2017 Year in Review: Recap of HY Performance and Capital Markets Activity

Below, we have included select High Yield indices produced by our U.S. credit strategist team, which are available on *Bloomberg* for reference. To remind readers, our *Real Estate* sub-sector index includes not only building product OEMs and distributors but also homebuilders as well. The fate of these participants in the value chain are highly correlated, in our view, so their inclusion in our index does not dilute from the overall message, in our view. As shown in Figure 21, the overall DB HY Index was +7.0% (as of 12/19/17), with the rating buckets as follows: BB-rated (+7.3%), single-B (+5.8%) and CCC-rated (+9.5%).

Real Estate sub-sector outperforms HY (again) on spread basis

Beginning in 2017, the OAS differential between the DB HY Index and the DB HY *Real Estate* index was about (72)bp – negative values show the sub-sector is trading inside of the comprehensive index. The differential remained at this level – narrowing slightly in 2Q17 – before widening further to roughly about (100bp) at 12/19/17. As shown in Figure 24 – 26, readers can see the differential by rating bucket. BB-rated names in *Real* Estate underperformed with the year beginning at (50)bp and narrowing to about (34)bp. The opposite was true for both B-rated and CCC-rated issuers. B-rated names in the *Real Estate* index began the year at (38)bp, and are now at about (108)bp. CCC-rated names outperformed markedly with the OAS differential positive at +124bp in the beginning of the year but not trading at a negative (237)bp. We do want to caveat that this appears driven by the bonds of K. Hovnanian (HOV) which saw its unsecureds start the year at around 80 cents on the dollar and are now trading at yield to call levels at around 106.5. HOV was also successful in refinancing its 7.25% first lien and 9.125% second lien notes in late-July. Overall, the sector's performance appears a logical reaction to what was a year of growth more-or-less in-line with our estimates as published in our *2017 Outlook*. It is also worth noting that while the S&P 500 was up about 18% YTD the *iShares U.S. Home Construction ETF* (ITB), which includes constituencies such as D.R. Horton, Lennar, Lowe's, and Home Depot, was up 58% YTD.

Figure 20: S&P 500 v. ITB

Source: Deutsche Bank

Figure 21: DB High Yield Index Total Returns (as of 12/19/17)

Index Levels	DB HY	DB (BB) HY	DB (B) HY	DB (CCC) HY
12/31/2016	348	347	298	476
12/19/2017	373	372	315	521
Return	**7.1%**	**7.3%**	**5.8%**	**9.5%**

Source: Deutsche Bank and Bloomberg Finance LP

Capital Markets Have Robust 2017

Using publicly available data and illustrations compiled by our *Leveraged Debt Capital Markets Building Products/Homebuilder team* we have included summary information encompassing the capital markets activity in Leveraged Finance for 2017. Looking at building products, at the time of this writing, 2017 brought the market about 45 deals (6 less than 2016) but representing about $25.2bn of notional, an increase of 16% y/y from $21.8bn in 2016. Of this figure however, 66% represented re-pricings (vs. 14% of 2016's total), followed by Acquisition at 16% (versus 34% in 2016) and 13% Refinancing