Commentary | 1Q25

Voya High Yield Bond Fund

# Comprehensive Research, Broad Diversification

## Strategy overview

Total return approach, investing in below investment grade corporate securities.

### Key takeaways

- The first quarter of 2025 was marked by volatility in the fixed income markets, primarily driven by tariff policies and associated economic uncertainty.
- For the quarter, the Class I shares of the Fund underperformed the benchmark on a net asset value (NAV) basis.
- The macro outlook is less supportive for spreads, as uncertainty around trade policy will continue to lead to higher volatility in risk markets.

## Portfolio review

**The first quarter of 2025 was marked by volatility in fixed income markets, primarily driven by tariff policies and associated economic uncertainty.** Despite robust job gains and a low unemployment rate, risk assets underperformed on the quarter. Uncertainty around the timing and magnitude of tariffs targeting Mexico, Canada and China, which were announced by President Trump at his inauguration, and the potential for an escalating trade war, drove credit spreads wider. Similarly, rates fell during the quarter in response to lower growth expectations, which helped deliver positive total returns for most fixed income sectors. The U.S. Federal Reserve maintained a cautious stance during the quarter, resisting further interest rate cuts after having cut rates by 100 basis points (bp) in 2024. The Fed cited stronger than expected economic data as reasons for not cutting rates further. However, in response to tariffs, the updated Summary of Economic Projections (SEP) released following the March meeting showed the median projection for growth moving lower, while inflation projections were higher; however, there was no change to rate expectations, with the median projection still indicating one to two cuts through year end.

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**High yield (HY) bond spreads widened by 60 bp on the quarter to an option-adjusted spread (OAS) of 347 bp.** Spreads traded sideways for the most part during the first two months of the year before widening in March amid weaker economic numbers and increased geopolitical risk. However, the Bloomberg High Yield 2% Issuer Cap Index still registered a positive return of 1.00% for the quarter, as the decline in yields offset the move wider in spreads. Unsurprisingly, the backdrop soured appetite for riskier credits, as higher-quality outperformed during the quarter, with BB, B and CCC rated bonds posting returns of 1.49%, 0.74%, and –0.44%, respectively. Issuance picked up in the primary market as borrowers capitalized on lower yields to refinance their debt, while mergers and acquisitions activity remained subdued. Demand for HY was strong during the quarter, as investors allocated to the asset class for most of the period before retreating in the last week as market volatility picked up.

**For the quarter, the Class I shares of the Fund underperformed the benchmark on a NAV basis.** Broadly speaking, the Fund's underweight in the stressed tail and more defensive posture within sectors most sensitive to tariff news and negative macro headlines provided a benefit to relative performance. Across sectors, the Fund benefited from security selection within energy, primarily due to its preference for midstream over exploration and production (E&P) and underweight in the rental car sector, most notably Hertz, which continued to face company-specific challenges. In contrast, negative performance drivers included the portfolio's exposure to Mativ Holdings within paper and packaging, which posted weak earnings, underperforming cable names including CSC Holdings and Direct TV, and the portfolio's modest exposure to bank loans, which underperformed HY during the period given the rally in rates. The underperformance was driven by fees as the Fund outperformed on a gross-of-fees basis.

## Current strategy and outlook

**The outlook for U.S. equities in the coming period remains cautious amid a mix of economic and market factors.** While the labor market remains strong and inflation pressures have eased, broader economic uncertainty and tariff uncertainties continue to pose significant risks. Policymakers will need to handle these challenges carefully to make sure the economy keeps growing and staying stable.

**The macro outlook is less supportive for spreads, as uncertainty around trade policy will continue to lead to higher volatility in risk markets.** Recent economic numbers have shown some pullback in activity as consumers and companies ponder the potential impact of U.S. trade policy. While we still believe growth remains sufficient to support credit fundamental factors, which also benefit from a relatively solid starting point, the risk of policy error and a more material slowdown in growth has increased in our view. As expected, market technical factors can turn quickly in a risk-off market with outflows picking up recently, but the underlying technical remains fairly positive with only modest expected net issuance. Although the risk of spreads moving wider in the near term remains elevated, valuations have improved with the recent back-up in spreads, and the elevated carry will continue to make it difficult for the market to print negative total returns for an extended period of time, barring an unforeseen shock.

**In terms of positioning, we remain modestly overweight to single-B rated bonds with a modest underweight in BB rated bonds and a continued underweight in the distressed tail of the market where idiosyncratic risk remains high.** As macro and policy uncertainties remain top of mind, our overall sector positioning remains defensive. To that end, we continue to favor defensive sectors such as healthcare and pharma and remain underweight in autos where tariff risks remain high and have become more selective in retail, favoring businesses that have manageable exposures to tariffs. Within cyclicals, we remain cautious with the view of global growth weakening. Single-name risk continues to be a key focus of ours, as dispersion remains elevated.

The **Bloomberg U.S. High Yield 2% Issuer Capped Index** is an unmanaged index comprised of fixed rate, non-investment grade debt securities that are dollar denominated and non-convertible. The index limits the maximum exposure to any one issuer to 2%.Index returns do not reflect fees, brokerage commissions, taxes or other expenses of investing. **Investors cannot invest directly in an index.**

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