PILFOR

LENDING SOUNDNESS

4th Quarter 2020

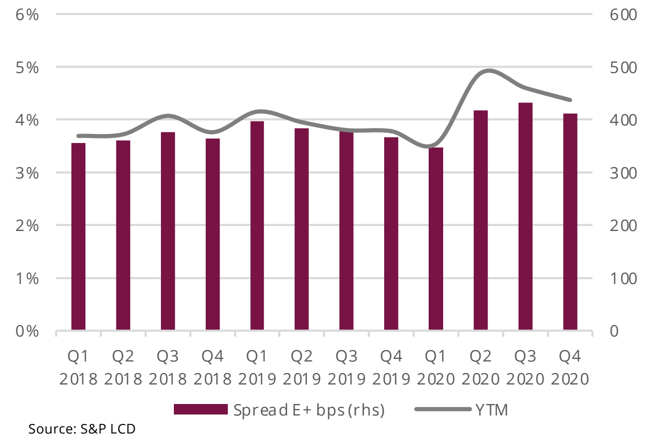
Quarterly Market Insights

9.2.2021

EMEA Financing Environment

The unprecedented actions taken by the central banks combined with large-scale government programs to stabilize the economy, markets, investors and above all companies continued to lend comfort and offered an ideal environment for issuers in Q4 2020, following a strong recovery in Q3 2020, with spreads tightening further on the back of yield-hungry / risk-off investors. Despite the roller coaster witnessed during 2020, European leveraged loans still recorded a return north of 2.7%. Needless to say, in the absence of the aforementioned measures taken there would have been quite a different bleak picture. With COVID-19 still holding the centre stage not only across Europe but globally despite the first roll-outs of vaccines, caution remains at the forefront of markets and investors. Only time will tell how much havoc the pandemic has caused across corporates. All the more so will investors tread carefully heading further into 2021, until visibility offers a better base for decision making.

Leveraged loan pricing changes EMEA (bps)

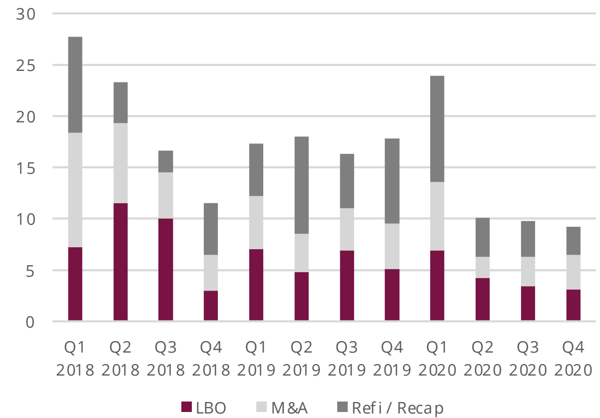


Source: S&P LCD

Leveraged Loan Market Insights

New European institutional loan issuance delinked by around 25% in 2020 YoY to EUR 51.7 bn. The decline marked the fourth consecutive year of declining issue volumes for the market, despite a strong bid for loan paper from CLOs. 2020 proved to be yet another year of suppressed buyout activity with volumes down 21% YoY, albeit further reduced by the pandemic. A sharp increase in loan pricing following the COVID-19 triggered sell off in March weighed on refinancing and dividend recapitalization activity for a large part of the year, cutting volumes by 35% YoY. Issuance activity in Q4 2020 dropped to a low of EUR 8.9bn, less than 50% of Q4 2019 levels. The low activity level was further compounded by Euro high yield issuance volumes reaching the highest level since 2017, with roughly EUR 160bn of new high yield bonds being issued in 2020. Volumes were fuelled by low interest rates and central banks supportive measures lending considerable comfort to yield seeking investors.

Leveraged loan issuance EMEA (EUR bn)

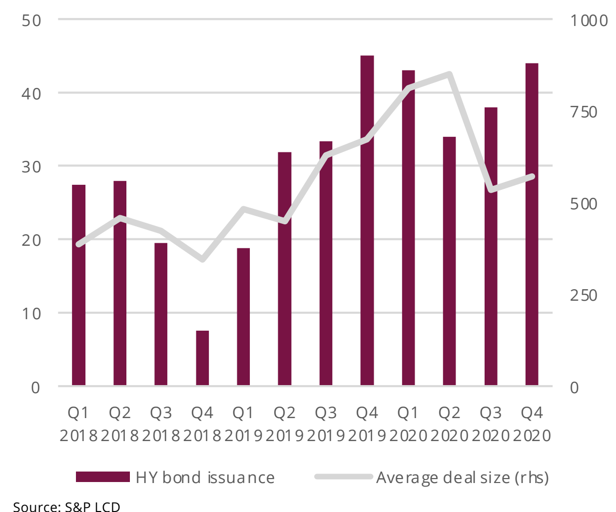


Source:,S&P LCD

Debt Capital Market Insights

The European high yield market recorded an issuance volume of EUR 160bn, up from EUR 152bn in 2019. While Q1 noted issuance in excess of EUR 40bn, Q2 and Q3 fell below EUR 40bn only to be surpassed by a very healthy Q4 2020 with EUR 44bn. Overall issue numbers varied over the quarters with Q1, Q3 and Q4 recording 70 or more issues, while Q2 with 42 issues was well below these levels. Following a decline in average issue size in Q3 with EUR 535m, Q4 noted a pick-up to EUR 571m. The market was clearly dominated by "BB" issuers, accounting for more than 60% of total deals. A good part of this dominance is due to the fallen angels that had lost their investment grade ratings during the course of 2020. Prominent examples are Marks & Spencer and Renault. In terms of sector issuance, Financials accounted for the largest part with 34%, followed by Telecommunications with 14%, Industrials with 13% and Consumer Services with 11%. The LBO of ThyssenKrupp Elevator represented the largest issue amounting to EUR 4bn, followed by Fiat Chrysler with EUR 3.5bn. Overall the 10 largest issues reached a total of roughly EUR 26bn.

High yield bond issuance EMEA (EUR bn)

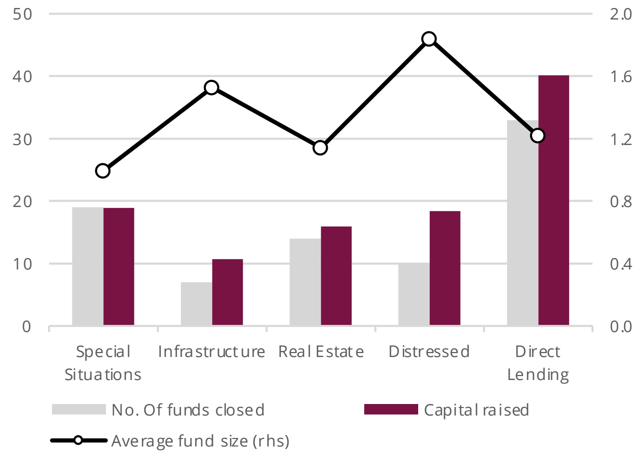


Source: S&P LCD

Private Debt Market Insight

Driven by the economic slowdown caused by the COVID-19 pandemic, the shift to remote fundraising vs. the historical face-to-face interaction and the fact that some of the largest funds had finished fundraising in the preceding couple of years, private debt fundraising decreased YoY to USD 110bn. 2020 noted fewer large distressed funds with some of the larger managers raising capital and closing funds pre 2020, bringing the share down to 16% of total capital. Senior debt made up around 40% of all capital raised, due to its relatively lower risk profile, making it a good place to invest in uncertain times. Average senior debt funds closed in 2020 stood north of USD 1bn for the first time since 2008, driven by the growth of private debt brand names with strong track records able to attract capital for larger funds leading to some consolidation of the market. The USD 12bn direct lending fund by Apollo offers an example. Europe-focused fundraising was nearly on par with the US, underlining its importance as a region for private debt as investors see good opportunities and arising corporate funding needs.

Private Debt raised by fund type 2020 (USD bn)

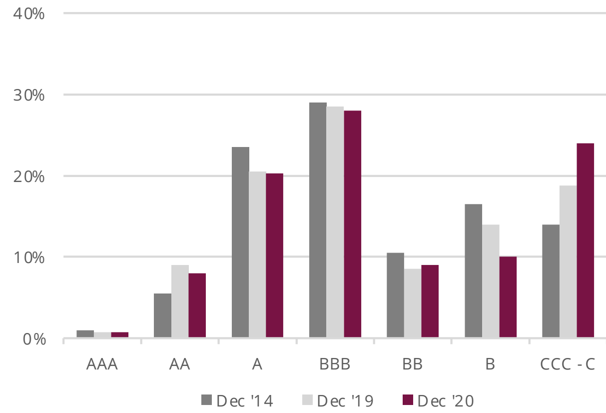


Source: Pitchbook

Rating Market Insight

With the outbreak of the pandemic, capital markets and investors witnessed an unprecedented wave of rating actions by the rating agencies. On top of this, the highly volatile oil price fuelled further rating actions, that had their peak in Q2 2020, followed by a decline of the actions in Q3 and Q4. Sectors most affected were capital goods, transportation, automotive, media and entertainment, retailing and energy. The overall rating deterioration witnessed in 2020 has continued the global bias towards non investment grade which accounts for more than 50% of global issuers. While Europe is faring slightly better with around 43%, the region has recorded a marked increase in the lowest rated "CCC-C" issuers, underpinning the expanding fragility and steady alignment to their US peers. While rating outlooks have taken a more stable stance heading into 2021, uncertainties related to the development of the pandemic, government actions and corporate financial policies continue to weigh on ratings.

Deteriorating ratings of European issuers (sen. unsec.)

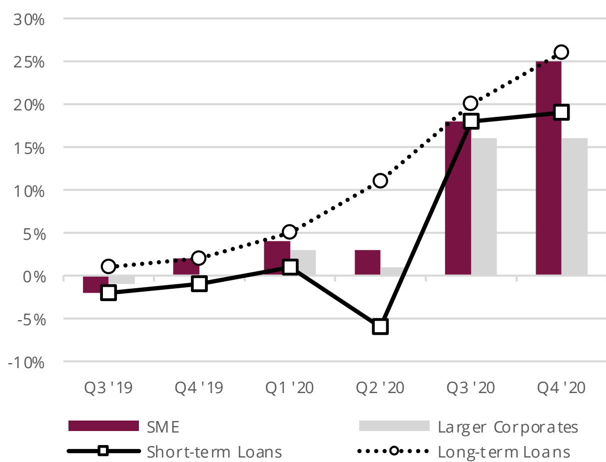


Sources: S&P, Moody's, Fitch

Brace for the de-masking of governmental measures

Interestingly pandemic-related damage in terms of defaults has been a lot lower than expected in spring 2020. Across Europe, some USD 36bn of rated debt defaulted vs. roughly USD 6bn in 2019. Given the aforementioned rating downgrade tsunami in 2020 and the very gloomy forecasts, defaults across Europe held up reasonably well. However, and this is key in our view, central banks and governments have been masking default developments during 2020, resulting in a de-coupling of market prices and fundamental developments from a capital market view. Nevertheless, defaults are expected to spike in Q1 / Q2 2021, possibly reaching up to 5%, in the down-side case even 9%. This differs largely to the European banking market, reflecting the perceived risks not only from larger corporates, but especially from SMEs. Not surprisingly, banks in Europe have turned a lot more negative on credit risk. The tightening on bank loans jumped in Q3 and Q4 2020, even more so for SMEs in anticipation of the time, when the de-masking of governmental measures gradually takes its way.

Bank loan tightening for corporates in Europe (net)



Source: ECB

Sources used in this report include Pitchbook, Preqin, ECB, Dealogic, Fitch, Moody's, Pitchbook, S&P

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