ARISTOTLE PACIFIC CAPITAL

CLO Monthly Monitor

March 2024

• CLOs delivered strong returns, with spreads across the capital stack continuing their tightening trend.

Loan Market Review

• The CS Leveraged Loan Index returned 0.83% in March. Loans had another coupon-like performance, supported by resilient U.S. economic data and sustained high reference rates.

• Institutional leveraged loan issuance reached $40.3bn in March, contributing to a first-quarter total of $141.9bn. This marks the largest quarterly volume since the third quarter of 2021 and represents over half of the total issuance for 2022.

• The sustained rally in the U.S. leveraged loan secondary market created a favorable environment for loans priced at or above par to reprice their debt. Including repricing and amend & extend activity, total loan issuance for the first quarter amounted to $325.9bn (Source: LCD).

• Strong CLO origination, with $15.5bn of issuance in March, drove loan demand capable of absorbing the increased issuance. CLO new issuance for the first quarter reached $48.8bn, the largest quarterly issuance since the fourth quarter of 2021. Retail fund activity saw a moderate increase with a $2.1bn inflow in March, totaling $2.6bn for the first quarter.

• Sector performance was positive across all 20 industries in March. Performance was led by Chemicals (1.23%), Consumer Non-Durables (1.21%) and Energy (1.14%), while Media/Telecom (0.03%), Financials (0.51%), and Metals/Minerals (0.64%) lagged the rest of the index.

• Performance by rating favored lower-rated CCC-rated loans, returning 1.88%. Loans rated Split-B and higher observed minimal dispersion, with returns ranging from 0.71% to 0.81%. The breakdown of returns by rating was as follows: BB (0.76%), B (0.81%), CCC (1.88%), and CC & Below (-0.06%).

• March had two loan issuer defaults (New Insight, Joann Stores), impacting $1.8 billion in outstanding loans. This brought the first quarter default activity to eleven issuers, affecting $7.2 billion in loans outstanding. Despite the recent increase in the number of issuers defaulting, the par-value of loan defaults continued to decline from peak levels in the first half of 2023. The trailing 12-month default rate, which ended the year at 2.10%, fell to 1.86%.

CLO Market Review

• CLO tranches enjoyed strong total returns in March, with the JP Morgan CLOIE Index reporting returns of 0.53% (AAA), 0.64% (AA), 0.83% (A), 1.37% (BBB), 2.56% (BB), and 3.30% (B).

• March's CLO origination volume surged to $15.5bn, bringing total quarterly issuance to a post-GFC first quarter record of $48.8bn. Issuance continued at a record pace, despite average CLO AAA primary spreads remaining flat from February, with the average deal still in the mid-150s basis points. Year-to-date issuance originated from 106 deals by 76 managers (Source: LCD).

• The range of new issue spreads based on manager size widened during the first quarter based on deals with a 5yr reinvestment period. The spread differential between the largest and the smallest CLO issuers was 10.3 bps, compared to 8.6 bps in the fourth quarter. This was still significantly tighter than the spread differentials observed prior to Q4 in 2023: 24.0 bps (Q3), 32.3 bps (Q2), and 18.3 bps (Q1).

• The recent spike in deals this quarter has prompted additional investment banks to revise their 2024 forecasted issuance upward. Particularly noteworthy was Citi Research also revising their issuance forecasts to $160bn, $130bn in BSL CLOs and $30bn in Private Credit CLOs.

• With earnings through December 2023 mostly released, loan issuers continued to see revenues and EBITDA both grow year-over-year albeit at a decelerated rate, however profit margins improved overall for the quarter. Additionally, sharply rising borrowing costs have led to interest coverage ratios falling below their long-term average. In response to these headwinds, loan issuers have taken a conservative approach to additional borrowing.

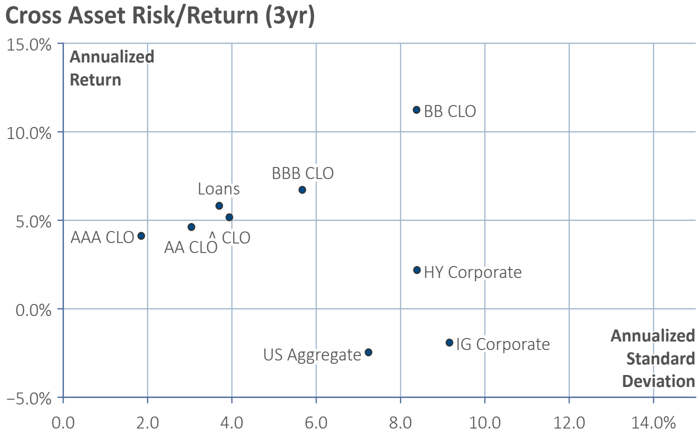
• Collateral managers were able to take advantage of the rally in lower credit quality loans to reduce their CCC-rated loan exposure, lessening the impact of par loss. The percentage of CLO deals breaching the 7.5% CCC-rated threshold by S&P rating fell to 26% through February, down from 37% in December.

• CLO spreads have significantly tightened since October 2023, yet coupons for CLO debt have remained nearly unchanged, offering substantially higher payments compared to corporate bonds. Throughout the capital stack, CLO debt coupons were double those of comparable fixed-rate corporate bonds. This coupon advantage may present an attractive return profile for CLO debt investors, especially in an environment where interest rates may remain higher than was anticipated at the end of 2023.

Charts of the Month

1. Investors that have maintained their exposure to loans and CLOs since the hiking cycle began have been rewarded.

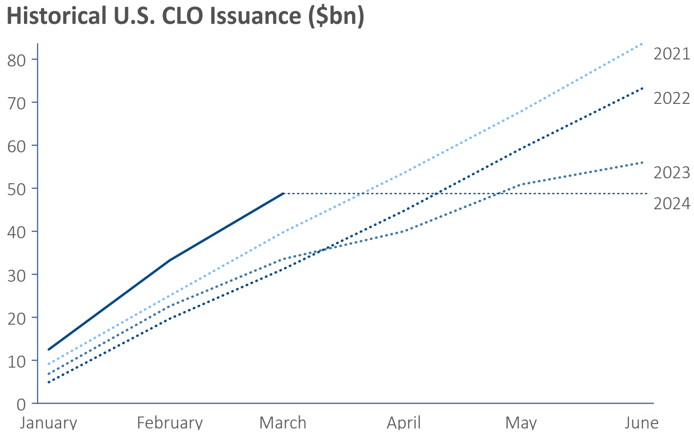
Cross Asset Risk/Return (3yr)



Source: Bloomberg, Credit Suisse, JP Morgan, as of March 31, 2024

2. U.S. CLO issuance continued its record pace, prompting additional revisions to full-year 2024 issuance forecasts.

Historical U.S. CLO Issuance ($bn)



Source: Pitchbook/LCD, as of March 31, 2024

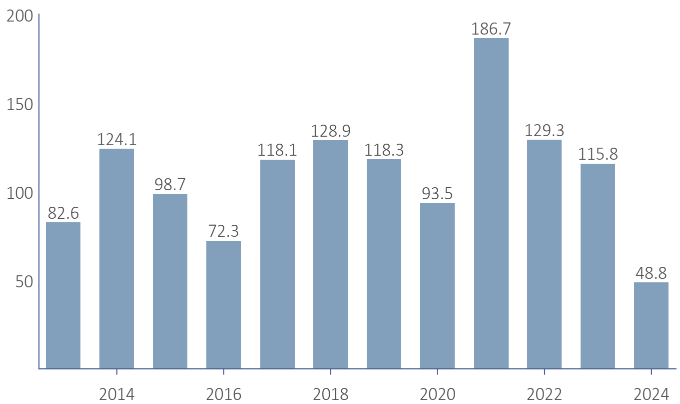
CLO MONTHLY MONITOR
MARCH 2024

Market Data	Mar-24 Return (%)	1-Year Return (%)	Yield (%)	Yield Change (%)	DM (BPS)	Price ($)
JP Morgan CLO Indices						
AAA-Rated	0.53	8.77	6.1	-0.1	105	100.1
AA-Rated	0.64	10.85	6.5	-0.1	179	100.0
A-Rated	0.83	13.96	6.9	-0.1	240	99.7
BBB-Rated	1.37	19.02	8.2	-0.1	362	99.3
BB-Rated	2.56	27.95	12.1	-0.5	766	95.3
B-Rated	3.30	35.97	19.5	0.3	1,434	75.2
Credit Suisse Leveraged Loan Index						
BB-Rated	0.76	9.70	7.4	-0.1	312	99.5
B-Rated	0.81	13.01	9.2	-0.0	494	97.8
CCC-Rated	1.88	20.06	16.9	-0.0	1,274	80.6
Distressed (CC, C, and Default)	-0.06	-5.80	31.4	-3.8	3,759	41.1

Source: JP Morgan, Credit Suisse, as of March 31, 2024

Technicals

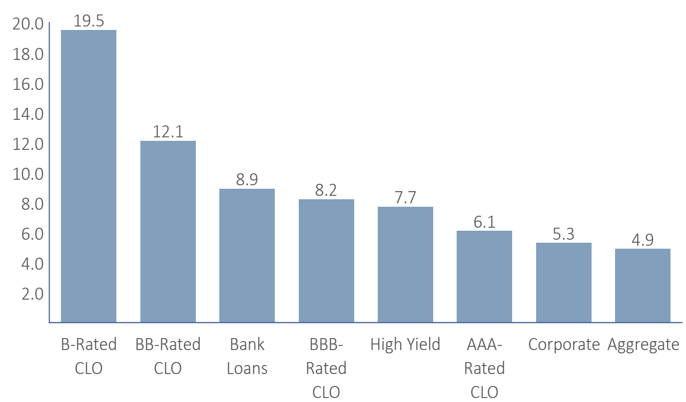
Annual CLO New Issuance ($bn)



Source: Pitchbook/LCD Research as of March 31, 2024

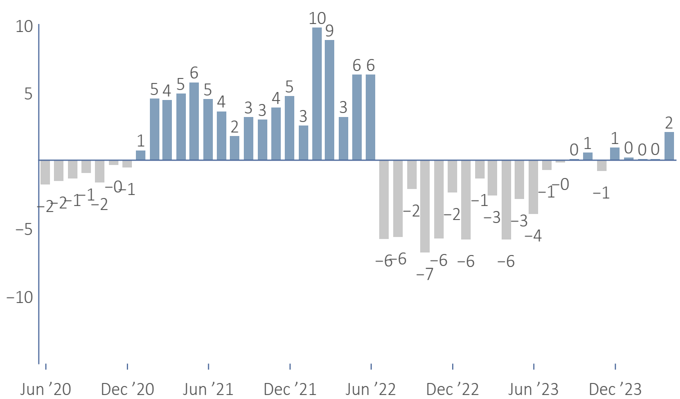
Valuations

Yields on Various Asset Classes (%)



Source: JP Morgan, Credit Suisse, Barclays, as of March 31, 2024

Monthly Bank Loan Fund Flows ($bn)



Source: Pitchbook/LCD Research, as of March 31, 2024

CS Leveraged Loan Index

Source: Credit Suisse, as of March 31, 2024

ABOUT ARISTOTLE PACIFIC CAPITAL

Aristotle Pacific Capital, LLC specializes in institutional fixed income management with a focus on corporate credit. As of March 31, 2024 the firm managed $27bn across bank loan, high yield, corporate, and CLO strategies.