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ASSET MANAGER'S LENS

Accessing Corporate Credit Through Middle Market CLOs



DAN RYAN
VP, Head of Consultant Relations
Senior Client Portfolio Manager

Asset managers face both challenges and opportunities as they construct diversified credit portfolios in an evolving fixed income landscape. With nearly half of U.S. debt trading outside the Bloomberg Aggregate Bond Index, traditional corporate bonds, although a popular choice, are far from the only tool available to allocate risk and generate income. One increasingly noteworthy option is middle market collateralized loan obligations (MM CLOs), which offer differentiated exposure to corporate credit compared to conventional bond investments.

Middle market companies are typically privately held firms with annual revenues between $10 million and $1 billion.

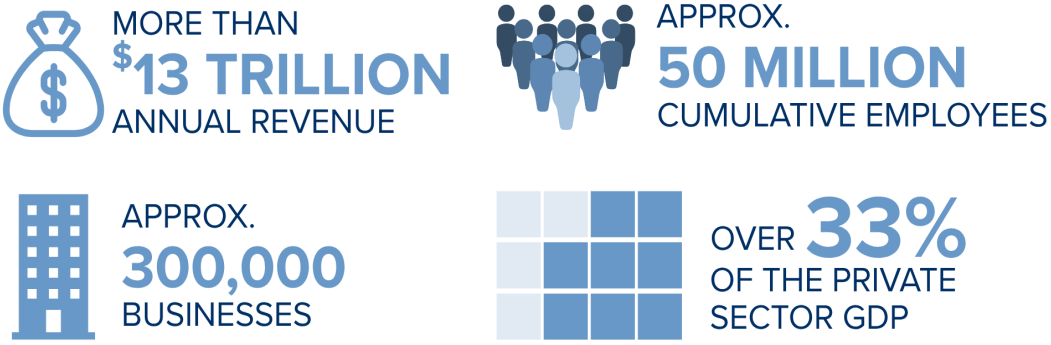
Middle market collateralized loan obligations (MM CLOs) provide investors with a differentiated path to corporate credit exposure. By pooling loans to privately held, mid-sized businesses, these vehicles offer broad diversification and a range of risk-return characteristics. For asset managers seeking to expand beyond traditional bonds, MM CLOs can represent a useful tool for building resilient, income-generating credit portfolios.

A SHIFT IN THE CREDIT ECOSYSTEM

The aftermath of the Global Financial Crisis (GFC) brought a wave of regulatory reforms that curtailed the capacity and willingness of traditional banks to lend, particularly to smaller and mid-sized companies. This retreat opened the door for private markets to step in—and they did so decisively. Among the vehicles that emerged to fill this financing void are CLOs, structured credit instruments that package loans to companies and offer investors access to this diversified pool of credit exposure.

While broadly syndicated CLOs tend to focus on larger, publicly traded companies, MM CLOs lend to smaller, privately held businesses—many of which form the backbone of the U.S. economy. These are companies that may not issue public debt and often require flexible, tailored lending solutions.

Middle Market Company Characteristics



Source: The Middle Matters: Exploring the Diverse Middle Market Business Landscape report by JP Morgan and State Street 2023.

PUBLIC VS. PRIVATE CREDIT ACCESS

At its core, corporate credit lending, whether public or private, offers investors exposure to the financial health and capital needs of businesses. What differs are the mechanisms through which this exposure is obtained.

In traditional public markets, investors purchase bonds issued by a single company, taking direct exposure to its balance sheet, creditworthiness, and capital structure. This method offers transparency and liquidity but also concentrates risk in a single issuer.

In contrast, MM CLOs offer a pooled approach. A sponsor originates and manages loans to a broad set of private companies. The CLO vehicle then slices this pool into tranches, each with different levels of risk and return. Investors

can choose where to participate in the capital stack, aligning their allocations with their specific risk tolerance and return objectives.

WHY MIDDLE MARKET CLOs STAND OUT

There are several key differentiators of Middle Market CLOs compared to traditional corporate bonds and broadly syndicated loan CLOs:

- **Diversification:** Exposure is spread across many private companies.
- **Sponsor Selection:** Investors can partner with CLO sponsors who specialize in sectors or credit profiles they find attractive.
- **Capital Stack Flexibility:** Higher-rated tranches may offer more stability, while lower tranches typically offer greater yield potential, echoing the trade-offs in public credit markets.
- **Risk-Adjusted Value:** On a relative value basis, we believe middle market CLOs can offer more advantageous risk/reward profiles, particularly in a market where many traditional bond sectors are tightly priced.

A COMPLEMENT, NOT A REPLACEMENT

Middle market CLOs are not intended to replace traditional corporate bonds but instead to complement them within a broader portfolio construction framework. By incorporating vehicles like CLOs, asset managers can build fixed income portfolios that are better diversified and potentially introduce additional income opportunities through varying market conditions.

In a world where the opportunity set is no longer confined to public markets, fixed income investors are wise to consider how private credit—especially in the form of middle market CLOs—can play a strategic role in delivering sustainable performance.

IMPORTANT DISCLOSURES

Holdings are subject to change and may not be representative of the Fund's current or future investments.

Consider these risks before investing: All investments involve risks, including possible loss of principal. Market risk includes political, regulatory, economic, social and health risks (including the risks presented by the spread of infectious diseases). Changing interest rates may have sudden and unpredictable effects in the markets and on the Fund's investments. The Fund may purchase lower-rated and unrated fixed-income securities, which involve an increased possibility that the issuers of these may not be able to make payments of interest and principal. See the Fund's prospectus for a further discussion of risks.

Investors should consider carefully the investment objectives, risks, and charges and expenses of the Funds before investing. This and other important information is contained in the prospectus and summary prospectus, which may be obtained at weitzinvestments.com.

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