



CREDIT SUISSE



Octagon

**GOLUB CAPITAL**

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# The Institutional Leveraged Loan Market

## Speakers

- Elliot Ganz, LSTA – *Moderator*
- Andrew Marshak, Credit Suisse Asset Management
- Michael Nechamkin, Octagon Credit
- Gregory Robbins, Golub Capital

Tel Aviv, November 16, 2022

# Presentation Themes

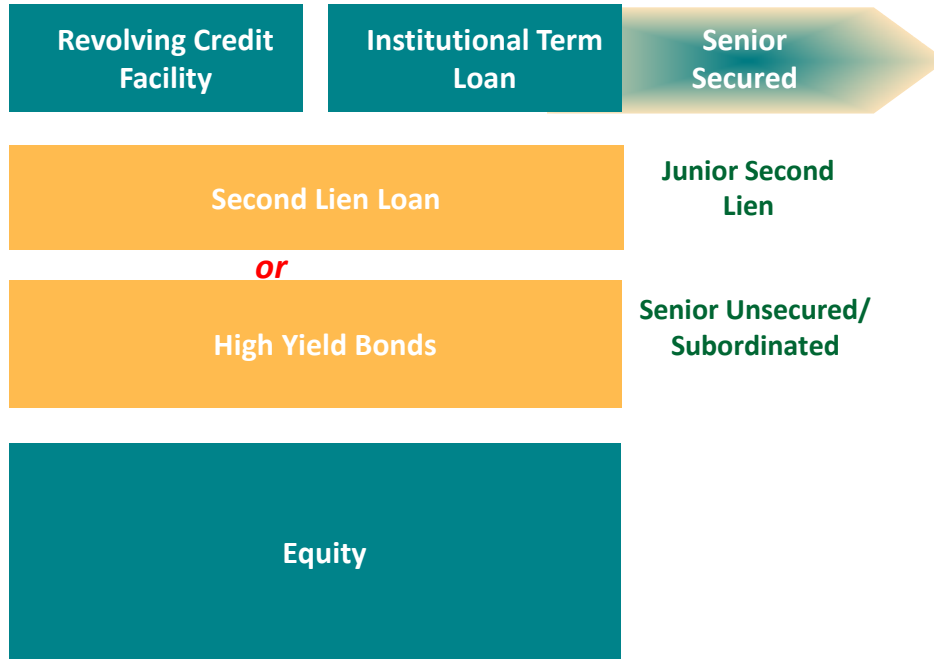
- What are Institutional Leveraged Loans?
  - Broadly Syndicated Loans
  - Private Direct Loans
- What is Happening in the Broadly Syndicated Loan Market?
- What is Happening in the Market for Private Direct Debt?
- What is the Outlook for the BSL and Private Direct Debt Markets?

# Two Side-by-Side Markets for Institutional Leveraged Loans

- Broadly Syndicated Loans
  - Originated and distributed by banks
  - Purchased by a large number of institutional investors
    - But mostly Collateralized Loan Obligations (“CLOs”)
- Private Direct Loans
  - Originated and held by a small group of non-bank relationship lenders
  - Often in the form of a “Unitranche”

# What are Syndicated Institutional Leveraged Loans?

## Corporate Capital Structure



### Senior Secured Loans

#### Senior

- Senior-most debt obligations in capital structure of non-investment grade companies
- Repaid before other debt obligations and equity holders

#### Secured

- Secured by collateral, generally a company's assets or stock
- Higher Recovery Value

#### Floating Rate

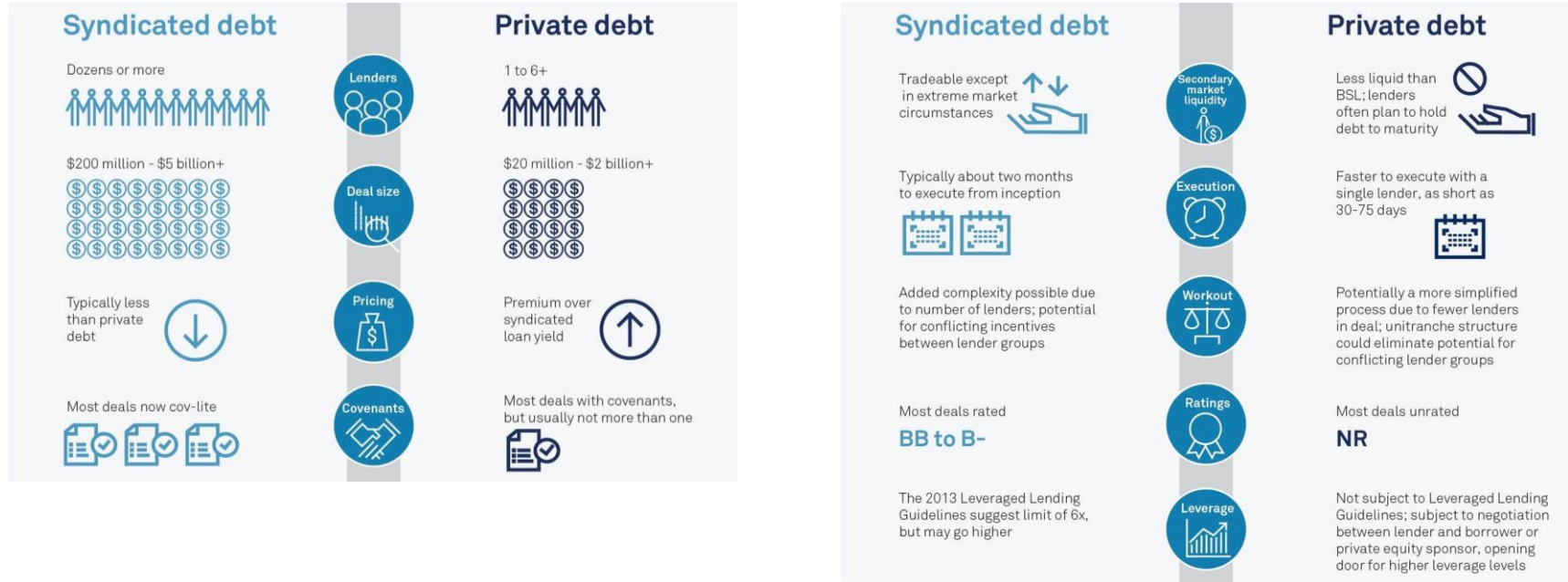
- Pays a base rate (moving from LIBOR to SOFR) plus an additional spread
- Coupons adjust in conjunction with changes in short-term interest rates
- Attractive yields

#### Covenants/Other

- Always benefit from Incurrence Covenants
- Normally rated by Rating Agency's

# What is Private Credit...

## Key differences between broadly syndicated loans and private debt



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# Level Setting: BSL vs Private Credit

## Broadly Syndicated Loans (BSL)

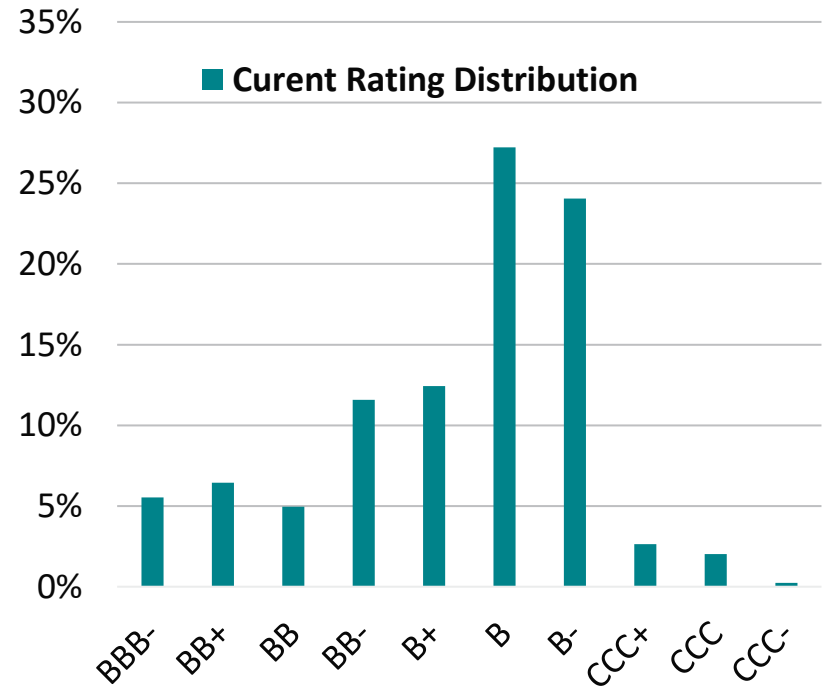
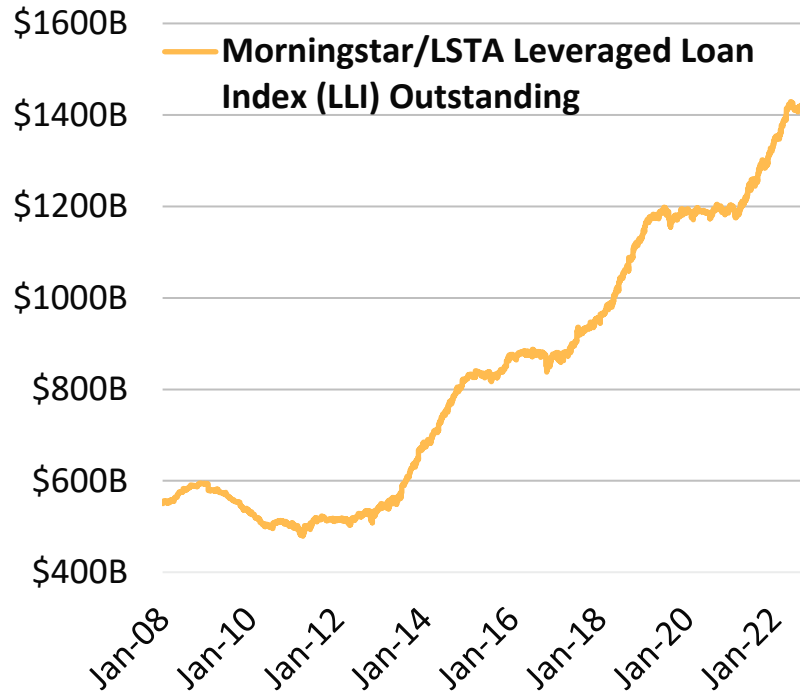
- **Market Size:** About \$1.4 trillion
- **Deal Size:** Large to very large; Jumbo \$5B+
- **Lender Group:** Can run into hundreds of lenders
- **Relationships:** Weaker than Private Credit
- **Structure:** Small RC, large institutional TL(s)
- **Ratings:** Required
- **Execution:** Slower
- **Pricing:** Lower, transparent
- **Flex:** Yes
- **Secondary:** ≈\$800B trading/year
- **Documentation:** Generally Looser
- **Financial Covenants:** Usually Cov-Lite

## Private Credit

- **Market Size:** \$1 trillion? \$2 trillion?
- **Deal Size:** Mostly MM, but many Jumbo Unitranche > \$1B now
- **Lender Group:** Small group of relationship lenders
- **Relationships:** Stronger than BSL
- **Structure:** Often Unitranche, DDTLs
- **Ratings:** Not required
- **Execution:** Faster, more certain
- **Pricing:** Higher, less transparent
- **Flex:** No
- **Secondary:** Generally not
- **Documentation:** Depends on segment.
- **Financial Covenants:** Usually, but may fall away on bigger deals

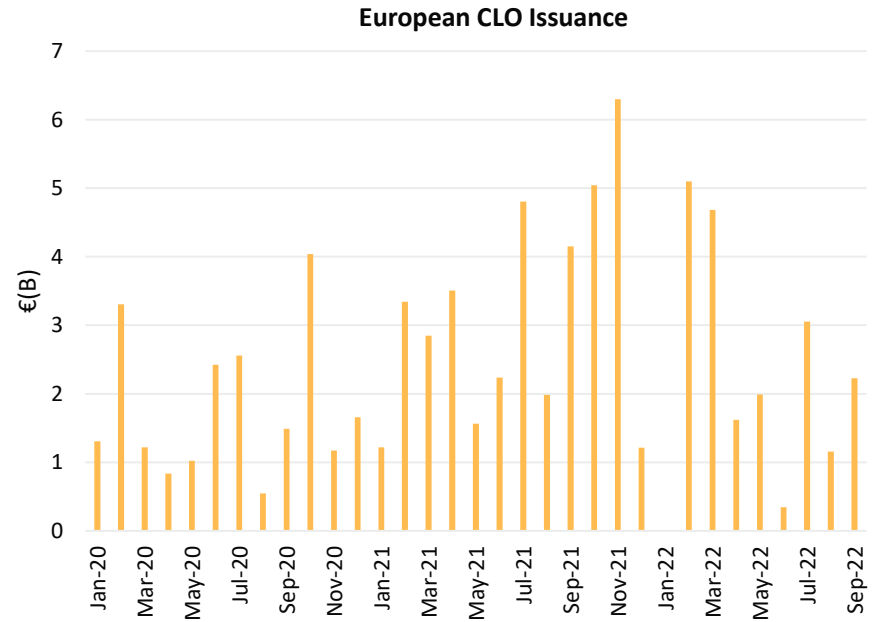
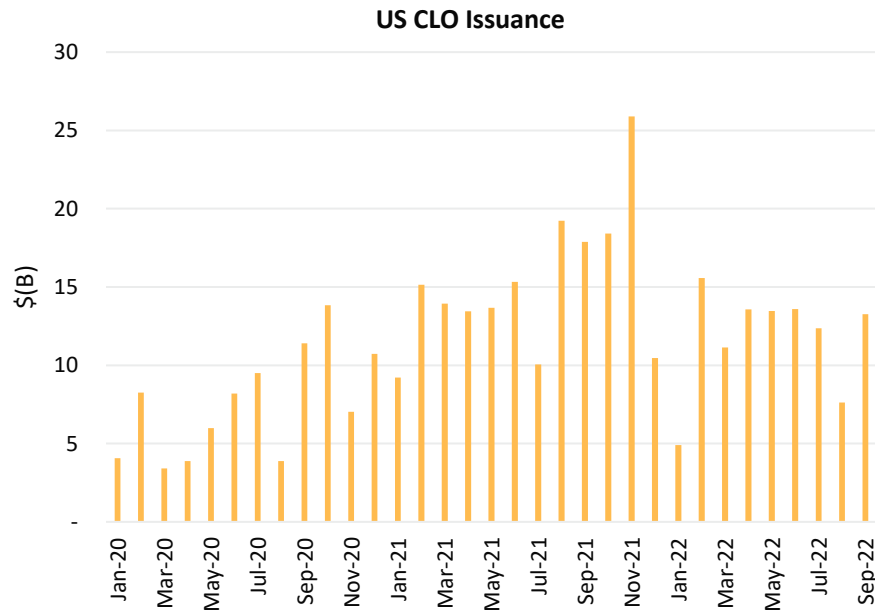
# What is Happening in the Syndicated Loans Market?

# The Size of the Loan Market has Grown 50% to \$1.4T Over the Last Five Years

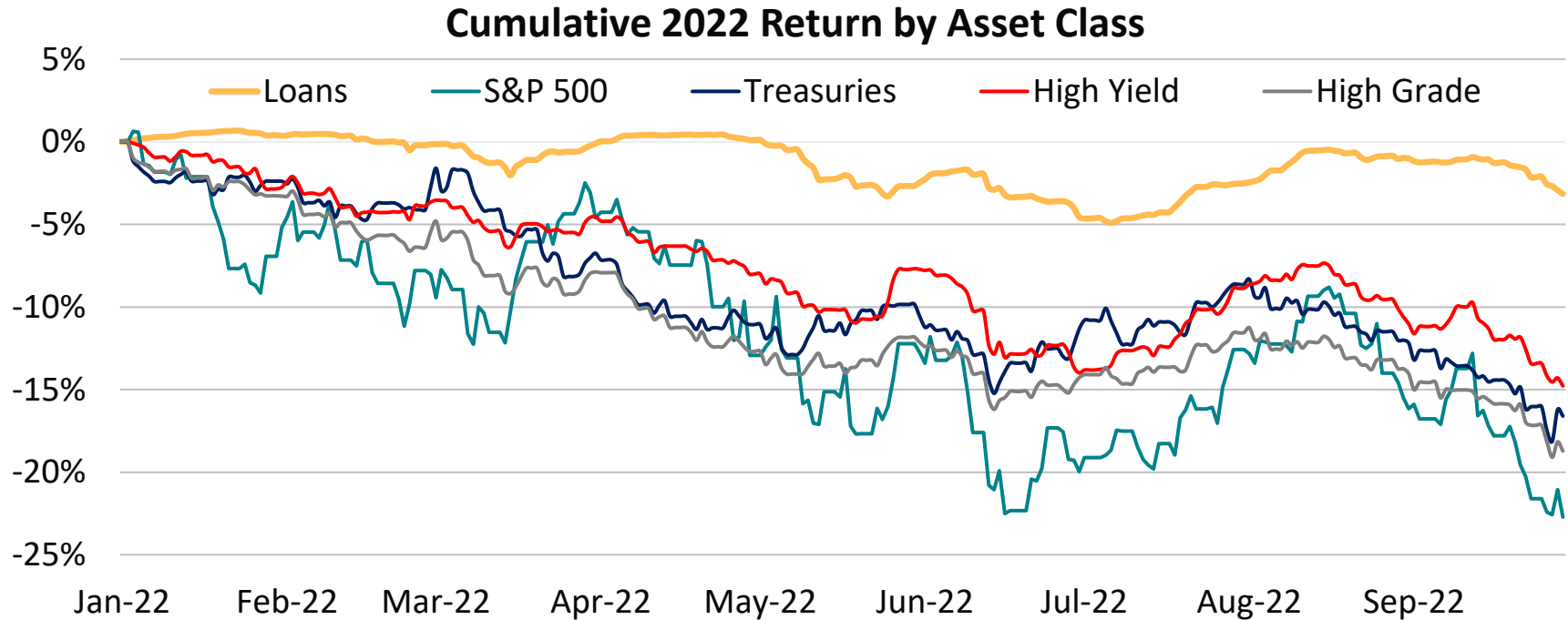




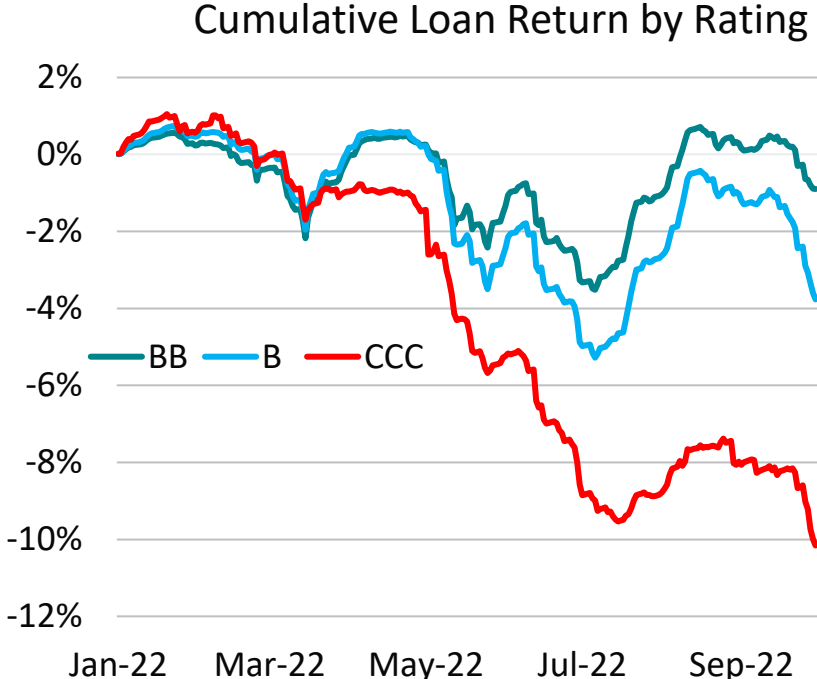
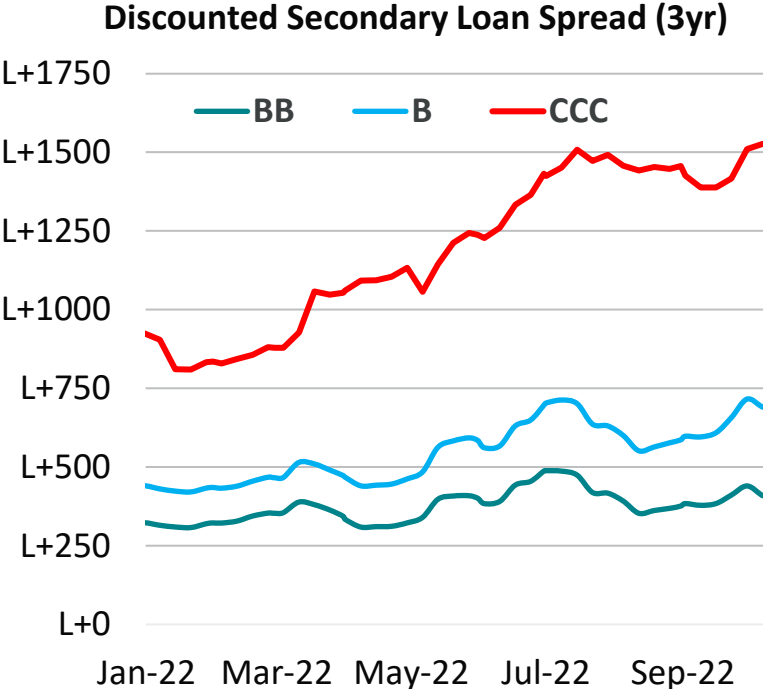
# US and European CLO Issuance



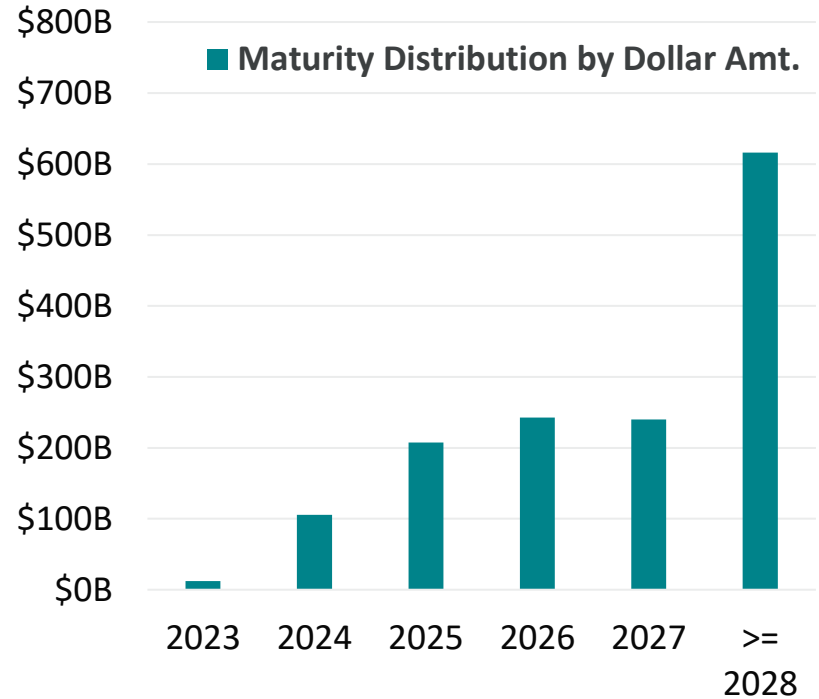
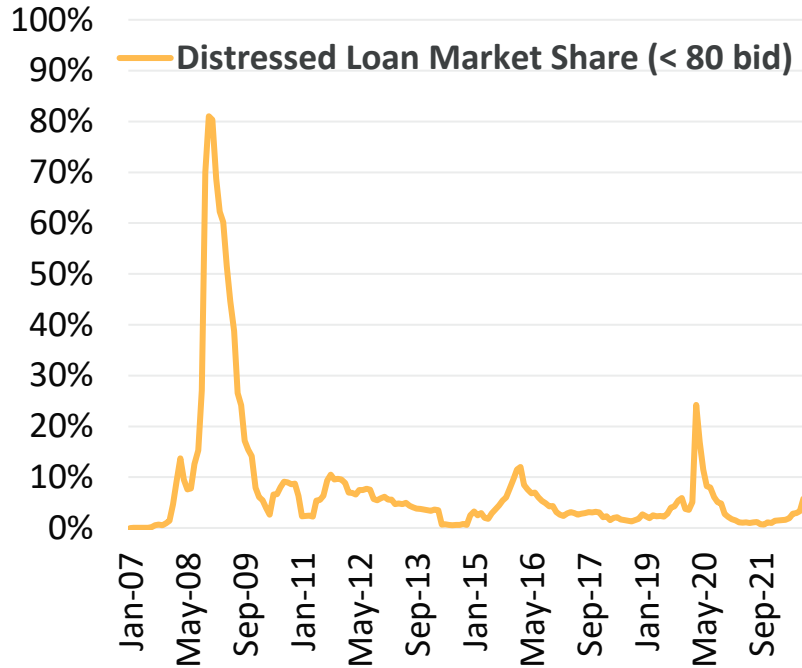
# 2022 Loan Returns Have Largely Been Driven by Contagion, Rather Than a Deterioration in Underlying Credit Quality



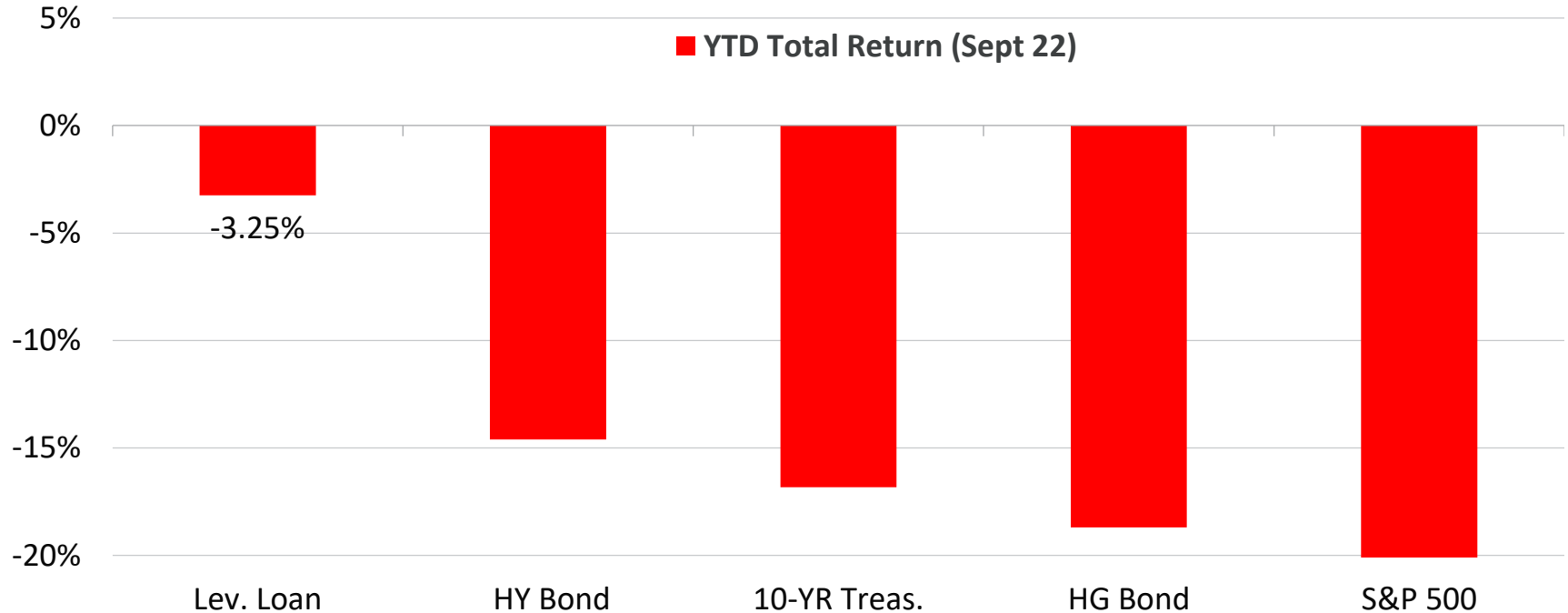
# Credit Spreads are Widening as a Flight to Quality Ensues



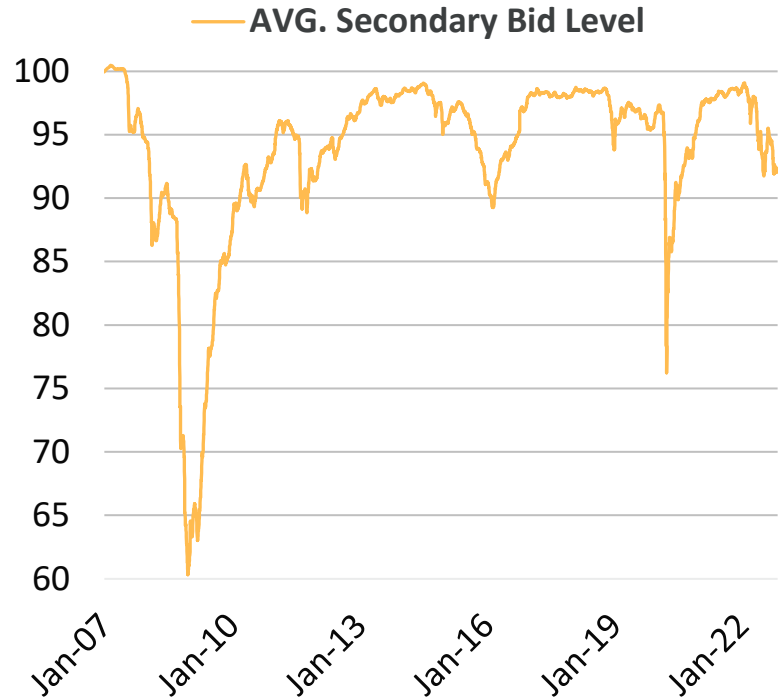
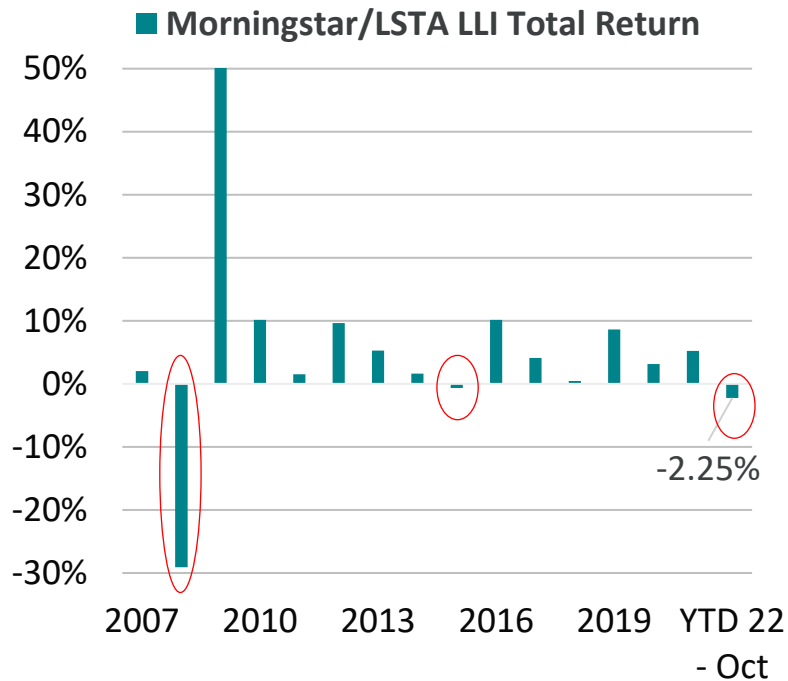
# Distressed Market Share Remains Low While Loan Maturities Have Been Pushed Out Several Years



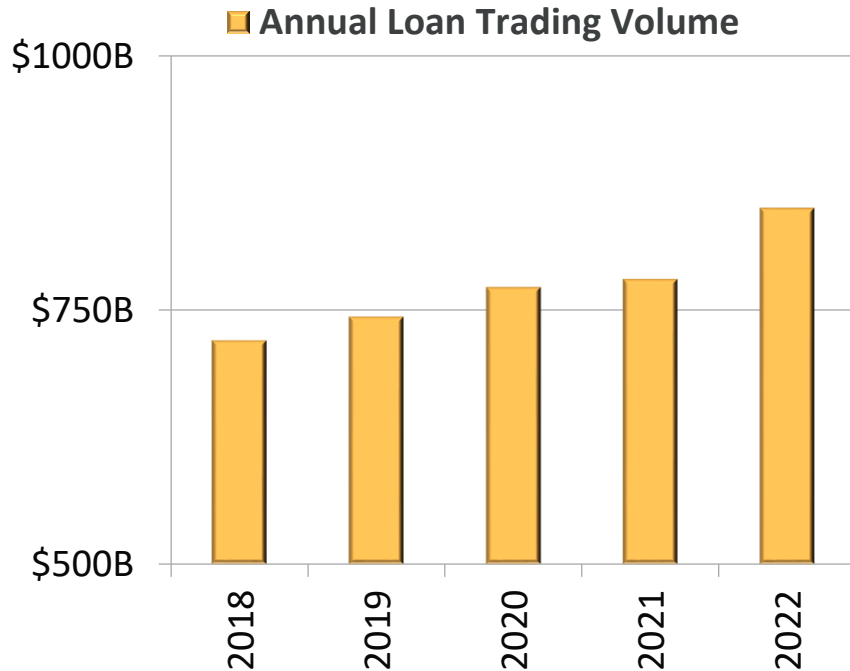
# With Exception of Loans, Losses Have Been Severe Across Asset Classes in 2022



# Over the Past 25 Years, Annual Loan Returns Were Negative Just Twice (2008 & 2015) Prior to 2022



# 2022 Annual Secondary Trading Volume is Projected at \$850B as Liquidity Levels Increased to Record Highs

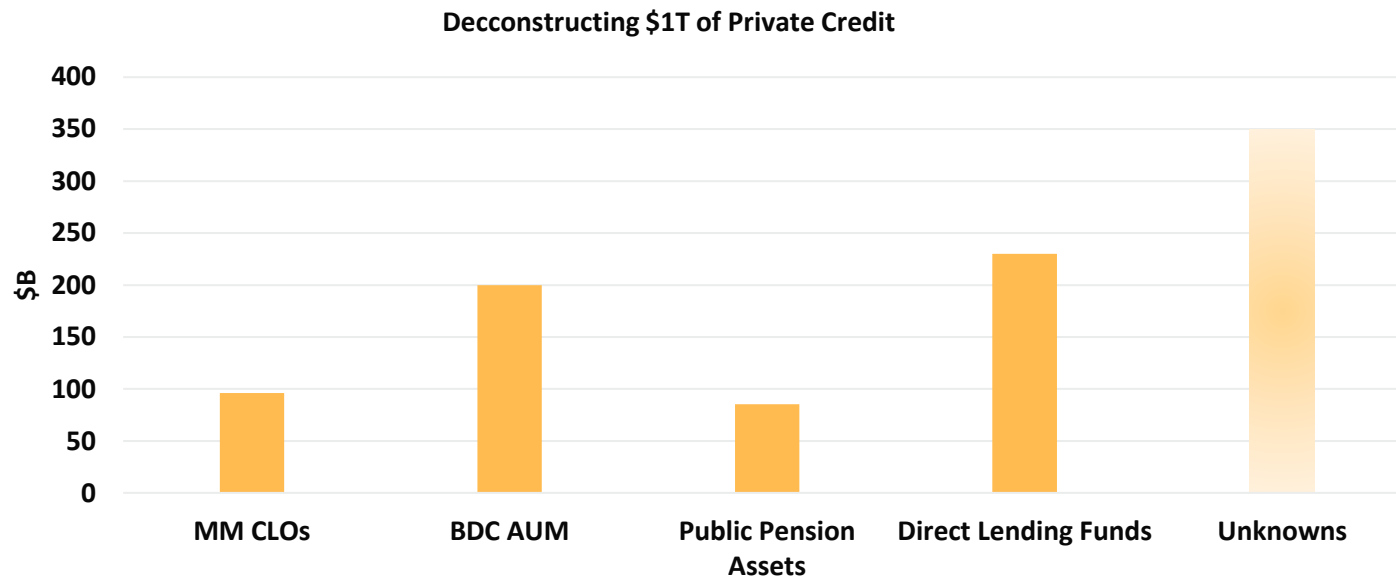


- 655 individual loans traded daily in 2022, averaging \$3.5B in activity
- 1,575 individual loans traded monthly in 2022, averaging \$71B in activity

# What is Happening in the Market for Private Direct Debt?



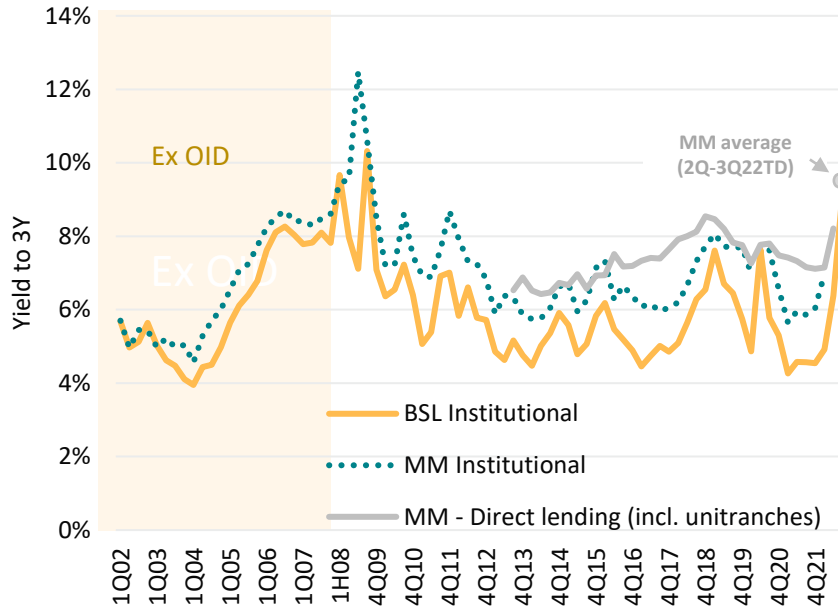
# How Big is Private Credit? Some Say \$1 Trillion-ish...



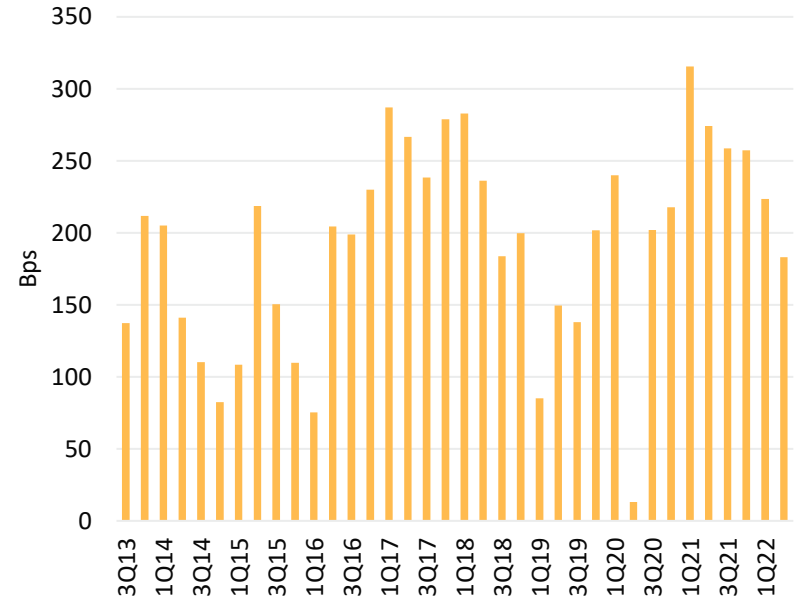
**DLD loosely estimates \$1 trillion.** Unlike liquid credit or high yield, tracking capital is harder in direct lending because of its private nature. Distribution and ratings are absent. Portions of allocations are squirreled away in separately managed accounts and other opaque funds and their feeder funds. Certain segments can be tracked, such as MM CLOs, BDCs, Public Pension Assets and Direct Lending Funds. Unknowns include private pension funds & endowments, insurance companies, family offices, HNW individuals, SMAs and SWFs.

# Historical Yield Premia on (MM) Direct Lending

## BSL Institutional vs Direct Lending Primary Yields

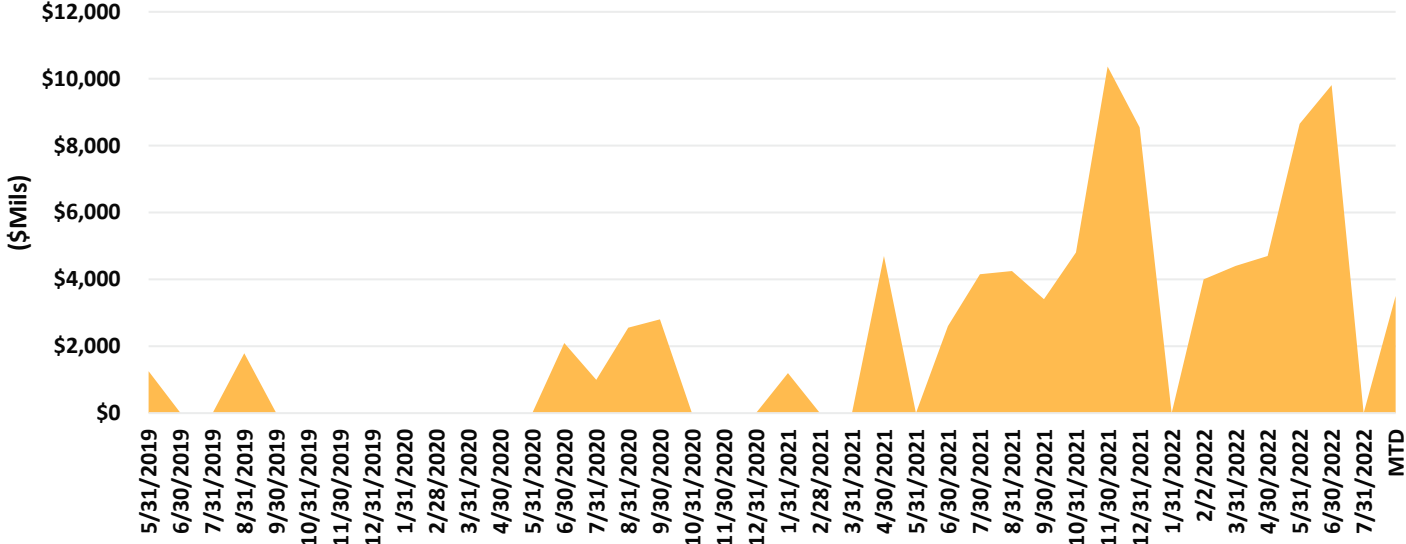


## Unitranche Yield Premium (bps) Over BSL Institutional



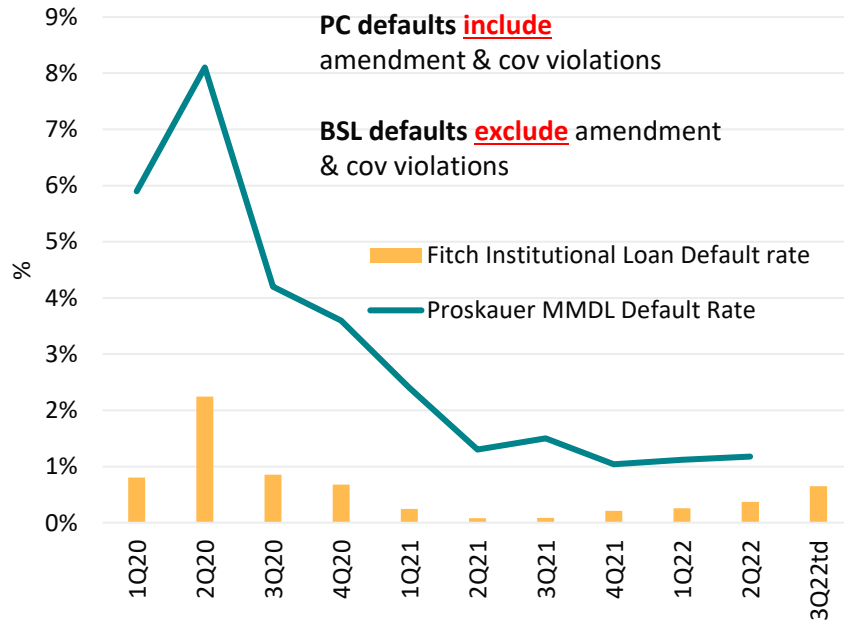
# Jumbo Unitranches (>=\$1B) Replace BSL in Dislocation

Jumbo Unitranches Soar, Substitute for BSL...  
But Slow in Late Summer

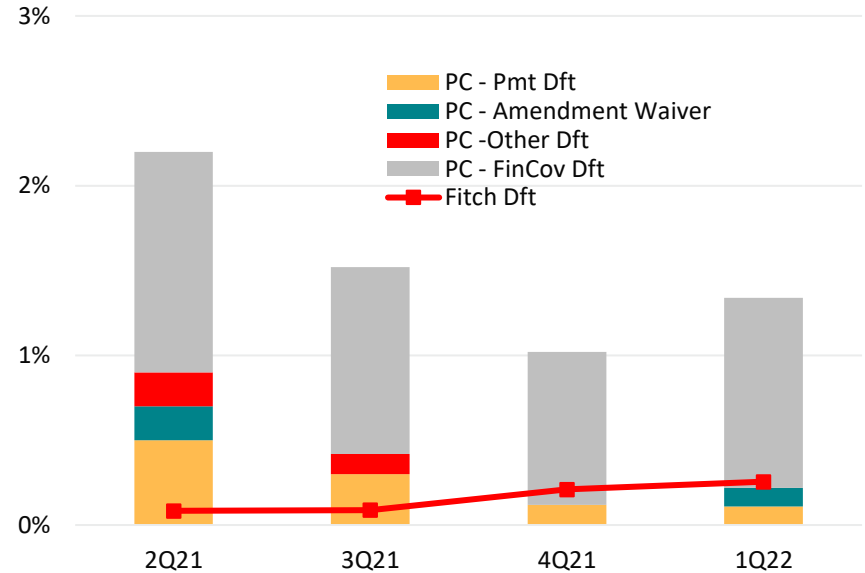


# Default Rates: BSL vs Private Credit

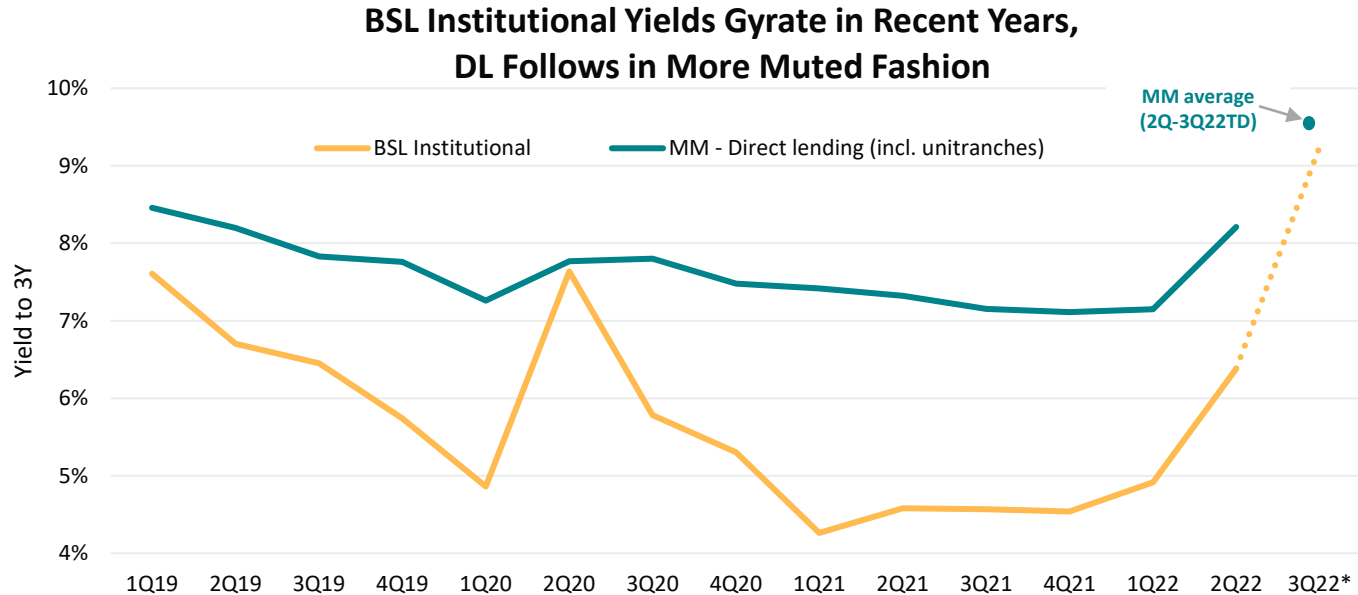
Quarterly Default Rates: Proskauer Private Credit vs Fitch BSL



BSL vs Private Credit Default Rate by Type (2Q21-1Q22)



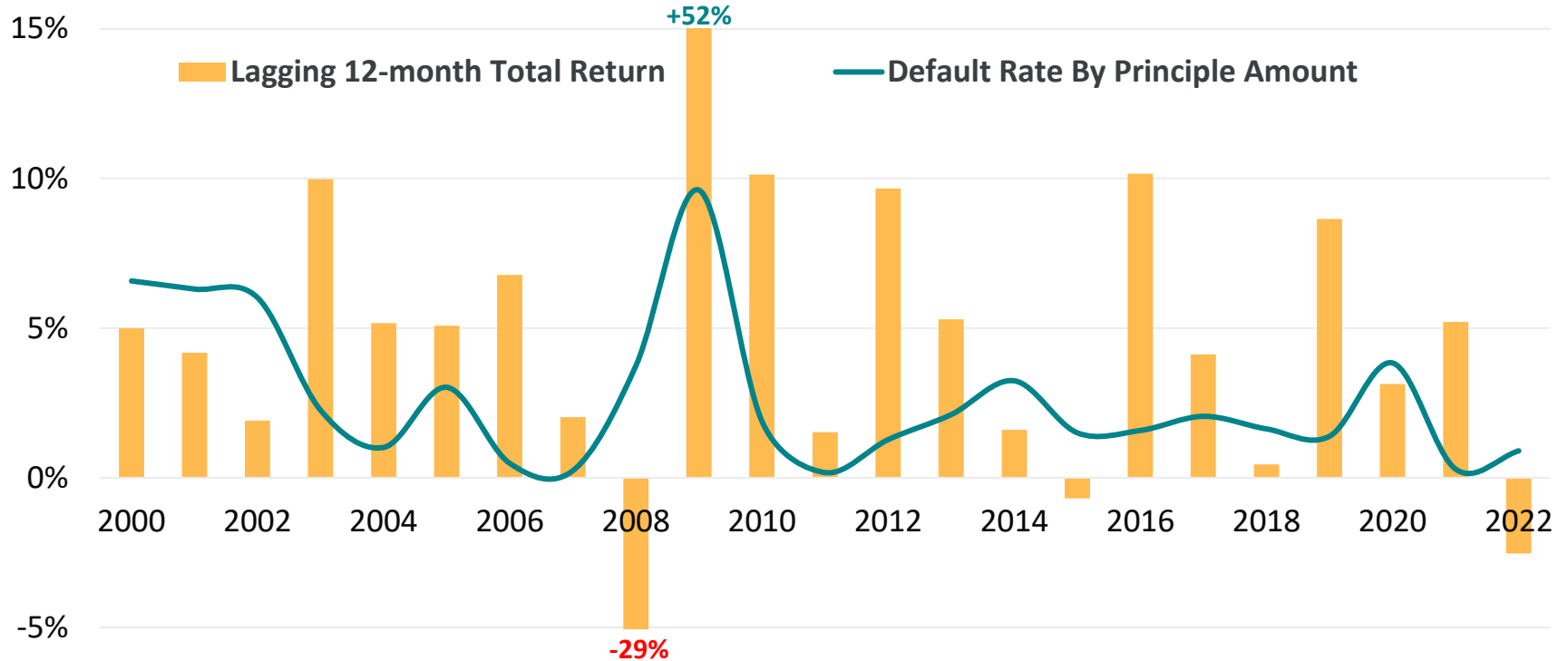
# BSL Primary Pricing More Volatile, Direct Lending More Stable (but Follows Suit)



# Outlook for BSL, Private Credit

- Performance of BSL vs Private Credit in a (coming?) recession
- How will the Private Credit market evolve? Will it become more “BSL-like”?
- Will investor appetite largely shift from BSL to PC? Or back?
- Will the markets be competitive? Symbiotic? Other?

# Expectations for 2023...

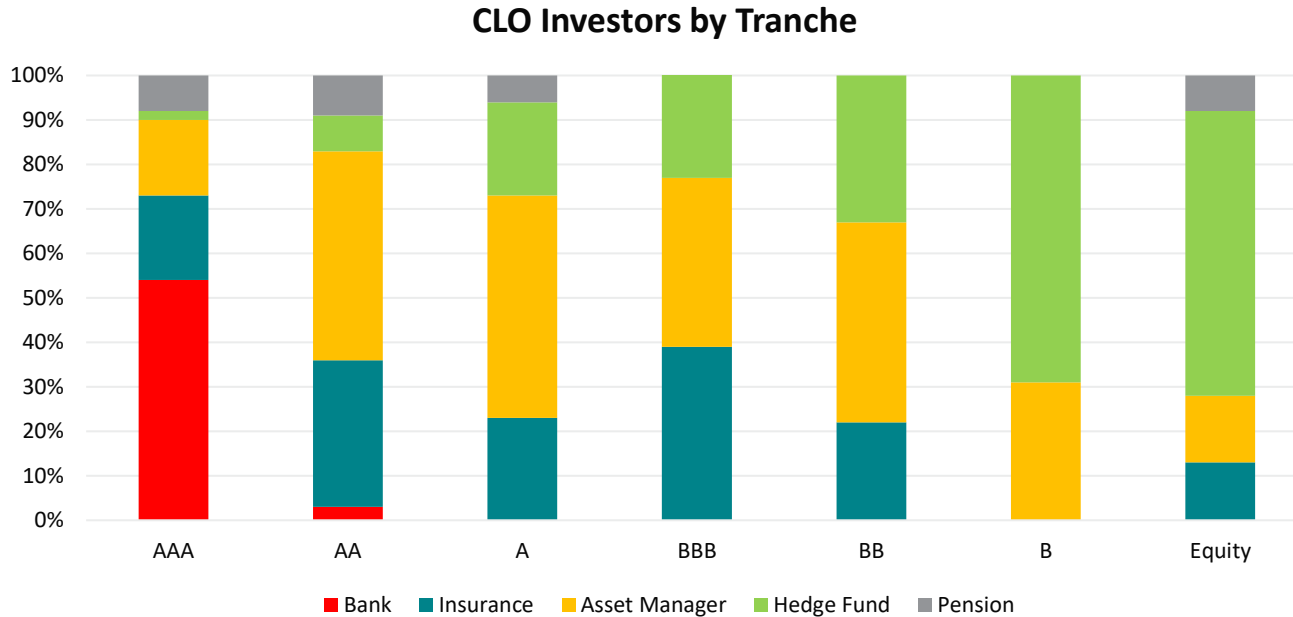


# ■ Questions



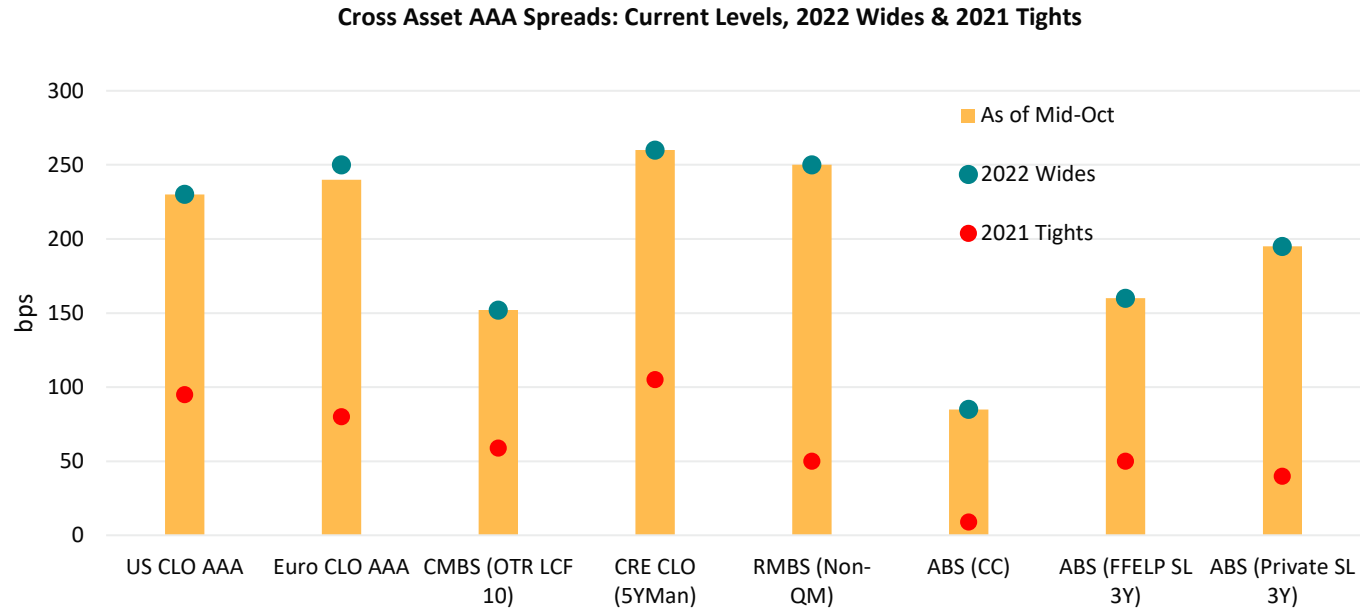
# Addendum: The CLO Story

# CLO Investors by Tranche

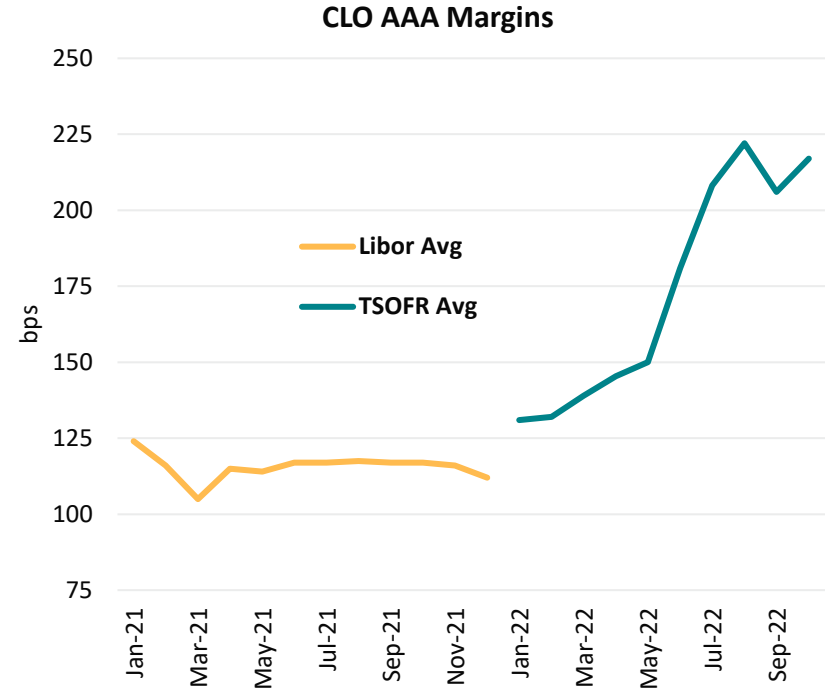
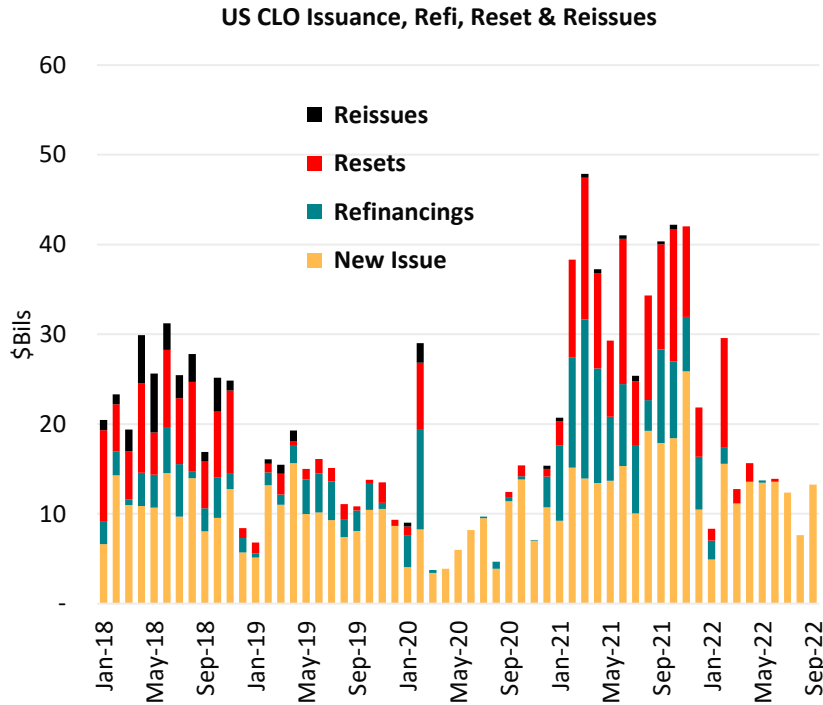


*Represents Barclays deals; may not be representative of overall CLO market*

# Cross Asset AAA Spreads

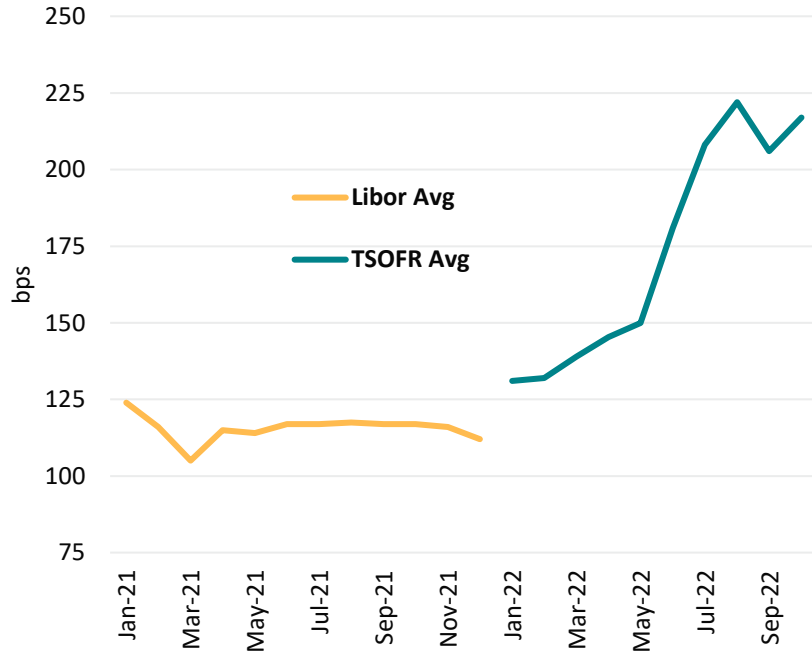


# Outlook: Where Will CLO Market Go?

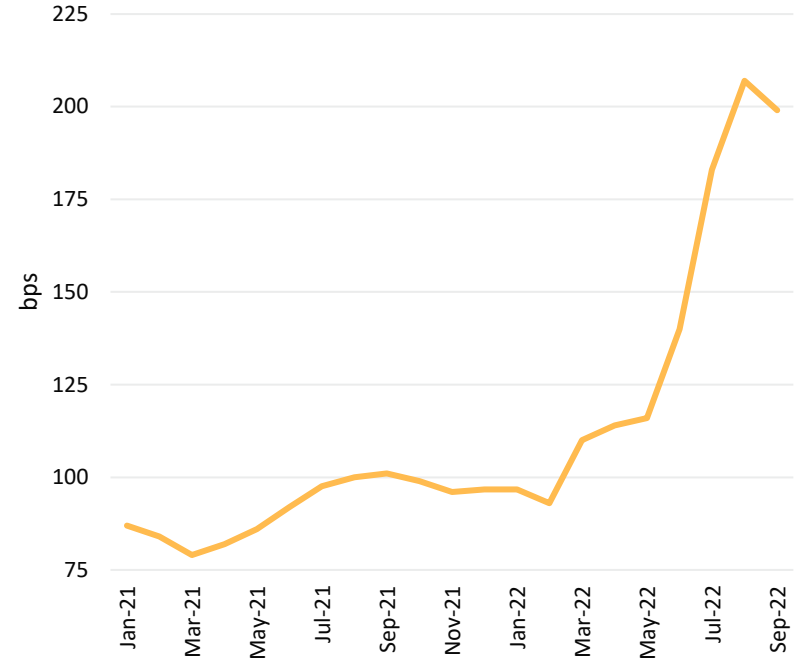


# US and European CLO AAA Margins

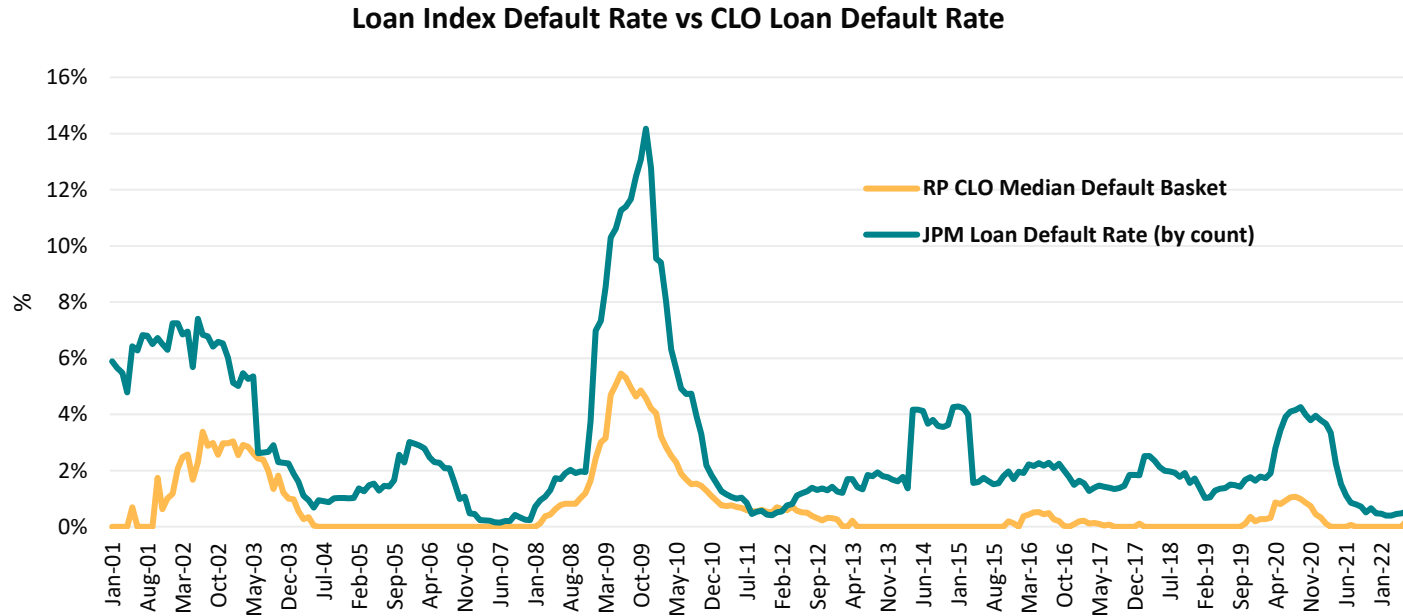
## US CLO AAA Discount Margins



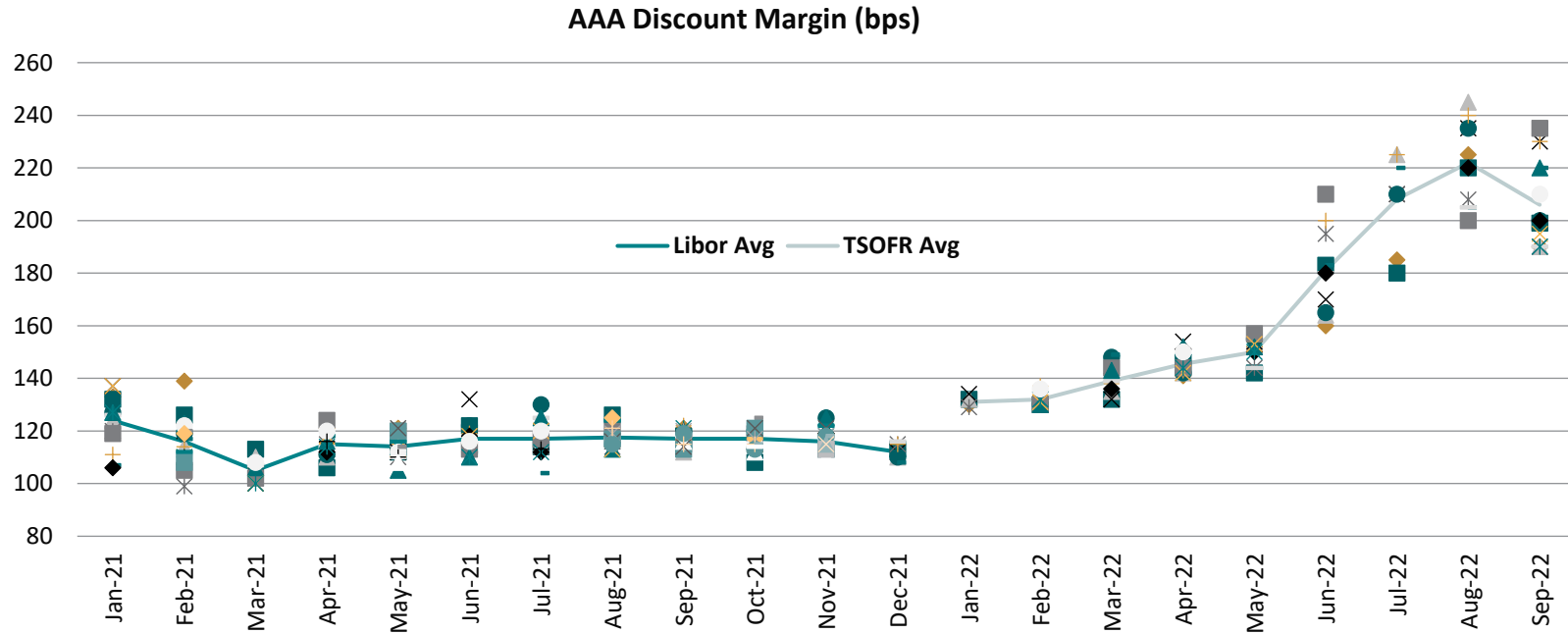
## European CLO AAA Discount Margins



# Loan Default Rate in CLOs Lower than Broader Index

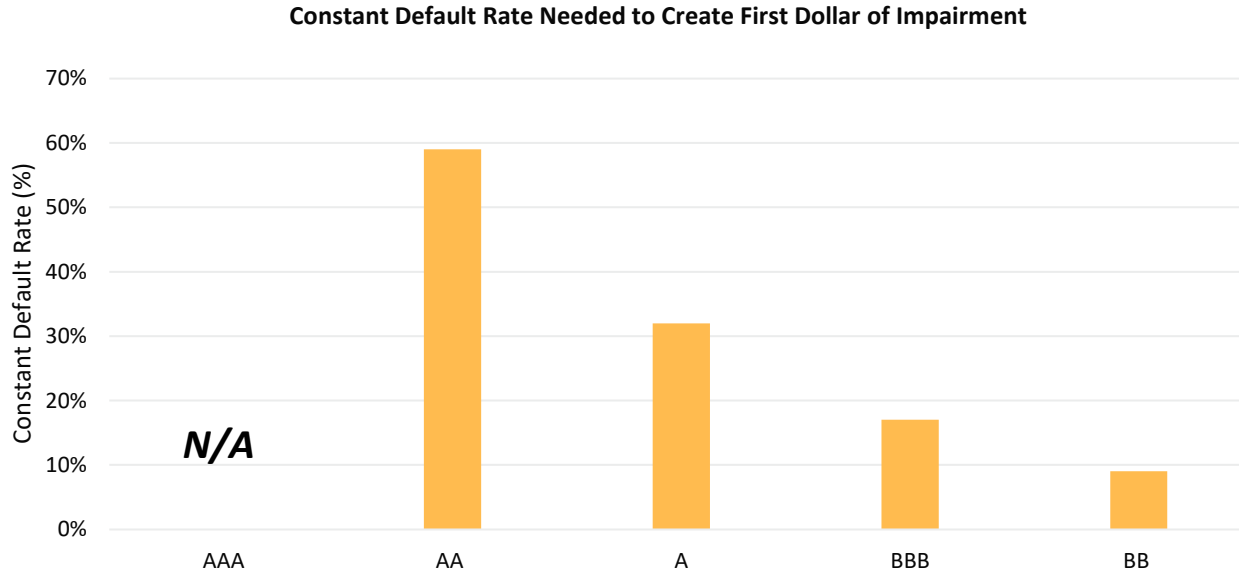


# New Issue US CLO AAA Spreads, 2021 & 2022



\*Based on deals where discount margin is available.

# Constant Default Rate Required to Create First Dollar of Impairment on CLO Tranches



- Assumptions: Sample uses eight representative deals, with a median 20 months of RP, constant repayment rate of 20%, RGD of 70%
- There is no default level at which the AAAs are impaired under the assumptions above



## ■ 2022: BSL vs Private Credit