Insights

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Tuesday, July 9, 2024

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LevFin Highlights 1H24

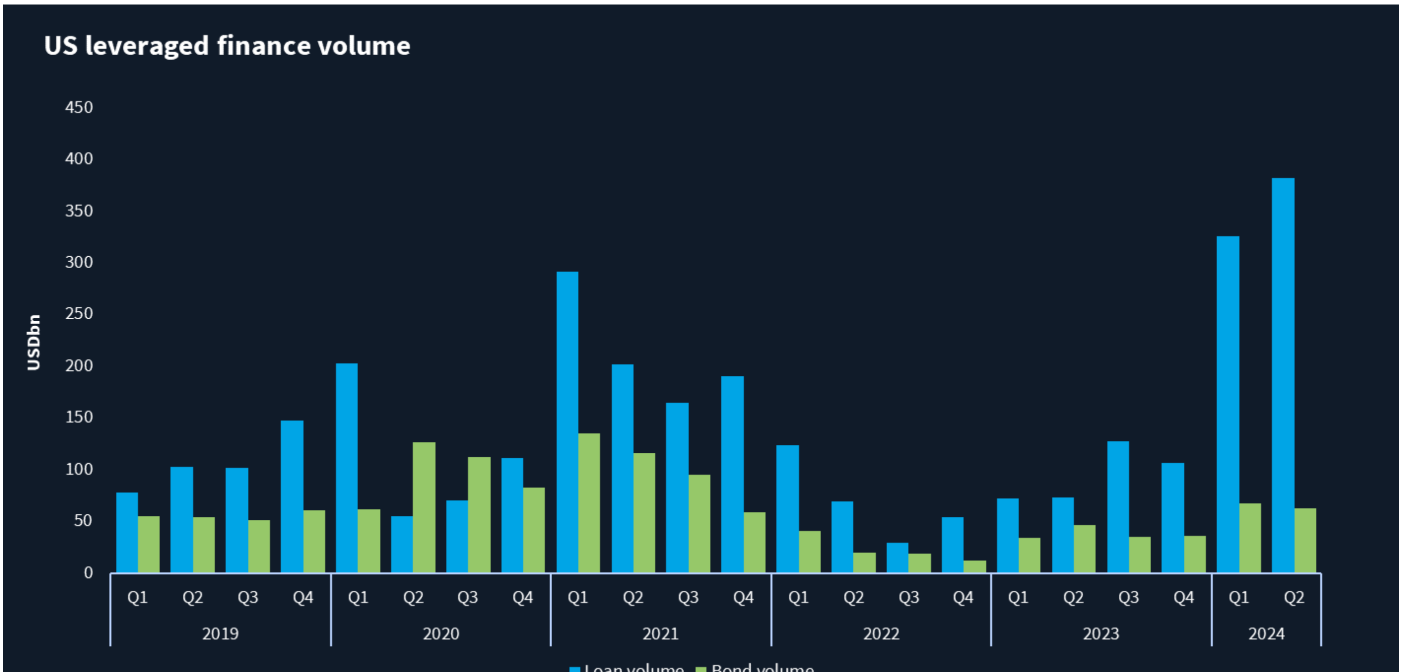
Rebound in issuance underpinned by strong investor demand

Leveraged finance (LevFin) issuance across the US and European institutional loan and high-yield (HY) bond markets in 1H24 more than tripled from a year ago, ballooning to USD 1trn. The rebound in issuance has been driven mainly by refinancing activity, while the undersupply of new-money paper amid strong investor demand has given rise to a deluge of loan repricing exercises on both sides of the Atlantic.

LevFin markets regained their appeal in 2024, as interest-rate hikes plateaued and fears of recession subsided. A rosier macroeconomic outlook and the prospect of rate cuts propelled investors to funnel money back into HY funds, while collateralised loan obligation (CLO) issuance also surged this year.

However, growing investor appetite for LevFin paper was not met by a meaningful revival in mergers & acquisitions (M&A) in the first half of the year. Although year-to-date (YTD) issuance for M&A transactions, including leveraged buyouts (LBOs), ticked up compared with a rather desolate 2H23, the gap in buyer and seller valuations continued to hinder dealmaking.

While LevFin bankers expect incremental increases in M&A financing in the coming quarters, the current pipeline indicates that a surge in M&A-related loan and bond issuance is not on the cards for 2024.

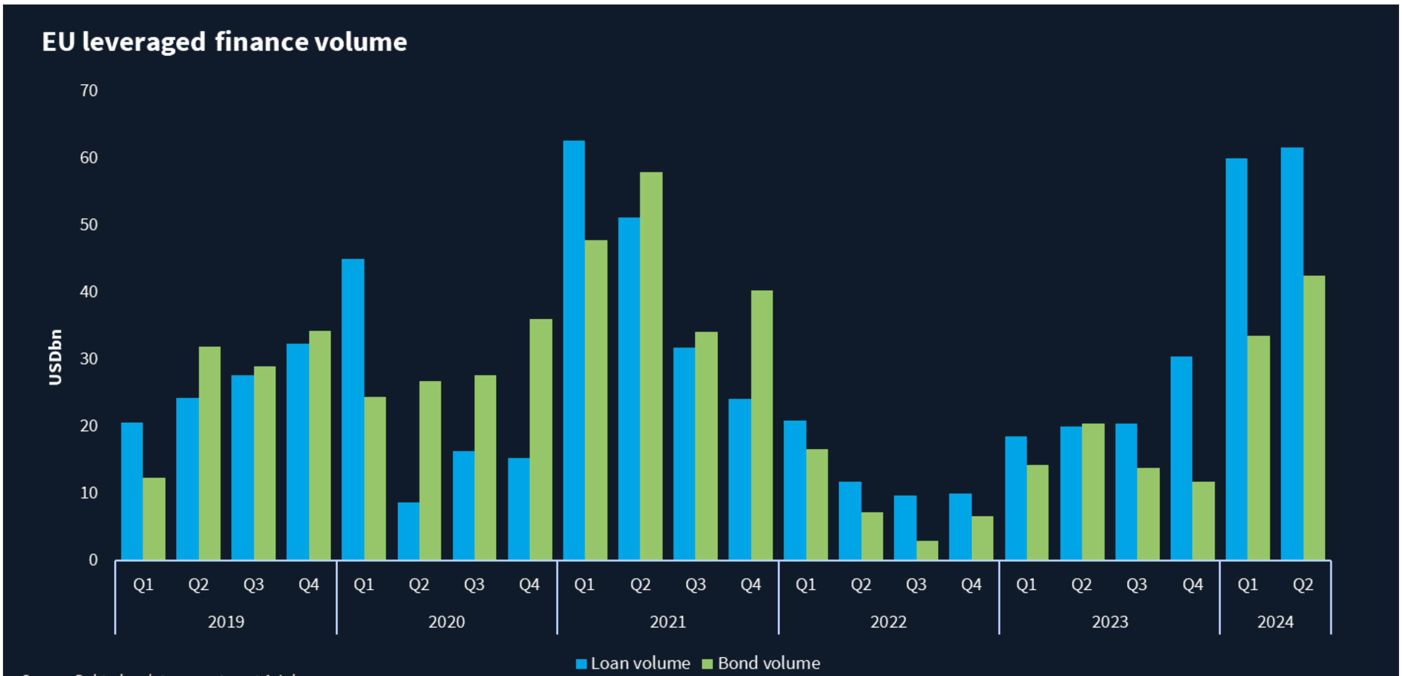


Source: Debtwire, data correct as at 1 July

In the US, institutional loan issuance reached record-breaking levels in the first half of the year, soaring to USD 707bn across 630 deals from only USD 145bn raised in 1H23. Coming in at just over USD 325bn in 1Q24 and USD 382bn in 2Q24, issuance represented a year-on-year (YoY) jump of nearly 400%.

However, a rather large boost to loan volumes came from an outpouring of repricing exercises that kicked off at the very start of the year and carried on throughout the period. This year's increase in CLO issuance amid slim M&A activity meant that demand for loans continued to outstrip supply, thereby squeezing spreads tighter and giving borrowers an opportunity to cut margins by around 50 basis points (bps) to as much as 125bps.

US HY bond issuance did not catch up with historical highs, but nevertheless climbed 62% YoY to USD 131bn across 172 deals in 1H24. At USD 68bn, issuance rose 8% in the first quarter, softening to USD 63bn in 2Q24, as market activity cooled in April.



Source: Debtwire, data correct as at 1 July

In Europe, HY bond issuance made a robust recovery, surging 120% YoY to USD 76bn across 174 transactions in 1H24. Quarterly volumes rose from USD 34bn to USD 42bn in 1Q24 and 2Q24, respectively.

The European loan market churned out an impressive USD 122bn across 191 institutional loans, marking a 216% YoY increase. At USD 60bn, loan issuance in 1Q24 was almost on par with the USD 62bn transacted in the second quarter.

As with the US LevFin markets, activity mostly centered on refinancing and maturity extensions, while a torrent of repricing transactions also swept through the European loan market.

Although new money from M&A/LBO activity remained thin on the ground, more than USD 10bn of debt supply migrated to the leveraged loan and HY bond markets from private credit this year. As borrowers sought cheaper refinancing options, syndicated markets recaptured part of the share they lost to direct lenders during more volatile periods in 2022 and 2023.

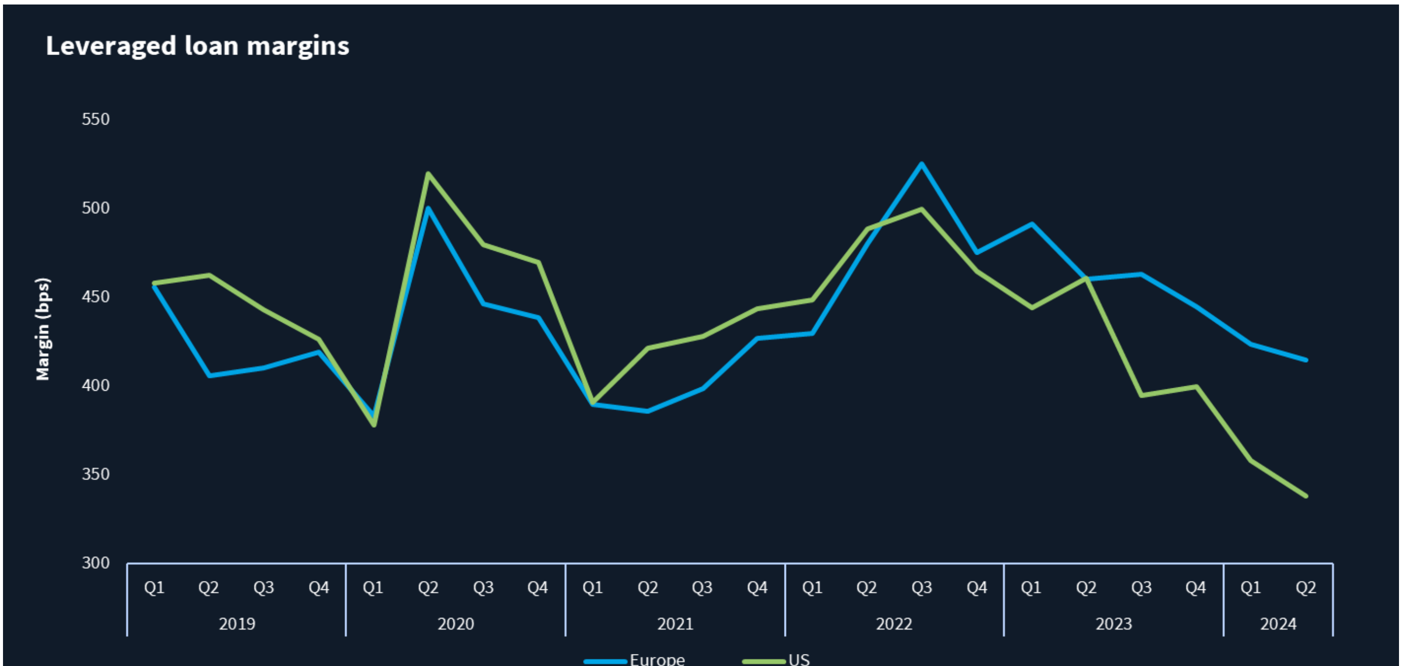
In response, private credit funds also lowered pricing, offering particularly competitive terms on sterling-denominated credit. Moreover, direct lenders have sought to compete with syndicates by offering higher leverage on M&A deals, including PIK instruments, as well as larger delayed-draw facilities that offer flexibility for bolt-on acquisitions in 'buy-and-build' models.

While competition with private credit will continue to feature, the asset class could also play a more complementary role to syndicated markets. One such example was **Ardonagh**'s refinancing deal from February, which included a mix of private debt funding, alongside euro-dollar HY bonds. In June, the UK-based insurance company also added leveraged loans to its capital structure. A candidate for hybrid financing involving both syndicated markets and private debt funds could be **Sanofi**'s consumer healthcare unit, whose potential sale could be funded with a mix of senior secured and PIK facilities.

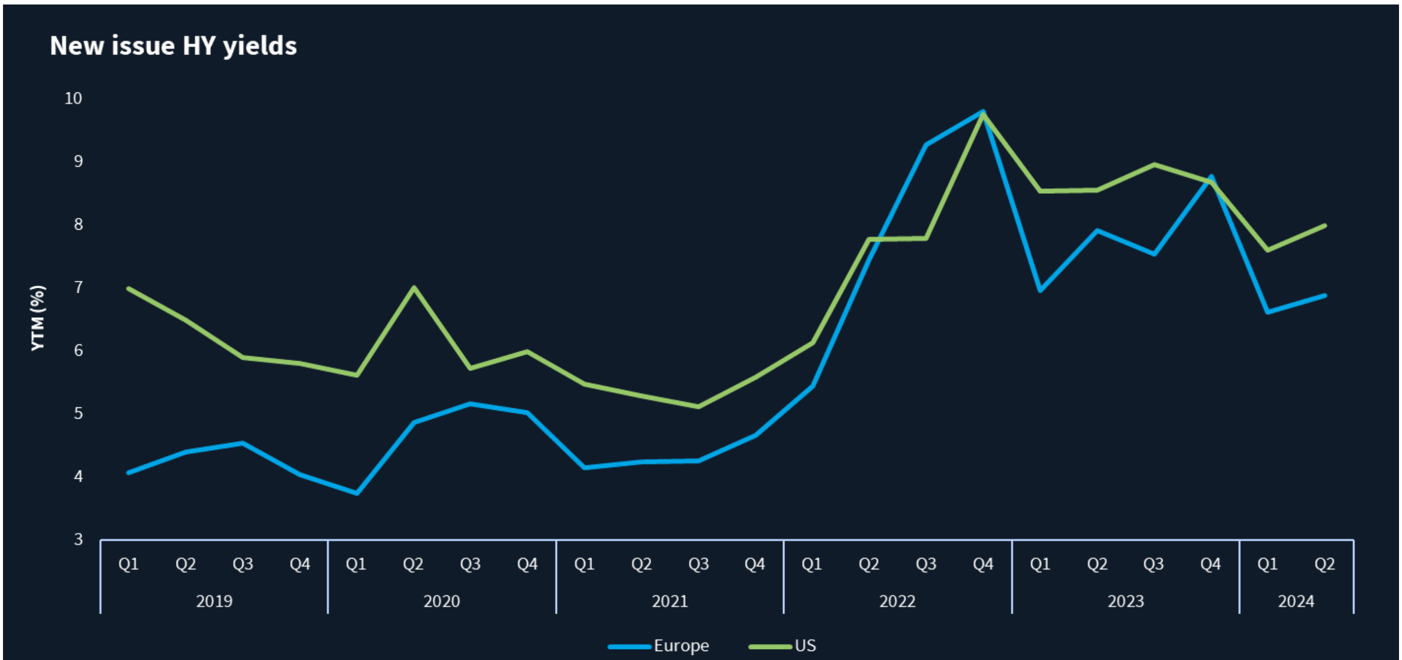
Margins continue to tighten

Loan spreads continued to tighten in primary, with the weighted average margin in the US falling to 337bps in 2Q24 from 400bps at the start of the year. In Europe, the average margin fell to 422bps in 2Q24 from 445bps at the end of 2023. Strong demand for loan paper also led to tighter original issue discounts (OIDs).

In the US and European primary HY bond markets, weighted average yields stood at 8% in 2Q24. Yields rose from 7.6% and 6.6%, respectively, in the preceding quarter, as interest-rate-cut expectations started shifting towards a higher-for-longer rate environment amid sticky inflation. Nevertheless, yields were still down from 8.7% in the US and 8.8% in Europe at the start of the year.



Source: Debtwire, data correct as at 1 July

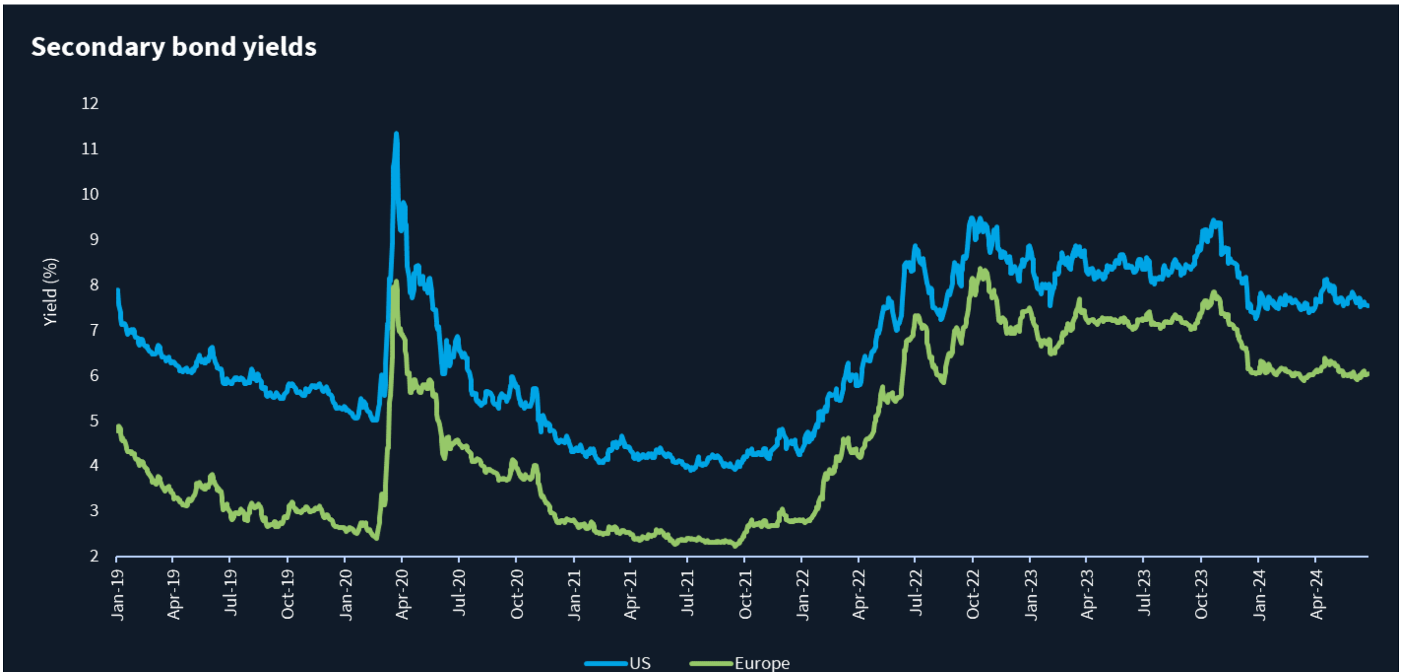


Source: Debtwire, data correct as at 1 July

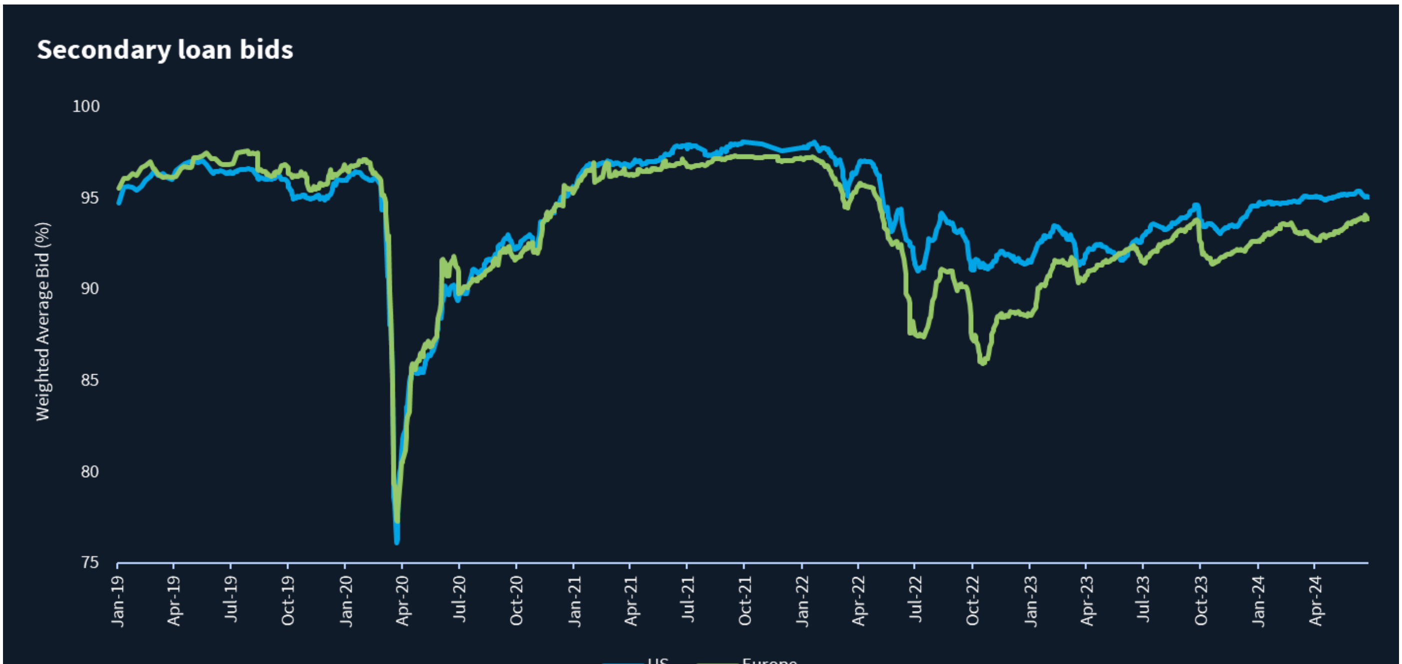
Sense of stability in secondary markets

In secondary HY bond markets, weighted average yields remained largely stable in 1H24, hovering around 7.6% in the US and 6.1% in Europe.

Secondary loan prices tightened from a year ago, with the weighted average loan bid in the US market rising to around 95.1 in June from 94.6 at end-December. In Europe, loans reversed gains made in 1Q24, widening back to 92.6 at the start of April. However, loan bids moved tighter again, reaching a 93.9 high in June.



Source: BofA HY Index, data correct as at 1 July



Source: Markit, data correct as at 1 July

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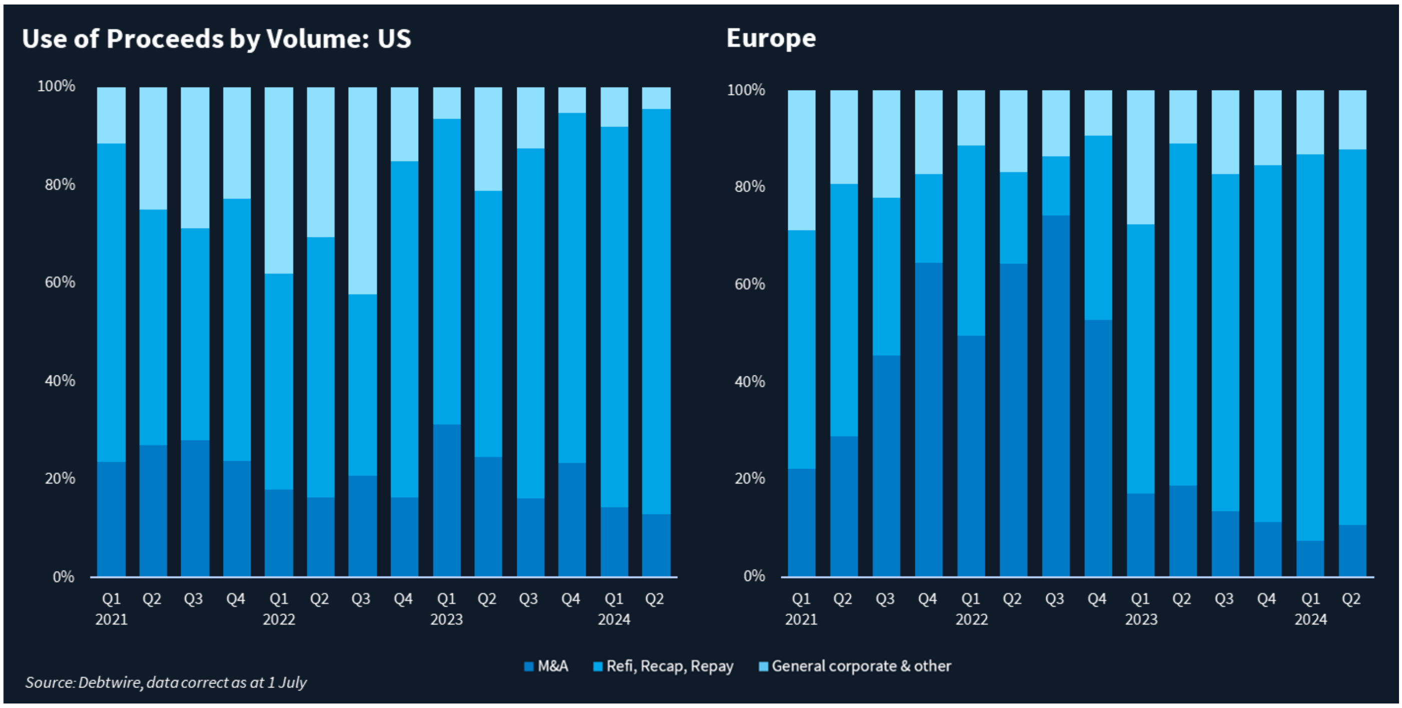
Refinancing and repricing abound

The repricing frenzy was one of the main drivers of loan market activity while refinancing transactions also featured heavily across the LevFin space, but M&A was largely missing in action. Private-equity (PE) sponsors also sought to claw back capital through dividend recaps, particularly when unable to find a buyer for their portfolio company to match their desired valuation.

In the US, refinancing, repayments and recaps totalled USD 698bn, accounting for 80% of total HY bond and institutional loan issuance in 1H24. In contrast, only USD 117bn was raised in M&A/LBO financing, representing only 14% of market volume. Financing for general corporate purposes (GCP) made up the remaining 6%, with USD 53bn raised during the period.

M&A/LBO financing was even more subdued in Europe, with only USD 17bn raised or just 9% of the total. Refinancing, repayments and recaps weighed in with USD 142bn, or 78% of the volume, while USD 23bn was hauled in for GCP financing.



CLO issuance builds momentum for record year

New CLO issuance across both sides of the Atlantic boomed during the first half of the year, reaching USD 98bn in the US and EUR 22bn in Europe. If issuance continues at the same pace in 2H24, it could surpass the record-high 2021 annual volume of USD 183bn in the US and EUR 38bn in Europe.

The asset class saw a surge in demand from a broadening global investor base this year, as the higher-for-longer interest-rate narrative and more benign economic outlook played in its favour at a time when underlying collateral health and loan prices remained broadly constructive.

Meanwhile, spreads continued to tighten on the back of strong investor demand, with benchmark triple-A tranches printing at as low as 138bps in the US and 134bps in Europe at end-2Q24, well below their respective spreads of 188bps and 172bps at the start of the year.

CLO refinancing and reset activity was also buoyant, reaching a total of USD 95bn in the US and EUR 5.35bn in Europe; CLO liquidations also featured. Reissues were absent in Europe in the second quarter, while USD 420m in reissues took place in the US. This followed the USD 430m of CLO reissues in the US and EUR 900m in Europe in 1Q24.

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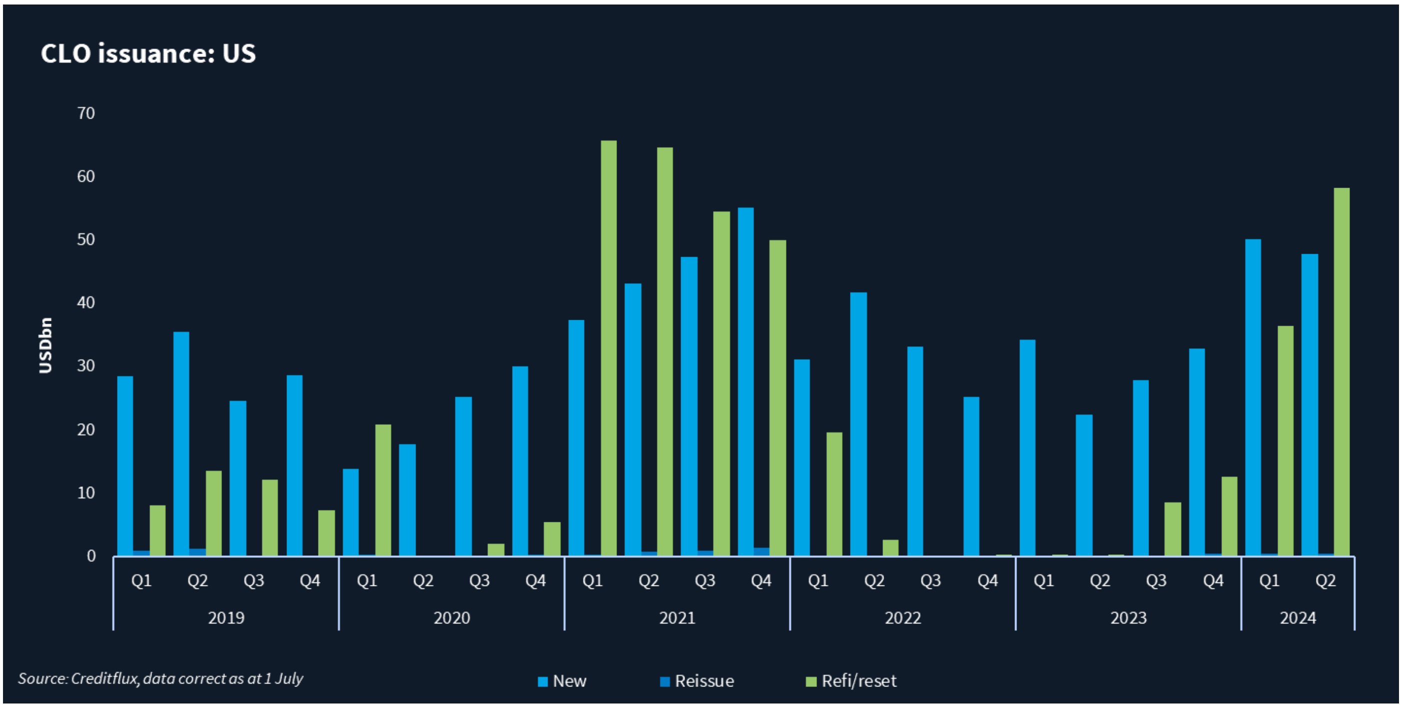

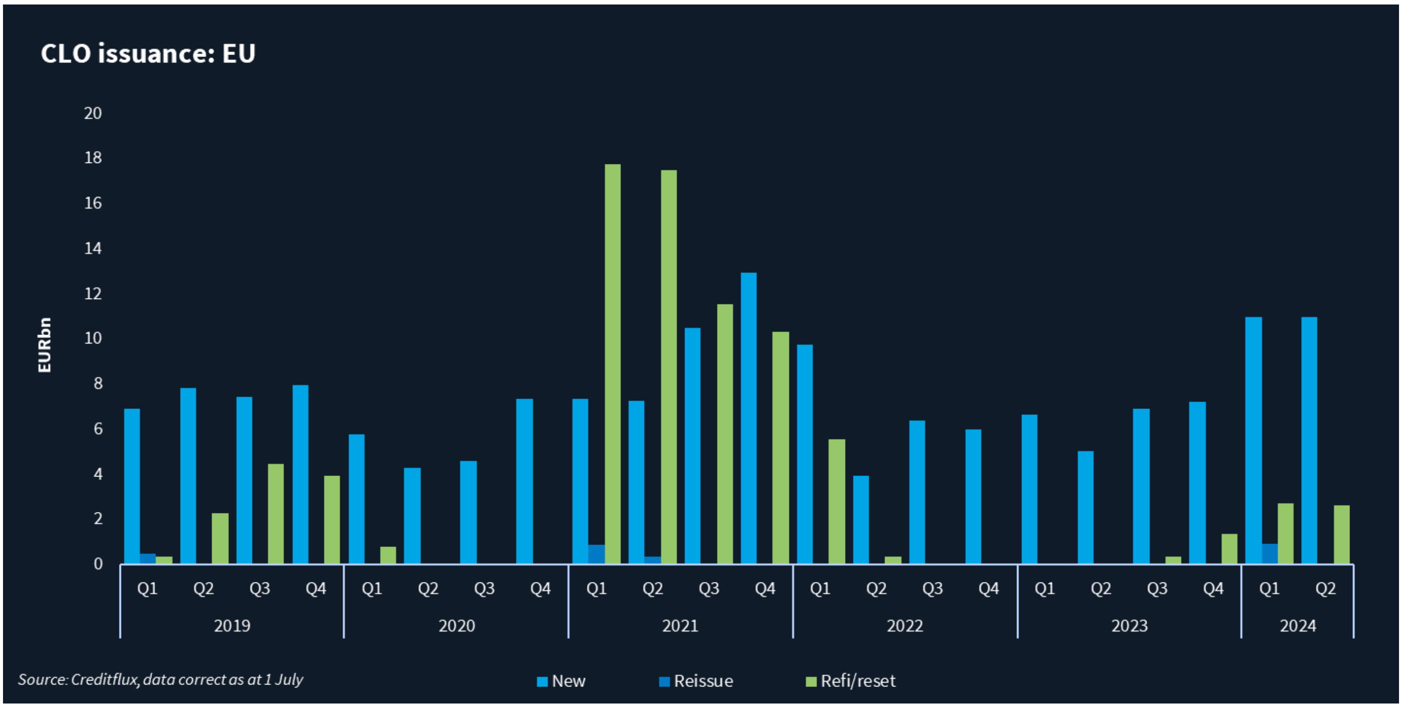

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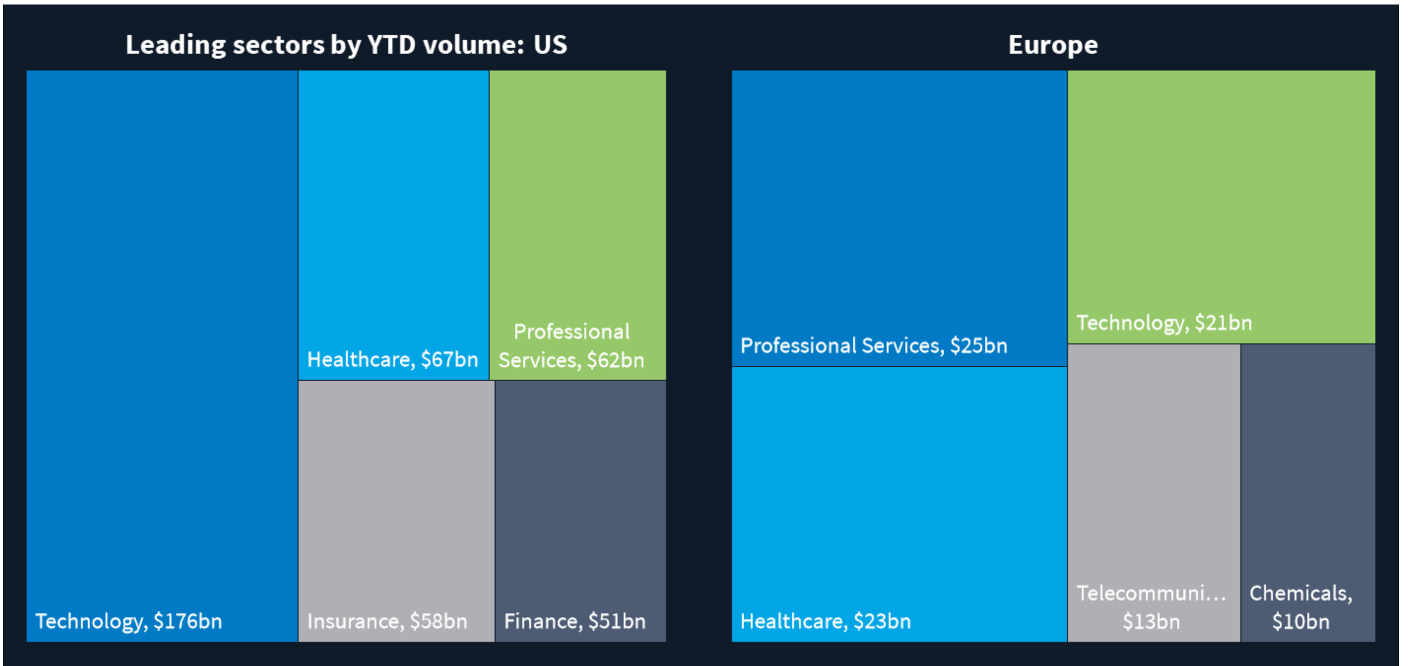
Popular sectors: technology reigns in US, professional services leads in Europe

The technology sector unequivocally dominated the US LevFin market, churning out a total of USD 176bn in 1H24. Healthcare and professional services and followed with USD 67bn and USD 62bn, respectively. The financial and insurance sectors came in fourth and fifth place with volumes of USD 58bn and USD 51bn, respectively.

In Europe, professional services topped the chart with USD 25bn, followed by healthcare and technology with USD 23bn and USD 21bn, respectively. The telecoms sector trailed with USD 13bn, while chemicals hauled in USD 10bn.



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