movements in US Treasury yields could cause us to hold a position longer than usual

## Inflation's Impact on Corporate Bonds Can Often Be Overstated

- Inflation can be a tailwind for many high yield corporate bond issuers, especially energy companies
- Inflation is an historical number and, therefore, doesn't speak to future price increases, which is what could *potentially* erode the value of certain securities
- While inflation is reported as one number, it's not the same for everyone:
  - For example, housing makes up a large weighting of the CPI, but for homeowners with fixed-rate mortgages, the impact can be negligible

**Inflation, however, does cause many bond investors to head for the exits, which can create buying opportunities**



## *The strong potential returns and relative safety of corporate bonds are too important to ignore*



**I founded BondSavvy to make bond investing easy and to increase investor returns**



**Host 11 webinars annually, where we make new recommendations, update existing recommendations, and answer subscriber questions**



**Supplement webcasts with regular email updates**



**View our “Returns” page to see how our performance has compared to the leading corporate bond ETFs**

## Next Subscriber Events:

**March 24 @ 4pm CDT: *The Super Bondcast***

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# Price increase March 20 at 11am CDT

- **\$150 increase for one-year subscription**
- **\$350 increase for two-year subscription**

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Thank you and stay well

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