

### Monthly European loan market update: June 2024

The Credit Suisse Western European Leveraged Loan Index (“CS WELLI” or “Index”) returned 0.09% this month, generated by an interest return of 0.64% but offset by a principal return of -0.55%.<sup>1</sup>

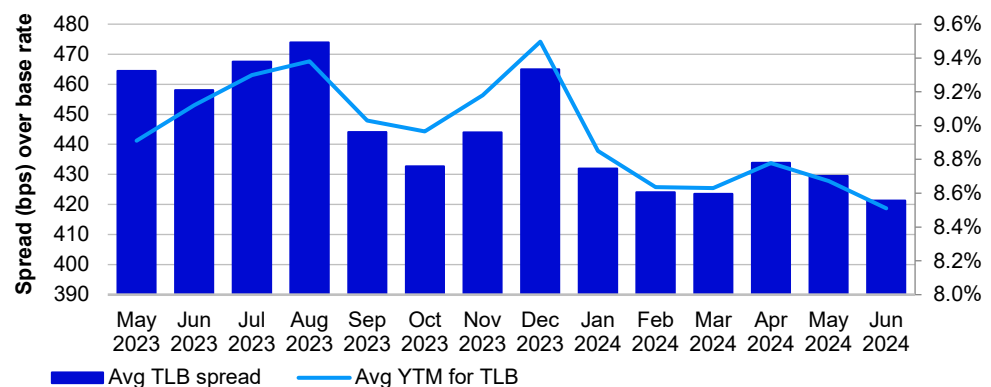
During the second quarter of the year, financial markets displayed a varied performance set as investors concentrated on multiple market risks. On the upside, equities continued to climb, with the S&P 500 reaching a new record high, driven by further gains from the Magnificent 7. However, these equity gains were not widespread, and the S&P 500 Equal Weight Index actually fell during the quarter.

Fixed rate bonds also faced difficulties: Even though the European Central Bank (ECB) enacted their first rate cut for five years, decreasing their deposit rate by 25 basis points (bps) to 3.75%; investors now anticipate fewer rate cuts for the rest of the year. Geopolitical risks were also a focal point and French assets declined after President Macron announced a snap legislative election.

The leveraged loan market fared relatively well in such environment, returning 2.1% in Q1, but saw some softness in June (total return of 0.09% driven by interest return but with the index trading down slightly to €97.10 from €97.22). This softness was largely caused by a very strong technical primary loan pipeline, which saw €14.4bn of institutional loan volume, the highest since June-2021, and significantly higher than the €4.9bn last month in May. Arrangers and issuer opportunistically took advantage of a strong market environment at the beginning of the month and launched a flurry of refinancing, repricing and add-on transaction. New money LBO supply improved as well with a handful of new sponsor buy-outs launching.

Towards the end of the month issuance has already slowed down, with the expectation of more moderate volumes for the remainder of the year. New issue yields compressed slightly to 8.51% with the typical B2/B rated loan now pricing around the E+425-450 level along with small original issue discount (OID) of approximately 0.5-1.0 points<sup>2</sup>.

**Figure 1: Average new-issue yields (rolling 3 months)**



Source: Pitchbook Data Inc. as of June 30, 2024.

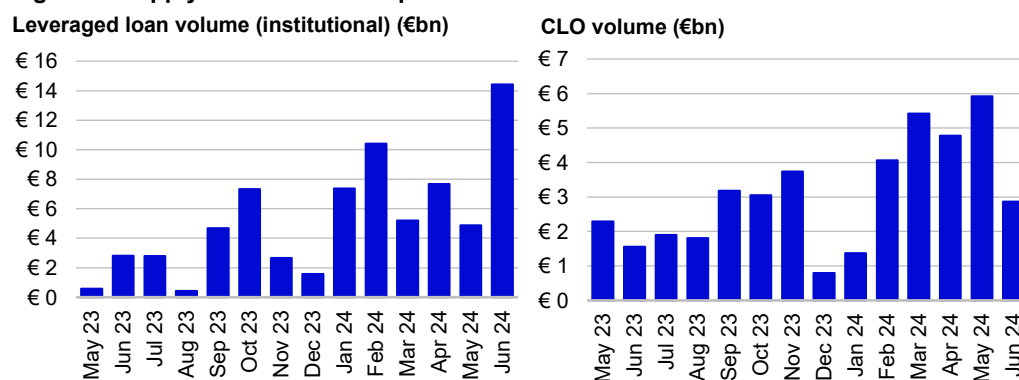
**Past performance is not a guarantee of future results.**

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European CLO activity remained very strong and year-to-date volumes stand at record high for the CLO 2.0 era. Sell-side analysts now expect around €40-€45bn of CLO new issue for the year, which would exceed the previous record of €38.6bn in 2021<sup>2</sup>. This also compares to initial forecasts at the start of the year of just around. €20bn.

AAA liabilities – whilst around the E+140-150 area for most of the year – have now tightened further with deals pricing around the E+135 area<sup>2</sup>. Even at such levels, CLO AAA continue to offer strong relative value compared to other AAA asset classes. The asset arbitrage to the loan market is well functioning and a stream of repayments from CLOs outside reinvestment period returning cash to investors means that there continues to be investor capital available to support further strong new issue levels going forward.

**Figure 2: Supply/demand backdrop**



Source: Pitchbook Data Inc. as of June 30, 2024.

## Returns

- The Food and Drug sector performed best this month, returning 1.15%, followed by Forest Products/Containers (0.65%) and Gaming/Leisure (0.36%).<sup>1</sup> Consumer Durables (-0.93%), Housing (-0.24%) and Media/Telecommunications (-0.20%) were the worst performing sectors during the month.<sup>1</sup>
- 'BB' rated loans performed best this month with a total return of 0.16%, followed by 'B' rated loans (0.11%), and 'CCC' rated loans (-0.17%).<sup>1</sup>
- At month end, the average price of the CS WELLI was €97.10, down €0.12 during the month.<sup>1</sup> The CS WELLI's three-year discount margin was EURIBOR + 4.90%, a widening of approximately 15bps during the month.<sup>1</sup>

## Fundamentals

- The second round of French elections have completed (early July) – in the later part of June, markets in general re-priced risk with the increased uncertainty and possibility of the far-right gaining more (outright) power. Another electoral shock has been delivered with the far-left New Popular Front securing the surprise outcome of being the largest group. The far-right party and allies has claimed 143 seats – so no majority. Tactical voting to block the far-right has swung the pendulum in the opposite direction without any group having an overall majority. At first glance, investors could be satisfied with the result of no clear winner, and especially no, so-called, 'extreme party' able to govern alone without making major compromises on their reform agenda, so risks of a massive political overhaul have been diluted.
- In the flash release, the Euro area composite output PMI declined 1.3pts to 50.8 in June – consensus was 52.5 - breaking the upward trend seen between November and May when the PMI cumulatively increased almost 6 points. The manufacturing sector was the main detractor, where the output index fell (by 3.4pt) to 46.0. Across countries, the decline in the area-wide index was broad-based.
- June flash Eurozone inflation edged down by 0.1percentage points (pp) to 2.5%, in line with consensus. The decline was driven by lower energy (-0.1pp to 0.2% year-over-year (yoy)) and food inflation (-0.1pp to 2.5% yoy). Core inflation was unchanged at 2.9% yoy, a miss to consensus expectations of 2.8%. Within core, both goods and services inflation were unchanged at 0.6% yoy and 4.1% yoy, respectively.
- As expected the ECB cut deposit rates at their June meeting – the first cut since 2019 – the deposit rate was lowered to 3.75% from 4.0%. President Lagarde commented there was a “strong likelihood” that the dialing back of the restrictive monetary policy has started, although the language used by the ECB was thought to be of a more hawkish in tone. The ECB says it will continue to follow a “data dependent and meeting by meeting approach to determining the

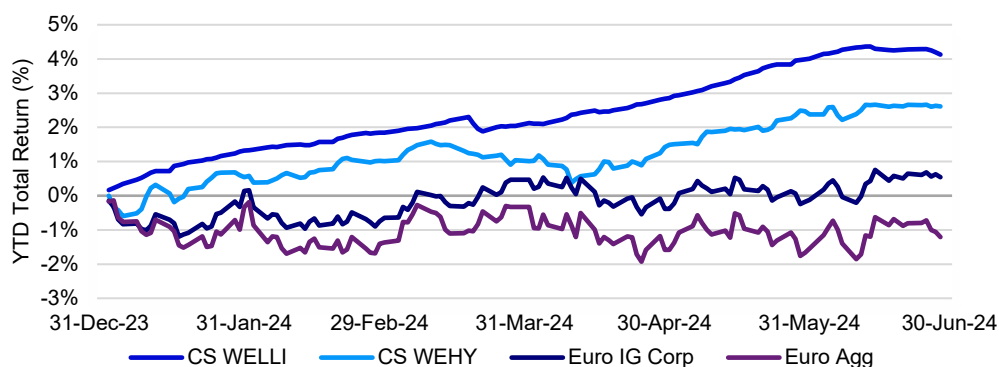
appropriate level and duration of restriction". It was also repeated that the ECB is "not pre-committing to a particular rate path".

- The last twelve-month default rate for the Morningstar European Leveraged Loan Index (based on principal amount) is 1.29%.<sup>3</sup> The historical average annual default rate is 2.84%.<sup>3</sup>

### Market opportunity

Improving macroeconomic trends have helped to facilitate a robust loan market. However, technical pressure from a large loan supply as well as softness following the French snap election pressured prices during the months. Going forward we believe funding costs likely become lower (base rates + credit/margin spreads) with demand from CLOs remaining strong. June already saw strong signs of pick-up of primary loan activity and we envision better M&A during the second half of the year (albeit most likely at lower levels compared to June). Overall, the supply/demand technical remains favorable for loan assets. Loans remained a popular destination for investor capital as an asset class uniquely well positioned for the improving growth dynamics (lower default risk) and interest rate environment. Loans have delivered low volatility – and thus high risk-adjusted returns – year-to-date as depicted in Figure 3, and are on track to deliver another year of exceptional returns.

**Figure 3: Year-to-date stable asset class performance**



Source: Credit Suisse, Barclays, Bloomberg as of June 30, 2024. **Past performance is not a guarantee of future results.** CS WELLI represents the Credit Suisse Western Leveraged Loan Index, CS WEHY represents the Credit Suisse Western European High Yield Index, IG Corp represents the Bloomberg Euro Aggregate Corporate Total Return Index, and Euro Agg represents the Bloomberg Euro Aggregate Total Return Index.

### Relative yield

	\$ Price	Yield to worst	Spread to	Duration (years)
Bloomberg Euro Aggregate Total Return Index	91.97	3.34	N/A	6.31
Bloomberg Euro Aggregate Corporate Total Return Index	94.12	3.82	N/A	4.44
Credit Suisse Western European High Yield Index (EUR-hedged)	93.63	7.23	4.05	2.97
<b>Credit Suisse Western European Leveraged Loan Index (EUR-hedged)</b>	97.10	8.32	4.90	0.25

Source: Barclays, Credit Suisse and Bloomberg L.P. as of June 30, 2024. Loan "yield to worst" and "spread to worst" incorporate the EURIBOR forward curve. An investment cannot be made in an index.

- 1 Credit Suisse Western European Leveraged Loan Index (CS WELL1) in EUR as of June 30, 2024. Past performance is not a guide to future returns. An investment cannot be made directly in an index.
- 2 Pitchbook Data Inc. as of June 30, 2024.
- 3 Morningstar European Leveraged Loan Index, average default rates covering June 1, 2007, through June 30, 2024.

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## About risk

The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested.

Many senior loans are illiquid, meaning that the investors may not be able to sell them quickly at a fair price and/or that the redemptions may be delayed due to illiquidity of the senior loans. The market for illiquid securities is more volatile than the market for liquid securities. The market for senior loans could be disrupted in the event of an economic downturn or a substantial increase or decrease in interest rates. Senior loans, like most other debt obligations, are subject to the risk of default.

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