US Loan Market Snapshot

Monthly US loan market update: July 2017

Senior secured loans returned -0.04% in June and 1.91% year-to-date.[1] Loan prices softened in June due to sector specific headwinds, contagion from volatility in high yield, growth in new issue supply, and receding expectations for rising interest rates. Investor concerns in energy and retail led to sector level losses of 3.92% and 1.49%, respectively.[1] Meanwhile, the pace of retail inflows into the loan asset class slowed but remained positive as the rate outlook has become murkier amid weakening inflation data.

Supply outpaced demand during the month as several large deals came to market, tilting the market's technical balance for the first time in several months. The growth in excess supply alleviated the compression on spreads as the pace of refinancing and repricings slowed. $53 billion of repricings and refinancings were completed, versus 2017's monthly average of $73 billion, and some repricing attempts were pulled in the face of lender resistance to coupon reduction. The percentage of loans trading above par is at a 2017 low of 56.2%.[1]

Loans were outperformed by peer asset classes in June as the High Grade Bond Index returned 0.25% and the High Yield Bond Index returned 0.11%.[2] The 10 year Treasury returned -0.74% as yields fluctuated to as low as 2.13% before ending the month at 2.31%, up 10 bps from last month, after policy-makers reiterated their rate outlook. Loans' lower yielding, higher quality "BB" (0.06%) and "B" (0.11%) ratings categories outperformed the "CCC's" (-1.46%).[1] The average price in the loan market was $97.95 at the end of June.[1] At the current average price, senior secured loans are providing a 5.76% yield.[1]

Fundamentals

- June's economic data releases, including falling unemployment and stable PMI's, reflected continued firmness in fundamentals. However, weakening inflation statistics have cast doubt on the pace of further monetary policy tightening.
- There were two new defaults in June, Gymboree and HCR HealthCare, causing the trailing 12 month default rate to rise from 1.42% to 1.54%.[1]

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

Technicals

- Technical conditions shifted in June as elevated net new supply from several large new deals and slowing repayments exceeded comparatively slower demand.
- Gross CLO volume was $34.4 billion in June, the largest monthly total on record, with $15 billion of issuance net of refinancings.[3] Year-to-date CLO issuance is $152.7 billion (gross) and $52.4 billion (net).
- Retail mutual funds and ETF's experienced two weekly outflows in June, and ultimately recorded a small $153 million inflow for the month. Despite slowing notably in the last two months, year-to-date inflows are $17.2 billion.[3] Meanwhile, demand from institutional investors has remained strong.
- New issuance volume was $87 billion in June, and $34.3 billion excluding refinancing and re-pricing activity. Year-to-date, gross and net issuance have totaled $577 billion and $140.2 billion, respectively.

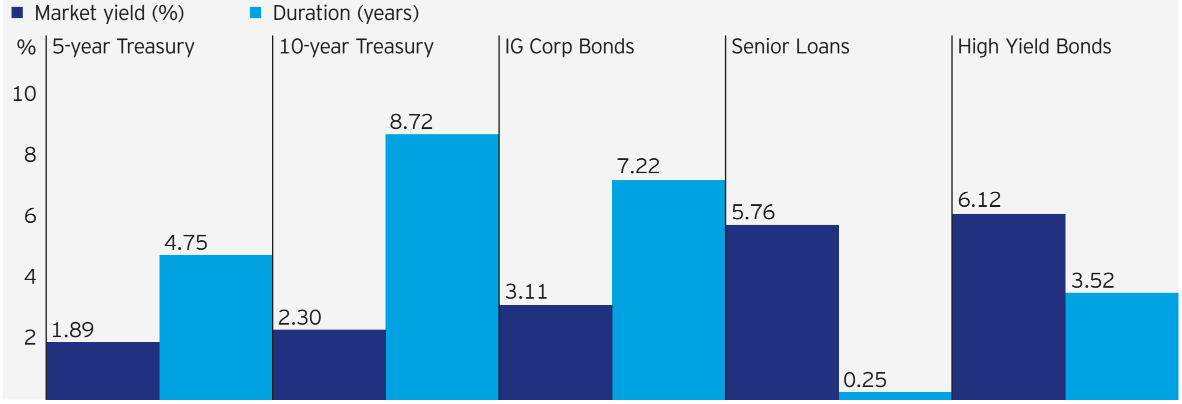
Relative value/market opportunity

Year-to-date, loans (1.91%) have lagged high yield (4.91%) amid a broadly positive environment for risk assets. Despite increased volatility in oil prices and rates in June, high yield outperformed slightly as investors viewed the recent decline in the long end of the yield curve as positive for high yield. However, the potential remains for rates to resume climbing given stable economic growth, the Federal Reserve's (Fed) continued bias towards rate hikes, and its intention to begin unwinding its balance sheet in the near future. With the yield differential between loans and unsecured bonds near historical lows, investors have an opportunity to own less volatile, more defensively positioned loans at a similar yield to unsecured bonds. With 3-month LIBOR at 1.30%, above loans' LIBOR floor levels, floating rate investments stand to benefit from any further increase in interest rates.

Senior secured loans currently offering similar yields as unsecured bonds

Source: J.P. Morgan, as of June 30, 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 June 30, 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 (%)	Spread to worst	At forward Libor	Duration (years)
5-year Treasury	99-11	1.89			4.75
10-year Treasury	100-20	2.30			8.72
Bloomberg Barclays US Agg Index	103.38	2.55	T + 0.59		6.01
Bloomberg Barclays IG Index	105.54	3.11	T + 1.05		7.22
J.P. Morgan US HY Bond Index	102.31	6.12	T + 4.41		3.52
S&P/LSTA Leveraged Loan Index	**97.95**	**L+4.17**	**T + 4.19**	**5.76%**	**90 days**

Source: Bloomberg L.P., J.P. Morgan and S&P LCD as of June 30, 2017. Loan yields incorporate LIBOR forward curve as of June 30, 2017. Loan "spread to worst" and "At Forward LIBOR" incorporate LIBOR forward curve as of June 30, 2017. Past performance cannot guarantee comparable future results.

1 S&P LCD (Leveraged Commentary and Data) as of June 30, 2017; Total returns and other data stated are for the S&P LSTA Leveraged Loan Index.
2 HY Bonds: BAML HY Master Index, High Grade Bonds: BAML High Grade Corp; data as of June 30, 2017. Returns stated are total returns.
3 J.P. Morgan as of June 30, 2017

Important information

All data provided by Invesco unless otherwise noted. All data is US dollar and as of June 30, 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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