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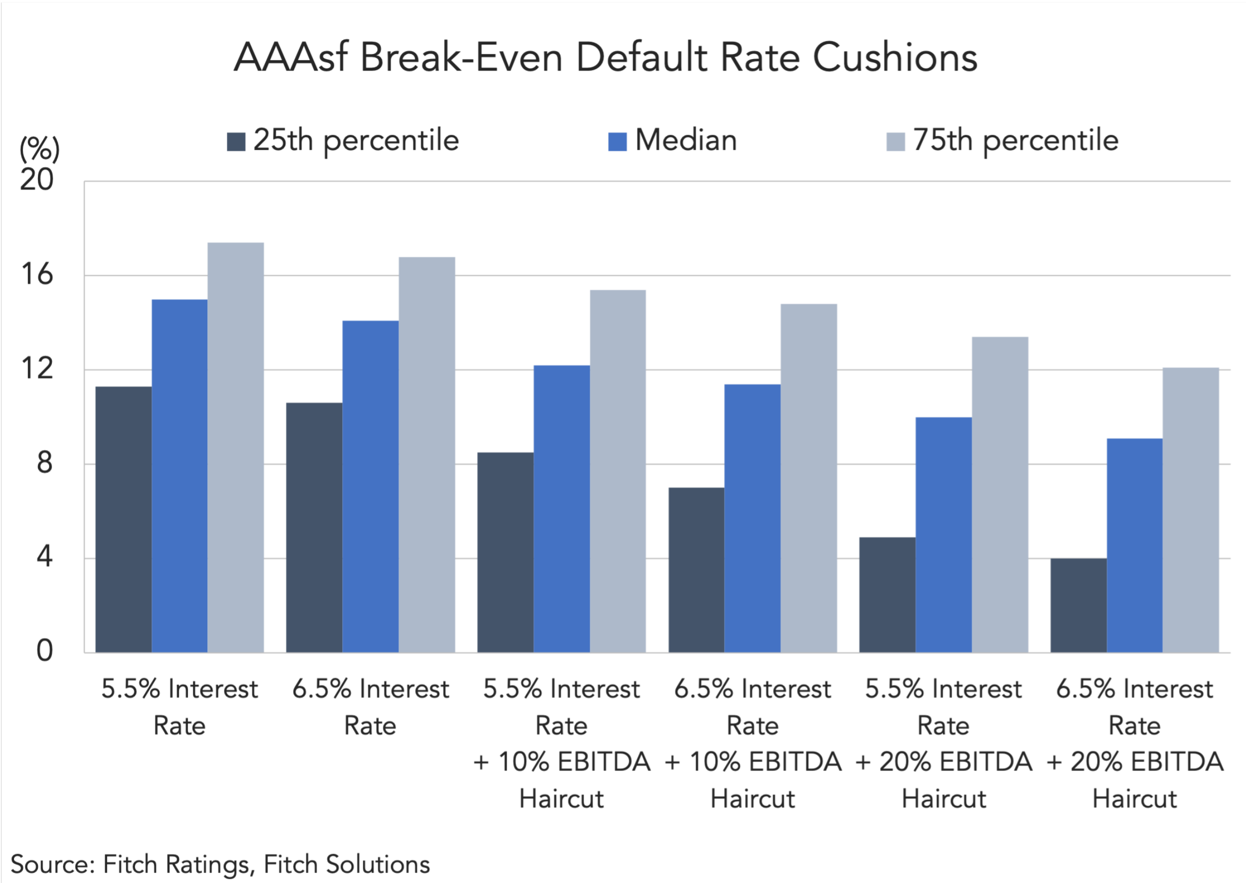
MM CLO Ratings Under High Rates and EBITDA Pressure

Fitch Ratings | August 8, 2023



How Might MM CLO Note Ratings Fare Amid High Rates and EBITDA Pressures?

To assess the effect of higher interest rates, Fitch applied a rate of 5.5%, and 6.5% to represent a longer rate hike cycle. These rate stresses were combined with EBITDA haircuts to represent cost pressures on loan issuers as a result of persistent inflation.

Although we observed pressure on IC cushions and leverage multiples in underlying MM issuers, performance of MM CLO notes remained robust. Only four Fitch-rated tranches out of 90 (4.4%) had a model-implied rating one notch below the current ratings under the more severe combined stresses.

MM CLO note ratings are largely unaffected under these stresses as they benefit from structural protections, primarily credit enhancement and overcollateralization tests, and Fitch’s rating methodology, which incorporates a Fitch Stressed Portfolio in its initial rating analysis.

Most of Fitch's portfolio of MM CLO notes is comprised of high investment-grade ratings. At the 'AAAsf' level, break-even default rate cushions remain positive, even for the 25th percentile.

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