NORTHEAST
INVESTORS TRUST
A No-Load Mutual Fund
Paying Dividends for Over 70 Years

Rising Yields: A Surge in Attractiveness

It is no secret that interest rates have risen recently, with the 10-year Treasury bond's yield reaching a 16-year high at 4.8%. The average yield in the high yield market crossed another milestone too, with that yield now exceeding 9.0%. What do these developments mean and what do they augur? As a threshold observation, the increasing adoption of the "higher-for-longer" interest rate thesis obviously means that the relative attractiveness of bonds and fixed income in general in relation to stocks has increased, and so investors should consider adding weight to their fixed income allocations.

Now, what's behind this move higher in interest rates? A variety of factors.

- Most notably, **economists have increasingly reduced their estimates of the probability of a hard recession**, thereby reducing the likelihood that the Federal Reserve will aggressively reduce interest rates in 2024. Bond investors no longer have to count on a recession around the corner in order to justify owning fixed income, which is a positive for valuation for those of us who were already more optimistic on the economy. The reduced probability of a hard landing is also good for the anticipated credit quality of the overall high yield market.

- We can find another reason for rising yields in **the anticipated supply of government bonds for sale**, both on account of budget deficits and the Federal Reserve's sales of the bonds it bought up to stabilize financial markets principally in 2020-2021.

- Investors may also be taking into account rising energy prices and the significant costs associated with the energy transition, deglobalization, and other geopolitical developments.

With yields in the high yield market now nearly double the earnings yield of the S&P 500, we think there is a compelling relative value case to be made for high yield, and especially short-duration/high-quality high yield bonds. Since short-term bonds yield more than long-term bonds despite having lower risk (that is, the yield curve remains "inverted"), we think that is best place to be positioned on the maturity spectrum. And it is worth thinking about the time horizons we might appropriately use to analyze bonds: today's two-year high yield bond will be only a one-year bond as we wait for developments to play out over the next 12 months, and a one-year bond a year from now would be considered a very short-duration instrument in bond market terms.

We should also add that bond yields are not only an outcome of developments, they are also an important variable that drives outcomes. To explain: as both short- and long-term interest rates have risen, they are doing the Fed's work for it by slowing the economy and thereby bringing forward the date when the Fed can begin to lower interest rates. In this way, **rising bond yields have themselves laid the groundwork for bond pricing to improve in the future.**

To reiterate, bond yields have moved up sharply, and the relative attractiveness of fixed income has increased. We think investors should take notice.

Bruce H. Monrad is chairman and portfolio manager of Northeast Investors Trust (NTHEX), a no-load, high-yield fixed income fund whose primary objective is the production of income. Bruce is among the longest-tenured bond fund managers in the industry, having run Northeast Investors Trust for more than 30 years.

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Mutual Fund investing involves risk. The Trust invests in lower rated debt securities which may be subject to increased market volatility based on factors such as: the ability of an issuer to make current interest payments, the potential for principal loss if an issuer declares bankruptcy, and the potential difficulty in disposing of certain securities in a timely manner at a desired price and therefore can present an increased risk of investment loss. Diversification does not eliminate the risk of experiencing investment losses.

Falling Interest rates and bond defaults may negatively impact the Trust's distributable income. In addition, during periods of declining interest rates, higher yield securities may be called and the Trust may be unable to reinvest those proceeds in similar yielding securities. Therefore, shareholders should expect the Trust's quarterly dividend distributions to decline under these circumstances. The Trust is generally for investors with longer-term investment horizons, and should not be used for short-term trading purposes. An investment in the Trust involves risk and should be part of a balanced investment program.

Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information about the Trust is contained in the prospectus or summary prospectus, either of which may be obtained by calling 1-800-225-6704 or by visiting www.northeastinvestors.com. Please read either one carefully before investing.

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