



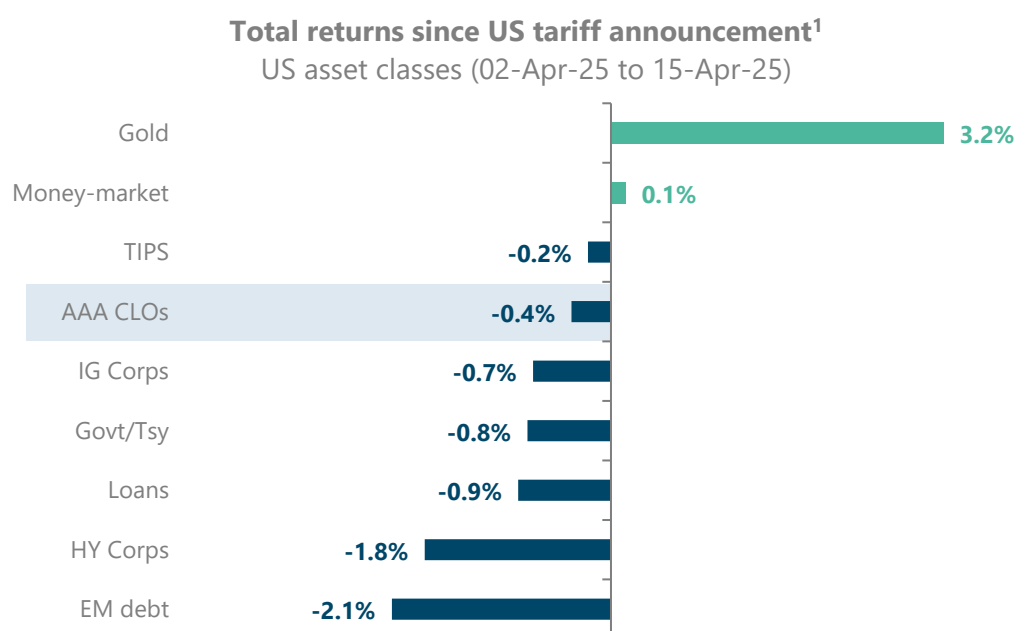
The CLO Investor

Brief insights into trends and news shaping CLO investing

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CLO resilience amidst volatile markets

Against the backdrop of current market confusion, CLOs have not been immune to the market volatility related to US tariffs. The recent global market sell-off has prompted a broad repricing of risk across fixed income markets. It has also allowed the CLO market to demonstrate its true capacity for liquidity. While AAA-rated CLOs have moved in a similar direction to other fixed income assets since the end of March, their move has been significantly less in magnitude and had lower levels of volatility.¹



Sources: JP Morgan and Bloomberg as at 15-Apr-25.

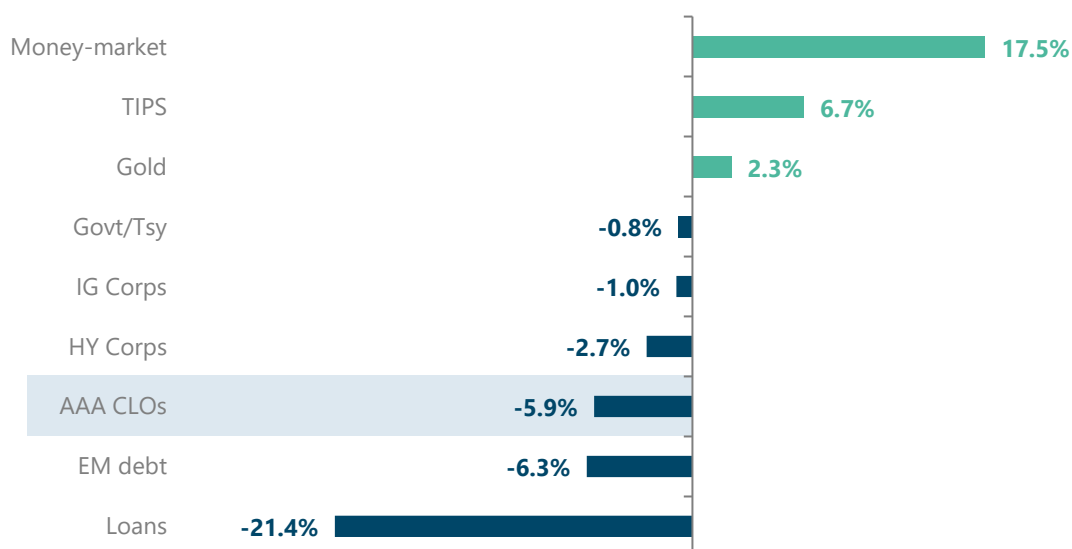
In times of stress, asset managers and investors often look to raise cash to meet upcoming liquidity needs (such as fund flows). If institutional investors have exposure to multiple asset types, they often opt to sell assets they feel confident they can execute quickly and in sufficient size without incurring significant transaction costs. Investors may also look to reduce positions in asset classes they perceive as riskier in favour of 'safe haven assets'. We think a mixture of these motivations have been driving recent fund rotations. There has been selling of some riskier assets, like high yield corporates but also the sale of high-quality liquid assets like AAA-rated CLOs.^{2,3}

News headlines have noted US AAA CLO ETF flows reach nearly \$600 million on Monday 7th April but did not consider the depth of liquidity the CLO market demonstrated in the process. They also remarked on some discounts to ETF NAV which emerged.⁴



ETF flows since US tariff announcement⁵

US assets (02-Apr-25 to 15-Apr-25)



Sources: Bloomberg and Fair Oaks Capital as at 15-Apr-25.

Firstly, on traded volumes. Through multiple market cycles, CLO auction volumes (known as “bids-wanted-in-competition” or “BWICs”) have often spiked during times of broader market stress, all while ensuring a market clearing level quickly becomes known and the market remains active. For example, global daily volumes have reached more than \$1.5bn in 2022 and multiple days of elevated volumes have regularly occurred. Secondary trading via BWICs during 2020 and 2022 saw 5-day trailing volumes reach \$2.4bn and \$3.3bn, respectively.⁶ It is important to remember that the deep liquidity of CLO notes is underpinned by a large and broad investor base, from the world’s largest banks and insurance companies to specialist asset managers. Additionally, BWICs only represent one method of CLO liquidity, as CLO notes trade bilaterally with banks over-the-counter too, similar to corporate bonds.

Secondly, on the discounts. ETF market stress is commonly measured by the discount between the market price and net asset value (“NAV”) of an ETF, given the otherwise available arbitrage opportunities. Provided the underlying ETF asset is liquid and the NAV value is current, discounts or premiums to NAV should not be able to occur for extended periods of time. However, it is important to consider that this measure often applied to equity ETFs cannot necessarily be applied with the same meaning to many fixed income ETFs – which includes CLO ETFs. While an intraday NAV can be calculated for an equity ETF, CLOs are only priced overnight so a CLO ETF share price that appears to be at a discount to NAV (of the previous day) may instead reflect market makers’ estimates of the next closing NAV.

While no market (including US treasuries!) is completely resistant to illiquidity during periods of market stress, we believe recent events should provide useful evidence of the CLO market’s ability to trade resiliently in response to changing market conditions and liquidity needs.

Should you have any queries, please do not hesitate to contact us.



Endnotes

1. JP Morgan and Bloomberg as at 15-Apr-25. Proxy returns for each asset class based on JP Morgan indices or US ETF total returns. EMB US Equity (EM debt), JP Morgan Domestic HY Summary Market Index Value (HY Corps), IEF US Equity (Govt/Tsy), JP Morgan Leveraged Loan Index Summary Market Index Value (Loans), JP Morgan JULI 3 - 5 Years Total Return (IG Corps), JP Morgan CLOIE AAA Index (AAA CLOs), VTIP US Equity (TIPS), PMMF US Equity (Money-market), GLD US Equity (Gold).
2. Bank of America, "The Flow Show", 11-Apr-25.
3. Barclays, "ETFs follow, not lead", 11-Apr-25.
4. Bloomberg, "Cracks Are Forming in CLO Market as ETFs on Record Selling Spree", 08-Apr-25.
5. Bloomberg and Fair Oaks Capital as at 15-Apr-25. Multiple US AAA CLO ETFs (AAA CLOs), BKLN US Equity (Loans), HYG US Equity (HY Corps), EMB US Equity (EM debt), AGG US Equity (IG Corps), PMMF US Equity (Money-market), GLD US Equity (Gold), VTIP US Equity (TIPS), IEF US Equity (Govt/Tsy).
6. Citi and Fair Oaks Capital as at 14-Apr-25.

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