ARISTOTLE PACIFIC CAPITAL

# CLO Monthly Monitor
## September 2023

• September returns were positive across the capital stack for the sixth-consecutive month.

### Loan Market Review

• The CS Leveraged Loan Index returned 0.88% in September. Loans continued to outperform the broader fixed income market, which has been challenged by ongoing interest rate volatility. The index's year-to-date return is now 9.91% and is on pace to become the strongest year since the Global Financial Crisis.

• While the leveraged loan market remained resilient trailed going into the final week of the month, posting the first weekly loss following a 17-week streak of positive performance. Prior to the final week of September, the average price of the loan index had increased to a 16-month high of $95.23, before finishing the month at $94.83.

• Leveraged loan issuance was $38.3bn in September, bringing 3Q23 issuance to $76.1bn and $178.6bn year-to-date. Issuance spiked quarter-over-quarter, up from $50bn last quarter, benefiting from a significant uptick in M&A activity.

• CLO origination was in line with the year-to-date average, with new issuance finishing the month at $9.6bn. Retail fund inflows were just over $1bn in September, which brought inflows for the quarter into positive territory for the first time since 1Q22.

• Sector performance was positive for all 20 industries again in September. Performance was led by Manufacturing (1.11%), Transportation (1.10%) and Information Technology (1.08%), while Retail (0.20%), Consumer Durables (0.41%) and Food (0.49%) lagged the rest of the index.

• Performance in September favored lower quality loans, with Split B-rated and CCC-rated loans returning 1.41% and 2.18%, respectively. B-rated loans also performed well at 0.95%, outperforming BB-rated rated loans, which returned 0.54%. Distressed loans by rating (CC, C and Default) returned -4.85%, bringing the trailing 12-month return to -34.09%.

• There were no loan issuer defaults in September. A total of 31 companies have defaulted year-to-date totaling $27.9bn in loans, which is tracking to become the loan market's third largest annual total. The distressed loan universe (Loans priced below $80) continued to shrink, down $49bn this year, representing just 6.2% of loans outstanding.

### CLO Market Review

• CLO tranches had positive total returns in September. JP Morgan estimated returns for September were 0.56% (AAA), 0.70% (AA), 0.72% (A), 0.67% (BBB), 0.76% (BB), and 1.25% (B).

• CLO origination ended the month with $9.6bn in new issuance, bringing 3Q23 issuance to $28bn. CLO new issuance this year has totaled $83.9bn and has come from 192 deals by 99 managers (Source: LCD).

• An improved CLO equity arbitrage provided an opportunity for aging warehouses to achieve sufficient returns to satisfy investors. With average AAA-spreads falling below 190bps for the first time since 2Q22, the primary market was significantly more accessible to mid-sized and smaller managers.

• The impact of manager size on primary CLO spreads has continued to wane since the end of the second quarter. Outside of debut issuers, primary AAA-spreads tightened across the size spectrum. Larger managers continue to price at the tightest levels, printing as low as 155bps above SOFR in September for shorter deals with 1-year reinvest and 1-year non-call terms.

• Reset and refinance volume was elevated again in September with another $3.1bn in activity, which is now at $9.9bn so far in 2023. Of that $9.9bn in Reset and refinance volume, $2.7bn was from refinance deals and the remaining $7.2bn was from reset activity.

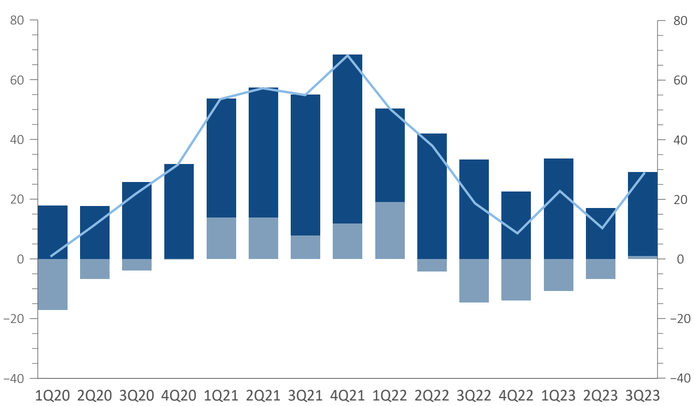
• Despite resilient economic data and core inflation trending lower, CLO spreads were essential flat for senior tranches and lower 5-20 basis points for mezzanine tranches. However, strong coupon returns helped to extend their outperformance over Investment Grade and High Yield bonds at each credit quality rating, which have been impacted by significant interest rate volatility in 2023. JP Morgan estimated year-to-date returns for CLOs were 6.36% (AAA), 8.05% (AA), 10.17% (A), 12.43% (BBB), 16.02% (BB), and 17.28% (B).

• Throughout the capital stack, coupons for CLO debt continue to offer substantially higher payments relative to corporate bonds, which are more than double what their comparable fixed rate corporate bond provided. We believe that this coupon advantage over investment grade and high yield corporate bonds may offer attractive return potential to CLO debt investors, particularly in an environment of higher for longer interest rates.

## Charts of the Month

**1. Supported by a directional shift in retail fund flows and elevated CLO origination, total demand for leveraged loans significantly increased.**

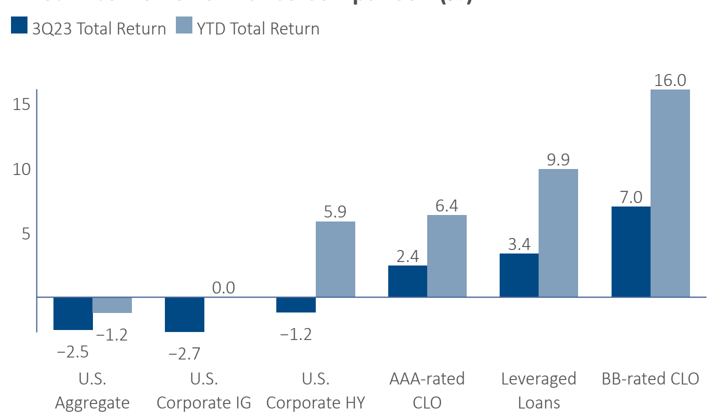
**U.S. Leveraged Loan Market Demand ($bn)**




*Source: Pitchbook/LCD Research as of September 30, 2023*

**2. Leveraged Loans and CLOs have continued to benefit from rising rates and fading recession concerns.**

**Fixed Income Performance Comparison (%)**




*Source: Bloomberg, Credit Suisse, JP Morgan, as of September 30, 2023*

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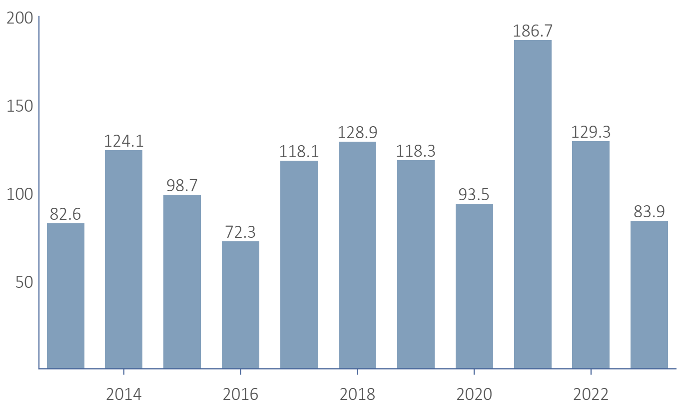
# CLO MONTHLY MONITOR
## SEPTEMBER 2023

| Market Data | Sep-23 Return (%) | 1-Year Return (%) | Yield (%) | Yield Change (%) | DM (BPS) | Price ($) |
|---|---|---|---|---|---|---|
| **JP Morgan CLO Indices** | | | | | | |
| AAA-Rated | 0.56 | 9.06 | 6.3 | 0.3 | 170 | 99.4 |
| AA-Rated | 0.70 | 11.54 | 6.8 | 0.3 | 232 | 98.7 |
| A-Rated | 0.72 | 14.69 | 7.4 | 0.3 | 291 | 98.1 |
| BBB-Rated | 0.67 | 17.79 | 9.1 | 0.4 | 458 | 95.9 |
| BB-Rated | 0.76 | 23.48 | 13.9 | 0.5 | 925 | 88.9 |
| B-Rated | 1.25 | 21.57 | 19.5 | 0.6 | 1,466 | 70.5 |
| **Credit Suisse Leveraged Loan Index** | | | | | | |
| BB-Rated | 0.54 | 11.05 | 7.98 | 0.3 | 337 | 99.06 |
| B-Rated | 0.95 | 13.7 | 9.92 | 0.2 | 531 | 96.95 |
| CCC-Rated | 2.18 | 10.25 | 18.44 | 0.2 | 1,393 | 79.79 |
| Distressed (CC, C, and Default) | -4.85 | -34.09 | 30.89 | -0.8 | 2,648 | 32.26 |

*Source: JP Morgan, Credit Suisse, as of September 30, 2023*

### Technicals

**Annual CLO New Issuance ($bn)**



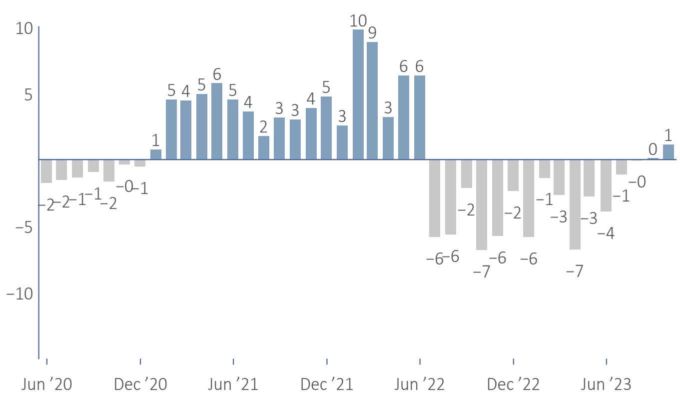

*Source: Pitchbook/LCD Research as of of September 30, 2023*

### Valuations

**Yields on Various Asset Classes (%)**


*Source: JP Morgan, Credit Suisse, Barclays, as of of September 30, 2023*

**Monthly Bank Loan Fund Flows ($bn)**




*Source: Pitchbook/LCD Research, as of of September 30, 2023*

**CS Leveraged Loan Index**


*Source: Credit Suisse, as of September 30, 2023*

**ABOUT ARISTOTLE PACIFIC CAPITAL**

Aristotle Pacific Capital, LLC specializes in institutional fixed income management with a focus on corporate credit. As of September 30, 2023 the firm managed $22bn across bank loan, high yield, corporate, and CLO strategies.

**IMPORTANT NOTES AND DISCLOSURES**

**For Institutional Investor use only.** This information is presented for informational purposes only. This is not to be construed as an offer to buy or sell any financial instruments and should not be relied upon as the sole investment making decision. CLO, Bank loan, corporate securities, and high yield bonds involve risk of default on interest and principal payments or price changes due to changes in credit quality of the borrower, among other risks. All material is compiled from sources believed to be reliable, but accuracy cannot be guaranteed. The opinions expressed herein are based on current market conditions and are subject to change without notice.