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News

CLO managers to ramp up mid-market loan holdings

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Mid-market loans may increasingly infiltrate broadly syndicated loan CLOs as managers seek to boost returns amid tighter leveraged loan spreads, say market sources.

Broadly syndicated loan CLOs that include middle-market debt price wider than vanilla deals, but post similar weighted average rating factor scores. They also often post higher returns than vanilla CLOs.

“I expect we’ll see more of a trend into the middle market space,” says Tricia Hazelwood, Mitsubishi UFJ Financial Group’s international head of securitised products. “It may be that we need three categories for CLOs: one of which is broadly syndicated loans, one of which is middle market, and one which is a hybrid.”

Late last year, ArrowMark Partners reissued its middle market CLO Peaks 3, transforming it into a regular CLO named Elevation 2021-15 in the process. The mid-market CLO already held liquid loans and, once reissued, it priced in line with broadly syndicated loan CLOs, though on the wider side of market averages.

“We may need three categories for CLOs: BSL, middle market and hybrid”

Tricia Hazelwood, International head of securitised products **| Mitsubishi UFJ Financial Group**

Another blurring of the line between broadly syndicated loan CLOs and mid-market deals is happening as mid-market managers sell CLO equity stakes to third parties. Many of the biggest managers of mid-market CLOs — such as Antares, Cerberus and Golub — hold all their own equity. But the likes of Barings, BlackRock, BMO, Brightwood, Churchill, First Eagle, Maranon, and Monroe are syndicating on occasion.

Shiloh Bates, managing director at Flat Rock Global, has repositioned his portfolio towards mid-market CLOs. His firm’s flagship CLO equity fund, Flat Rock Opportunity Fund, returned an estimated 25% in 2021.

“Debt investors look at broadly syndicated loan and mid-market CLOs in a binary way,” says Bates. “If it’s broadly syndicated, the CLO gets lower cost of debt and higher leverage.” Middle-market deals tend to get a bigger triple C bucket, high-yielding loans with covenants and a better original issue discount.