

## Up Next: Single-Issuer Corporate Bond ETFs

September 29, 2022

Fixed-income ETFs have proven to be the savior the bond market never knew it needed. Not everyone agrees, of course, (active managers among them), but from my perspective, it was ETFs that brought automated market makers into corporate bonds, which, in turn, increased liquidity available electronically, which then drew even more investors to trade electronically, which encouraged more dealers to trade electronically, ultimately increasing market transparency and liquidity overall.

### The Evolution of Credit Derivatives

Over time, ETFs have also acted as the credit “derivative” product the market long awaited. The [single-name credit-default swaps \(CDS\) market is a shell of its former self](#). Index CDS are liquid but too blunt an instrument for those looking for specific exposures, credit futures have yet to make any headway, and other OTC derivatives such as total-return swaps (TRS) remain bespoke and are available only to those with the wherewithal to put ISDA agreements in place.

ETFs (and options on ETFs) now act as a hedging tool—a method of quickly speculating on the direction of credit markets and as a way to put cash to work while the trading desks look for the bonds a fund intends to hold on to for the long term. So while they are not technically, or from a regulatory perspective, a derivative, their use by institutional market participants in these instances suggests otherwise.

So what’s next? We’ve already seen the launch of fixed-income ETFs focused on sectors, ratings, maturities, and durations. More recently, we saw the [launch of single U.S. Treasury ETFs](#), allowing the buyer to get exposure to just the on-the-run 10-year Treasury. The latter followed the launch of single-stock ETFs, a product many were surprised the SEC approved, that have thus far proven popular with retail investors. These announcements made me wonder—where are the single-issuer corporate bond ETFs?

### Single-Issuer Corporate Bond ETFs: The Next Frontier?

One of the main reasons cited for the corporate bond market’s liquidity problems is the sheer number of tradeable bonds, known in market structure circles as the CUSIP problem. As of September 21, 2022, General Motors has 581 bond issues outstanding. There is no easy or cost-effective way to get exposure to all of the outstanding debt of GM (or any other company) today. Buying the bonds one at a time or via a portfolio trade would get you there, as would entering into a bespoke total return swap, but both options are expensive and time consuming, especially given the relatively illiquidity of many of the bonds needed.

So why not a single-issuer ETF? This would leave it to the ETF issuer to manage that portfolio, while providing the buyer quick, easy and relatively cheap (assuming the issuer can keep fees down) access to the needed exposure. In addition to providing investors with the same ETF benefits listed above, single-issuer ETFs would

also allow investors to easily go short that credit, whether to hedge or speculate. Shorting bonds is not easy today, as they're hard to borrow, and gaining short exposure through derivatives isn't much easier, especially given the small size of the single-name CDS market.

And maybe there would even be retail interest, especially now that higher yielding bonds provide a real alternative to equities. Clearly, investors love to buy Apple's equity, so why not its debt? They don't buy its debt today because buying single bonds for most retail investors feels complicated and expensive. Don't get me wrong, we should continue to work on improving retail investor education and access to the bond market itself (more on this coming from us soon). Owning individual bonds rather than ETFs can be advantageous to buy and hold investors, particularly in this market (not to mention the tax benefits). But, right now, ETFs could act as a more accessible gateway drug.

## If It Was Easy...

There are some headwinds. The ETF issuer would have to utilize what was effectively an index for the single corporations' credit. Continuing with the GM example, buying all 581 different bond offerings would be difficult if not impossible, as many of those bonds are likely sitting with buy and hold to maturity investors. That means an index that tracks GM corporate bonds without holding all GM corporate bonds while still limiting basis risk must be created.

ETF market makers would also have to feel like they could effectively manage the risk of trading these products, without always have full access to the underlying bonds in the index. Derivatives would have to play a part in that process - perhaps CDS or TRS. But both can be costly to trade and introduce basis risk, which means wider quoted spreads on the ETF.

Nevertheless, given the current market volatility and potential for more stable returns via bonds in the year ahead, making access to popular bond issuers easier for both institutional investors and the Robinhood crowd feels like a step forward.

---

[www.greenwich.com](http://www.greenwich.com) | [ContactUs@greenwich.com](mailto:ContactUs@greenwich.com)

Coalition Greenwich, a division of CRISIL, an S&P Global Company, is a leading global provider of strategic benchmarking, analytics and insights to the financial services industry.

We specialize in providing unique, high-value and actionable information to help our clients improve their business performance.

Our suite of analytics and insights encompass all key performance metrics and drivers: market share, revenue performance, client relationship share and quality, operational excellence, return on equity, behavioral drivers, and industry evolution.

### About CRISIL

CRISIL is a leading, agile and innovative global analytics company driven by its mission of making markets

function better. It is majority owned by S&P Global Inc., a leading provider of transparent and independent ratings, benchmarks, analytics, and data to the capital and commodity markets worldwide.

CRISIL is India's foremost provider of ratings, data, research, analytics, and solutions with a strong record of growth, culture of innovation, and global footprint.

It has delivered independent opinions, actionable insights and efficient solutions to over 100,000 customers through businesses that operate from India, the U.S., the U.K., Argentina, Poland, China, Hong Kong, and Singapore.

For more information, visit [www.crisil.com](http://www.crisil.com)

## Disclaimer and Copyright

This Document is prepared by Coalition Greenwich, which is a part of CRISIL Ltd, an S&P Global company. All rights reserved. This Document may contain analysis of commercial data relating to revenues, productivity and headcount of financial services organisations (together with any other commercial information set out in the Document). The Document may also include statements, estimates and projections with respect to the anticipated future performance of certain companies and as to the market for those companies' products and services.

The Document does not constitute (or purport to constitute) an accurate or complete representation of past or future activities of the businesses or companies considered in it but rather is designed to only highlight the trends. This Document is not (and does not purport to be) a comprehensive Document on the financial state of any business or company. The Document represents the views of Coalition Greenwich as on the date of the Document and Coalition Greenwich has no obligation to update or change it in the light of new or additional information or changed circumstances after submission of the Document.

This Document is not (and does not purport to be) a credit assessment or investment advice and should not form basis of any lending, investment or credit decision. This Document does not constitute nor form part of an offer or invitation to subscribe for, underwrite or purchase securities in any company. Nor should this Document, or any part of it, form the basis to be relied upon in any way in connection with any contract relating to any securities. The Document is not an investment analysis or research and is not subject to regulatory or legal obligations on the production of, or content of, investment analysis or research.

The data in this Document may reflect the views reported to Coalition Greenwich by the research participants. Interviewees may be asked about their use of and demand for financial products and services and about investment practices in relevant financial markets. Coalition Greenwich compiles the data received, conducts statistical analysis and reviews for presentation purposes to produce the final results.

THE DOCUMENT IS COMPILED FROM SOURCES COALITION GREENWICH BELIEVES TO BE RELIABLE. COALITION GREENWICH DISCLAIMS ALL REPRESENTATIONS OR WARRANTIES, EXPRESSED OR IMPLIED, WITH RESPECT TO THIS DOCUMENT, INCLUDING AS TO THE VALIDITY, ACCURACY, REASONABLENESS OR COMPLETENESS OF THE INFORMATION, STATEMENTS, ASSESSMENTS, ESTIMATES AND PROJECTIONS, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE ARISING OUT OF THE USE OF ALL OR ANY OF THIS DOCUMENT. COALITION GREENWICH ACCEPTS NO LIABILITY WHATSOEVER FOR ANY DIRECT, INDIRECT OR CONSEQUENTIAL LOSS OR DAMAGE OF ANY KIND ARISING OUT OF THE USE OF ALL OR ANY OF THIS

DOCUMENT.

Coalition Greenwich is a part of CRISIL Ltd, an S&P Global company. ©2024 CRISIL Ltd. All rights reserved.