Invesco Senior Secured Loans

US Loan Market Snapshot

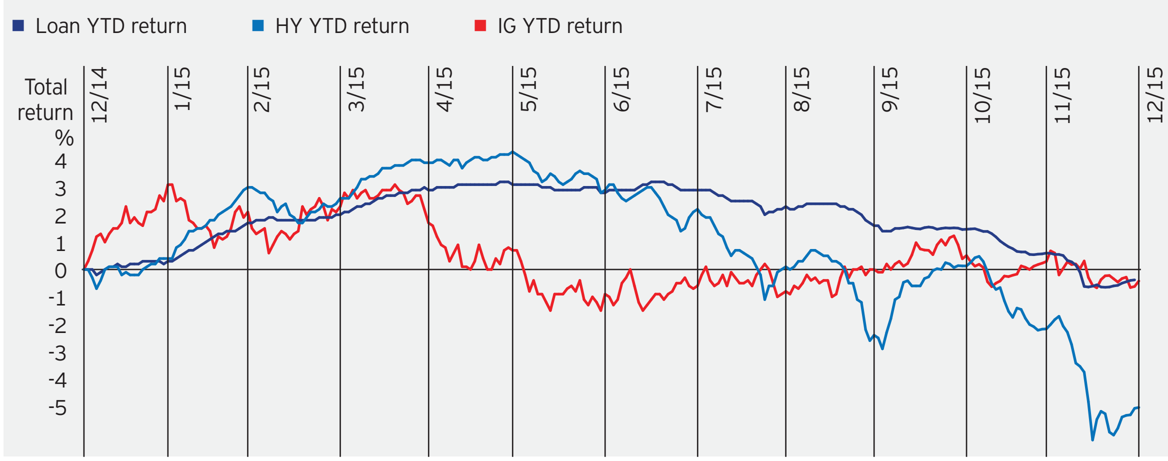
Monthly US loan market update: January 2016

Senior secured loans had another negative return for December (-1.05%) resulting in a 2015 year-end total of -0.69%.[1] December was the worst monthly performance for the loan index during 2015 and the negative total return for the year marked only the second annual loss for the index in its 19-year history. Key drivers of returns during the month were a continuation of many of the themes that have weighed on the market over the last few months: (1) continued declines in commodity prices (2) weaker technicals (3) a bifurcation in performance across the risk spectrum with higher quality credits significantly outperforming the broader index (4) contagion from weaker performance in US HY Bonds, and (5) a general "risk-off" tone across the broader capital markets.

Despite the headwinds facing the market, fundamentals in general remain supportive—with small pockets of weakness—particularly in commodity related sectors weighing on the market averages. As in previous months, higher quality "BB" rated loans continued to outperform the lower quality single-B and CCC issues. BB-rated loans returned -0.43% during December versus -1.35% for single-B rated loans, -2.76% for CCC-rated issues, and -8.23% for loans rated D.[1]

Despite the relatively weak stretch of returns following the summer, loans continued to perform well on a risk-adjusted basis—underperforming the S&P 500 by 2.1% for the year but exceeding US HY bonds by 3.95%-- albeit with much lower volatility.[2]

Loans have provided relatively stable returns despite broader market volatility



Source: Credit Suisse as of Dec. 31, 2015. Loans represented by the Credit Suisse Leveraged Loan Index; HY represented by the Credit Suisse High Yield Bond Index; IG represented by the Credit Suisse Liquid US Corporate Index.

Average loan price includes all loans January 1997 through December 2015.

Rising Interest Rates

During the month, the US Federal Reserve (US Fed) implemented its first interest rate increase since 2008 and continued to imply that the path to normalization will be "gradual". We reiterate that the macroeconomic conditions in the US of steady GDP growth and low unemployment are supportive of credits in the senior secured loan space and loan fundamentals overall. The average price in the loan market at the end of December was $91.72. At the current price senior secured loans are providing a 7.3% yield.[1]

Fundamentals

- There was one new default in December—Energy & Exploration Partners—bringing the trailing 12 month default rate by principal amount to 1.54% from 1.47% in November.[1]
- We view the US Fed's decision to increase rates at the December meeting as a positive indicator for loan issuer's fundamentals—reflecting the US Fed's confidence in macroeconomic trends.

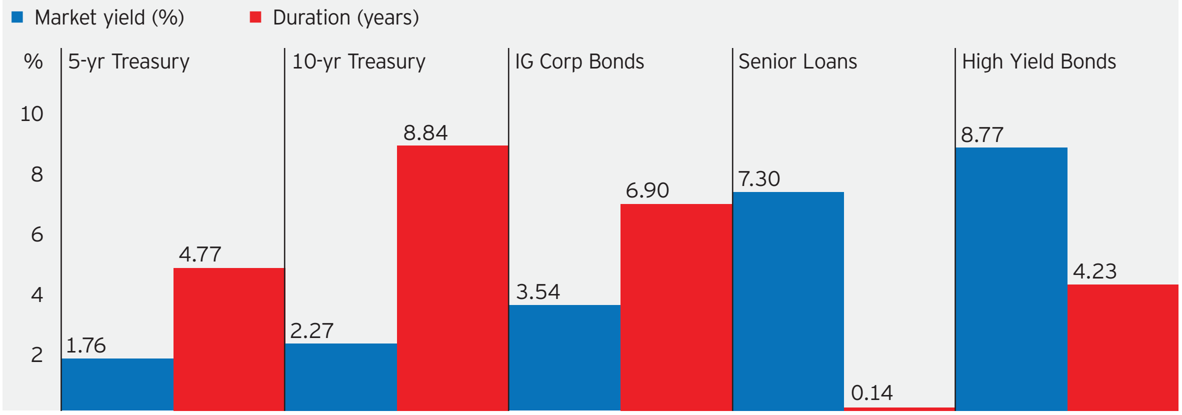
Technicals

- Despite the US Fed actions during the month, outflows from retail mutual funds continued during the month with the week ending December 18 witnessing the largest weekly outflow in four years (-$2.04 billion).[3] The week's outflow was the second largest on record- trailing only a week during August of 2011. Outflows from retail mutual funds totaled ~$4.8 billion in December and have persisted for 23 consecutive weeks.[3]
- CLO issuance accelerated in the first half of December but slowed in the second half largely due to normal seasonality. Total CLO issuance during the month was $7.8 billion bringing the year to date total to $110.8 billion.[3]
- The "risk-off" tone continued in the new issuance market as investor's lack of appetite to add incremental risk, combined with the seasonal slowdown led to relatively light new issue volumes. New loan issue volumes totaled $9.4 billion during the month, below 2015's monthly average of $27.2 billion.[3] Higher quality BB-rated new issue deals continued to be well received by the market. Notable deals this month included a $1.7 billion loan backing Microsemi's acquisition of PMC Sierra. The deal priced at L+450 with a 0.75% floor and $97 issue price. This is over 200 bps wide of the historical average BB new issue spread. The BB-rated deal was upsized by $275 million after gaining traction with more favorable terms.

Relative value

Despite the asset class' underperformance versus our expectations in 2015, the volatility-adjusted performance was compelling in our view as loans were relatively insulated from the broader macroeconomic headlines that profoundly impacted other "risk" asset classes. We believe that the underpinnings of the loan market remain supportive and loans continue to be well positioned heading into 2016—providing a high coupon with short duration in a benign default rate environment, while currently trading at a discount. With the US Fed finally ending its zero interest rate policy, it is important to note that loans have historically performed well during rising interest rate environments.

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



Source: Bloomberg L.P., Barclays, BAML, S&P LCD as of Dec. 31, 2015. Investment grade corporate bonds represented by a subset of Barclays U.S. Aggregate Index; the senior secured loan asset class is represented by S&P/LSTA Leveraged Loan Index; and high yield corporate bonds represented by BAML High Yield Master 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 (%)	Spread to worst	At forward Libor	Duration (years)
5-Year Treasury	99-30	1.76%			4.77
10-Year Treasury	99-26	2.27%			8.84
Barclays US Agg Index	103.10	2.59%	T + 0.78		5.68
Barclays IG Index	102.74	3.54%	T + 1.62		6.90
ML US HY Index	88.82	8.77%	T + 6.98		4.23
S&P/LSTA Leveraged Loan Index	**91.72**	**L + 7.14**	**T + 6.00**	**7.30%**	**45-60 Days**

Source: Bloomberg L.P., Barclays, BAML and S&P LCD as of Dec. 31, 2015. Loan yields incorporate LIBOR forward curve as of Dec. 31, 2015. Loan "spread to worst" and "At Forward LIBOR" incorporate LIBOR forward curve as of Dec. 31, 2015.

1 S&P LCD (Leveraged Commentary and Data) as of Dec. 31, 2015; Returns stated are for the S&P LSTA Leveraged Loan Index
2 Credit Suisse, BAML as of Dec. 31, 2015; Loans as represented by the Credit Suisse Leveraged Loan Index; US HY bonds as represented by the BAML HY Index. Performace stated is Total Return.
3 J.P. Morgan as of Dec. 31, 2015

Important information

All data provided by Invesco unless otherwise noted. All data is US dollar and as of Dec. 31, 2015, unless otherwise noted. Average loan price includes all loans January 1997 through December 2015.

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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