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Global credit funds & CLOs

August breaks historic trend with busiest month for CLOs

The US CLO market defied conventional wisdom in August by notching up its busiest month of new issuance ever. $16.1 billion of new issue CLOs backed by broadly syndicated loans had priced with six days of the month to go as *Creditflux* goes to press, well ahead of the traditionally busier months in the first half of the year, such as June ($14.01 billion) and February ($13.3 billion).

Historically August has been a slower month of issuance as the market enjoys a summer break after CLOs' July payment dates.

Market participants expect the rate of issuance to increase heading into the latter months of the year. Roughly 200 warehouses are thought to be open, with one trustee said to have opened 20 warehouse facilities in July alone.

"Even though we've seen triple A spreads widen a little, the arb is still attractive because loan supply is still high," says Palak Pathak, trader in TCW's securitised products group. "It's the optimal time to be issuing deals and opening warehouses."

Los Angeles-based Pathak says the market has seen huge demand from equity investors, with new investors entering the market and existing investors raising new funds. This gives managers confidence the equity will be spoken for when they open a warehouse.

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> **Robert Grunewald**
> *Chief executive*
> Flat Rock Global

"We've really seen the equity part of the market become institutionalised over the past year," Pathak adds. "Minority equity is being sold in an almost b-wic fashion."

Flat Rock Global is modelling returns of 15% to 16% in the new issue market, compared to its business plan at launch three years ago, when returns of 12% to 13% were expected.

"It's a great time to invest in CLO equity," says Flat Rock chief executive Robert Grunewald.

"The fact that we got through a recession means the new CLOs that are being created are some of the cleanest CLOs formed, and we think there's a reasonable chance that loss assumptions are actually lower than expected."

With new issue loan supply so strong, only around 10% of CLO collateral is trading above par, meaning the bulk of the market is not at risk of refinancing. Much of the heavy M&A supply is from deals delayed from 2020, and the issuance is keeping spreads at levels where they're unlikely to refinance.

Additionally, with three-month Libor hovering around the 0.13% level, Libor floors continue to provide a pickup to the first loss tranche holder.