US Loan Market Snapshot

Monthly US loan market update: August 2017

Senior secured loans returned 0.69% in July and 2.62% y ear-to-date.[1] This was the loan market's strongest monthly return of 2017, driven by the recovery of loan prices from a soft month in June as new issue activity slowed and demand was stable. Risk assets broadly performed well during July, adding to the resurfacing technical tailwind for loans. Meanwhile, a benign start to earnings season indicated ongoing fundamental credit stability across much of the market. Sectors of investor concern, including energy, mining, retail, and utilities, delivered the strongest monthly returns from an industry perspective.[1]

Unlike in June, demand outpaced supply during the month, an environment which supported loan prices. However, the market experienced a notable decline in repricing and refinancing activity relative to earlier in the year, perhaps an inevitable consequence now that 49% [2] of outstanding loans have done so year-to-date. New issuance in July slowed to a 12-month low of $39.1 billion, including just $27 billion of repricings and refinancings, versus a monthly average of $73 billion during the first half of 2017. The percentage of loans trading above par climbed back to 72.2%, ne ar the 2017-high.

Despite strong results in July, loans were again outperformed by peer asset classes as the High Grade Bond Index returned 0.75% and the High Y ield Bond Index returned 1.15%. [3] The 10 year Treasury returned 0.29% as yields held s teady at 2.29%. L oans' lower yielding, higher quality "BB" (0.65%) and "B" (0.72%) r atings categories underperformed the "CCC's" (1.09%). [1] The average price in the loan market was $98.39 at the end of July.[1] At the current average price, senior secured loans are providing a 5.75% yield. [1]

Fundamentals

- The first estimate of Q2 GDP was 2.6%, in line with the c onsensus of economist estimates. Growth was fueled by firm consumer spending and non-residential investment, and was consistent with other monthly indicators which had pointed to stable economic growth.
- There were no new defaults in July, causing the trailing 12 month default rate to fall from 1.54% to 1.36%. [1]

Average loan price includes all loans January 1997 through July 2017.

Technicals

- Technical conditions tightened in July; demand was firm while net new supply declined as a result of less issuance and modest paydown activity.
- Gross CLO volume was $18.5 billion in July, a step back from June, with $7.5 billion of issuance net of refinancings.[2] Year-to-date CLO issuance is $171.2 billion (gross) and $59.9 billion (net).
- Retail mutual funds and ETF's recorded a small but positive $365 million inflow for the month. Despite slowing notably in the last three months, year-to-date inflows are $17.9 billion[2] with thirteen consecutive positive months. Meanwhile, demand from institutional investors has remained strong.
- New issuance volume was $39.1 billion in July, and $12.2 billion excluding refinancing and repricing activity. Year-to-date, gross and net issuance have totaled $616 billion and $152.6 billion, respectively.

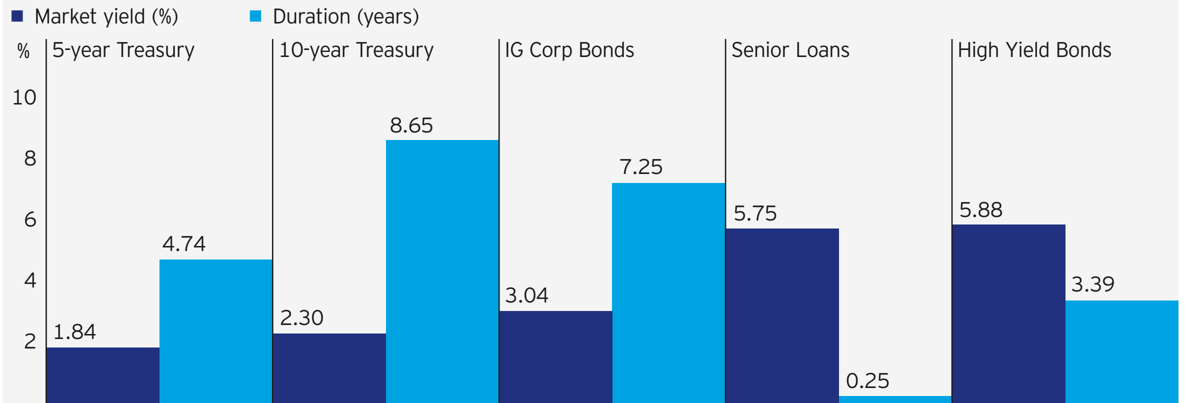
Relative value/market opportunity

Year-to-date, loans (2.62%) ha ve lagged high yield (6.12%) amid a br oadly positive environment for risk assets. High yield bond yields have declined to a 3-year low as stock markets have surged, earnings have grown, oil has stabilized, and rates have remained relatively benign. As a result, the yield differential between loans and unsecured bonds has narrowed to nearly zero, near historical lows. Thus, investors are able to own less volatile, more defensively positioned loans at a similar yield to unsecured bonds, while avoiding interest rate risk. With 3-month LIBOR at 1.31%, the ris e in loans' base rate has partly offset the compression of spreads stemming from repricings. Moreover, the level of income received by loan investors is positioned to benefit from any further increase in interest rates.[1]

Senior secured loans currently offering similar yields as unsecured bonds

Source: J.P. Morgan, as of July 31, 2017. High yield represented by the J.P. Morgan US HY Bond Index; Loans represented by the J.P. Morgan Leveraged Loan Index. Past performance cannot guarantee comparable future results.

Loans continued to offer investors a high level of current income with short duration



Source: Bloomberg L.P., J.P. Morgan, S&P LCD as of July 31, 2017. Investment grade corporate bonds represented by a subset of the BBG BARC U.S. Aggregate Index; the senior secured loan asset class is represented by S&P/LSTA Leveraged Loan Index; and high yield bonds represented by the J.P. Morgan US HY Bond Index. Past performance cannot guarantee comparable future results. An investment cannot be made directly in an index. Diversification does not guarantee a profit or eliminate the risk of loss.

	$ Price	Yield to worst (%)	Spread to worst	At forward Libor	Duration (years)
5-year Treasury	100-06	1.84			4.74
10-year Treasury	100-22	2.30			8.65
Bloomberg Barclays US Agg Index	103.57	2.51	T + 0.56		5.99
Bloomberg Barclays IG Index	105.95	3.04	T + 0.99		7.25
J.P. Morgan US HY Bond Index	103.06	5.88	T + 4.23		3.39
S&P/LSTA Leveraged Loan Index	**98.39**	**L+4.05**	**T + 4.24**	**5.75%**	**90 Days**

Source: Source: Bloomberg L.P., J.P. Morgan and S&P LCD as of July 31, 2017. Loan yields incorporate LIBOR forward curve as of July 31, 2017. Loan "spread to worst" and "At Forward LIBOR" incorporate LIBOR forward curve as of July 31, 2017. Past performance cannot guarantee comparable future results.

1 S&P LCD (Leveraged Commentary and Data) as of July 31, 2017; Total returns and other data stated are for the S&P LSTA Leveraged Loan Index.
2 J.P. Morgan as of July 31, 2017.
3 HY Bonds: BAML HY Master Index, High Grade Bonds: BAML High Grade Corp; data as of July 31, 2017. Returns stated are total returns.

Important information

All data provided by Invesco unless otherwise noted. All data is US dollar and as of July 31, 2017, unless otherwise noted.

Most senior loans are made to corporations with below investment-grade credit ratings and are subject to significant credit, valuation and liquidity risk. The value of the collateral securing a loan may not be sufficient to cover the amount owed, may be found invalid or may be used to pay other outstanding obligations of the borrower under applicable law. There is also the risk that the collateral may be difficult to liquidate, or that a majority of the collateral may be illiquid.

Compared to investment grade bonds, junk bonds involve a greater risk of default or price changes due to changes in the issuer's credit quality. Diversification does not guarantee a profit or eliminate the risk of loss.

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