markit

4th floor
Ropemaker Place
25 Ropemaker Street
London
EC2Y 9LY
United Kingdom

tel +44 20 7260 2000
fax +44 20 7260 2001
www.markit.com

Markit Commentary

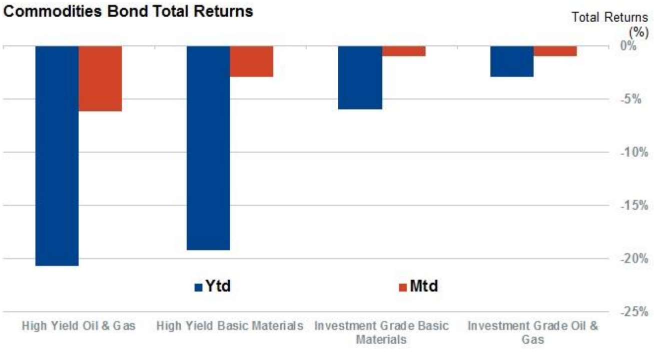
December 10th 2015

IG oil proves winning bet in commodities rout

The commodities slump has hurt resources bond returns on both ends of the quality spectrum but highly rated oil and gas bonds have proven more resilient than the rest of the pack.

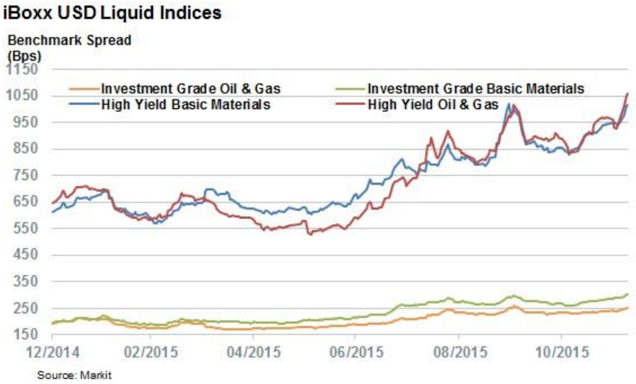
- iBoxx USD Liquid Investment Grade Basic Materials index spreads 6bps off yearly highs
- The iBoxx USD Liquid Investment Grade Basic Materials index has fallen twice as much as its oil & gas peer
- High yield oil and gas and commodities bond spreads now back above 1,000 bps

The commodities rout continued in earnest this week as oil prices hit recent multi year lows, while industrial metal prices also retreated to levels lower than those seen in the depths of the volatility earlier in the year. These developments are not surprisingly translating into further pain for bond investors in resource dependent sectors with both investment grade and high yield bonds in the oil & gas and resources sector posting steep losses for the month so far.



Source: Markit

While the entire commodities sector has been tricky for bond investors, high quality oil & gas bonds have proven to be a spot of relative calm in the recent selloff given that their credit risk as gauged by the benchmark spread priced into the Markit iBoxx USD Liquid Investment Grade Oil & Gas index is below yearly highs seen earlier in the year. That spread now stands at 250bps, 6bps off the yearly highs seen at the start of October. Oil traded at $45 a barrel during the previous peak in credit risk which goes to show that while the current price slump has had an impact on the asset class, the relatively diverse business models and cash positions of the large established players have provided a cushion for bond investors.



Resources names have not been given the same benefit of the doubt from the market given that the benchmark spread of the iBoxx USD Liquid Investment Grade Basic Materials index now trades just shy of 300 bps which is 40 bps more than their oil & gas peers. These spreads marks a four year high for the asset class.

This differential in credit risk that the iBoxx USD Liquid Investment Grade Basic Materials index has delivered negative total returns of 6% for the year to date, twice those seen by the Markit iBoxx USD Liquid Investment Grade Oil & Gas index.

Pain felt in high yield

While both investment grade materials and oil & gas bonds have been tough trades in the current market, their performance over their high yield peers makes them relative high flyers given that both the iBoxx USD Liquid High Yield Basic Materials and iBoxx USD Liquid High Yield Oil & Gas indices are down 3% and 6.2% respectively so far in December. This poor performance marks a new yearly low for both sets of indices as both their year to date total returns now stands at -20%.

These negative returns are driven by a total collapse in investor confidence in the sector given that the benchmark spread of both indices is now back above 1,000bps, a level viewed by many as a sign of distress.

Simon Colvin

Analyst

Markit

Tel: +44 207 260 7614

Email: simon.colvin@markit.com

For further information, please visit www.markit.com