THE LEAD
https://theleadpc.com/the-price-of-everything-first-of-a-series/

The Price of Everything (First of a Series)

THE LEAD | December 5, 2018

Being off-kilter made it world-famous, but that condition is slowly being remedied.

Almost since it was built in 1173, the Leaning Tower of Pisa has been sinking and slanting. But recent repair efforts by Italian engineers seem to be paying off. The 190-foot celebrated structure has now eased to the vertical by 1.5 inches.

Not that the "most monitored monument in the world" is in danger of perfect straightening anytime soon. "At the current rate," says Professor Nunziante Squeglia, "[it] would take around 4000 years."

That same sinking feeling seemed to hit capital markets these past two weeks, as volatility in public equities began to impact the perceived value of leveraged loans.

As our *Chart of the Week* highlights, the bid price of liquid names as measured by the S&P/LSTA Leverage Loan Index has slumped by nearly two points since early October. LPC also noted a similar drop. Its SMi index declined to 97.64, the lowest in over two years, and 127 bps below the year's high of 98.91 on October 8.

As is often the case with loan index moves, the situation was driven by secondary trading in specific names. This time they included Western Digital, SeaDrill Partners, and TransDigm. And it seems to be true with borrowers outside just the energy and tech sectors.

Softer secondary bids have also infected primary issuance spreads. A number of transactions being launched needed tweaks – pricing, structure, other terms – to wrap up. In part this may be time of year. Many shops have already made budgets and aren't willing to do much heavy lifting on anything short of compelling.

It's tough to say where loan prices go from here. As readers of this space know, large cap technicals are pretty much a supply/demand affair. When money leaves retail accounts – Lipper recorded $4.4 billion of fund outflows in the last six weeks – yields widen and prices decline. If overall volatility stabilizes, the reverse can happen.

The Fed's recent dovish posture is also a factor. If rate hikes moderate, that could lessen the attractiveness of floating rate instruments for high-yield accounts.

Analysts are already weighing the costs of a sooner-than-expected recession. A Financial Times piece pointed out that large cap liquidity is not always a good thing. "In a downturn," one manager said, "loan liquidity would likely become even more scarce as investors rush to sell their shares at the same time."

That effect was illustrated by November's negative return of 0.90% for Index investors; showing how price moves create headaches for broadly syndicated loaners. That will take a dent out of an asset class whose 2018 performance had topped the S&P 500 and other assorted investment buckets through last month.

Next week we'll look at a loan class whose illiquidity may today be considered more of a virtue.