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Global Fixed Income

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Are high yield bonds still attractive despite low credit spreads?

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It isn't hard to find commentary highlighting the apparent expensive valuations in credit markets. Equally, it doesn't take long to find a high yield manager encouraging investors to take the view "spreads may be expensive, but the all-in yield is attractive."

As a credit investor, I've always found one part of equity investing mysterious: the difficulty of knowing when markets are "too expensive." In equities, valuation tools – price/earnings ratios, cyclically-adjusted multiples – are hotly debated but rarely decisive. In credit, by contrast, commentators have a cleaner metric; spread – the excess yield above government bond yields – serves as a yardstick of whether markets are cheap or rich. When spreads are wide, credit looks attractive; when spreads are tight, it looks expensive. As an aside, I have always been a little surprised that many investors use high yield in their funds only on this basis, effectively 'renting' the asset class for capital upside, and not using it for long term income.

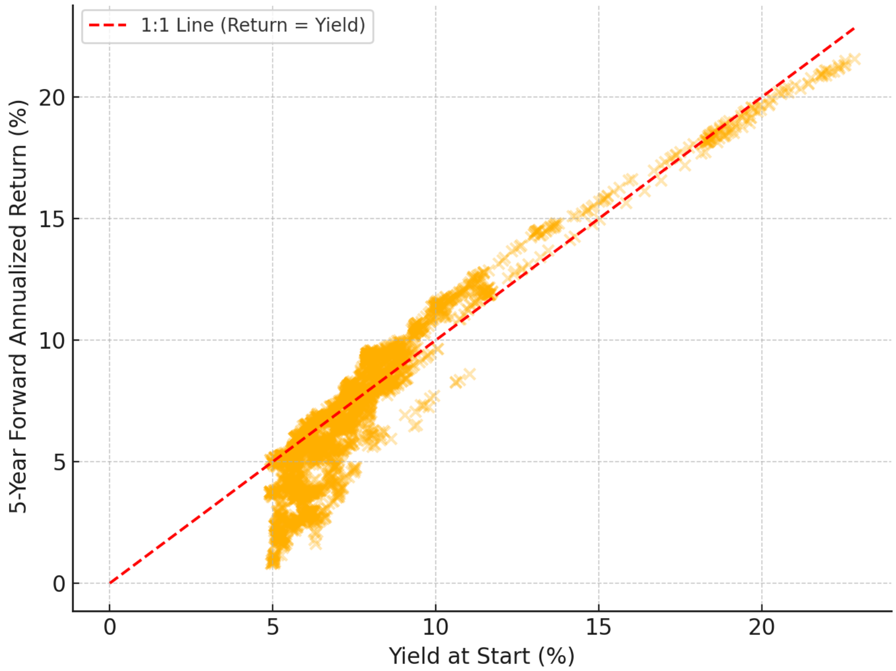
So which is it, yield or spread? To answer this question I thought I'd use our favourite new (robot) colleague, ChatGPT. I gave it the data and asked the question: which is the better predictor of long-term returns, spread or yield?

The results were useful for my confirmation bias. Spread did a respectable job on its own, explaining about 62% of the variation in subsequent five-year returns. But yield was far more powerful. Starting yield explained close to 87% of the variation in returns. Put simply: spreads contain useful information, but yield is the anchor.

While I was at it, I asked ChatGPT to make me a chart to emphasise the predictive power of starting yield. The scatter plot below makes the same point visually. Each dot shows the market's starting yield against the actual five-year return which followed. The red dashed line is the simple "what you yield is what you earn" relationship.

Based on ChatGPT's analysis, the clustering around that line tells its own story: yield today could be a remarkably good guide to the return you get tomorrow.

Global high yield bonds: starting yield versus subsequent five-year investment returns.



Source: ICE BofA, Liontrust, August 2025. Chart plot via ChatGPT. Past performance does not predict future returns.

So what does this mean for today's market? With global high yield offering an all-in yield of around 7%, that figure shouldn't be dismissed as just another statistic. History suggests it's a pretty good anchor for what investors are likely to earn over the medium term. And to put it in perspective: the long-run return on equities has been about 7–10% per year in the US, and 6–7% globally.

In other words, high yield today offers prospective returns in line with equities, while sitting higher in the capital structure and having very rarely delivered negative outcomes over five-year horizons.

So yes, spreads may be tight. Yes, the cycle will ebb and flow. But the evidence is clear: yield is the best predictor of long-term credit returns. And right now, 7% is not just attractive—it's a guidepost.

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For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance does not predict future returns. You may get back less than you originally invested. We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.

The Funds managed by the Global Fixed Income Team:

Consider environmental, social and governance ("ESG") characteristics of issuers when selecting investments for the Funds.

May hold overseas investments that may carry a higher currency risk. They are valued by reference to their local currency which may move up or down when compared to the currency of a Fund.

Hold Bonds. Bonds are affected by changes in interest rates and their value and the income they generate can rise or fall as a result; The creditworthiness of a bond issuer may also affect that bond's value. Bonds that produce a higher level of income usually also carry greater risk as such bond issuers may have difficulty in paying their debts. The value of a bond would be significantly affected if the issuer either refused to pay or was unable to pay.

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The use of derivative instruments that may result in higher cash levels. Cash may be deposited with several credit counterparties (e.g. international banks) or in short-dated bonds. A credit risk arises should one or more of these counterparties be unable to return the deposited cash.

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May target an absolute return. There is no guarantee that an absolute return will be generated over the time period stated in the fund objective or any other time period.

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