The State of Private Credit in Europe (Third of a Series)

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For a sense of overall credit conditions, we tuned last week into the European Leveraged Finance Mid-Year Update hosted by Fitch. The discussion – covering the economy, ratings, covenants, and structures – was virtually indistinguishable from recent US market conferences. Apart from these panelists' distinguished accents.

For example, activity for leveraged loans in Europe has generally returned to that of pre-Covid levels. The pendulum for terms, that had swung investor-friendly a year ago, is much more issuer-friendly this year. Also, the asset recovery from last year's downturn is so complete that there's hardly an element of caution remaining to tamp down frothy conditions.

Our friends at Tikehau reported in a private note that 1Q European leveraged finance activity, combining both loans and bonds, was just under €80 billion; more than double 4Q's performance. New-issue institutional loan volume for 1Q showed even greater growth, to more than €35 billion from under €10 billion from the previous quarter (data courtesy S&P Global Market Intelligence).

On the pricing front, average term loan B yields have slipped to just under 4.00%, having gapped out at the onset of Covid last year to about 5.00%. A Credit Suisse research piece echoed this development. While all-loan spreads spiked to 750 bps last May, they bottomed to "new tights" last month. Loan prices, conversely, have reached new highs (98.7).

Yet it speaks to the stability of the asset class that Euro yields (and spreads) have otherwise remained range-bound since 2016. It's thus not unusual for investors to toggle between the US and Europe, depending on conditions for pricing and terms.

Five years ago, as we reported in our white paper, the US was challenged by energy concerns and loan fund outflows, while Europe was still in its early QE days. Good for European issuers, not as great for investors. But then, as often happens, capital flowed to fill the vacuum. That changed investing dynamics and the US became cheaper and Europe more expensive.

All of which underlies the finding that opportunistic value plays are no substitute for a long-term investing strategy.

From a cross-border borrower's perspective, competitive relative pricing means issuers have more options in structuring their financings. As our *Chart of the Week* highlights, the pandemic caused spreads to widen in Europe and contract in the US. This means other elements come into play, such as covenants and debt allowances.

No surprise, then, that being a debt advisor in Europe today carries special opportunities and challenges. Never have the choices for issuers been more varied, yet never have global and national market dynamics been more complex.

Next week, we’ll speak with such an advisor and learn what it takes to be competitive in an emerging post-Covid European private credit world.