



JULY 2025

Understanding US convertibles and why they're attractive today

Over the last 35-plus years, US convertibles have produced equity-like performance but with lower volatility. And thanks to accelerated new issuance at favourable terms, today's opportunity set has expanded, adding to the appeal of this unique asset class.



Ethan Turner,
CFA, Portfolio
Manager –
Income & Growth,
Voya Investment
Management

A convertible security is a traditional bond that can be converted or exchanged into a specific number of shares of the issuer's common stock. Convertibles have characteristics of both bonds and stocks, which can help improve a portfolio's overall risk-adjusted returns (see Exhibit 1).

The bond component provides income potential and reduced volatility, derived from the stated coupon and maturity and the claim to principal. Like other bonds, a convertible's value can fluctuate with changes in interest rates and the credit quality of the issuing company. Convertible securities generally have a lower coupon than corporate bonds, but they usually offer a yield advantage over the common stock dividend.

Key takeaways

- Convertible securities have offered equity-like return potential with reduced volatility, allowing for gains during market ups and benefiting from protection when markets decline.
- Increasing new issuance at more attractive terms expands the opportunity set of total return convertibles, which offer a compelling asymmetric risk/reward profile.
- We believe active management is key to unlocking opportunities and managing risks in the evolving market environment.

The equity component provides unlimited capital appreciation potential, derived from an option (determined at issuance) that provides the right to convert into a fixed number of common shares. Because of this feature, when convertible securities mature, they can be redeemed at the market value of the underlying common shares or at their face value – whichever is higher.

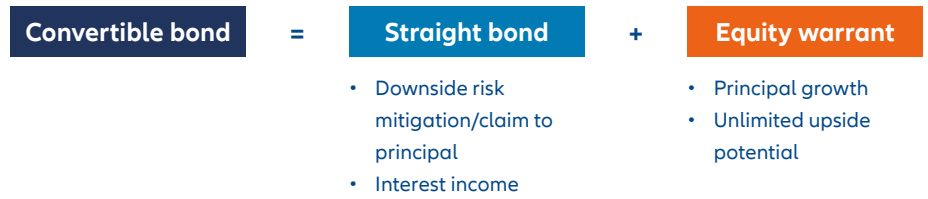
How do convertible securities behave?

The behaviour of a convertible security may take on either stock-like or bond-like characteristics, depending upon where the underlying stock is trading in relation to the bond's conversion price. The security tends to become more equity-like as the price of the common shares rises (see Exhibit 2), which means its participation in the stock's upside may increase. As the underlying stock price falls, the convertible may act more bond-like, which means its participation in the stock's downside tends to decrease. It is important to note that convertibles are subject to the same risk factors as stocks and bonds, including market, interest rate and credit risks.

1. Yield/busted

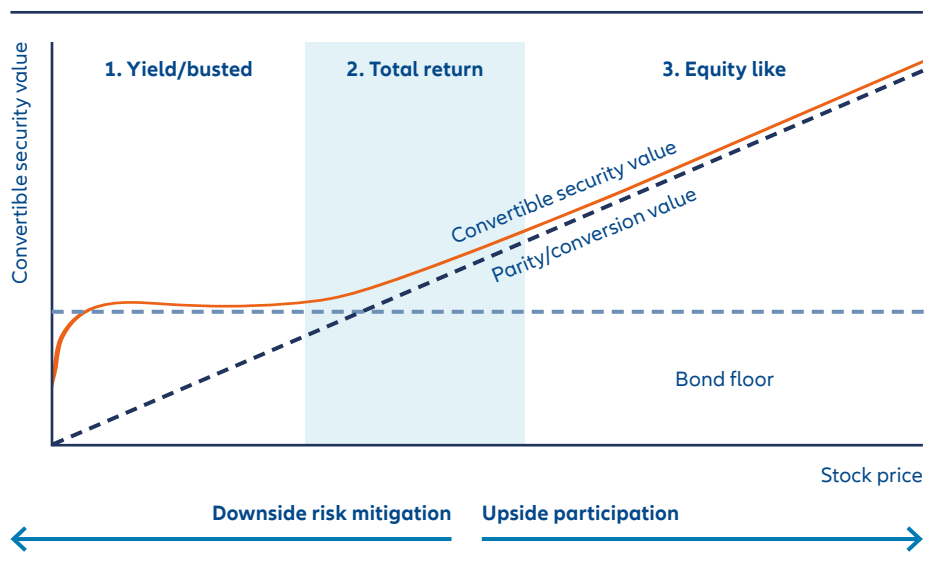
- Convertibles in this category are characterised by high yields and high conversion premiums. Given that the equity option is out of the money, these securities behave more like corporate bonds, with little regard given to the option value.
- Behave more like fixed income instruments
 - Low correlation to the underlying equity
 - Delta below 0.41¹

Exhibit 1: A simplified structure showing the basic components of convertibles



Source: Voya IM. For illustrative purposes only.

Exhibit 2: Three types of convertibles



Source: Voya IM. For illustrative purposes only.

2. Total return

- Convertibles in this category exhibit ideal qualities, characterised by moderate conversion premiums and some equity sensitivity.
- Provide an asymmetric risk/reward profile
 - Capture more of the upside and less of the downside of the underlying equity
 - Delta between 0.4 and 0.81¹

3. Equity like

- Convertibles in this category behave like equity investments, characterised by lower conversion premiums and a high degree of equity sensitivity.
- Behave more like equity instruments
 - High correlation to the underlying equity
 - Delta greater than 0.81¹

1) BofA Global Research, as of 28/02/25. Deltas below 0.1 indicate distressed debt.

Why consider investing in convertible securities?

Asymmetric risk/reward

Convertible securities offer an asymmetric risk/reward profile in which the upside opportunity (reward) can exceed the downside capture (risk). Over the last 35 years, which have included multiple periods of elevated volatility, US convertibles have produced equity-like performance but with lower volatility (see Exhibits 3 and 4).

Improving new issuance

US convertible new issuance not only accelerated in 2024, but exceeded estimates as higher debt financing costs drew issuers to the convertible market for coupon savings (Exhibit 5). Looking ahead, market analysts estimate that new issuance in 2025 should remain steady due to coupon savings demand and elevated refinancing needs, despite increased market volatility.

Due to the rise in interest rates over the last few years, new issuance carries much more attractive terms for convertible security investors. Coupons rose from about 1.5% (record low) in 2021 to about 3.2% through December 2024.

Exhibit 3: US convertibles have captured more of the stock market's upside than downside

Jan 1988 – Dec 2024

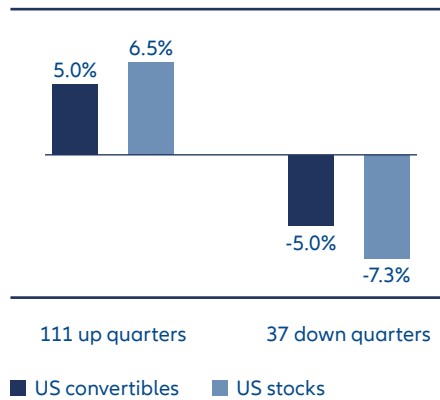
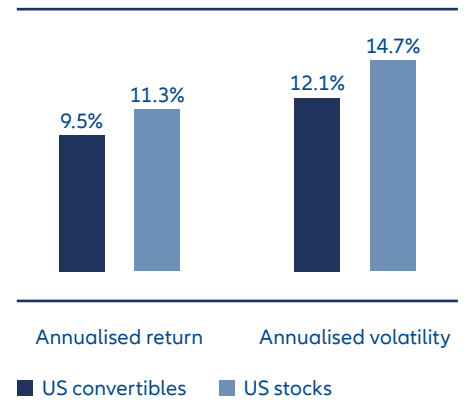


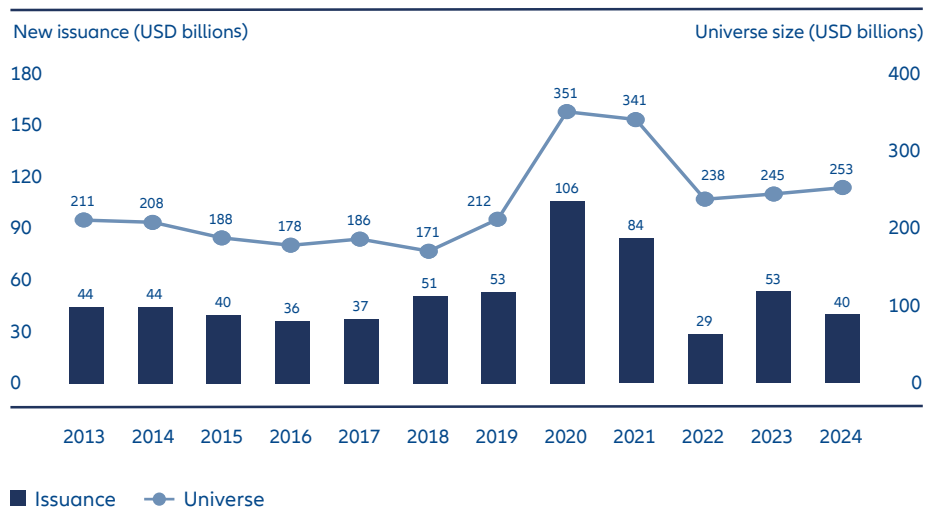
Exhibit 4: US convertibles have delivered equity-like returns with lower volatility

Jan 1988 – Dec 2024



As of 31/12/24. Source: FactSet, ICE Data Services, Voya IM, Morningstar. Past performance is not indicative of future results. This statement reflects performance and characteristics for the time period shown; results over a different time period may have been more or less favourable. US convertibles: ICE BofA US Convertibles Index. US stocks: S&P 500 Index. See end notes index definitions and additional disclosures.

Exhibit 5: New US issuance in line with or above pre-Covid levels



As of 31/12/24. Source: Voya IM (using data from ICE Data Indices, LLC). Projections are based on assumptions with respect to future events. The actual future events may differ from the assumptions. Past performance is not indicative of future results. This statement reflects performance and characteristics for the time period shown; results over a different time period may have been more or less favourable.

Terms to know

Conversion ratio

The number of common shares into which a convertible bond can be exchanged.

Conversion price

Equal to the face value of the bond divided by the conversion ratio.

Conversion premium

The price an investor must pay above the conversion value (number of shares represented in the conversion ratio, multi-plyed by the common share price). Typically, the higher the conversion premium, the less equity sensitive the convertible security is; the lower the conversion premium, the more equity sensitive.

Delta

A measure of the convertible security's price sensitivity to underlying stock price movements. The lower the delta, the less equity sensitive the convertible security is; the higher the delta, the more equity sensitive.

In addition, average initial conversion premiums narrowed from 36% (record high) to about 33% over that same period.²

Increasing new issuance at more attractive terms expands the opportunity set of total return convertibles, which offer a compelling asymmetric risk/reward profile.

Active managers can take advantage of market opportunities

Passive investment strategies may not find it easy to adjust to changes in the convertible market's composition,

issuer fundamentals or individual issue characteristics, among other factors. In addition, these strategies may not have discretion related to new issuance.

We therefore believe that active management is critical to minimising portfolio risks – such as fundamental/credit and concentration risks – while adjusting to changing risk/reward profiles (ie, delta, conversion premiums) of individual issues, which are driven by the movement of the underlying equity.

To summarise, we think US convertibles have an attractive asymmetric return profile, providing

upside participation potential when stock prices rise and downside mitigation when stock prices fall. Accelerated new issuance at favourable terms has expanded the opportunity set of convertible investments with the desired risk/reward characteristics. We believe active management can help mitigate risks and capture opportunities arising from shifting market dynamics.

²) FactSet, ICE Data Services, Voya IM, Morningstar, as of 31/12/24.

A note about risk

All investing involves risks of fluctuating prices and the uncertainties of rates of return and yield inherent in investing. All security transactions involve substantial risk of loss.

Debt instruments: Debt instruments are subject to greater levels of credit and liquidity risk, may be speculative, and may decline in value due to changes in interest rates or an issuer's or counterparty's deterioration or default.

Market volatility: The value of the securities in the portfolio may go up

or down in response to the prospects of individual companies and/or general economic conditions. Price changes may be short or long term. Local, regional or global events such as war, acts of terrorism, the spread of infectious illness or other public health issue, recessions, or other events could have a significant impact on the portfolio and its investments, including hampering the ability of the portfolio's manager(s) to invest the portfolio's assets as intended.

Issuer risk: The portfolio will be affected by factors specific to the issuers of securities and other instruments in which the portfolio

invests, including actual or perceived changes in the financial condition or business prospects of such issuers.

Interest rate risk: The values of debt instruments may rise or fall in response to changes in interest rates, and this risk may be enhanced for securities with longer maturities.

Credit risk: If the issuer of a debt instrument fails to pay interest or principal in a timely manner, or negative perceptions exist in the market of the issuer's ability to make such payments, the price of the security may decline.

UNDERSTANDING US CONVERTIBLES AND WHY THEY'RE ATTRACTIVE TODAY

Investors cannot invest directly in an index. Index returns are presented as net returns, which reflect both price performance and income from dividend payments, if any, but do not reflect fees, brokerage commissions or other expenses of investing. The ICE BofA U.S. Convertibles Index is a cap-weighted index of domestic U.S. corporate convertible securities, including mandatory convertible preferreds. The S&P 500 Index is an unmanaged index that measures the performance of securities of approximately 500 of the largest companies in the United States.

Past performance does not guarantee future results. This market insight has been prepared by Voya Investment Management for informational purposes. Nothing contained herein should be construed as (i) an offer to sell or solicitation of an offer to buy any security or (ii) a recommendation as to the advisability of investing in, purchasing or selling any security. Any opinions expressed herein reflect our judgment and are subject to change. Certain statements contained herein may represent future expectations or other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. Actual results, performance or events may differ materially from those in such statements due to, without limitation, (1) general economic conditions, (2) performance of financial markets, (3) interest rate levels, (4) increasing levels of loan defaults, (5) changes in laws and regulations and (6) changes in the policies of governments and/or regulatory authorities. The opinions, views and information expressed in this commentary regarding holdings are subject to change without notice. The information provided regarding holdings is not a recommendation to buy or sell any security. Fund holdings are fluid and are subject to daily change based on market conditions and other factors.

Allianz Global Investors (AllianzGI) and Voya Investment Management (Voya IM) are in a long-term strategic partnership through which Voya IM acts as delegated manager for certain AllianzGI investment vehicles that utilise Voya IM strategies.

The document is for use by qualified Institutional Investors (or Professional/Sophisticated/Qualified Investors as such term may apply in local jurisdictions).

This document or information contained or incorporated in this document have been prepared for informational purposes only without regard to the investment objectives, financial situation, or means of any particular person or entity. The details are not to be construed as a recommendation or an offer or invitation to trade any securities or collective investment schemes nor should any details form the basis of, or be relied upon in connection with, any contract or commitment on the part of any person to proceed with any transaction.

Any form of publication, duplication, extraction, transmission and passing on of the contents of this document is impermissible and unauthorised. No account has been taken of any person's investment objectives, financial situation or particular needs when preparing this content of this document. The content of this document does not constitute an offer to buy or sell, or a solicitation or incitement of offer to buy or sell, any particular security, strategy, investment product or services nor does this constitute investment advice or recommendation.

The views and opinions expressed in this document or information contained or incorporated in this document, which are subject to change without notice, are those of Allianz Global Investors at the time of publication. While we believe that the information is correct at the date of this material, no warranty of representation is given to this effect and no responsibility can be accepted by us to any intermediaries or end users for any action taken on the basis of this information. Some of the information contained herein including any expression of opinion or forecast has been obtained from or is based on sources believed by us to be reliable as at the date it is made, but is not guaranteed and we do not warrant nor do we accept liability as to adequacy, accuracy, reliability or completeness of such information. The information is given on the understanding that any person who acts upon it or otherwise changes his or her position in reliance thereon does so entirely at his or her own risk without liability on our part. There is no guarantee that any investment strategies and processes discussed herein will be effective under all market conditions and investors should evaluate their ability to invest for a long-term based on their individual risk profile especially during periods of downturn in the market.

Investment involves risks, in particular, risks associated with investment in emerging and less developed markets. Any past performance, prediction, projection or forecast is not indicative of future performance. Investors should not make any assumptions on the future on the basis of performance information in this document. The value of an investment and the income from it can fall as well as rise as a result of market and currency fluctuations and you may not get back the amount originally invested.

Investing in fixed income instruments (if applicable) may expose investors to various risks, including but not limited to creditworthiness, interest rate, liquidity and restricted flexibility risks. Changes to the economic environment and market conditions may affect these risks, resulting in an adverse effect to the value of the investment. During periods of rising nominal interest rates, the values of fixed income instruments (including short positions with respect to fixed income instruments) are generally expected to decline. Conversely, during periods of declining interest rates, the values are generally expected to rise. Liquidity risk may possibly delay or prevent account withdrawals or redemptions.