

» Six myths about convertible bonds and one real comeback



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Marketing material



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As the stock market euphoria fizzles and global trade rhetorics take centre stage, convertible bonds (CBs) are quietly making their comeback as a top-performing resilient asset class. Hybrids securities with both equity and bond features, CBs are showing their strengths and outperforming traditional stocks with more new issuance.

2023 and 2024 were very kind years to most investors. Equity markets put the losses of the 2022 sell-off behind and rushed from one record high to the next. However, the mega-cap technology stocks (the so-called “Magnificent 7”) contributed a lot of the gains while the rest were, on average, less impressive.

Now the stock market and its magnificent leaders are forced into a reversal (in particular by the new global trade and tariff paradigm), the lesser-known CB market is regaining lost ground. Recently shunned in favour of the better-performing stocks and a handful of hyped alternative assets, the prospects for CBs to once again prove their worth are bright with increased issuance and resilient returns.

The basics

CBs have an asymmetrical payoff structure: They gain when the issuer’s stock price goes up, while mitigating drawdowns through the fixed income features of bonds. Often issued by high-growth companies large and small, CBs enable investors to retain exposure to secular themes, such as AI and healthcare innovation, while shielding themselves from some of the inherent volatility of those stocks. Over the long term, CBs have delivered nearly all the returns of the global stock market with much lower volatility. This relationship is anything but linear, however, largely because the companies that issue CBs differ from the major stock market leaders. For example, some of the largest equity index-driving companies, like Apple and Nvidia, currently do not have convertibles.

Myths about investing in CBs

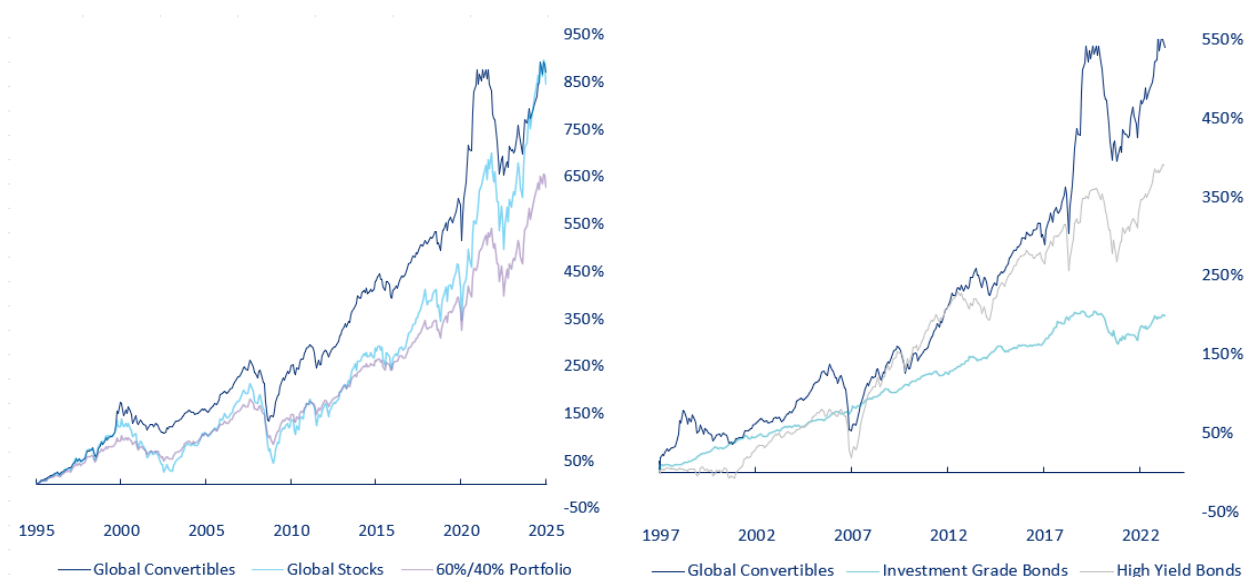
As a relatively niche asset class, convertible bonds are often subject to misconceptions within the broader investment community. Here, we try to debunk some popular myths and rules of thumb that could lead to confusion and false expectations.

Myth 1: CB returns are in the middle of global stocks and bonds

Reality: Over the long term, CB returns are closer to the global stock market but with much lower volatility

Rising stock prices are driving the CB performance, and over the last three decades, global CBs generated all of the returns of global stocks, much higher than most other fixed income assets. This ratio is not constant over time though: CBs largely outperformed stocks in the 2000s, underperformed in the late 1990s and late 2010s, outperformed again in 2020 and underperformed after, until recently when they started outperforming again. Most of these differentials are not, however, driven by any CB-specific valuation or features, but rather by the kinds of companies that issue CBs at the time. Changing market leaders and mean reversion then strengthen the argument for long-term strategic allocations to CBs.

Chart: CBs perform in line with equities and outperform corporate bonds



Source: MSCI World Net Total Return USD, Bloomberg Global Aggregate Total Return Hedged USD, 60/40 Monthly Rebalancing, FTSE Global Convertible Vanilla USD Hedged, ICE BofA Global High Yield Index USD*, Fisch Asset Management. 30-year returns as of 31 Mar 2025. *Only available since 31 Dec 1997.

Myth 2: CB issuers are representative of the global stock market

Reality: The CB universe is a dynamic growth-oriented subset of the stock market

» The CB universe is dynamic and constantly evolving.

There are currently less than 400 underlying companies in the broad FTSE Global Vanilla CB index compared to over 2400 in the Bloomberg World Equity index. Moreover, the convertible universe is rather dynamic and constantly evolving: Many companies do not always re-issue CBs (so they exit at maturity), while new companies access the market opportunistically. Some of the largest capitalisation stocks, like Apple and Nvidia, do not have CBs currently outstanding. While often changing, CB issuers do have common traits: higher earnings growth and exposure to secular investment themes. The lower interest costs of CBs (vs normal bonds without conversion option) naturally attract issuers that are looking to preserve and reinvest their cash to grow.

	Growth	Value	Size	Volatility
Z-score	0.5	-0.1	0.3	0.8

Source: FTSE Global Convertible Vanilla index weighted z-scores (range -3 to +3), calculated by the Blackrock Fundamental Equity Risk model, calibrated based on a broad global equity universe. Data as of 31 Mar 2025.

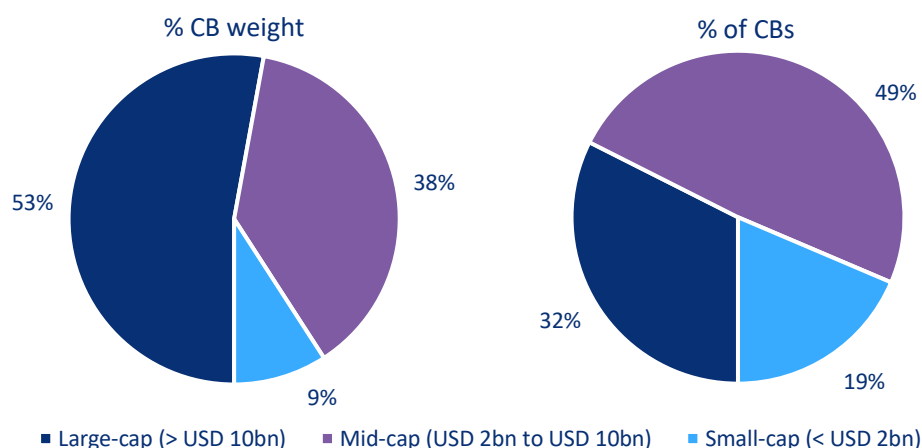
Our factor analysis of the current opportunity set confirms the growth tilt, yet also demonstrates that it does not necessarily come at the equivalent expense of value or size. Still, we see a clear bias towards higher volatility companies, which strengthens the case for an asymmetric-payoff convertible bonds exposure even further in this unique equity subset.

Myth 3: Small-cap companies and start-ups dominate CBs

Reality: More than half of the CB market is large cap

A relatively anchored belief is that most CBs belong to the small-cap space. Actually, convertible issuers do come in all shapes and make attractive financing tools for both large- and small-capitalisation listed companies. Currently, more than half (53%) of the weight of the broad FTSE Global Vanilla CB index is attributed to large-cap (USD 10bn+) issuers vs just 9% to small-cap (<USD 2bn).

Chart: 32% of large-cap CBs make up 53% of the market weight



Source: FTSE Global Vanilla Convertible Bond Index by underlying stock, Bloomberg. Data as of 31 Mar 2025.

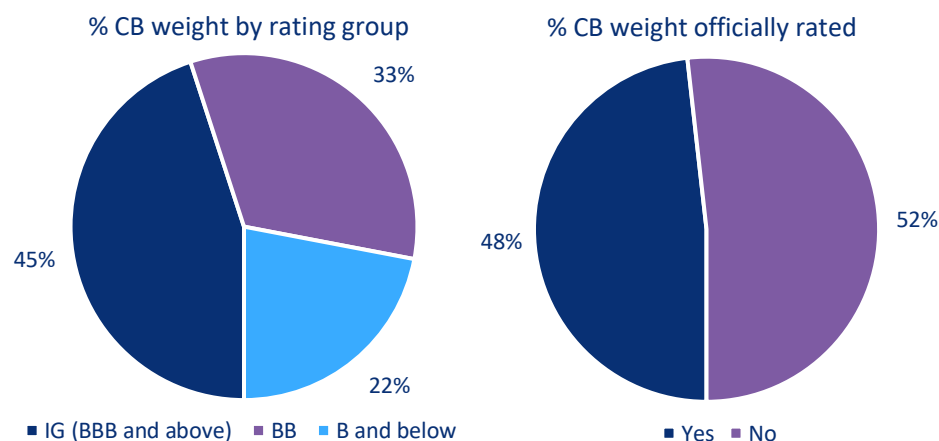
Myth 4: CB issuers are mostly low quality

Reality: Most of the CB market implies investment grade or crossover quality

The majority of CB issuers are not rated by major credit rating agencies and CBs are often the only bonds in the capital structure. This lack of official ratings creates a (false) perception of low quality. Nevertheless, our analysis has shown that more than 50% of the broad index implies investment grade and crossover (BB+) quality. This is confirmed by the historic default rates of CBs that tend to average around half of high yield credit (source: Bank of America).

» The majority of the CB universe comprises IG or crossover-like quality.

Chart: The majority of the CB universe comprises IG or crossover-like quality



Source: FTSE Global Vanilla Convertible Bond Index, Bloomberg, Fisch Asset Management. Data as of 31 Mar 2025. Includes Fisch implied ratings if no official issue or issuer rating available from S&P, Moody's and/or Fitch.

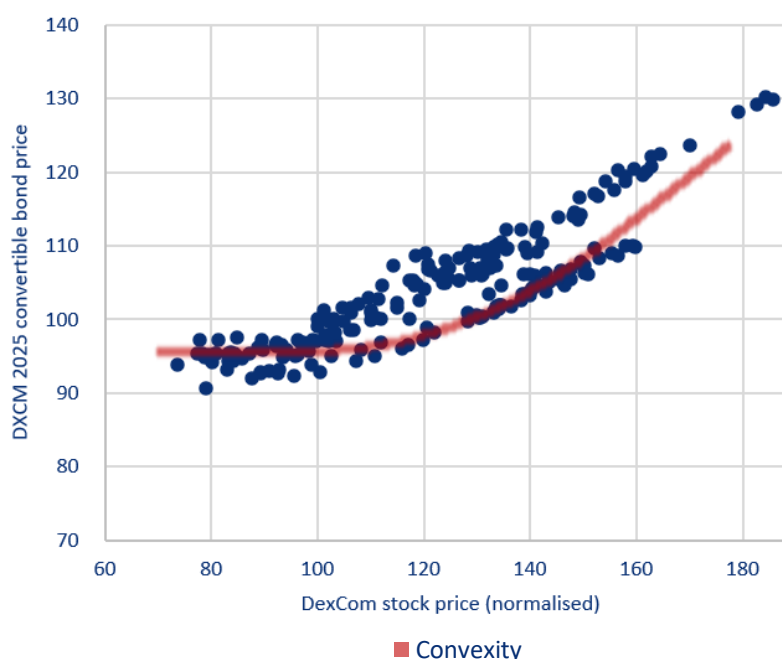
Myth 5: Convexity in all CBs

Reality: Payoff profiles vary – active selection is key

» CBs allow for alpha generation through objective analysis.

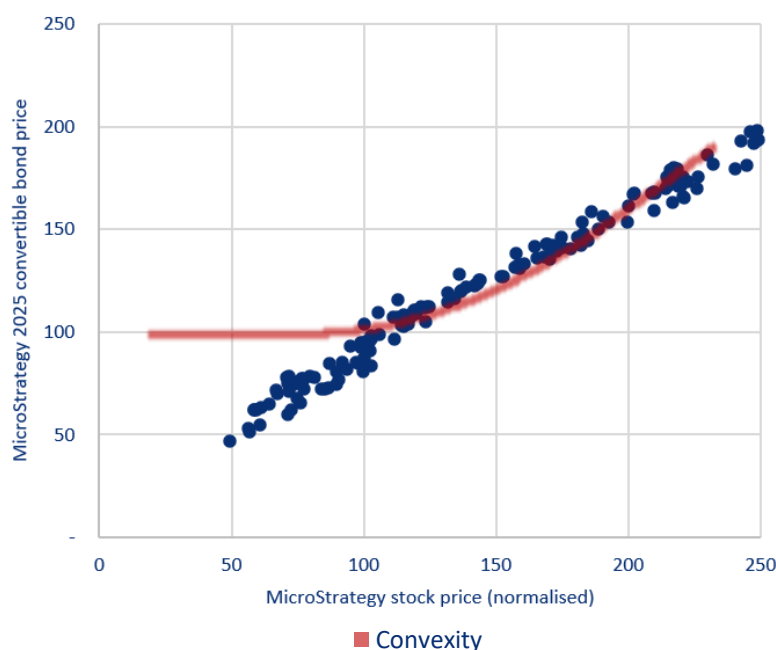
Convexity, i.e. the asymmetrical payoff with more gains than losses from equity moves, is a feature which is not universally distributed throughout the investable index universe. This means that convertibles do not all come alike. Hence, unlike traditional stock and bond portfolios where alpha depends on forward-looking predictions, CBs also allow for alpha generation through objective analysis.

The 2025 CB from medical device maker DexCom is a solid example of true convexity as it benefited from the sound capitalisation and cashflows of the issuer when growth expectations disappointed and the stock plummeted. When the DexCom stock price lost more than 50% last year, the DXCM 0% 2025 CB dropped just 15%, successfully mitigating the downside (see below).



Source: Bloomberg, Fisch Asset Management. Historic weekly data between 2020 issue and March 2025.

On the other hand, high financial leverage, questionable business models/governance and/or high cash burn rates could all result in inferior CB payoff profiles. In such scenarios, as evidenced by the 2025 MicroStrategy CB, the high correlation between the stock price and the default risk/credit spread limits the benefits of a CB vs a stock in terms of risk and drawdowns. In 2022, when the price of the MicroStrategy CB was more sensitive to credit and default risk than to the underlying stock price, investors would have been better off avoiding what was effectively a linear equity-like payoff with similar volatility but lower upside (see graphic on page 6).



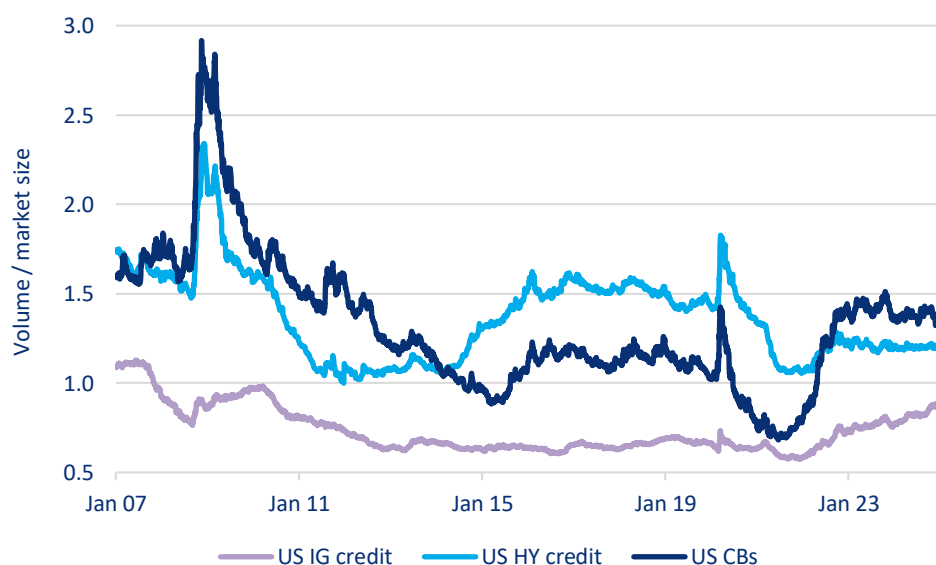
Source: Bloomberg, Fisch Asset Management. Historic data between 2020 issue and Jul 2024 issuer call. As MSTR stock continued to increase the CB continued to exhibit a linear relationship.

Myth 6: CBs are less liquid than credit

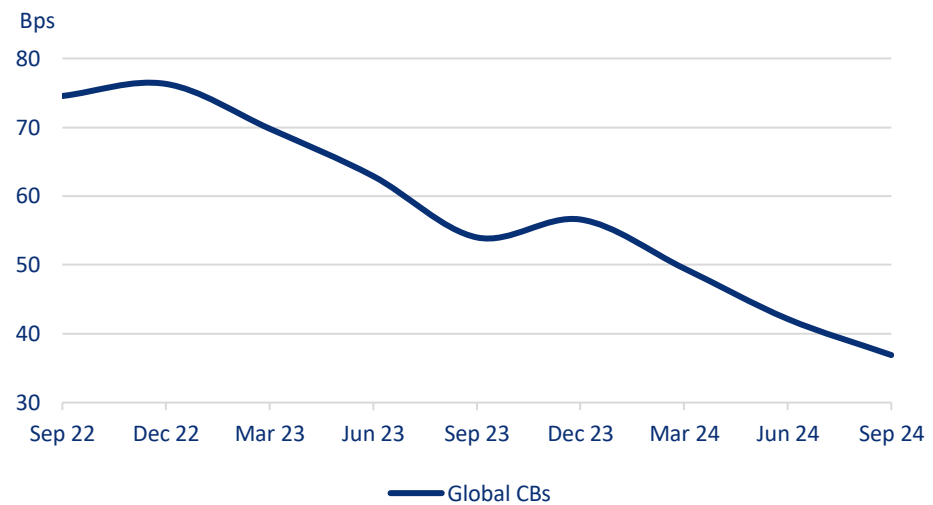
Reality: CBs often trade more actively than other corporate bonds

Thanks to an active secondary market with balanced representation from both hedge funds and active long-only funds, CBs benefit from increasing liquidity, often better than other credit asset classes, and decreasing trading costs. In fact, CB trading liquidity has been improving lately both in terms of volumes and bid/ask spreads.

Chart: 1-year-rolling trading volumes relative to market size



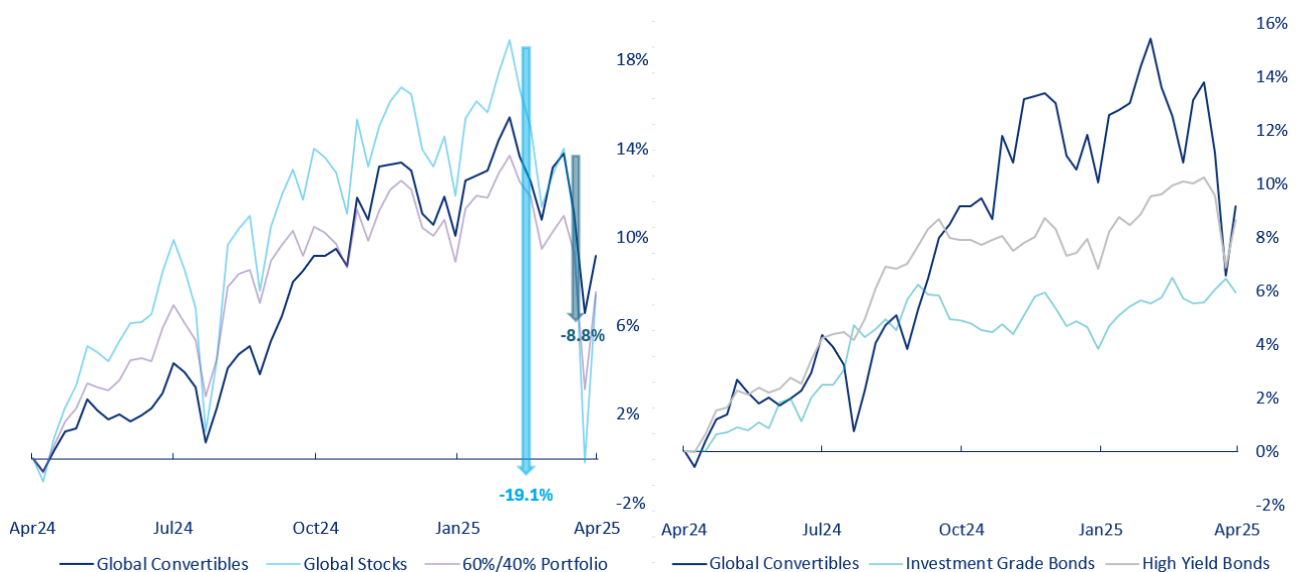
Source: Bank of America

Chart: Median global CB bid/ask spreads

Source: Bank of America

A comeback and a timely opportunity

CBs are showing a glimpse of their return potential again. In the past 12 months, CBs started outpacing the broader stock market, with the CB index returning 9.2% vs 7.4% for equities (both in USD, to 14 Apr 2025). Increased breadth, i.e. their performance is no longer concentrated in a handful of mega-caps, and near-record 2024 global CB issuance both play key roles here. Moreover, asymmetric payoffs do indeed limit drawdowns significantly in times of market stress and geopolitical change. The latest tariff-inspired sell-off is the perfect example: CBs registered less than half of the drawdown in stocks (8.8% vs 19.1% respectively).

Charts: CBs' convex payoffs limit drawdowns in times of market stress

Source: MSCI World Net Total Return USD, Bloomberg Global Aggregate Total Return Hedged USD, 60/40 Monthly Rebalancing, FTSE Global Convertible Vanilla USD Hedged, ICE BofA Global High Yield Index USD, Fisch Asset Management. Data as of 14 Apr 2025.

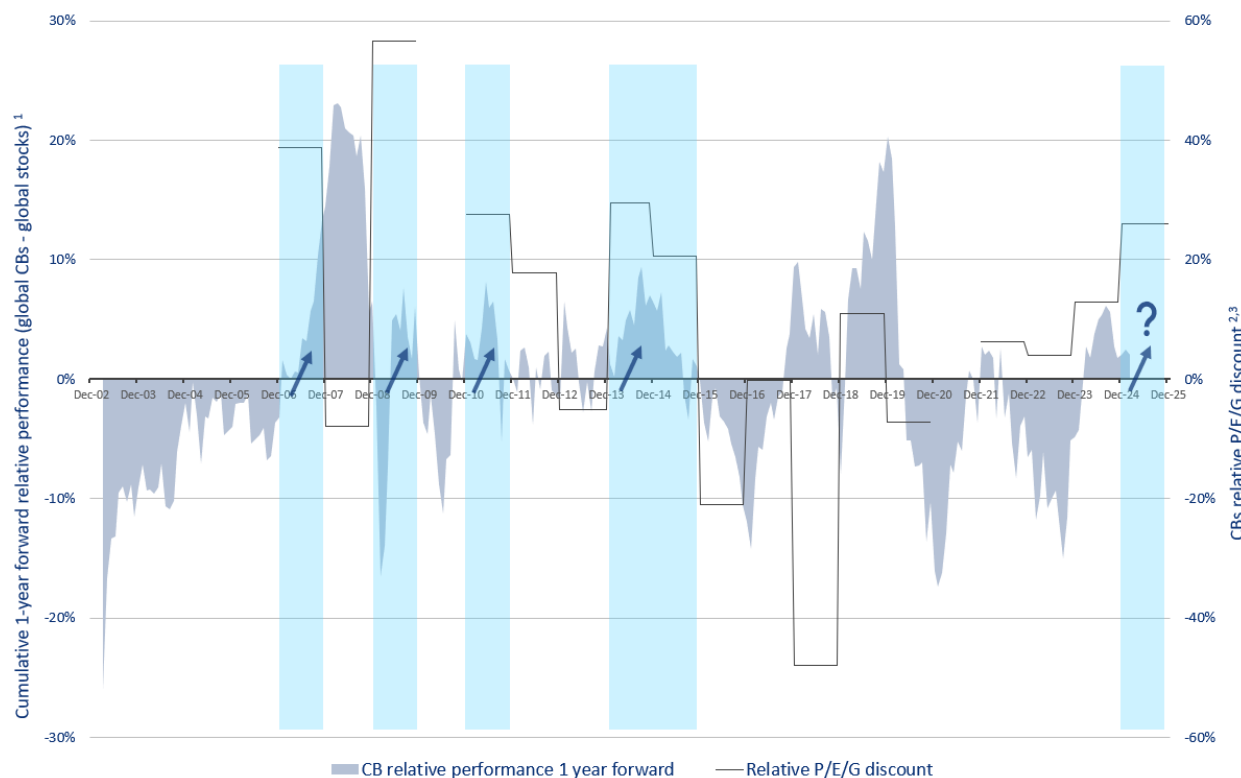
» **2024 was the most active year for CB issuance since Covid.**

The primary market is the lifeblood of the CB asset class. Issuance broadens the investment universe and creates more alpha opportunities for active investors. With near USD 120bn, 2024 was the most active year for convertible issuance since the Covid pandemic, when in 2020 convertibles also outperformed stocks. We expect this recent issuance trend to persist, driven by looming refinancing needs, high overall interest costs and, last but not least, mergers & acquisitions (M&A). M&A activity has been on the rise (Bank of America research, Feb 2025), not least because of a US administration expected to be more deal-friendly and supportive of (domestic) growth with less regulation, at least in the medium term. For CBs, M&A is not only a catalyst for issuance but also for returns: Growth company issuers are often takeover targets, and many CBs come with valuable clauses triggering additional returns upon a takeover, sometimes even higher than the stock price appreciation itself.

Growth at a more reasonable price

Another supportive indicator is the relative under-valuation of the earnings growth of CB issuers vs the stock market average. The average expected 3-year earnings-per-share (EPS) growth rate stood at 18.6% for CB issuers at the end of 2024, more than 70% higher than the average for the stock market. Even more importantly, CBs offer growth at a much more reasonable price with a more than 20% discount in price/earnings-to-growth (PEG) ratio. Such differentials in the past were early signals of outperformance for CBs (also see table overleaf).

Chart: Growth at a reasonable price: a catalyst for a CB renaissance



Source: FTSE Global Vanilla Hedged Convertible Bond Index (USD), Bloomberg World Index (USD), Fisch Asset Management. Data as of 31 Mar 2025.

¹ Forward 12-month performance data from Mar 2024 is projected based on cumulative returns from each respective date to the most recent available data point.

² P/E/G data available only from the end of 2006 onwards and is calculated annually at the close of each year end. Growth defined as the next 3-year EPS compound annual growth rate (CAGR) expectations at each respective point in time.

³ P/E/G data differentials for 2009 and 2020 are unavailable due to market dislocations in these periods.

Valuations: Will history repeat itself in 2025?

Years when the relative PEG discount of CB issuers to the stock market average was greater than 20% at the start of the year	FTSE Global Vanilla Hedged CB Index (USD)	Bloomberg World Equity Index (USD)	Difference
2009	38.6%	36.1%	2.6%
2011	-5.9%	-7.2%	1.3%
2014	6.6%	4.9%	1.7%
2015	2.5%	-1.7%	4.1%
Average	10.5%	8.0%	2.4%
2025	?	?	?

Source: FTSE Global Vanilla Hedged Convertible Bond Index (USD), Bloomberg World Index (USD), Fisch Asset Management. Data as of 31 Mar 2025.

Conclusion

Traditionally, CBs offer a compelling middle ground for investors seeking higher growth exposure with a buffer against volatility. However, the dynamism of the convertible investment universe should be kept in mind: Large-cap and quality companies are a major part of the market, however many of the largest stocks are often not part of it. Long-term CB returns are closer to global stocks with much lower volatility, but CBs could both outperform and underperform in the short and even medium term, driven by the type of issuance. CBs may be niche in investors' portfolios but not in terms of liquidity.

Now, more arguments set the stage for a renaissance in investors' convertible allocations:

- An expanded opportunity set with more new issues from exciting companies
- Growth offered at a more reasonable price
- Less regulation and more support for growth and M&A
- And, of course, convex payoffs to limit drawdowns in times of market stress.

How to invest – why Fisch Asset Management?

Fisch is one of the most established specialists in the convertibles asset class globally – we celebrated our 30th anniversary in 2024. With one of the largest teams dedicated to the asset class, we have a long track record in managing open-ended funds as well as client-tailored mandates to suit the different objectives and constraints of our investor base.

Our investment philosophy stems from what we see as the key benefits of convertible bonds investing:

- Equity upside with lower volatility and less downside risk
- Exposure to key growth themes and disruptive technologies
- Low interest rate sensitivity
- Credit exposure diversification

We believe we can deliver those benefits to our investors through active selection of the best combinations of stock price appreciation potential, credit resilience and convertible bond convexity:

- Long-only active management
- Holistic research process encompassing both credit and equity
- Focus on convex CB profiles with solid bond floors
- Investment selection and sizing driven by both fundamental analysis and momentum
- Strict and disciplined portfolio construction and risk controls
- Long-standing CB market position and relationships beneficial in both primary and secondary transactions

Please reach out *to us.*



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