Bank Loans

Bank Loans Are Off to a Solid Start

Positioning for rising defaults as macroeconomic challenges mount.

The leveraged loan market is experiencing a solid start to the year despite the March turmoil driven by regional bank failures. Returns have been strong, helped by good credit performance, a slowdown in new deal activity and secondary market activity. Through April 21, the Credit Suisse Leveraged Loan Index Total Return index is up 4 percent, the strongest return over the same period since 2019. This positive performance was led by B-rated loans (4.7 percent), followed by CCC-rated loans (3.6 percent) and then BB-rated loans (2.9 percent). Three-year discount margins tightened year to date to 595 basis points from 650 basis points.

Loan prices took a hit in March, falling to as low as 92 percent of par before bouncing back to 93, and this price volatility caused borrowers to step back from new issuance to await calmer markets. Less than half as many deals were launched in March as in February, and for just 40 percent of the volume: Just $10 billion in institutional loans were issued in March versus $28 billion the prior month. Virtually all issuance year to date has come from BB and B-rated loans as investor demand shifted toward higher quality, and 63 percent has been for refinancing activity. Issuers have been pushing upcoming maturities further out into the future, with a large portion of BB and B-rated loans coming due in 2028. However, due to the lack of activity in CCC-rated loans, the maturity wall for this cohort is more evenly distributed over the next several years, with 18 percent of CCC loans coming due before 2025, compared to just 1 percent for split BBBs/BBs and 3 percent for split BB/Bs. We have been focused on secondary market opportunities given the slow new issue market.

The 12-month trailing par-weighted default rate is just 1.3 percent as of March 2023, below the historical average of 2.7 percent dating back to 1999, but it is trending upwards. Last year the default rate troughed around 0.2 percent. As CCC-rated loans face upcoming maturities in a more challenging credit environment characterized by slowing corporate earnings growth and tighter lending standards, we continue to expect the default rate to increase. As our strategy in this environment remains more defensive in nature, we have been focused on re-underwriting our existing portfolio companies and evaluating relative value in the wake of current macroeconomic conditions.

By Christopher Keywork and Maria Giraldo

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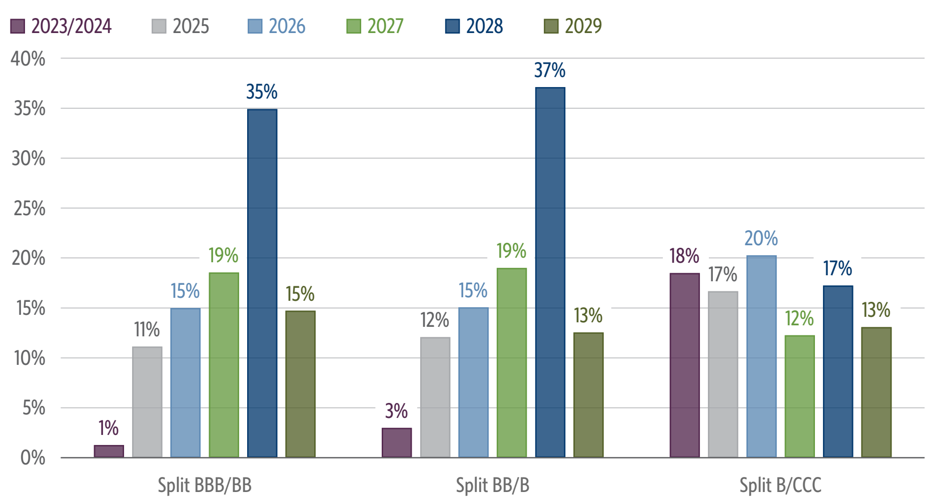
Nearly 20% of CCC Loans in the Index Mature Before 2025

Share of Debt Coming Due by Schedule Maturity Year and Rating



Source: Guggenheim Investments, Credit Suisse. Data as of 4.21.2023.

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