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Floating-rate loans at midyear: Helping investors as the economy — and perceived inflation risks — grow

By: Andrew N. Sveen, CFA | & Christopher Remington | July 22, 2021

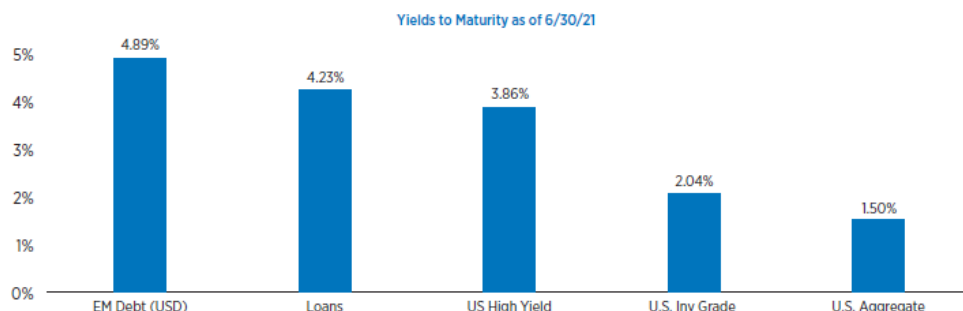
Boston - Wrapping up the series of midyear outlook blogs from Eaton Vance fixed income investment experts, our floating-rate loan team outlines why loans may offer a valuable tool for investors seeking to increase income, while also gaining a potential hedge against possible rising rates as the U.S. economy improves.

The first half of 2021 presented fixed-income investors with an all-too-familiar problem coupled with a rather unfamiliar risk. Investors still struggle with historically low yields, as they have since the 2008 financial crisis. But now they also face the possibility that resurgent inflation could put upward pressure on rates and inflict losses on bonds that surpass any gains from income.

As inflation concerns have grown, the need for fixed-income diversification has become increasingly timely. Because they offer an attractive level of income while minimizing interest-rate risk, floating-rate loans can be a valuable diversification tool in this environment.

With a yield to maturity for the S&P/LSTA Leveraged Loan Index of 4.23% as of June 30, loans are the highest-yielding major U.S. fixed-income sector, notable for clients concerned about income generation as well as total return potential.

Loans are offering the highest yield of major U.S. fixed-income sectors



Sources: Bloomberg Barclays, JPMorgan, ICE BofA and LCD, an offering of S&P Global Market Intelligence, as of 6/30/21. EM Debt (USD) is represented by the JPMorgan Emerging Markets Bond Index (EMBI) Global Diversified Index. Loans are represented by the S&P/LSTA Leveraged Loan Index. U.S. High Yield is represented by the ICE BofA U.S. High-Yield Index. U.S. Inv Grade is represented by the Bloomberg Barclays U.S. Corporate Investment Grade Index. U.S. Aggregate refers to the broad U.S. investment-grade bond universe. Data provided is for informational use only. It is not possible to invest directly in an Index. Past performance is not a reliable indicator of future results. Diversification does not ensure a profit or eliminate the risk of loss. See index definitions below.

In a new midyear update, the Eaton Vance floating-rate loan team outlines "How Loans Can Help Investors as Economy — and Perceived Inflation Risks — Grow" (see link below). We see fundamental and technical factors, taken together, as converging in a favorable environment for the asset class. Key takeaways include:

- Loans have again proven their potential as diversifiers this year, with their minimal duration helping boost relative loan returns 488 basis points (bps) ahead of the broad U.S. fixed-income market, through June 30.
- As credit instruments, loans have also benefited from the improving economy, at the same time that issuer fundamentals like cash flow and interest coverage have surged. Market stress has faded and upgrades are surpassing downgrades.
- The attractive profile of the asset class is feeding a "virtuous circle," as loans are drawing investor demand from both sides of the retail and institutional buyer base; this, in turn, is feeding new deal flow, with ample issuer access to the capital markets.

Bottom line: We believe floating-rate loans offer a valuable tool for fixed-income investors seeking to increase income and gain a potential hedge against possible rising rates as the U.S. economy improves.

J.P. Morgan Emerging Markets Bond Index (EMBI) Global Diversified Index is an unmanaged index of USD-denominated bonds with maturities of more than one year issued by emerging markets governments.

S&P/LSTA Leveraged Loan Index is an unmanaged index of the institutional leveraged loan market.

ICE BofA U.S. High Yield Index is an unmanaged index of below-investment grade U.S. corporate bonds.

Bloomberg Barclays US Aggregate Index is an unmanaged index of domestic investment-grade bonds, including corporate, government and mortgage-backed securities.

Bloomberg Barclays U.S. Corporate Investment Grade Index is an unmanaged index that measures the performance of investment-grade corporate securities within the Bloomberg Barclays US Aggregate Index.

All investing involves risk, including the risk of loss.

Loans are traded in a private, unregulated inter-dealer or inter-bank resale market and are generally subject to contractual restrictions that must be satisfied before a loan can be bought or sold. These restrictions may impede the strategy's ability to buy or sell loans (thus affecting their liquidity) and may negatively impact the transaction price. It may take longer than seven days for transactions in loans to settle. Due to the possibility of an extended loan settlement process, the strategy may hold cash, sell investments or temporarily borrow from banks or other lenders to meet short-term liquidity needs. Loans may be structured such that they are not securities under securities law, and in the event of fraud or misrepresentation by a borrower, lenders may not have the protection of the anti-fraud provisions of the federal securities laws. Loans are also subject to risks associated with other types of income like high-yield bonds described above. Investments in foreign instruments or currencies can involve greater risk and volatility than U.S. investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. Changes in the value of investments entered for hedging purposes may not match those of the position being hedged.

Related Content

[How Loans Can Help Investors as Economy — and Perceived Inflation Risks — Grow](#)



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