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Grinding it Out

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Last week's feature on Hershey PA proved to be one of our more popular commentaries. Several faithful Lead Lefters recounted their favorite childhood reminiscences of the American epicenter of all things chocolate.

According to one senior banker who grew up in Hershey, Milton Hershey established the town's K-12 school in 1909. Today the school's endowment has grown to almost $10 billion. "It must have a heck of an auditorium" was our considered reply.

Figuring out how to deploy unused cash is also much on loan managers' minds as the year winds down. As usual for the season, most transacting consists of wrapping up existing deals, rather than launching new ones. Fresh buyouts will be considered 2018 business.

Unlike year-ends of yore, there's no mad rush to get things done by December 31. Tax considerations can drive deal timetables, but the impact of this nearly-completed tax reform bill is uncertain. Thanks to the haste with which the bill sped through Congress, not all its details are fully understood. Some edits were apparently scribbled in the final document's margins. Comforting.

While there's relief legislators finally showed they can get something passed, market optimism may dim as the bill's long-term effects become clear. Whatever boost economists forecast to economic growth may be dimmed by the drag of future budget deficits.

Other uncertainties are weighing on loan buyers. Will unfavorable supply/demand dynamics for investors, particularly in the broadly syndicated universe, improve in 2018? What will be the impact as the loan and bond classes continue to converge? Finally when will loan managers decide the loan risk premium no longer exists?

All good questions. The middle market has certainly provided a good value alternative all year, though with some structural and spread erosion at its upper end. Yet here too concerns abound that issuer-friendly trends, such as cov-lite dipping below the $50 million ebitda benchmark, will worsen as public markets continue to bubble.

Add one more variable to the equation. Will Janet Yellen use the Fed's December meeting to push for a 50 bps hike rather than 25 bps? Some believe this could be her swan-song warning to markets that this tax measure is inflationary and needs to be addressed now.

Perhaps relative value is all you can ask for today. Our experience through multiple cycles is to stick to the same investment philosophy in a sell-side market you used when buyers had the upper hand. You need to run harder – source more deals – and read documents more carefully, but sound risk management doesn't change much.