INCOME RESEARCH + MANAGEMENT

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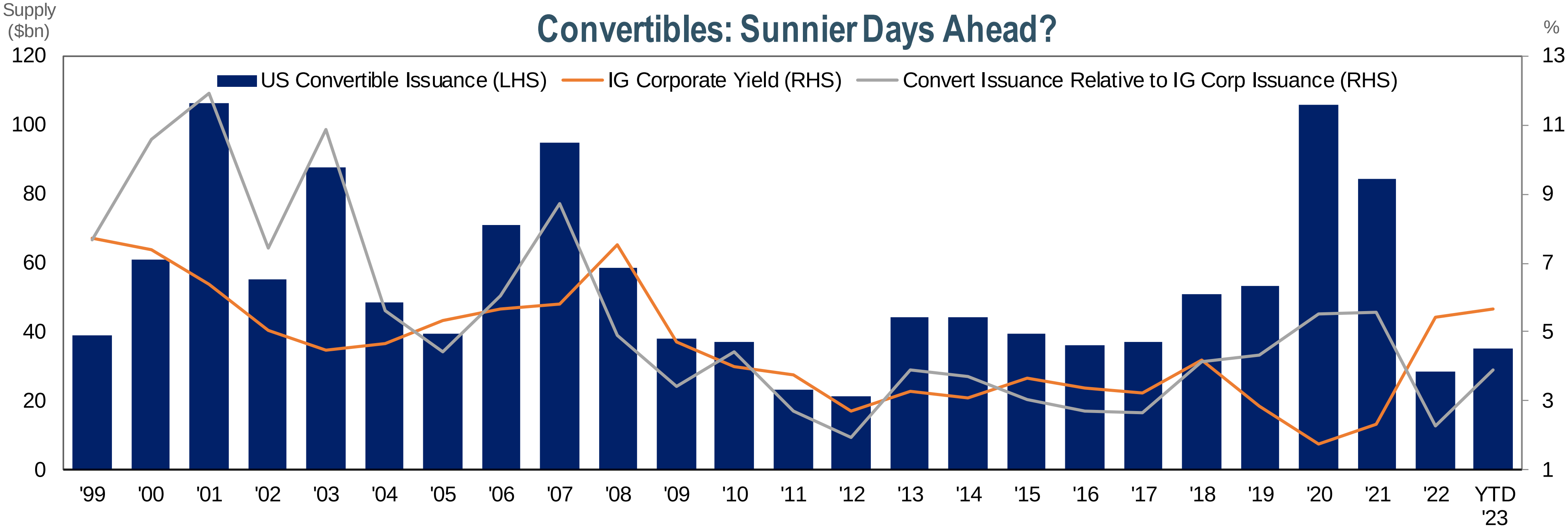
Convertibles: Sunnier Days Ahead?



- **Looking in the rearview mirror.** Some companies prefer to issue convertibles instead of corporates during periods of higher rates because convertible debt can price with a lower coupon (the covid period of 2020/2021 was an outlier as most companies had to access debt markets for liquidity). This trend has continued as US convertible issuance has already surpassed last year's annual total.
- **Feel the [tail]winds in your hair.** The "higher for longer" rate narrative could bring ongoing supply to the convertible market, as companies continue to look for ways to reduce interest expense. Higher yields, coupled with the removal of an accounting rule, should continue to bolster issuance.
- **There are several possible routes.** The tradeoff of lower coupons is the possibility of diluting shares outstanding, which is why more companies do not regularly tap that market; issuers are typically growth-oriented and/or unrated. However, in 2023, investment-grade (IG) issuers have represented 34% of total issuance – a new record – with the first IG utility convert in nearly twenty years.
- At IR+M, we think the healthy resurgence of supply can help investors build a more diversified portfolio in the sector, especially if investors are allowed to purchase high-yield and unrated securities.

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