

CLO Equity

KEY TAKEAWAY

- > CLO equity has historically provided investors with consistent, low double-digit income from a pool of diversified loans that sit near the top of the capital stack

For investors seeking a recurring source of income, the equity tranche of a collateralized loan obligation (CLO) is a lesser-known opportunity to consider. Simply put, a CLO is a special purpose investment vehicle that issues bonds at different rating levels as well as an unrated equity tranche to raise funds. The CLO then invests those proceeds in a diversified pool of floating rate loans. Bond investors are paid on a quarterly basis according to their seniority in the capital structure, while equity tranche investors receive all of the excess payments each quarter. The equity tranche bears the risk of the first loss but also captures the potential upside. Over the past 10 years, CLO equity investors have received low double-digit cash-on-cash returns over a yearly basis. Invested capital is then returned at the end of the structure's life after payments to the CLO's debt investors.

In addition to income, CLO equity can provide additional benefits to investors. Since CLOs typically begin making quarterly payments within the first six months of closing, investing in the equity tranche can be seen as a complement to private equity commitments where early returns may be delayed due to the J-curve impact. CLOs also provide diversification as the structure contains between 250 and 300 loans representing a wide range of sectors with no single industry in excess of 15% of the portfolio. This underlying collateral typically consists of high yield, senior secured loans which sit near the top of the capital stack, ranking ahead of unsecured bonds and equity.

A key feature of CLOs is that the portfolio can be actively managed during the reinvestment period (which is typically five years) to optimize for various market conditions. For example, in late 2025, the PPM CLO team worked with our Technology sector credit analysts to rank software names on their susceptibility to AI risk. The results led to the portfolio being underweight software ahead of the selloff that began in February 2026. We then opportunistically added names in May that have since experienced price increases.



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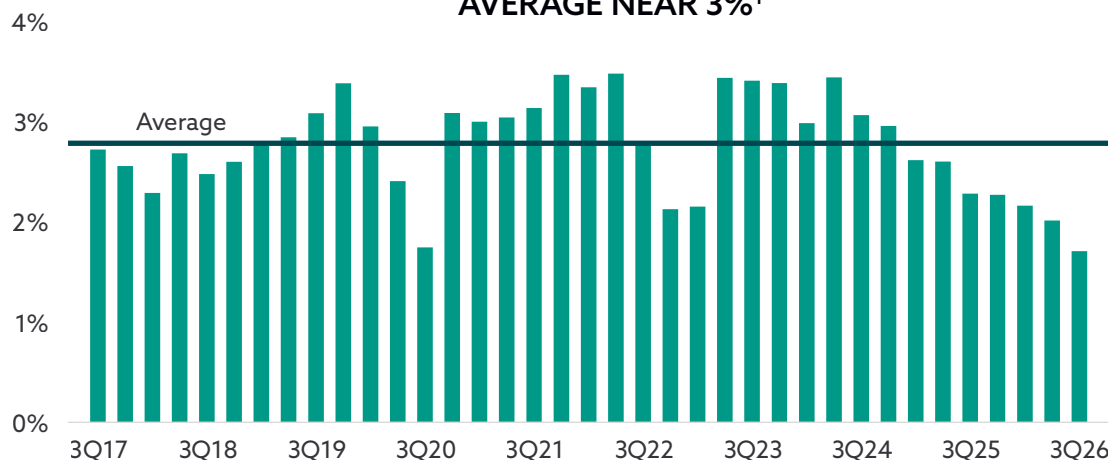


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HISTORICALLY, QUARTERLY CLO EQUITY RETURNS AVERAGE NEAR 3%¹



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In our view, this focus on identifying downside risk early with insights from industry specialists can support performance of the CLO platform and improve CLO equity returns.

Currently, we are constructive in healthcare technology, which may be beneficiaries of AI, as their proprietary data systems leave them less vulnerable to disruption from our perspective. We also favor utilities that are participating in the AI grid buildout, especially independent energy providers. Conversely, the portfolio is underweight the chemical and building products spaces. The team is looking for opportunities in these areas but have yet to add names, since we do not expect any positive movement over the next 12 months.

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