

Delta Investment Management is a registered investment advisory firm headquartered in San Francisco. Delta welcomes discussions with individuals seeking investment advice and advisors seeking a new partner. Delta manages portfolios at TD Ameritrade and Schwab. Please contact Delta at info@deltaim.com or 415-249-6337 to learn more.

April 13, 2018

Float Like a Butterfly, Sting Like a Bee

“The Greatest” (Muhammad Ali) followed this approach in the boxing ring with some success. In the fixed income investment ring, floating like a butterfly is also a viable approach when interest rates are rising.

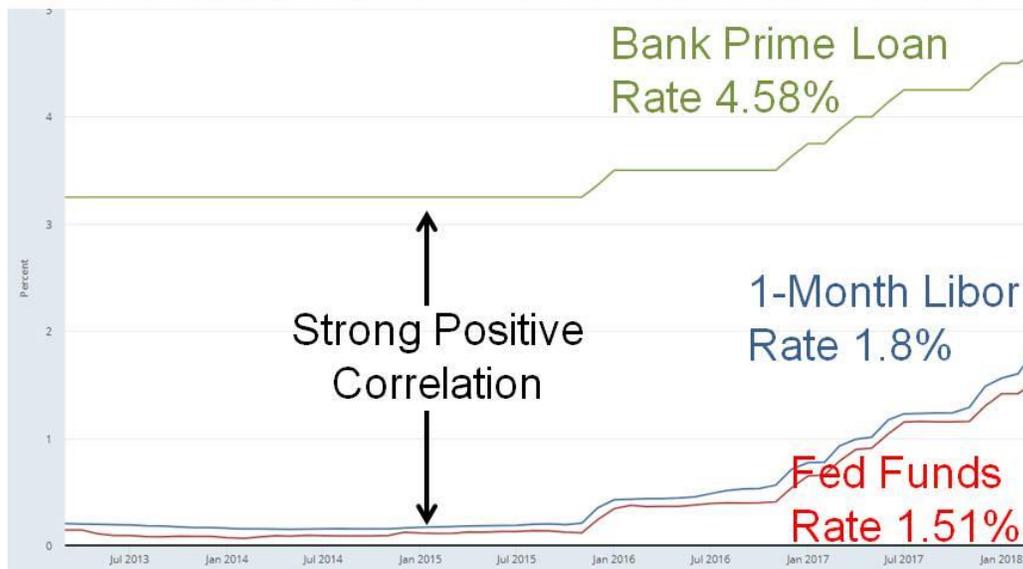
Impact of a 1% Rise in Interest Rates



Of the twelve bond types listed in the chart above, only three appreciate in a rising rate environment. Of the three, two are somewhat dependent on a rising stock market and an improving economy to show solid returns. Only one, floating rate, is a winner simply by the fact that rates are rising.

Floating rate loans have a yield that floats. When rates rise, as when the Federal Reserve raises the Fed Funds rate, floating rate yields rise. Floating rates are tied to short-term (1-month and 3-month LIBOR) interest rates. The floating rate is LIBOR plus a lender margin of 3-5%. Historically, LIBOR rates have traded at a 30-50 basis point premium to the Fed Funds rate.

Fed Funds, 1-Month LIBOR and Prime Rates



Because floating rate loans are tied to 1-month and 3-month LIBOR rates, they have short duration. Duration is the time the yield is constant. Floating rate loans adjust yield based on changes in LIBOR as often as one to three months. As the duration of a bond shrinks, the bond's interest rate sensitivity also shrinks. In the first chart above, floating rate loans are the only fixed income instrument shown to have almost no price loss when interest rates rise by 1%. Notice that the 30-year treasury performs the worst when rates rise, losing roughly -15% with a 1% rise in interest rates.

There are floating rate loan funds that offer close to a 5% annual yield today. This could improve as the Fed continues to raise rates this year and next. This is also materially better than the Credit Suisse Leveraged Loan Index and the S&P Leveraged Loan 100 Index.

Floating rate loans are made to corporations and secured by corporate assets. High-yield bonds are not secured. Historically in very difficult economic times, the principal recovery on defaulted floating rate loans has been about 70%. High-yield bonds have a recovery rate of about 25%.

In the fixed income ring, floating rate loans stand-out currently:

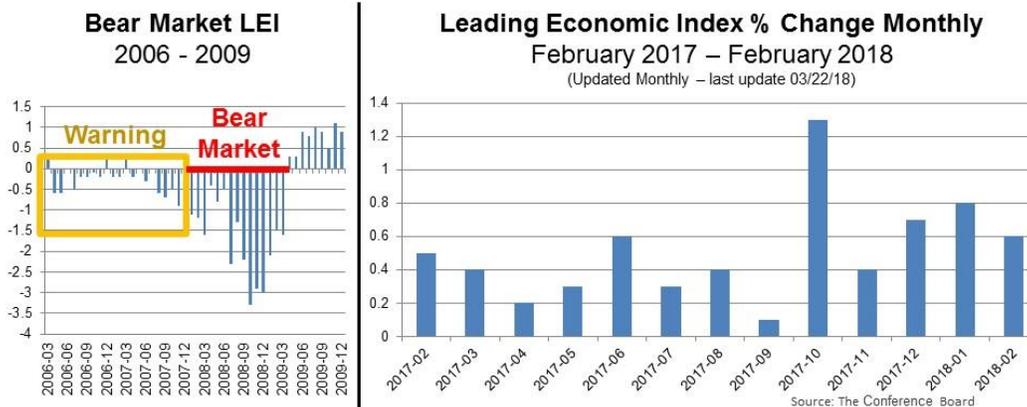
1. Rates are rising making other bond choices much less attractive.
2. It is hard to find a 5% yield on a relatively stable, short-duration fixed income investment.
3. The trailing 12-month default rate is currently about 1.4%. Since the late 1990s, it has averaged roughly 3%.

If you have an interest in exploring investing in floating rate loans further, give us a call at **(415) 249-6337** or send us an email at info@deltaim.com.



"I see no new taxes, followed by some new taxes."

Delta Stock Market Dashboard



MARKET SENTIMENT IS

BEARISH

THIS WEEK'S NUMBER IS

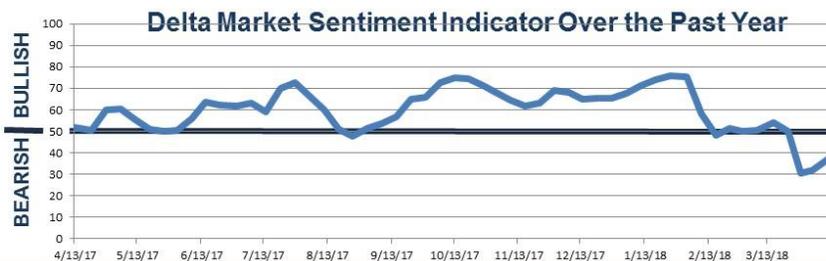
37.7

Our technical indicator increased
this week from 31.7 to 37.7

INDICATOR STATISTICS

Consecutive Bearish Weeks:	3
Cycle Inception Date:	3/29/2018
Range:	30.7 – 37.7
Mean:	33.4
Bullish Weeks YTD:	12
Bearish Weeks YTD:	3
*S&P 500	0.8%
*DJIA	1.4%
*NASDAQ	0.9%

* Percentage change during current cycle



(Delta MSI is published every week in *Barron's*)

Pursuant to the provisions of Rule 206(4)-1 of the Investment Advisors Act of 1940, we advise all readers to recognize that they should not assume that recommendations made in the future will be profitable or will equal the performance of past recommendations. This publication is not a solicitation to buy or offer to sell any of the securities listed or reviewed herein. The contents of this letter have been compiled from original and published sources believed to be reliable, but are not guaranteed as to accuracy or completeness. Nicholas Atkeson and Andrew Houghton are also principals of Delta Investment Management, a registered investment advisor. Clients of Delta Investment Management and individuals associated with Delta Wealth Adviser may have positions in and may from time to time make purchases or sales of securities mentioned herein.

THIS NEWSLETTER IS PROTECTED BY COPYRIGHT LAW. UNAUTHORIZED DISTRIBUTION AND/OR REPRODUCTION BY PHOTOCOPY OR ANY OTHER MEANS IS STRICTLY PROHIBITED AND PUNISHABLE BY A FINE OF UP TO \$25,000.