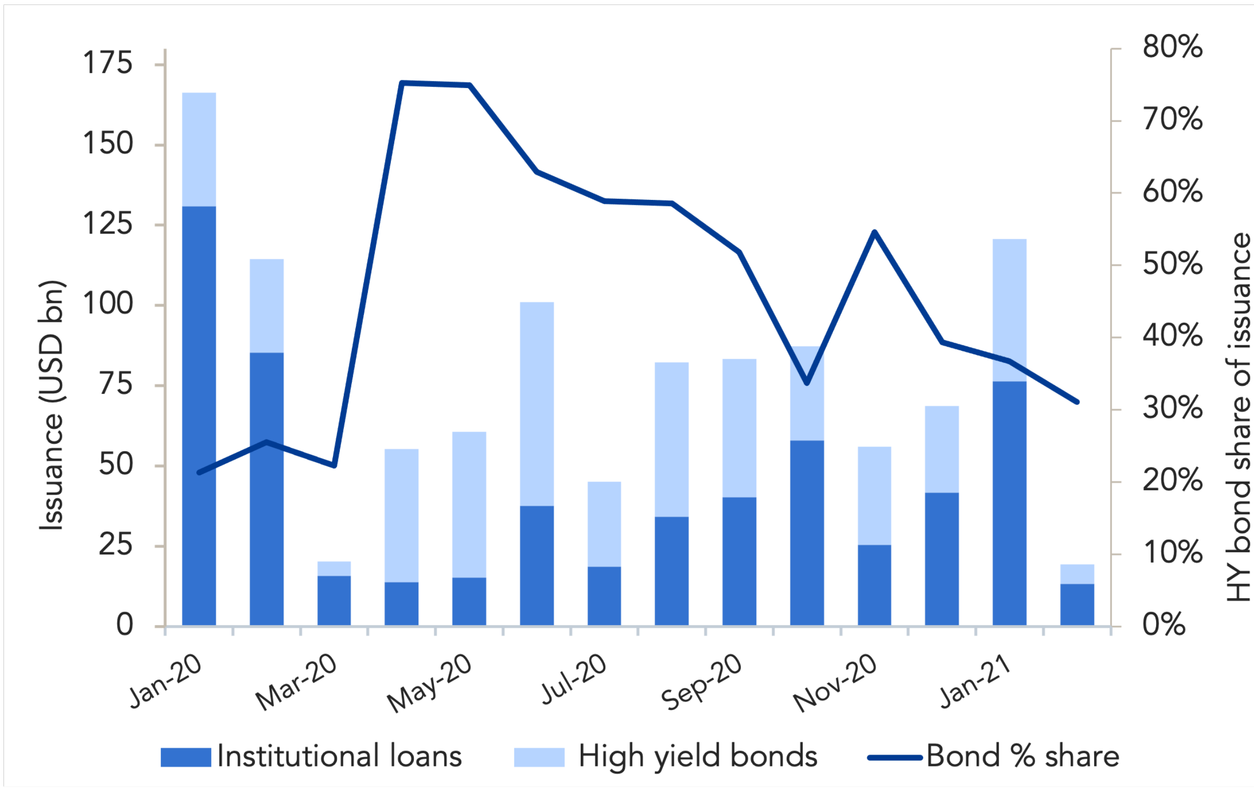
Convergence of market dynamics brings loans back into focus

Debtwire | February 10, 2021



Source: Debtwire Par

The convergence of several market factors has led loans to the forefront of the leveraged debt markets in 2021. Institutional loans made up roughly two thirds of combined loan and bond issuance in January, one of the highest proportions seen since this time last year. The trend has continued through the early days of February, marking a reversal from last year when high yield bonds were dominant. A surge in high yield lending followed the Federal Reserve's announcement of unprecedented support for the broader bond markets and interest rate cuts, which ultimately calmed the debt markets and restored investor confidence during the height of the coronavirus (COVID-19) pandemic.

Hopes around vaccination programs worldwide have led to expectations of greater growth and in turn the possibility of higher inflation this year. Paired with ambitious fiscal stimulus packages proposed by the Biden administration, the stage is set for loans to see increased investor interest.

Evidence for the return to favorability of leveraged loans can be seen in the strong demand from CLOs to begin the year plus inflows into other loan funds, which have outweighed new money loan supply in January and pushed yields lower in both the primary and secondary loan markets. With new-issue CLO volume of USD

8.1bn to start the year, the highest level of January CLO issuance in more than five years, CLO appetite for loans remains strong. On top of this, loan mutual funds & ETFs turned the corner and pulled in over USD 3bn through 24 January, according to Lipper. The last time loan funds saw inflows at this level was back in 2018, before the Federal Reserve’s final interest rate hike.

Secondary market loan prices have appreciated as more investors jumped into the market and pushed valuations higher, with the weighted average bid at 96.84, roughly half a point over the year-ago level. Illustrating the appreciation in loan valuations is that 32% of loans are now in the par-plus area, having reached as high as 44% in January, with another 41% of the market in the 99-100 range. These valuations prompted many borrowers to take a closer look at repricing their loans, driving loan volume in January. This trend has continued into February, albeit at slightly more modest levels compared to the USD 43.6bn of loan repricings completed last month. That said, in addition to the USD 4.3bn loans repriced month-to-date (through 9 February), another USD 7.9bn of repricings are currently working their way through syndication.