

Situation Room

Higher for longer will dent IG coverage

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Higher for longer US policy rate could make a dent in the IG corporate market coverage ratio. Historically, the coverage ratio followed interest rates with about a two-year lag. That makes sense due to 1) interest rates are much more variable than debt levels and 2) it takes time for old debt to roll off. Based on this historical relationship the current 10yr Treasury yield of about 4% implies IG coverage ratio of about 10x in 2025, down from 11.9x as of 1Q-2023. That would be just 13th percentile since 2010 (when interest rates were relatively low), but 37th percentile for the full history going back to 1Q-1997.

A simple projection

Of course, the impact on the coverage ratio will depend on how long rates remain high. Our rates strategists expect the yield on 10yr Treasuries to decline to 3.25% by YE-2024 (see [Global Rates Weekly](#)). However, we estimate that rolling maturing debt at the current IG index yield of 5.5% (and assuming no change in debt or earnings) would take the coverage ratio to 10.3x by YE-2024 and to 8.7x by YE-2025. Hence, should interest rates remain high for the next two years, the US IG corporate coverage ratio could drop to some of the lowest levels since 2003.

Daily credit snapshot

US IG issuance totaled \$3.5bn across 1 deal today, \$8.7bn WTD and \$63.3bn MTD. The average new issue concession was 24.0bps today from 3.5bps yesterday. This week's new issues are trading 8bps tighter on average from pricing. S&P 500 closed +0.28%, 10-year Treasury yields +2bps, CDX IG -0.1bps, CDX HY -\$0.08pts, and cash bond spreads quoted from Unched to 3bps tighter today, LQD closed 0.01bp wider today.

Daily dealer inventories update

\$346mn (notional), -\$291,000 (DV01) today. Maturities and sectors inside.

Daily foreign demand tracker

We track dealer-to-affiliate volumes on Trace that are correlated with foreign buying.

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United States
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Research Overview — The Situation

Higher for longer will dent IG coverage

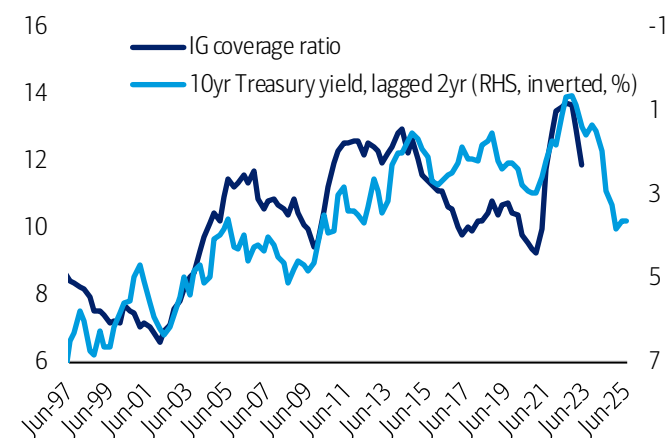
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Figure 1: Rates tend to drive IG coverage ratio

US IG coverage ratio tends to follow interest rates with about 2yr lag.

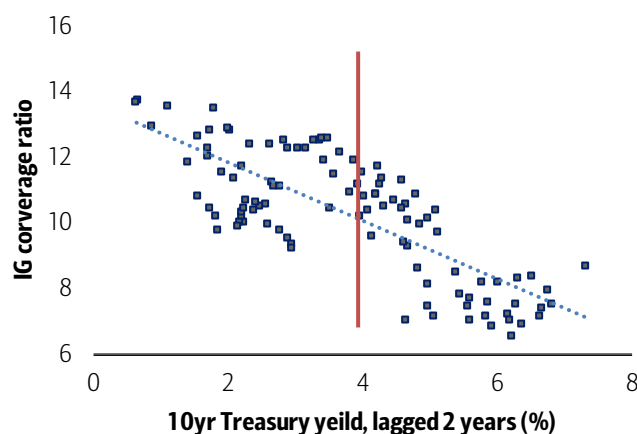


Source: BofA Global Research, Bloomberg

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Figure 2: Current interest rates imply coverage of 10x by 2025.

The current 10yr Treasury yield of 4Y implies IG coverage ratio of about 10 two years from now.

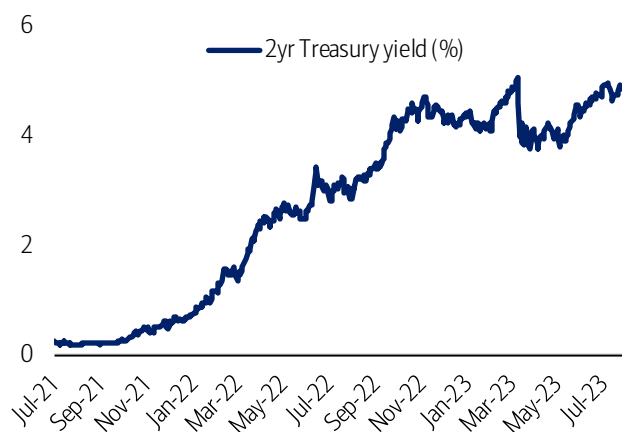


Source: BofA Global Research, Bloomberg

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Figure 3: 2yr Treasury yield is 4.9% currently

That suggests short-term interest rates are expected to remain around 5% over the next two years.

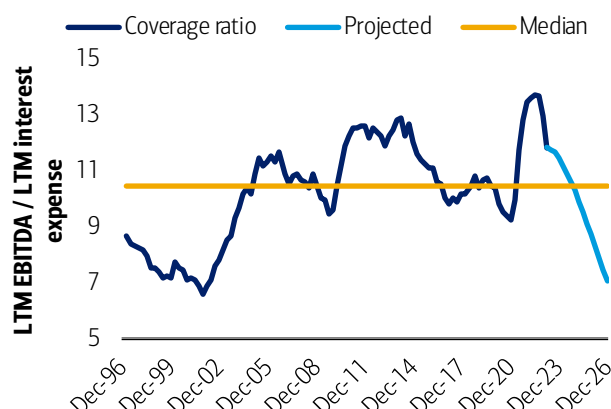


Source: Bloomberg.

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Figure 4: Rolling IG debt at 5.5% yield -> coverage ratio of 8.7 by '25.

Assuming IG companies roll debt at the current IG index yield of 5.5% could bring coverage to 10.3 by YE-2024 and to 8.7 by YE-2025.



Note: the projected coverage ratio assumes no change in debt or earnings, and that maturing debt is refinanced at the current IG index yield of 5.5%.

Source: BofA Global Research, ICE Data Indices, LLC

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Credit Strategy

Daily credit snapshot

US IG issuance totaled \$3.5bn across 1 deal today, \$8.7bn WTD and \$63.3bn MTD. The average new issue concession was 24.0bps today from 3.5bps yesterday. This week's new issues are trading 8bps tighter on average from pricing.

S&P 500 closed +0.28%, 10-year Treasury yields +2bps, CDX IG -0.1bps, CDX HY - \$0.08pts, and cash bond spreads quoted from Unched to 3bps tighter today, LQD closed 0.01bp wider today.

Figure 5: Recent new issue pricing and new issue concessions

List of new issues in the IG corporate bond market today along with performance metrics.

Date	Ticker	Name	Tenor	Size (\$mm)	Moody's/S&P Rating	Coupon (%)	Px Spread (bps)	New Issue Conc. (bps)	* Break performance	Current spread (bps)
2023-07-24	AHTLN	Ashtead Capital Inc	10	750	Baa3/BBB-	5.95	210	3	-4	206
2023-07-24	FITB	Fifth Third Bancorp	6NC5	1,250	Baa1/BBB+	6.339	220	n.a.	-17	200
2023-07-24	KORELE	Korea Electric Power Corp	3	1,000	Aa2/AA	5.375	100	n.a.	n.a.	n.a.
2023-07-24	PSA	Public Storage	2	400	A2/A	FRN	SOFR+60	n.a.	n.a.	51
2023-07-24	PSA	Public Storage	5	500	A2/A	5.125	100	4	-5	96
2023-07-24	PSA	Public Storage	10	700	A2/A	5.1	125	n.a.	-3	122
2023-07-24	PSA	Public Storage	30	600	A2/A	5.35	143	n.a.	-7	137
2023-07-25	AXP	American Express Co	4NC3	1,200	A2/BBB+	5.389	88	22	n.a.	n.a.
2023-07-25	AXP	American Express Co	4NC3	300	A2/BBB+	6.05202	n.a.	n.a.	n.a.	n.a.
2023-07-25	AXP	American Express Co	6NC5	1,500	A2/BBB+	5.282	113	26	n.a.	n.a.
2023-07-25	AXP	American Express Co	11NC10	500	A3/BBB	5.625	175	n.a.	n.a.	n.a.

Note: We calculate new issue concessions by estimating the difference between new issue bond spread and interpolated G spread from comparable liquid secondary bonds of the same issuer prior to the new issue deal announcement, adjusted for the spread impact of dollar prices deviating from par. Break performance is computed as the difference between new issue pricing and secondary closing spread on the first day of trading.

Source: BofA Global Research, Bloomberg

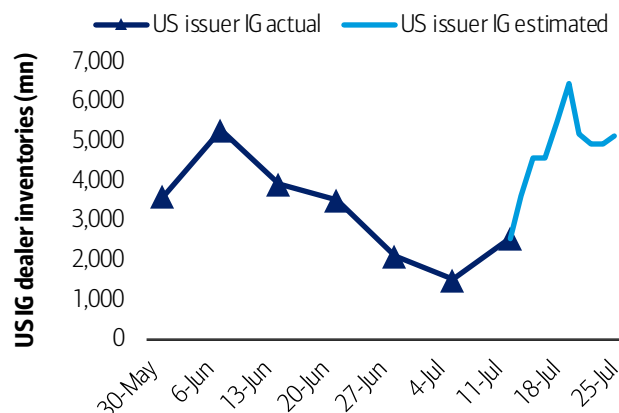
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Daily dealer inventories update

Below we estimate dealer inventories for the IG corporate bonds based on TRACE data. The actual inventories of US issuer bonds based on NY Fed survey, as well as the estimated change since the latest Fed report are plotted in Figure 6 and Figure 7. We estimate the corresponding DV01 equivalent in Figure 7. More details by sector and maturity are available in Figure 8 and Figure 9. Finally, note that the data for the current date is through about 4:40 p.m. Eastern Standard Time.

Figure 6: Estimated dealer inventories of IG corporate bonds.

We estimate IG dealer inventories of US issuer bonds increased to \$5.1bn currently from \$2.5bn on Jul-12.



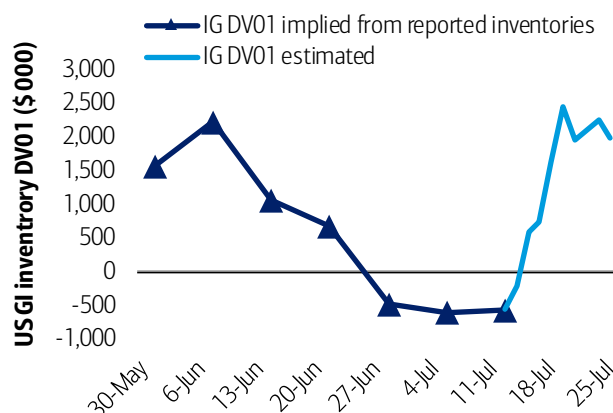
Note: data for US issuer bonds only, maturities 13M or longer. Actual dealer inventory data is from Primary Dealer Statistics survey by the NY Fed. The subsequent change in inventory is estimated based on TRACE.

Source: BofA Global Research, FINRA, TRACE, Federal Reserve

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Figure 7: Estimated dealer inventory DV01 for IG corporate bonds.

We estimate IG dealer inventory DV01 of US issuer bonds increased to \$2.0mn currently from -\$0.6bn on Jul-12.



Note: data for US issuer bonds only, maturities 13M or longer. Actual dealer inventory data is from Primary Dealer Statistics survey by the NY Fed. The subsequent change in inventory is estimated based on TRACE.

Source: BofA Global Research, FINRA, TRACE, Federal Reserve

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Figure 8: Estimated changes in IG dealer inventories by maturity and broad sector.

We estimate IG dealer inventories increased \$346mn today and increased \$3mn over the prior week.

Sector	Net dealer buy (\$mn)					Net dealer DV01 change (\$thousand)					Trading volumes on 25-Jul-23 (\$mn)			
	25-Jul	24-Jul	1 W	2 W	4 W	25-Jul	24-Jul	1 W	2 W	4 W	Buy	Sell	Dealer	Total
High grade (13M+)	346	25	3	5,716	7,127	-291	281	593	4,709	3,893	10,700	10,353	6,428	27,482
<3yr	488	-304	-625	-90	1,573	98	-51	-87	21	341	1,884	1,397	1,256	4,537
3-5yr	386	133	856	1,776	2,126	140	54	302	601	679	2,249	1,862	1,432	5,543
5-11yr	-163	-175	-1,191	1,186	1,054	-149	-155	-869	682	276	3,773	3,935	2,113	9,821
11+yr	-365	372	963	2,844	2,374	-380	433	1,247	3,405	2,597	2,794	3,159	1,628	7,581
Fin	10	-250	-942	-211	1,685	77	-72	-263	392	717	4,128	4,117	2,256	10,501
Non-Fin	336	275	945	5,926	5,442	-368	353	856	4,317	3,176	6,572	6,236	4,172	16,980
Fixed	341	75	108	5,969	7,164	-305	309	615	4,711	3,869	10,592	10,250	6,375	27,217
Floating	5	-50	-105	-253	-36	14	-28	-21	-3	24	108	103	54	265
US issuers	219	-40	-365	4,732	4,112	-277	171	338	3,982	2,396	8,322	8,103	5,284	21,709
DM Yankees	125	2	133	652	2,328	-7	79	144	554	1,138	2,012	1,887	1,048	4,947
EM Yankees	3	62	236	332	687	-7	31	112	172	359	366	363	97	826

Note: data for maturities 13M or longer. Changes in inventories are estimated based on TRACE.

Source: BofA Global Research, FINRA, TRACE.

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Figure 9: Estimated changes in IG dealer inventories by sector.

We estimate today IG dealer inventories declined -\$203mn for Banks/Brokers and increased \$138mn for Energy.

Sector	Net dealer buy (\$mn)					Net dealer DV01 change (\$thousand)					Trading volumes on 25-Jul-23 (\$mn)			
	25-Jul	24-Jul	1 W	2 W	4 W	25-Jul	24-Jul	1 W	2 W	4 W	Buy	Sell	Dealer	Total
Aerospace/Defense	16	-30	-38	-7	-2	-3	6	-17	32	75	412	396	217	1,025
Automobiles	0	17	159	276	247	-6	-12	33	55	25	228	228	177	634
Banks/Brokers	-203	-298	-1,057	-1,162	1,739	1	-109	-350	-213	759	2,803	3,006	1,578	7,387
Basic Materials	79	65	-128	-5	194	-11	44	-134	-128	39	418	339	228	985
Commercial Services	30	7	-17	47	104	17	1	-19	14	15	179	149	98	426
Energy	138	14	307	727	620	46	43	300	490	490	639	501	425	1,565
Finance	77	78	4	430	48	-15	40	-25	287	96	784	707	398	1,889
Food, Bev, & Bottling	3	88	142	502	544	-77	80	41	229	163	309	306	205	820
Health Care	107	-52	284	884	838	7	-17	282	917	662	1,125	1,017	608	2,750
Industrial Products	-73	-74	-196	-115	-35	-76	-54	-113	-62	-82	183	256	176	615
Insurance	74	-23	-76	66	-170	71	-17	-11	38	-150	251	178	112	541
Media & Entertainment	96	29	227	877	964	53	14	139	666	644	479	384	246	1,109
REITs	63	-7	187	455	69	19	13	123	279	12	289	227	168	684
Retail	68	73	252	607	379	37	71	255	524	363	351	283	255	889
Technology	-34	139	407	924	1,307	-118	110	219	574	557	598	632	532	1,762
Telecom	-112	-97	-130	569	615	-77	-39	86	505	634	388	500	281	1,170
Tobacco	27	8	56	67	165	10	8	37	62	122	135	107	110	351
Transportation	154	-9	188	403	163	61	2	162	370	192	379	225	110	714
Utilities	-189	38	-749	-102	-729	-242	67	-527	-88	-790	623	813	401	1,838
Other	26	58	180	272	70	10	30	111	158	68	124	99	105	328

Note: data for maturities 13M or longer. Changes in inventories are estimated based on TRACE.

Source: BofA Global Research, FINRA, TRACE.

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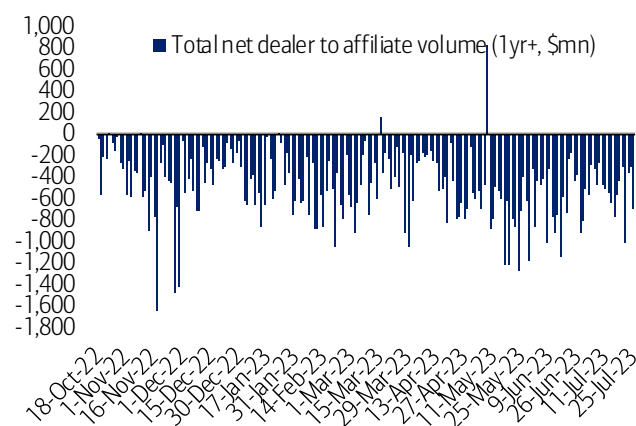
Daily foreign demand tracker

We believe net dealer-to-affiliate volumes from Trace are correlated with foreign buying of US HG corporate bonds - i.e., negative numbers mean foreign investor buying (US dealers taking down inventory in favor of foreign affiliates). For supporting material see our "primer" on tracking foreign inflows (See: [Credit Market Strategist: One year round-trip in spreads 15 July 2016](#)). Figure 10 shows the overall daily dealer-to-affiliate volumes while Figure 11, Figure 12 and Figure 13 show subsets of this data. In particular Figure 11 shows net dealer-to-affiliate volumes for longer maturity (12+ years) bonds, Figure 12 displays volumes reported to Trace before 8am NY time (biased toward Asian buying) and Figure 13 shows the subset of net trades reported between 8am and noon (biased toward European buying).



Figure 10: Net dealer buying from affiliate (1yr+)

Figure shows inconsistent overall foreign buying of US IG corporate bonds for some time.



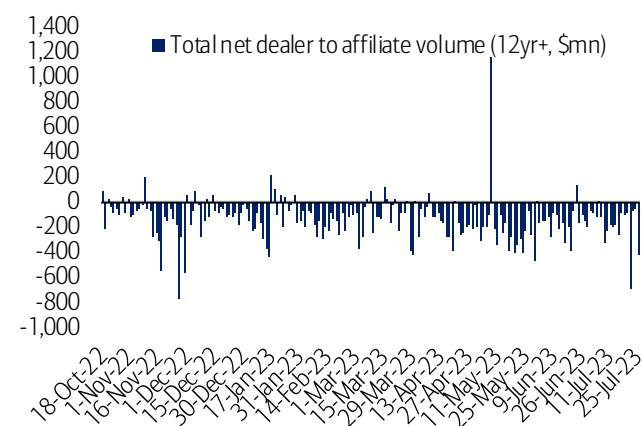
Note: Net dealer-to-affiliate volumes are correlated with foreign buying/selling. Negative numbers indicate foreign buying.

Source: Bloomberg, TRACE

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Figure 11: Net dealer buying from affiliate (12yr+)

Foreign buying of longer maturity US IG corporate bonds has been consistent this year



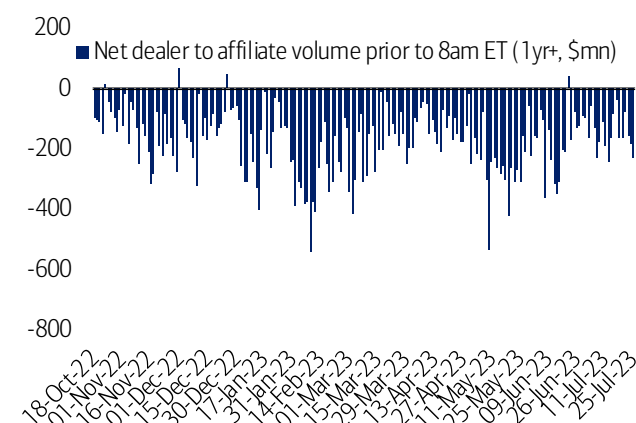
Note: Net dealer-to-affiliate volumes are correlated with foreign buying/selling. Negative numbers indicate foreign buying.

Source: Bloomberg, TRACE

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Figure 12: Net dealer-to-affiliate trading volumes before 8am ET

Foreign buying before 8am NY time is dominated by Asia and has been consistent this year



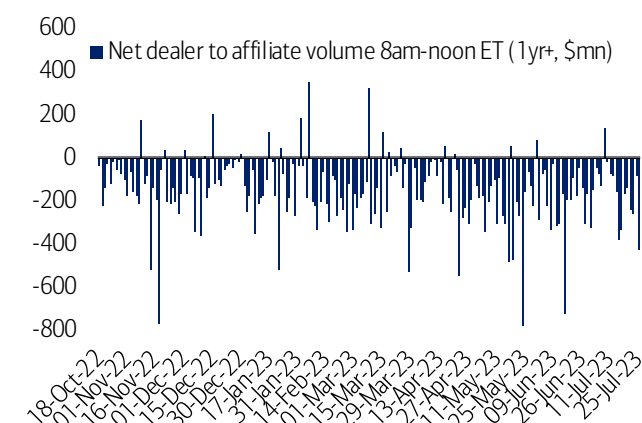
Note: Morning share of daily trading volume is correlated with secondary market activity of foreign investors due to different time zones.

Source: BofA Global Research, TRACE

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Figure 13: Net dealer-to-affiliate trading volumes 8am - noon ET

Foreign buying 8am-noon NY time is dominated by Europe and has been inconsistent this year



Note: Morning share of daily trading volume is correlated with secondary market activity of foreign investors due to different time zones.

Source: BofA Global Research, TRACE

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Common abbreviations:

IG: Investment Grade
 HG: High Grade
 LQD: iShares iBoxx \$ Investment Grade Corporate Bond ETF
 DV01: Dollar value of a basis point
 CDX IG: The Markit CDX North America Investment Grade Index
 CDX HY: Markit CDX North America High Yield Index
 ECB: European Central Bank
 QE: Quantitative Easing
 CSPP: corporate sector purchase programme
 Unchd: Unchanged
 CPI: Consumer Price Index
 FOMC: The Federal Open Market Committee

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