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9fin-9Questions 9fin-Structured Credit

9Questions — Mehdi Kashani, Arini — prepping CLOs for change in the new year (9fin)

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9Questions is our Q&A series featuring key decision-makers in the corporate credit markets — get in touch if you know who we should be talking to!

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Just over a year since their debut CLO, **Arini Capital Management** has already made waves.

Arini printed four European deals and has a fifth in the works, after only debuting in November 2023, even as some more seasoned managers did not print a single new issue this past year. The firm's namesake, the Arini tribe of parrots, contains many avian species of dazzling coloration, so it's only fitting that the CLO side has also caught the eye.

Arini is set to enter the US market soon as well, having recently hired **Jonathan Abramson** from **Sculptor**. The firm secured **Goldman Sachs** as arranger on its debut US CLO and had plans to pitch investors for both its US and European platforms at Opal, *9fin* reported in November.

It helps that the firm had experienced talent. Arini in 2022 hired Mehdi Kashani, its current head of structured credit, from BNP Paribas to launch its CLO business.

9fin caught up with Kashani for his thoughts on the year ahead, what the CLO market is watching as a new US president is set to take office in January, how to evaluate and handle credits given loans' elevated pricing and vulnerability to LMEs, and what to eat this holiday season once we catch a break from pricings.

1. Following your debut as a CLO manager last year, you've printed four deals and the third one priced near market tights in June. What helped you accomplish that?

We've been very deliberate in how we've built and scaled the platform since day one; for example, making a substantial up-front investment to ensure we had the best talent and systems and being hugely selective around who to partner with. This, combined with our fundamental approach to credit investing, supported by an experienced team of sector analysts who create a wealth of in-house IP, has enabled us to quickly establish ourselves.

We've also had a very clear long-term vision for the platform from the outset – to be a consistent issuer and key contributor to the European CLO market – which I think is another important reason why we've received such strong demand across our first four deals and quickly overcome the so-called "new manager premium".

2. This year has seen growing interest in CLOs, including from retail investors via CLO ETFs. What new investors have you observed, and what effect are they expected to have on CLOs?

So far, CLO ETFs have been more prevalent in the US but we're starting to see them emerge in Europe. Other new investors include institutions looking to increase their sub-IG exposure via CLO equity and existing investors increasing their allocations to the asset class. All these developments appear to be structural, indicating the maturity of this market.

This influx of capital has been a catalyst to the growth of the market, particularly as awareness and understanding continues to improve. We anticipate this trend continuing as long as the performance and track record of the asset class remains strong enough to position it favorably alongside more established asset classes, like traditional fixed income and equities.

One by-product of growth is greater choice for investors, which is driving tiering between managers. Those with good track records, experienced analyst teams and platforms built for the long term are being rewarded with more favourable pricing across the capital structure.

3. What are some examples of ways you've tailored your deals to answer the needs of investors across the capital structure?

I spent more than a decade on the sell side trading CLOs, so we've tried to apply the feedback I heard from investors on managers and the learnings from representing many managers whilst selling their platforms. This experience has played a large part in why we were so intentional in the way we set up our platform at Arini.

We believe that we can manage a CLO to generate attractive returns throughout the cap stack through our approach to credit selection, portfolio management and broadening the investor base for our issuances. The European loan market has evolved as such that credit selection is more important today than it has been for more than a decade.

4. We've reported that you've opened a warehouse for your fifth CLO. How are loan ramping and sourcing looking for European CLO managers right now?

This is always a challenge for managers which is why we developed a multi-faceted approach to sourcing and liquidity from day one. We leverage our deep relationships with sponsors and arrangers and proactively maintain dialogue with issuers, as well as having a skilled trading team in place. All these factors have enabled us to ramp four CLOs in a year, despite many complaining of a lack of supply, and we continue to construct high quality, conservative portfolios that deliver strong equity returns at the same time.

5. What factors are key when evaluating a credit for alignment with your investing vision? And given lower loan supply this year, how do you decide when to walk away?

Our underwriting and investment philosophy is consistent across all our strategies and is based on credit fundamentals – we're obsessed with understanding the downside in a credit.

Lower loan supply doesn't impact how we underwrite, although we've seen an uptick in our decline rate recently due to a deterioration in the quality of the credits coming to market.

We're not willing to chase spread by sacrificing on credit quality. In fact, it's quite the opposite. In this type of environment, we have become more defensive and are comfortable running a low beta portfolio whilst the market technical re-approaches an equilibrium.

6. Revisiting the topic of credit analysis. How have LMEs factored into your strategy this year and how does that compare to past years?

In all our underwriting, we evaluate the potential paths to our downside analysis. Our approach is premised on what the downside cases are in the first place, so it's a case of following these paths. We have a dedicated investment lawyer who sits on the desk, enhancing our ability to assess evolving situations in any given LME.

In any case, LMEs are currently less prevalent in Europe than the US which is largely due to the multiple structural differences between the US and European markets. Principally, the European whitelist concept mutes risk transfer from primary to secondary investors, removing a key ingredient required for creditors to be willing to participate in discounted exchanges: an entry price materially below par.

Another important structural difference is the European maturity wall being closer than in the US leaving less breathing room between an LME and maturities, further dissuading sponsors from engaging in aggressive LMEs or antagonising their creditors. There will continue to be cases where US techniques are utilised in Europe of course, but we believe these will be few and far between and that robust underwriting of the credit itself is a powerful insurance policy.

7. Given the results of the US elections, how do you expect CLO managers and investors will respond?

We are likely to see a range of responses from managers and investors. The incoming administration is considered positive for markets but comes with increased uncertainty around international trade.

Our expectations are that CLO managers in general will become more cautious regarding tariff-impacted sectors. The differentiator will be having sector-based analysts to determine which are good credits in a troubled sector or bad credits in a well-liked sector. Investors remain generally constructive on CLOs, given the pick-up to traditional credit and we ultimately expect to see continued appetite aided by the results of the election.

Nevertheless, it has become apparent to us that the market wants to price the most aggressive/negative scenarios for tariffs in both Europe and China, including emerging markets more broadly, very quickly.

FX markets continue to re-price post-election, which is reflective of the aggressive divergence we're beginning to see between the US and the rest of the world's equity markets. The potential for inflation, fiscal deficit and the repercussions for global growth all pose risks, but we remain open minded when thinking about both upside and downside risks to the global economy.

The impact of tariff policy on European industrials, autos and energy markets are a particular area of focus. Increased dispersion and strong bottom-up credit analysis has always been a decisive positive for our strategy, and this is expected to benefit us in a rapidly evolving global economic landscape.

8. CLO equity in particular can be challenging to place, although arb has improved this year. How can newer European CLO managers stand out to potential equity investors at this moment, whether through third-party equity or captive fundraising?

The general market perception is that managers who are mainly focused on equity performance are generally targeting riskier portfolios. Therefore, I think the key here is, how can a manager drive their equity performance while minimizing risk?

And this really comes down to the DNA of each individual manager and how they view the return attribution of equity. For example, at Arini, we are a fundamentals-first shop, so credit selection is the core of our CLO portfolio build, which also drives equity performance and has helped us stand out from the crowd. We have a proactive approach to portfolio management that is designed to help us steadily build par in our portfolios, which is beneficial to the debt and consistently accretive to equity performance. So far, we have achieved 18% and 34% annualized returns on our Arini CLO 1 and Arini CLO 2 equity respectively.

Our deep bench of sector-focused analysts allows us to proactively focus on active portfolio management with appropriately scaled risk allocation. We also believe managing access to primary and secondary loan markets is key, as is active liability management to ensure the best terms.

9. With the holidays approaching, what’s a food you enjoy eating at this time of year that you wish more people would try?

One holiday treat that I absolutely love and wish more people would try is Kipferl. It’s a traditional German biscuit that my wife’s family bakes every year when we visit them for the holidays. For those that don’t know, they are a crescent-shaped buttery biscuit made with ground almonds or hazelnuts and dusted with icing sugar.

They’re so special because despite their simplicity they are so delicious and manage to evoke such amazing memories. It’s often that the simplest foods are hardest to get right, but when you do, they are excellent, perhaps like CLOs…