alegra capital

Pfaeffikon, June 13, 2024

Newsletter June 2024

Dear Investor

Economic data releases and interest rate decisions have dominated the calendar of late. In the US, weak manufacturing data and a softer demand outlook in the labour market has helped to lower bond yields almost 20bps since the end of May as well as reignite talk of a possible rate cut by the Federal Reserve later this year. In Europe, where inflation has accelerated slightly, the European Central Bank followed the Bank of Canada in reducing interest rates by 25bps. It is widely anticipated that the ECB will keep rates on hold for now and monitor the impact of recent wage gains across the Eurozone. Meanwhile, investors are clearly growing more sensitive to the increasing needs of the US to issue more debt with recent Treasury auctions weaker than anticipated. As some economic data is also coming in lower, appetite for more cyclical parts of the market is limited: the Russell 2000 Index of small and mid-cap US equities remains unchanged this year. In the second half, investors will be focusing on key elections in the US, UK and now in France, with immigration and trade policies likely to have the most impact on market sentiment.

CLO investors, managers and arranging banks attended this year's Global ABS Conference in Barcelona confident that new CLO creation will continue to be strong for this year. Appetite for AAA debt is predicted to grow as regular investors increase their exposure and new investors are attracted to the high yields on offer. As a result, AAA margins are expected to soon tighten into the 130bps area on primary deals. Also widely discussed were documentation standards of the underlying borrowers and the resolution of credit issues such as Altice France. Overall, there was optimism that any marginal stress in portfolios can be offset through active management of the CLO vehicles which not only continue to have sufficient subordination to protect the rated debt notes, but also are making outsized distributions to equity holders to compensate them.

As the European Leveraged Loan Index moves above 98 and loans are repaid via refinancing activity, we have seen further deleveraging and full liquidations of CLOs. This has crystalised gains across some of our positions, including a CLO equity holding that was liquidated above our marked price and through debt holdings that have been sold close to par. If CLO liability spreads tighten further, there may be scope to perform reinvestment period resets on CLOs where we own majority equity rather than opt for an eventual liquidation. Several discussions with managers are already underway to explore options, with either outcome (reset or eventual liquidation) expected to result in further gains being realised.

Alegra Capital Ltd.
[Disclaimer]

Alegra
Capital Ltd.

Churerstrasse 22
CH-8808 Pfaeffikon SZ

Tel.: +41 43 305 00 70
Fax: +41 43 305 00 71