

CLO MONTHLY MONITOR

JUNE 2022

• June returns were negative across the CLO capital structure, driven by spread widening that offset the current high coupons.

LOAN MARKET REVIEW

• The CS Leveraged Loan Index returned -2.06% in June, bringing the year-to-date return of the asset class to -4.35%. Leveraged loans experienced their second consecutive month of weakness, both of which have been driven by the combination of broad risk-off sentiment and large investor outflows.

• Concerns surrounding inflation, rising rates, slowing growth, supply chain issues and an ongoing war in Ukraine continue to weigh on the minds of investors, driving outflows from U.S. speculative grade credit. While leveraged loans held onto assets better than high yield bonds, which had outflows exceeding \$10bn, loans had their first quarterly net outflow (\$-3.8bn) since the onset of the global pandemic.

• CLO origination, which accounts for more than half of leveraged loan demand, increased quarter-over-quarter despite challenging conditions. The increased quarterly CLO issuance at \$38.3bn, which came from steady monthly origination of \$12-\$14bn, helped to offset retail fund outflows and support total measurable demand.

• Institutional leveraged loan issuance was again suppressed amid the market volatility, finishing the month at \$15.9bn. While higher than last month's \$6.50bn, the cumulative issuance ended the quarter at its lowest level since the second quarter of 2020.

• Sector performance was negative across all 20 industries in June. Similar to May, commodity-related sectors fared the best in the widespread selling, while Housing (-2.96%), Gaming/Leisure (-2.66%), and Retail (-2.37%) were among the laggards.

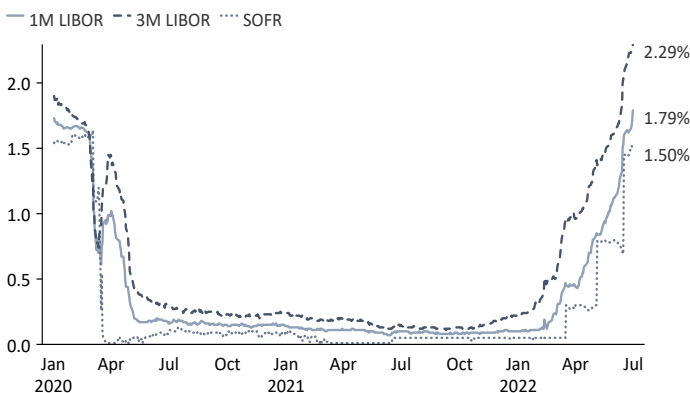
• Credit quality returns favored higher versus lower ratings for the month. BBB-BB rated loans were the best performers, with B-rated and CCC/below returning -2.18% and -2.62%, respectively.

• There were two loan issuer defaults (Endo, Revlon), affecting \$4.6bn in loans. This brings the trailing 12-month issuer default rate to 0.74%, which remains well below the long-term average of 3%.

CHARTS OF THE MONTH

1. Reference rates for Loans and CLOs continue to climb...

Leveraged Loan Reference Rates (%)



Source: Bloomberg, as of June 30, 2022

CLO MARKET REVIEW

• CLO tranches had negative total returns in June. JP Morgan CLOIE index return estimates were -0.32% (AAA), -0.49% (AA), -0.30% (A), -1.27% (BBB), -1.14% (BB), and -3.79% (B).

• CLO issuance remains strong, with \$12.6bn issued in June, bringing cumulative issuance for 2022 to \$69.0bn. CLO new issuance this year has come from 142 deals by 75 managers (Source: LCD).

• Elevated spreads continue to impact refinance and reset volume, which had just \$0.3bn in reset volume. This brings 2022 cumulative refinance and reset volume to \$4.8bn and \$19.6bn, respectively.

• The sell-off in leveraged loans over the last two months, which has seen average prices fall below \$92 from the start of the year, has improved the attractiveness of the CLO equity arbitrage for "print-and-sprint" deals in particular. Instead of spending months ramping up warehouse portfolios mostly from the primary loan market, print-and-sprint CLOs quickly buy loans almost exclusively in the secondary loan market to complete their ramp. As is typical in more volatile markets, an elevated amount of shorter CLO structures continues to price as issuers look to secure shorter non-call periods for their transactions.

• Full-year 2022 issuance forecasts have been revised down by JP Morgan, Barclays and Deutsche Bank. Consensus estimates are now closer to \$100bn, compared to their \$120-\$150bn range at the start of the year.

• Despite concerns over corporations maintaining their profit margins, underlying loan issuers fundamentals continue to strengthen. With earnings through March 2022 released, U.S. leveraged loan issuers have seen the fifth consecutive quarter of double-digit earnings growth. Stronger earnings and a shrinking debt-to-EBITDA ratio, currently down to 4.46x from the 7.70x pandemic high, have provided an increasingly supported backdrop for debt servicing for loan issuers.

• The yield pickup relative to corporate bonds at each credit rating is substantial, without the addition of interest rate risk. BBB-rated CLOs are out-yielding BBB-rated investment grade bonds by 306 basis points (8.13% versus 5.07%) and moving to BB-rated CLOs provides a 540 basis point advantage over BB-rated high yield bonds (12.64% versus 7.24%).

2. ...As well as Discount Margins, increasing coupons and bringing back a more attractive CLO equity arbitrage.

4-Year Discount Margins (bps)



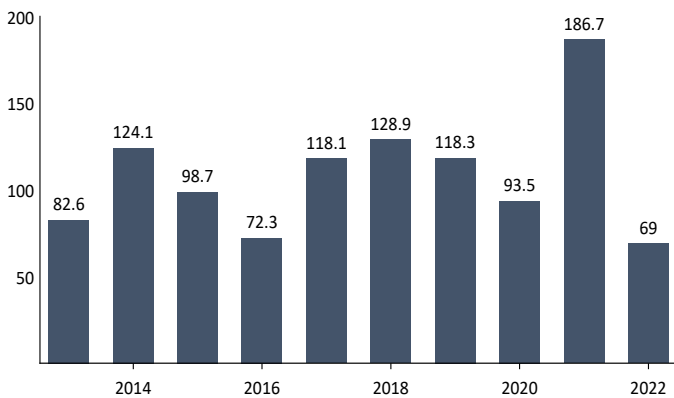
Source: Credit Suisse, as of June 30, 2022

Market Data	Jun-22 Return (%)	1-Year Return (%)	Yield (%)	Yield Change (bps)	DM (BPS)	Price (\$)
JP Morgan CLO Indices						
AAA-Rated	-0.32	-1.10	5.11	60	192	97.34
AA-Rated	-0.49	-2.68	5.81	56	265	95.14
A-Rated	-0.30	-3.56	6.48	52	332	93.66
BBB-Rated	-1.27	-4.72	8.13	72	494	90.75
BB-Rated	-1.14	-4.11	12.64	83	934	85.39
B-Rated	-3.79	-0.52	16.70	170	1327	74.55
Credit Suisse Leveraged Loan Index						
BB-Rated	-1.72	-1.72	7.80	98	472	94.65
B-Rated	-2.17	-2.71	9.89	117	681	92.26
CCC-Rated	-2.35	-6.87	15.63	20	1244	82.13
Distressed (CC, C, and Default)	-4.79	-15.98	40.06	801	3634	53.03

Source: JP Morgan, Credit Suisse, as of June 30, 2022

Technicals

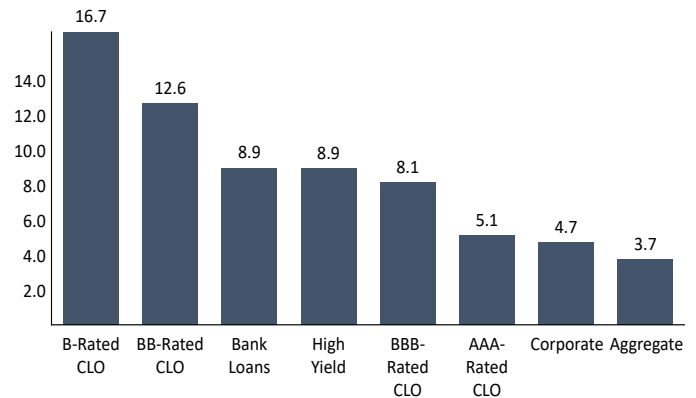
Annual CLO New Issuance (\$bn)



Source: S&P Global Research as of June 30, 2022

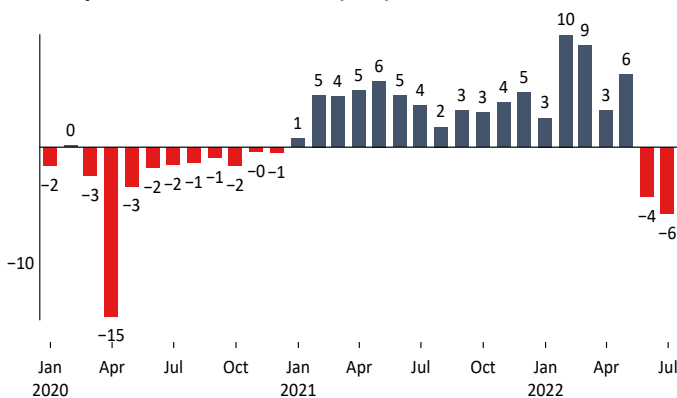
Valuations

Yields on Various Asset Classes (%)



Source: JP Morgan, Credit Suisse, Barclays, as of June 30, 2022

Monthly Bank Loan Fund Flows (\$bn)



Source: S&P/LCD Research, as of June 30, 2022

CS Leveraged Loan Index



Source: Credit Suisse, as of June 30, 2022

ABOUT PACIFIC ASSET MANAGEMENT

Founded in 2007, Pacific Asset Management LLC, specializes in institutional fixed income management. As of March 31, 2022 the firm managed \$20bn across bank loan, high yield, corporate, and CLO strategies.

IMPORTANT NOTES AND DISCLOSURES

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