

**Episode 44:**  
What's next for the Fed and the high-yield bond market?

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Listen to Fixed Income Portfolio Manager Jim Dudnick discuss the current investment landscape for the asset class, especially what's ahead for the high-yield market. Also: Jim and host J.P. Vicente talk about where to find value amid quickly widening and shrinking spreads, the outlook for corporate credit, potential advantages of short-duration exposure in uncertain times, and the challenges ahead for the Federal Reserve, including potential yield curve inversion and economic slowdown.



Jim Dudnick  
CFA, Director, Portfolio  
Manager

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## Show notes

### The Investment Intelligence Podcast: What's next for the Fed and the high-yield bond market?

**Host:** J.P. Vicente, Head of US Marketing & Client Engagement at Allianz Global Investors

**Featured guest:** James Dudnick, CFA, Portfolio Manager and Director at Allianz Global Investors

#### Notes, quotes and references:

J.P. talks with Jim about the outlook for high yield bonds as the US Federal Reserve works to get the balance right normalizing monetary policy, the role of fixed-income assets in portfolios when interest rates are rising and the potential advantages of short-duration exposure in uncertain times.

#### Some key thoughts and topics from this episode:

**Are you concerned about a recession that could portend rising high-yield debt defaults?**

"We have a hard time seeing a significant number of defaults ... It's much more likely that we will have a sub-2% default environment in 2022 and even into 2023 right now, with some (forecasts) as low as even 1%."

**Do you still give Fed Chairman Jerome Powell a positive review for his handling of monetary policy?**

"He is an amazing leader of central banking policy. Orchestrating a potentially rising-rate regime

with the ability that he's been able to do it, I think has been heroic."

#### **Are you concerned that the Fed might be behind the curve in trying to tame inflation?**

"No. I think if they were behind the curve, you would see higher 30-year Treasury yields and you would see longer-term expectations of inflation getting out of the barn. Looking at the break-evens part of the curve (the difference in the yield of a nominal Treasury security and a Treasury Inflation-Protected Security), break-evens have shot up for one-year and two-year expectations ... but five-year to 10-year expectations have not moved that much higher. Investors still expect, over that period of time, 2-3% inflation—not very high inflation expectations—over the longer term."

#### **How can investors mitigate the negative impact of interest rate risk today?**

"It's really about where do you want to take risk—interest rate risk, credit risk, or liquidity risk? The overwhelmingly negative factor so far, year-to-date in 2022 has been the amount of interest rate risk that's in your portfolio. So, I think investors should probably be taking some credit risk right now as long as you are aligned with an investor that's seeking out (companies) that are re-prioritizing paying down debt."

#### **What role do short duration high yield bonds play in a portfolio?**

"This (type of) strategy is not aiming to produce capital gains. It's just trying to give a tortoise and the hare type of exposure for fixed income, which is how we think about fixed income for most investors: They want to take an asset class that sometimes is spicy and make it boring. Whether it's part of a liquidity bucket or just general fixed income to meet longevity goals, we think it fits really well right now."

The full episode has even more details on the topics above. Check it out.

### Cultural recommendations:

J.P. just added *Kenny Burrell & John Coltrane* to his vintage record collection, an album that includes the guitar sideman and tenor saxophone legend performing *Why I Was Born*, which [allmusic.com](#) calls, 'a once-in-a-lifetime duet. Together they weave an uncanny and revealing sonic tapestry that captures a pure and focused intimacy.'"

Jim recommends the global bestseller *Surrounded by Idiots*, by Thomas Erikson, which categorizes people into four types — Reds, who are dominant/commanding, Yellows, who are social/optimistic, Greens, who are laid back/friendly, and Blues, who are analytical/precise. [Goodreads](#) says the book offers "a groundbreaking new method of understanding the people around you that will change how you interact with everyone from your coworkers to your spouse."

Creativity and editing: Peter Lennox.

Production: Mark Egan.

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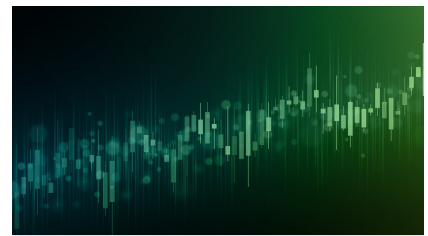


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