Invesco Senior Secured Loans

US Loan Market Snapshot

Monthly US loan market update: September 2017

Senior secured loans returned -0.04% in August and 2.57% year-to-date.[1] Weakness in loan prices stemmed from elevated volatility across the risk spectrum. Despite continued signs of macroeconomic durability and broadly healthy corporate earnings, risk assets softened during the month under the cumulative weight of domestic and international political tensions. Declining investor confidence in prospects for a near-term fiscal policy lift has, in turn, curbed interest rate expectations, which had buoyed interest in the loan asset class year-to-date. With the technical landscape characteristically neutral for loans at the end of summer, loan prices dipped enough to offset coupon income. Amid the weaker market dynamic, energy and retail were the worst performing sectors.[1]

After a busy first couple of weeks, new issue supply slowed to a trickle as is seasonally typical in August. New issuance in August of $64 billion, including $42.8 billion of repricings and refinancings, was above July's 12-month low, but below 2017 averages. Meanwhile, demand for loans was firm amid modest retail fund outflows but solid new CLO volume. The percentage of loans trading above par fell back to 63%.[2]

Loans performed in line with high yield bonds, with the High Yield Bond Index returning -0.03%. The lower risk, higher duration High Grade Bond Index gained 0.85%.[3] The 10 year Treasury surged 1.62% as yields dipped 17 basis points to 2.12%. Loans' lower yielding, higher quality "BB" (-0.01%) and "B" (-0.10%) ratings categories matched the performance of "CCC's" (-0.12%).[1] The average price in the loan market was $97.96 at the end of August.[1] At the current average price, senior secured loans are providing a 5.70% yield.[1]

Fundamentals

- The Q2 GDP estimate was upwardly revised from 2.6% t o 3.0%, r eflecting firm household spending and non-residential investment.
- There were no new defaults in August, causing the trailing 12 month default rate to remain 1.36%.[1]

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

Technicals

- Technical conditions were moderately supportive in August; demand was positive while net new supply remained below yearly averages.
- Gross CLO volume was $20.4 billion in August, with $12.1 billion of issuance net of refinancings.[2] Year-to-date CLO issuance is $192.9 billion (gross) and $72.9 billion (net).
- Retail mutual funds and ETF's recorded a small outflow of $511 million for the month. Despite slowing notably in the last four months, year-to-date inflows are $17.5 billion.[2] Meanwhile, demand from institutional investors has remained solid throughout the year.
- New issuance volume was $64 billion in August, and $21.2 billion excluding refinancing and repricing activity. Year-to-date, gross and net issuance have totaled $680 billion and $173.6 billion, respectively.

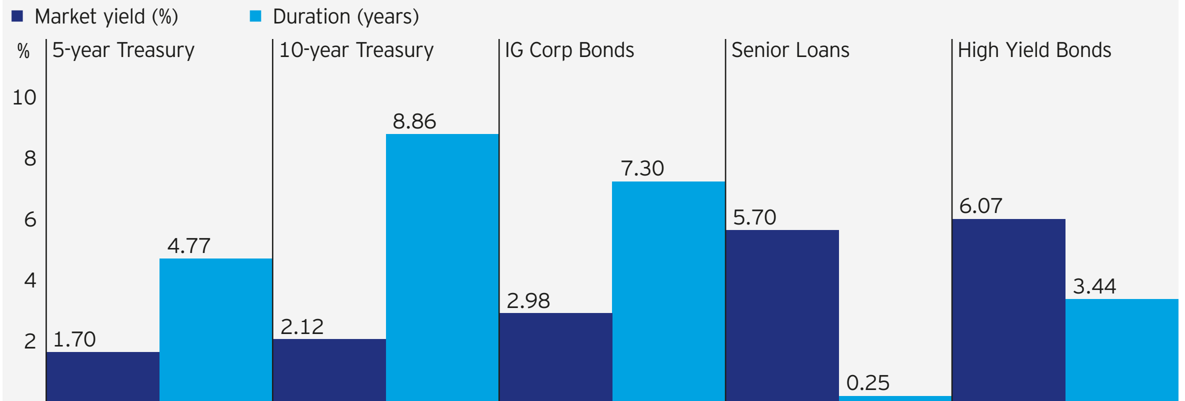
Relative value/market opportunity

Year-to-date, loans returns (2.57%) c ontinue to lag high yield (6.09%) as risk as sets have broadly trended higher. High yield bond yields are near 3-year lows driven by numerous tailwinds: stock markets gains, healthy earnings, stabilizing oil, and relatively benign interest rate movements. As a result, the yield differential between loans and unsecured bonds has narrowed to nearly zero, close to historical lows. Thus, the opportunity remains for investors 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 Aug. 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 Aug. 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	99-20	1.70%			4.77
10-year Treasury	101-06	2.12%			8.86
Bloomberg Barclays US Agg Index	104.25	2.42%	T + 0.60		5.93
Bloomberg Barclays IG Index	106.46	2.98%	T + 1.06		7.30
J.P. Morgan US HY Bond Index	102.57	6.07%	T + 4.49		3.44
S&P/LSTA Leveraged Loan Index	**97.96**	**L+4.18%**	**T + 4.27**	**5.70%**	**90 Days**

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

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