European Loan Market Snapshot

Monthly European loan market update: March 2017 (covering February 2017)

Returns

- The Credit Suisse Western European Leveraged Loan Index ("CS WELLI") returned 0.46% during the month of February, representing interest income of 0.35% and principal return of 0.11%.[1]
- Every industry had a positive return during the month of February. Consumer Non-durables was the highest returning industry, posting a return of 1.49% while Consumer Durables posted the lowest return for the month at 0.07%. In terms of risk appetite, the European loan market continued to be risk-on during February, with CCC-rated assets returning 1.89%, single-B rated assets returning 0.46% and BB-rated assets returning 0.27%.[1]
- New institutional loan volume for the month of February was €5.1 billion (compared to €1.1 billion for the same period last year) – this is a reflection of a slow start to 2016 as well as a high number of repricings/refinancings in 2017. Demand for loans by CLOs and institutional buyers continued to be very strong in February. Thus, while the primary market remained active in February, the percentage of the new volume attributable to repricings and refinancings continued to increase during the month to 89% (versus 75% in January 2017 and 66% for 4Q 2016).[2]
- We attribute the continued strong demand for loan assets to be due to (1) The general demand for risk assets as the default environment remains low, (2) The desire to reduce duration risk as investors focus more on the factors that may indicate a risk of the increased rhetoric from the European Central Bank's (ECB) around tapering later in 2017 or early 2018 (inflation), and (3) The halo effect from the ECB's monetary support through their Asset Purchase Program ("APP").
- The average price of loans in the European market ended February at 99.02. At February month end, European loans were providing a spread to three years of 4.67%.[1]

Fundamentals

- Building on the positive economic momentum from 4Q 2016 and January 2017, the February Euro-zone Purchasing Managers' Index ("PMI") composite strengthened further to 56.0, from 54.4 in January (a reading above 50 illustrates managers' confidence in the economy). This represented the highest reading since August 2011. The main driver of the improvement in the PMI composite was the Services PMI, which increased to 55.6, from 53.6 in January. At a country level, Germany and France composite PMI both increased to 56.1 and 56.2 (a 69 month high), respectively.[3]

Average loan price includes all loans January 1997 through February 2017.

- Euro-Zone Consumer Price Index (CPI) increased again in February to 2.0% from 1.8% in January and 1.1% in December and but was in line with consensus estimates. Core inflation, however, remained flat once again at 0.9% and remains below the ECB's target level of 2.0%. The main driver of the difference between headline CPI and core inflation continues to be Energy costs, which increased 9.2% in February from 8.1% in January.[3]
- There were no new defaults in February. Accordingly, the trailing 12 month default rate on the CS WELLI was unchanged at 0.50% at the end of the month.[1]

Technicals

- New institutional loan volume for the month of February was €5.1 billion (compared to €1.1 billion for the same period last year).
- 16 deals were repriced in Europe during February, up from 13 in January. Borrowers and their sponsors were able to take advantage of the strong demand for institutional loans by reducing their average spreads by 105 basis points (bps).[2]
- Notable loan deals in syndication in the period included:
  - £575 million of senior secured loan (SSL) facilities to support Onex's acquisition of Parkdean Resorts the Euro-tranche priced at L+425 with a 0% floor and an issue price of 99.5.
  - €1.4 billion of SSL facilities to support the refinancing of Ineos' existing high yield bonds. The deal included an €875 million of Euro-denominated term loans and $555 million of USD term loans. The Euro facility priced at E+250 with a 0.75% floor and an issue price of par, in addition to the new SSL facilities, Ineos also repriced and extended the maturity of its existing $1.45 billion and €1.725 billion SSL facilities (same terms as outlined above).
- Two CLOs printed during the month of February (compared to one during the same period last year), representing €800 million of fresh capital (compared to €400 million for the same period last year). For the 2017 year-to-date period, three CLOs have priced with a value of €1.2 billion (compared to €800 million over two deals for the same period last year).[2]
- CLO liability spreads continued to tighten over the course of February bolstered by continued positive sentiment in the European credit markets and increased demand from real money buyers. Spread compression has brought CLO AAA tranche pricing to the 90-105 bps range and CLO BB tranche pricing to 515-585 bps, representing respectively approximately 12 bps and 90 bps of year-to-date tightening.
- While we expect the solid trend of CLO issuance to continue based on our understanding of the number of open warehouses (which we believe is unchanged), we note that the arbitrage between CLO assets and CLO liabilities has compressed, which could dampen net new issuance compared to the high end of our full year 2017 forecast of €15-20 billion of new CLO issuance.

Valuations

- Primary Loan Market:
  - The average lagging three month all-in-yield on new primary deals during the month of February was 4.22% (compared to 4.30% for the prior month and 5.75% for the same period last year). In comparison, the average lagging three month all-in-yield on single-B rated assets was 4.30% (compared to 4.28% for the prior month and 6.18% for the same period last year).[2]
- Secondary Loan Market:
  - At February month end, European loans were providing a spread-to-three year takeout of 4.67% (compared to 4.86% at the prior month's end and 6.33% at the same time last year). In comparison, the spread-to-worst for European high yield bonds was 4.27% (compared to 4.34% at the prior month's end and 6.94% at the same time last year).[3]

Figure 1

Total return (EUR, in %)	2015	1Q 16	2Q 16	3Q 16	4Q 16	2016	Jan-17	Feb-17	2017 cumulative
Credit Suisse Western Europe Leveraged Loan Index (EUR-HDG)	3.14	0.78	1.49	2.80	1.31	6.52	1.00	0.46	1.47
Credit Suisse Western Europe HY Index (EUR-HDG)	1.36	1.70	1.75	3.67	2.20	9.63	0.70	1.21	1.94

Source: Credit Suisse, as at 28 February 2017. Past performance is not a guide to future returns. An investment cannot be made directly in an index.

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