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A NEW YORK LIFE INVESTMENTS COMPANY

INSIGHTS & PERSPECTIVES

from MacKay Shields Global Fixed Income Team

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Five High Conviction Ideas for a Post-Pandemic World

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While the broad global economy has bounced back from the worst of the COVID-19 downturn, some badly hit sectors and industries haven't regained pre-pandemic levels and continue to trade at discounts, offering investors what we believe is compelling value.

With rates hovering near all-time lows and U.S. central bank policy remaining accommodative, investors continue to search for non-traditional sources of yield and income-generating opportunities without taking on excessive risk.

The MacKay Shields Global Fixed Income Team seeks to invest in the less efficient areas of fixed income to generate alpha for our clients. In the current environment, we have five high conviction ideas that we believe offer great value, income and total return opportunities for investors all with less interest rate risk. On average, these five high conviction categories equate to BBB credit quality and intermediate maturity, offering greater income and potential total return advantages than the overall BBB market—and with much less interest rate risk.

1. COVID RECOVERY SECTORS
Some companies in the hardest-hit industries such as airlines, hotels, retail and leisure will eventually thrive and outperform as the pandemic wanes.

2. HOUSING MARKET
A shortage of homes and enormous demand have turned the residential real estate market upside down.

3. CONSUMER CREDIT
Robust personal savings and low unemployment have consumers in excellent fiscal shape.

4. SUBORDINATED FINANCIALS
Subordinated instruments offer compelling yield and total return attributes, with lower risk versus similar-yielding securities.

5. PREMIUM MORTGAGE-BACKED SECURITIES
Premium MBS should perform well, even in a rising interest rate environment, as housing should remain in strong demand for many years.

1. COVID Recovery Sectors: An Uneven Future for the Hardest-Hit Industries

As the U.S. economy snapped back to life after the worst of the pandemic lockdowns, it was apparent some industries were hit harder than others. Restaurants, airlines, in-person retail and leisure suffered most as society grew more comfortable meeting virtually, shopping online and getting food delivered. While these industries were tagged as "social distance losers," not all companies in this category are falling in a downward spiral into non-existence. Some of these companies will rebound and thrive, while others will struggle.

We believe the U.S. airline industry, for example, remains an attractive re-opening investment trade. The airlines have strong support from the U.S. government while also doing whatever it takes to raise liquidity, including issuing debt backed by airline mileage and loyalty programs, routes, slots, and gates. Airline bonds rallied last year, reflecting investor enthusiasm for the coming end to the pandemic and the subsequent expected rise in airline travel. However, the Delta COVID variant resulted in airline traffic stabilizing at 75-80% of

2019 levels. We expect this holding pattern to continue over the near term until travel ramps back up to pre-pandemic levels.

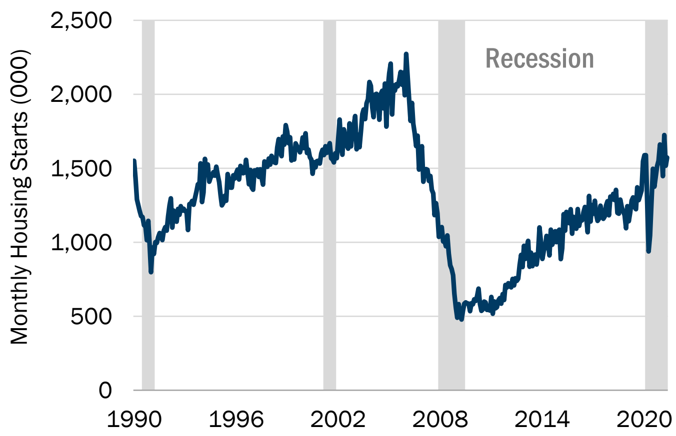
2. Housing Market: A Seller's Market, But No One's Selling

Demand for residential real estate skyrocketed during the pandemic, although would-be-buyers discovered a market devoid of supply. Low rates, limited supply and high demand have led to all-out bidding wars.

At the root of the overheated housing market is a chronic lack of new home supply, which pre-dates the pandemic. The home building industry never fully recovered from the 2008 crash, causing a massive under-supply of new homes across the country (Figure 1). The U.S is about 4 million homes short of meeting current demand, according to Freddie Mac.

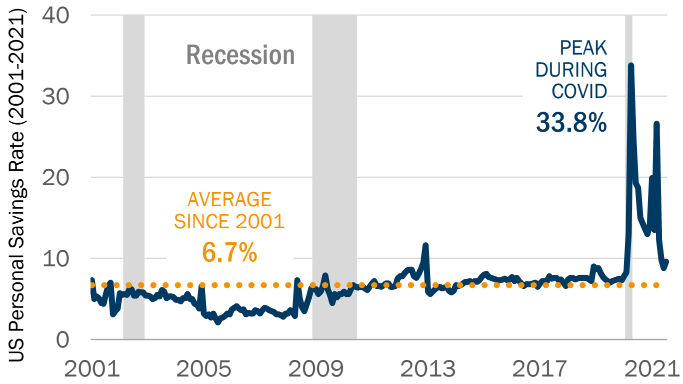
The supply shortage is estimated to last another decade or so. Like most industries, homebuilders are having trouble hiring workers. In the meantime, we believe the favorable supply/demand imbalance creates opportunities for investors in several asset categories, including credit risk-transfer securities, legacy, non-agency mortgages and mortgage loan originators that issue unsecured credit.

FIGURE 1: NEW HOUSING STARTS NEVER RECOVERED FROM THE LAST BUST (as of May 31, 2021)



Source: U.S. Census Bureau, U.S. Department of Housing & Urban Development

FIGURE 2: PERSONAL SAVINGS RATE SKYROCKETED DURING THE PANDEMIC | As of June 30, 2021



Source: U.S. Bureau of Economic Analysis

3. Consumer Credit: Healthy Personal Balance Sheets

The first wave of the pandemic—the second quarter of 2020—will always be remembered for the lockdowns, school closures and the social distancing that changed everyday life for millions of people. Trapped at home with little else to do, Americans stashed more cash into their savings accounts than ever, and the personal savings rate skyrocketed to 33.8% in April 2020, an all-time high (Figure 2). Although it has fallen since last year, the savings rate remains elevated versus the long-term average and the consumer is in better financial shape today than before the pandemic.

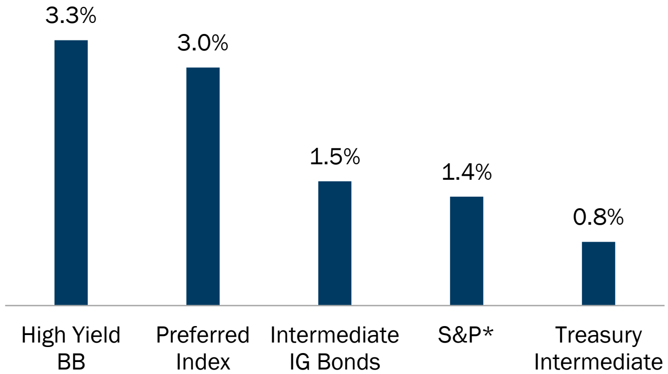
In this environment, we favor securitized credit and asset-backed securities, in addition to certain consumer-oriented financial companies. With robust savings and a strong employment market, American consumers are in great fiscal shape.

4. Subordinated Financials: Higher Yields with Favorable Risk/Reward

We think preferred subordinated securities, such as preferred stock, offer relatively attractive yields in today's low-rate macro environment. As shown in Figure 3, preferred equity yields are similar to those of high-yield bonds. But not all issuers are created equal. We seek out high-quality preferred issuers to help protect against potential risks such as bankruptcy to take advantage of these attractive yields.

While preferred debt provides income opportunities, they also feature less sensitivity to interest rate changes. Preferred income may also be tax advantageous as qualified dividends are taxed at a lower rate than ordinary income.[1] Preferreds also have characteristics that make them less correlated with other asset classes giving them a place in investors' portfolios. These securities are generally issued by banks, insurance companies, REITs and other diversified financials as well as utility, energy, pipeline and telecommunications companies.

FIGURE 3: PREFERRED SECURITIES OFFER COMPELLING YIELD OPPORTUNITIES (as of September 30, 2021)



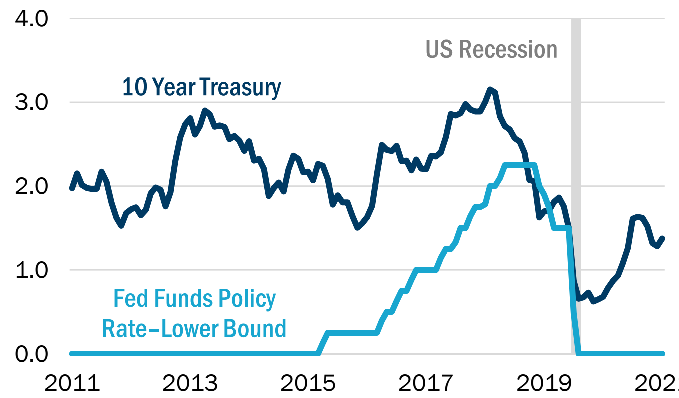
*Dividend Yield
Source: Bloomberg

5. Premium Mortgage-Backed Securities: Not Afraid of Rising Rates

The Fed has set its key policy rate near zero while simultaneously purchasing billions in Treasuries and MBS each month. But today's central bank worries are much different from prior periods when rising rates were most concerning to investors. The Fed's biggest worries today are rising inflation and maintaining price stability (Figure 4). Given these headlines, investors are nervously anticipating the potential taper of the Fed's current bond purchase program, which includes about $120 billion combined in Treasuries and MBS per month.

Regardless of what happens with rates, we think the conditions for high coupon, premium MBS will remain attractive for some time. We believe some borrowers will not refinance. We look for borrowers who previously fit this pattern while also targeting areas of the country with a higher threshold to refinance.

FIGURE 4: 10-YEAR TREASURY YIELD AND FEDERAL FUNDS POLICY RATE (as of September 30, 2021)



Source: Board of Governors of the Federal Reserve System

Our theme regarding the housing market also applies here. We see demand for homes remaining solid for years to come, as the supply shortage will persist. Rates should stabilize at an acceptable level for many home buyers and borrowers, offering support to MBS investors.

Conclusion: An Uneven Recovery Suited for Active Managers

We expect economies and markets to continue recovering for the foreseeable future. While it's impossible to say when we will put COVID in the rearview mirror, we expect the more challenged industries to bounce back gradually. However, not all will enjoy the same degree of recovery, which is why an active, risk-managed approach is critically important in today's market. That's why the MacKay Shields Global Fixed Income team invests in high conviction ideas, which employ a top-down, bottom-up approach. In today's challenging markets, we focus on strong risk controls and seek diversified sources of return and income generation. Our team has demonstrated how a broad investment approach that considers an expansive multi-asset universe can surface compelling investment opportunities, including in low-yield and volatile times like these.

1. Not to be construed as tax advice. Consult your professional tax advisors for specific guidance.

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