Private Credit

Government buys AAA CLO new issues, pipeline grows

David Graubard • April 13, 2020 1 minute read

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Last Thursday's action by the Federal Reserve included the reigniting of a collateralized loan obligation (CLO) buyback program, but with conditions.

De-escalating pressure on the 72 CLO warehouses is a TALF (Term Asset-Backed Securities Loan Facility) revision that makes new issue AAA static CLO tranches eligible for purchase at 150 basis points over the 30-day average Secured Overnight Financing Rate (SOFR), according to a client alert by Mayer Brown.

TALF will make it easier for warehouse facilities to exit via the term market if they choose, said a source close to the matter.

Overall CLO issuance is returning even with the market being closed, but it is mostly static. GSO/Blackstone priced last week via Citi. Lining-up static CLOs this month is Palmer Square Dislocation Financing via Jefferies and Dryden 48 for PGIM via Barclays.

Ares LV via JPMorgan is marketing a CLO with a reinvestment period, the first non-static transaction since the market closed.

The best option for CLO managers with warehouse facilities is to raise fresh investments from equity investors that could profit handsomely in a V-shaped recovery.

“2007 was the best vintage in the history of the CLO market,” said one CLO attorney. Bigger deep pocket managers are putting equity in themselves. In addition, managers are posting collateral per dealer requests and curing OC tests.

The CLO is designed to withstand stress, but below investment grade there is a clear lack of confidence losses won’t occur in the market. Nonetheless, equity investor sources they anticipate missing possible distributions because of losses, but it is expected to be temporary.

Anchor equity sponsors have managers generally show no signs of pulling out of deals or the market. All three static CLOs in the market retain below investment grade tranches.

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