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High Yield commentary

Market commentary

The high yield market was buffeted by contradictory forces throughout the first quarter, as investors wrestled with announcements from a steadfastly hawkish Fed and worries over the health of the banking system. Despite the volatility and uncertainty, the high yield market ended the quarter in positive territory. The Bloomberg Barclays High Yield Index finished up +3.57%. The Credit Suisse Leveraged Loan index also recovered from mid-March lows and ended up 3.11% for the quarter.

In January, credit markets overall were buoyed by positive data releases and improving economic conditions - namely slowing inflation, a resilient US labor market, China reopening and more optimistic economic outlooks from Europe. The market viewed these developments as supporting an impending moderation (if not a complete end) to the Fed's rate increases, along with a higher likelihood of the US avoiding a painful recession.

That optimism collapsed in February, as robust US data collided with a hawkish Fed. Markets finished the month pricing in a 5.5% rate peak and backtracking on any cuts in 2023. Volatility continued in March as news of trouble at Silvergate, Signature Bank and Silicon Valley Bank spread and roiled the markets. At their lows, the S&P 500 dropped 2.88%, the Bloomberg U.S. Corporate High Yield Index dropped 1.27% and the Credit Suisse Leveraged Loan Index fell 1.08%. Treasury rates were also markedly lower, with 5-year and 10-year rates down 58bp and 42bp respectively by month end. But swift action of central banks to address each event evidently appeased investors, and most markets came off their lows by quarter end. Despite the rebound, broader concerns remained.

In terms of ratings, only Caa-rated bonds were down in March. While Caas had outperformed all other rating cohorts earlier in the year, they finished the month down -1.37%. Meanwhile, Ba-rated and B-rated bonds were up +1.99% and +0.73% respectively. Ba bonds, being the most sensitive to rate moves, experienced a tailwind from falling rates. Caas, conversely, were hurt by an increasing likelihood of recession given the turmoil in the banking sector.

The head start of Caas earlier in the year, though, meant that the cohort was still the strongest performer over the quarter. Caas were up +4.96% in Q1 and outperformed B-rated (+3.47%) and Ba-rated bonds (+3.44%) over the period.

Similar to ratings performance, industry performance in March was mixed. Unsurprisingly, banking was the worst performing industry in the index falling 3.18% in March. However, wirelines also dropped 3.07% for the month, followed by retailers which fell 1.48%. The best performing industries by comparison were restaurants (+3.13%), electric (+2.83%), and lodging +2.74%. Over the quarter, leisure was by far the best performer (+9.38%) and wirelines the worst (-3.94%).

The varying performance of different issue sizes was also notable, with large issue bonds(1bn+) outperforming during the quarter.

	Return (%)
Issue size cohort	**QTD**
0-200MM	2.57
200-500MM	3.07
500MM-1BN	3.53
1BN+	3.89

Source: Bloomberg.

High yield mutual funds and ETFs continued to experience outflows, with March outflows totaling $4.3bn and year-to-date outflows totaling $17.9bn (Lipper.) Default activity decreased in March with US high yield bond and loan default rates (including distressed exchanges) falling 21bp and 5bp m/m to 1.91% and 2.22% respectively for the last 12 months. (JPM).

Source: Bloomberg, JPMorgan. Past performance is not necessarily indicative of future results. Performance shown above is gross and does not reflect the deduction of management fees. Please see disclosure at end for additional, important information. Please see the GIPS Reports attached for complete performance, including net, and benchmark descriptions. Any targeted performance results mentioned herein may not be achieved and materially different performance results may occur.

Strategy commentary

Mesirow's High Yield strategy began 2023 well, with the strategy besting its benchmark, the Bloomberg US Corporate HY Index over Q1. Strong credit selection was the main driver of outperformance over the period, with the rebounding of Caas also providing a modest tailwind.

As discussed, Caa bonds outperformed higher quality bonds during the quarter, a welcome reversal after underperforming the majority of last year. And given the strategy's overweight allocation, this aided portfolio performance in Q1. However, the benefit from the strategy's overweight of Caas was marginal compared to the value add generated by superior security selection.

Our underweight of large issue size bonds impeded our relative returns as large bonds outperformed small and mid-size bonds during the quarter. Large bonds almost always outperform in periods when the market is very strong. This is because once portfolio managers sense momentum -- or receive new allocations -- they try to buy the most liquid issues to limit drag from cash. Q1 was no exception. Fortunately, that was overcome by the strong performance of individual holdings.

From an industry standpoint, security selection was particularly strong in the communications sector and a key driver of outperformance for the quarter. Technology, conversely, was the most significant laggard in the portfolio, also due to security selection.

Looking forward to Q2, we are seeing less attractive buying opportunities in the loan market, which is a change from a year ago. Leveraged loans have experienced a stall in net new issuance, while CLO formation has continued to move forward. As a result, CLO managers are now being forced to ramp up portfolios almost exclusively by bidding up loans in the secondary market. Loan prices are thus increasing, relative values are falling, and we are decreasing the loan allocation in the strategy as a result.

However, our strategy's yield advantage remains outsized, and we continue to see a relatively benign default outlook in the near term. Therefore, we believe the portfolio remains well positioned for continued excess returns going forward.

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About Mesirow

Mesirow is an independent, employee-owned financial services firm founded in 1937. Headquartered in Chicago, with locations around the world, we serve clients through a personal, custom approach to reaching financial goals and acting as a force for social good. With capabilities spanning Global Investment Management, Capital Markets & Investment Banking, and Advisory Services, we invest in what matters: our clients, our communities and our culture. To learn more, visit mesirow.com.

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GIPS REPORT – HIGH YIELD COMPOSITE

Gross and Net of Fees Total Returns from March 1, 1999 – March 31, 2023

	Year end						Annual performance results				3-year annualized dispersion[2]	
Year	No. of portfolios	Composite Asset at end of period ($MM)	MHY Assets at end of period ($MM)	Total Firm Assets ($MM)	Non paying fee (%)	Carve out (%)	MFIM (gross) Composite (%)	MFIM (net) Composite (%)	Bloomberg US Corp. High Yield Index (%)	Composite Dispersion [1] (%)	MFIM (gross) Composite (%)	Bloomberg US Corp. High Yield Index (%)
1999	5 or fewer	507	507	–	1	1	4.81	4.38	1.49	n/a	n/a	n/a
2000	5 or fewer	465	465	–	1	1	-8.42	-8.88	-5.86	n/a	n/a	n/a
2001	5 or fewer	648	648	–	1	1	7.14	6.60	5.28	n/a	n/a	n/a
2002	5 or fewer	888	888	–	1	1	11.63	11.08	-1.41	n/a	8.01	10.34
2003	5 or fewer	1,265	1,265	–	1	1	23.64	23.03	28.97	n/a	7.03	10.65
2004	5 or fewer	1,522	1,522	–	1	1	16.00	15.43	11.13	n/a	4.14	8.38
2005	5 or fewer	1,536	1,536	–	1	1	6.81	6.28	2.74	n/a	4.48	5.55
2006	5 or fewer	14	14	–	100	100	18.61	18.03	11.85	n/a	4.63	3.95
2007	5 or fewer	11	297	–	100	100	7.59	7.06	1.87	n/a	4.70	4.74
2008	5 or fewer	8	207	–	100	100	-17.70	-18.12	-26.16	n/a	10.14	13.41
2009	5 or fewer	10	270	–	100	100	44.33	43.63	58.21	n/a	11.57	16.93
2010	5 or fewer	11	295	–	100	0	16.94	16.36	15.12	n/a	11.72	17.03
2011	5 or fewer	27	310	–	0	0	4.44	4.06	4.98	n/a	7.23	11.09
2012	5 or fewer	40	334	–	0	0	14.63	14.00	15.81	n/a	5.40	7.08
2013	7	520	817	–	1	0	9.41	8.90	7.44	n/a	5.33	6.41
2014	8	593	797	–	1	0	3.14	2.68	2.45	0.7	4.01	4.50
2015	8	617	757	–	1	0	-1.02	-1.45	-4.47	0.7	4.26	5.26
2016	7	742	841	–	–	–	15.18	14.67	17.13	n/a	4.57	6.00
2017	5 or fewer	512	526	4,772	–	–	8.90	8.45	7.50	n/a	4.24	5.65
2018	5 or fewer	859	873	4,137	–	–	-1.02	-1.37	-2.08	n/a	3.76	4.59
2019	5 or fewer	1,124	1,199	3,895	–	–	13.02	12.58	14.32	n/a	3.74	4.02
2020	5 or fewer	1,338	1,407	6,706	–	–	9.00	8.55	7.11	n/a	12.23	9.24
2021	5 or fewer	1,301	1,421	6,168	–	–	12.12	11.67	5.28	n/a	12.08	9.00
2022	5 or fewer	717	898	3,616	–	–	-10.38	-10.76	-11.19	n/a	12.70	10.97
Current Performance Results												
2023 YTD	5 or fewer	749	1,115	3,609	–	–	4.11	3.99	3.57	n/a	7.79	8.87

Past performance is not necessarily indicative of future results

Mesirow Financial Investment Management Institutional – Fixed Income claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Mesirow Financial Investment Management Institutional – Fixed Income has been independently verified for the periods 01.01.1996 through 12.31.2021. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards. Verification provides assurance on whether the firm's policies and procedures related to composite and pooled fund maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. The High Yield Composite has had a performance examination for the periods from 03.01.1999 to 12.31.2021. The verification and performance examination reports are available upon request.

Creation date is 03.01.1999. Performance and Composite inception are 03.01.1999.

Mesirow Financial Investment Management, Inc. ("MFIM") is an investment advisor registered with the Securities and Exchange Commission under the Investment Advisers Act of 1940. The "Entity" is defined as Mesirow Financial Investment Management Equities and Fixed Income, which is comprised of the GIPS-compliant units of MFIM which specialize in managing portfolios for institutional clients adhering to an investment process geared towards institutional investors. The historical performance presented prior to the creation of the division was managed by MFIM or its predecessor firms prior to 01.01.2005. For purposes of claiming GIPS compliance, as of 01.01.2010, the "Firm" is further defined as the Fixed Income business unit, Mesirow Financial Investment Management Institutional – Fixed Income, which manages portfolios primarily for institutional investors adhering to an investment process, incorporating fundamental analysis of security valuation factors and drivers.

Effective 10.23.2017, the Firm completed the lift out of the High Yield Team, now Mesirow High Yield ("MHY"), from a former and unaffiliated registered Investment Advisor, Pacific Income Advisers. The High Yield Team, along with the High Yield Composite, became an integral part of the Firm. The current Portfolio Management Team consists of the original members, less one, and they are the only individuals responsible for selecting the securities to buy and sell.

The list of composite descriptions, the Firm's list of pooled fund descriptions for limited distribution pooled funds and the Firm's list of broad distribution pooled funds is available upon request. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. Benchmark returns are not covered by the report of independent verifiers.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. The Performance presented from 03.01.1999 to 4.30.2010 was generated while the Portfolio Managers were affiliated with a prior firm. Prior to 05.01.2010, the track record was reviewed for conformance with the portability requirements of GIPS standards. The predecessor firm was also verified, and the composite underwent a performance examination from inception in 03.01.1999 to 12.31.2009 by Ashland Partners & Company LLP. The High Yield Composite had been examined for the period of 05.01.2010 – 06.30.2016 while at Pacific Income Advisers (PIA). PIA had been verified for the period of 01.01.1994 – 06.30.2016.

The High Yield Composite consists of portfolios whose major concentration is in high yield bonds, both public and private. Equity-linked securities purchased in conjunction with debt securities, and equity securities obtained in exchange offers or insolvency proceedings, as well as leveraged corporate loans, and ETFs (in certain circumstances when onboarding a new account) may also be included. The portfolios are considered to be substantially fully invested, with minor cash holdings, at such time as the portfolio consists of at least 85% high yield bonds. This High Yield Composite definition was amended as of October 2019 to more fully reflect the intended strategy. On 01.01.2009, a substantially large equity position (comprising several securities) became non-discretionary and was transferred from the High Yield Composite portfolio when the client restricted the portfolio manager from selling the positions due to tax consequences.

Prior to 11.01.2010, the High Yield Composite was named the U.S. High Yield Composite. It is not for use with the general public and may not be redistributed. Please reference the last page of this presentation for important additional information.

Beginning 05.01.2010, composite policy requires the temporary removal of any portfolio incurring a client initiated significant cash inflow or outflow of 20% of portfolio assets or greater. Additional information regarding the treatment of significant cash flows is available upon request. The U.S. Dollar is the currency used to express performance.

Prior to 01.01.2010, carve-outs reflect the capping of cash to 8% of Net Asset Value on an account which represents the personal holdings of one of the portfolio managers in order to align such cash amount to the level typical of an institutional account.

Calculation of Risk Measures: Annual / 3 Years Dispersion

(1). N/A = Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. Composite dispersion presented is the equal-weighted or asset-weighted standard deviation of the gross annual returns of portfolios in the composite for the entire year.

(2). N/A = The 3-year Ex-post standard deviation isn't presented since there aren't 36 monthly returns available prior to this period. 1999 is a partial period from March 1 through December 31. The three- year annualized Ex-post standard deviation measures the variability of the composite gross returns, and the benchmark returns over the preceding 36-month period. It is not required to be presented for annual periods prior to 2011, or when a full three years of composite performance is not yet available.

Performance / Net of Fee Disclosure

Returns are presented gross and net of management fees and include the reinvestment of all income. Returns do not reflect the deduction of investment advisory fees. Client returns will be reduced by such fees and other expenses that may be incurred in the management of the account. Advisory fees are described in Part 2 of Form ADV of MHY. As of 10.01.2013, net of fee performance was calculated using actual management fees. Prior to 10.01.2013, net of fee performance was calculated using the highest annual management fee applied to the gross results on a monthly basis. For the period 04.01.2011 through 09.30.2013, the highest management fee was 0.65%. Prior to 03.31.2011, the highest management fee was 0.50%. Actual investment advisory fees incurred by clients may vary. When applicable the standard deviation will be calculated as an equal-weighted standard deviation calculated for the accounts in the composite the entire year. The management fee schedule is as follows:

High Yield Composite Strategy (*described in MHY's Form ADV, Part 2*)

0.60% on the first $25 million
0.55% on the next $25 million
0.50% on the next $50 million
0.45% on the balance.

High Yield CIT Strategy

0.40% on all assets – Founder Class (First $100 million) [Closed]*
0.55% on all assets – Class A (under $25 million)**
0.48% on all assets – Class L ($25 million and above)**

*The Founders share class was closed to new investors 01.21.2022 after reaching $100 million in assets under management.

**Class A Units are available to Participating Plans investing less than $25 million and Class L Units are available to Participating Plans investing $25 million or more.

An actual fee charged to an individual portfolio may vary by size and type of portfolio. Fees are collected quarterly, which produces a compounding effect on the total rate of return net of management fees. As an example, the effect of investment management fees on the total value of a client's portfolio assuming (a) $1,000,000 investment, (b) portfolio return of 8% a year, and (c) 0.60% annual investment advisory fee would reduce the portfolio's value by $6,292 in the first year, by $36,614 over five years and $89,411 over 10 years. Actual investment advisory fees incurred by clients will vary.

Benchmark Definition

The primary benchmark was formerly the Credit Suisse High Yield Index. The benchmark was changed to the Barclays U.S. Corporate High Yield Index on 05.01.2010, since the Portfolio Management Team believes it is more commonly recognized as the industry standard index for the high yield asset class. The index was renamed the Bloomberg Barclays U.S. Corporate High Yield Index, following Bloomberg's acquisition of Barclays Risk Analytics and Index Solutions (BRAIS) in August of 2016. The Bloomberg Barclays fixed income benchmark indices have since been rebranded as the "Bloomberg Indices" as of 08.24.2021, further updating the benchmark name to the Bloomberg U.S Corporate High Yield Index. The Bloomberg U.S. Corporate High Yield Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on Bloomberg EM country definition, are excluded.

Mesirow Financial Investment Management, Inc. and its affiliated companies and/or individuals may, from time to time, own, have long or short positions in, or options on, or be a market maker in, any securities discussed herein and may also perform financial advisory or investment banking services for those companies.

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