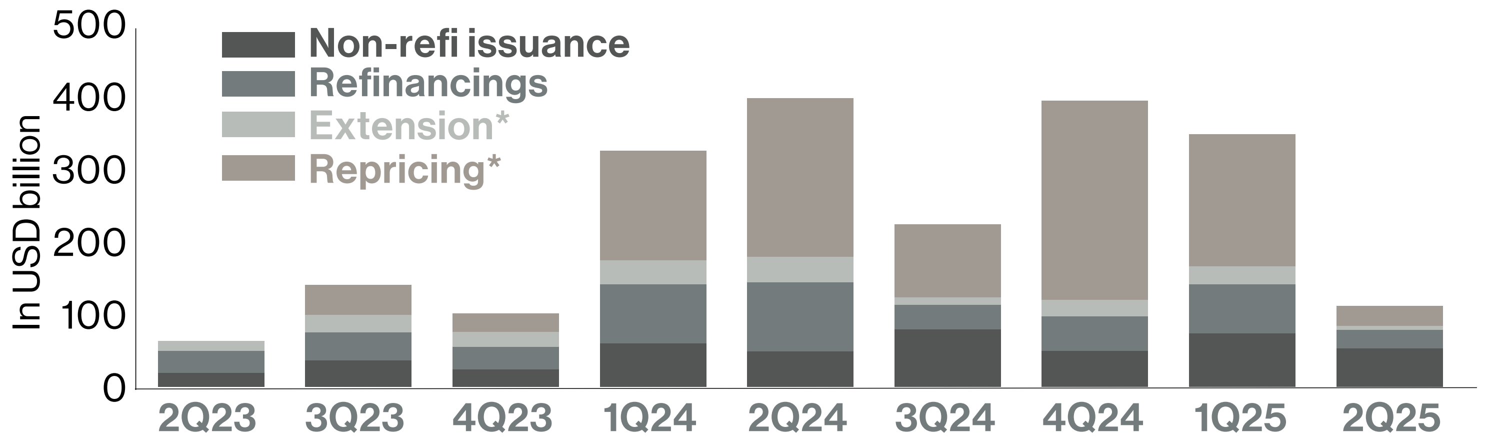
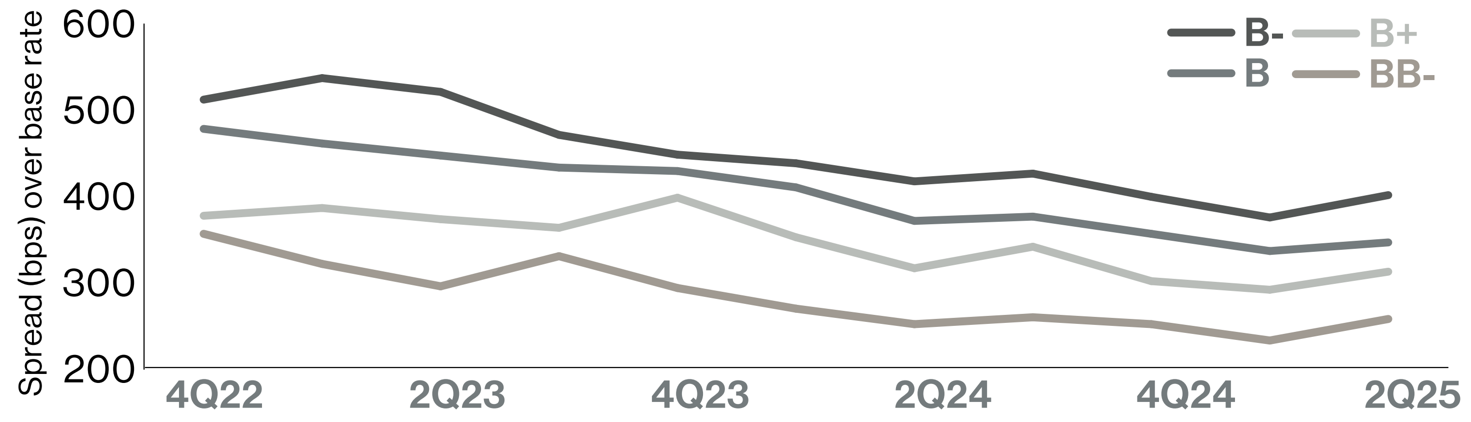
Quarterly Liquid Credit Market Commentary Q2 2025 Issue 24

US new-issue institutional loan volume

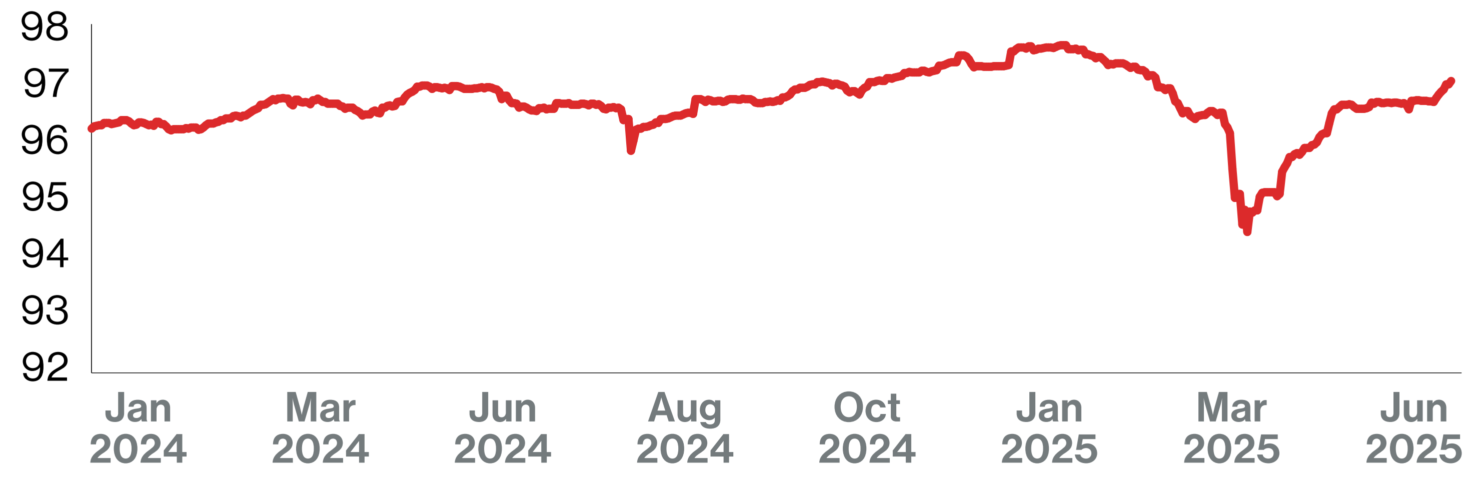


*Reflects extensions and repricings done via amendment process only.

US new-issue loan spreads



US loans index average bid (LLI)



Source: PitchBook | LCD • Data through 30 June 2025. For illustrative purposes only.

US liquid loan market overview

The US liquid loan market once again showed resiliency in Q2 2025, even as capital markets fretted over the uncertainties and implications triggered by the 2 April "Liberation Day" tariff policy announcements as well the Congressional battles over President Trump's tax cut bill. Following a three-week market slide and freeze in new loan issuance activity at the beginning of Q2, investors viewed the tariff moderation news spin from the White House in late April as sufficient reason to return to a buy or risk-on investor sentiment for loans. Secondary loan prices, which fell rapidly in early April, reversed course after the mid-April Easter holidays and improved further through late-June. With the uncertainties of US trade and tax policies looming, M&A activity (the main driver of new US loan volumes) once again struggled in Q2, forcing loan investors to remain focused on secondary markets to deploy cash. Opportunistic loan repricing and refinancings also slipped during Q2, despite their recent momentum in Q1, as loan issuers questioned investor willingness to engage in April and May. Overall, second quarter US loan activity could be best described as underwhelming.

US loan activity

As US tariff and tax policy took centerstage to start Q2, loan investors and issuers initially retreated to the sidelines to spectate. Not surprising, loan activity dropped significantly for the quarter, falling to USD 113.4 billion, compared to the sizeable USD 353.7 billion executed in Q1. Loan repricing activity, which has been the driving force of the loan market for the past year, experienced the biggest decline in activity during Q2, plummeting to USD 28.5 billion, compared to USD 185.6 billion in Q1. New-issue loan volumes disappointed again, totaling just USD 53.3 billion in Q2, down from USD 74.3 billion in Q1.

Other opportunistic transactions such as loan refinancings and maturity extensions also fell notably in Q2, posting just USD 26.4 billion and USD 5.2 billion in volume, respectively, for Q2, compared to USD 69.2 billion and USD 24.6 billion in Q1. Drilling down further into the new loan issuance activity, Q2 could only deliver USD 33.1 billion of LBO and M&A activity, USD 11.4 billion in dividend financings, and USD 8.8 billion of other corporate activity. Lastly, it is worth highlighting that most of the loan activity for the quarter occurred during the month of June, after wider market concerns subsided and investor cash deployment resumed.

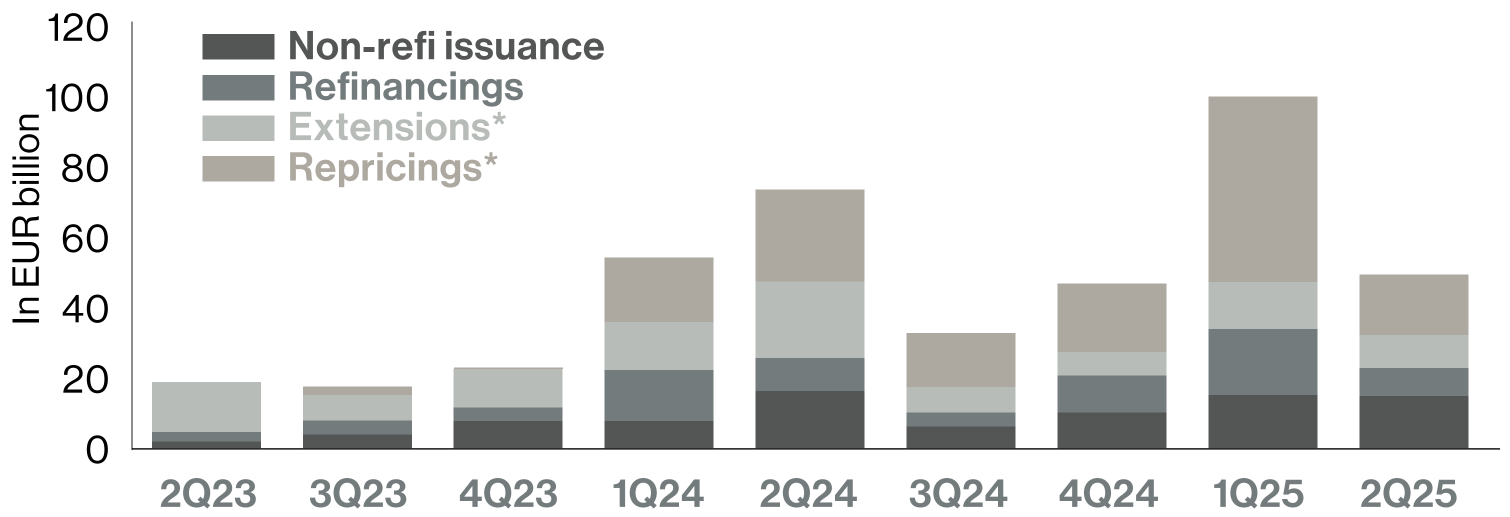
US new-issue loan spreads

Following steadily tightening loan spreads dating back to 2023, the market inertia in April and May forced loan spreads to widen, albeit against a smaller sample size of loans, as volumes declined further. Spreads for new-issue loans rated B and B- climbed to 344bps and 399bps respectively in Q2, compared to 334bps and 373bps in Q1, while spreads for issuers rated BB- and B+ rose to 255bps and 310bps, respectively, in Q2 compared to 230bps and 289bps during Q1. Despite this slight rise in Q2, loan spreads remained near the pre-COVID lows. After investors returned to the primary issuance market in May and June, their growing demand could push spreads even tighter immediately in Q3. It remains to be seen, however, whether this could be a catalyst for greater new-issue loan activity over the second half of the year.

US secondary loan trading

After Q1, secondary loan trading showed the first real signs of price volatility in over a year. Q2 loan bid declines in April reminded the market how quickly prices can drop when demand pulls back unexpectedly. The Morningstar LSTA US Leveraged Loan Index (LLI), which began Q2 at 96.31%, declined sharply after the 2 April "Liberation Day" announcement and slipped 1.90% over nine days before stabilizing near 95.75% by April's end. With new loan issue languishing, investors with building cash balances slowly began to purchase again and the LLI enjoyed a decent bid throughout May, rallying back to the end of Q2 at a respectable 97.07%. While perhaps not really a flight to quality, investors showed stronger bid interest in more familiar loans typically populating the loan index.

European new-issue institutional loan volume



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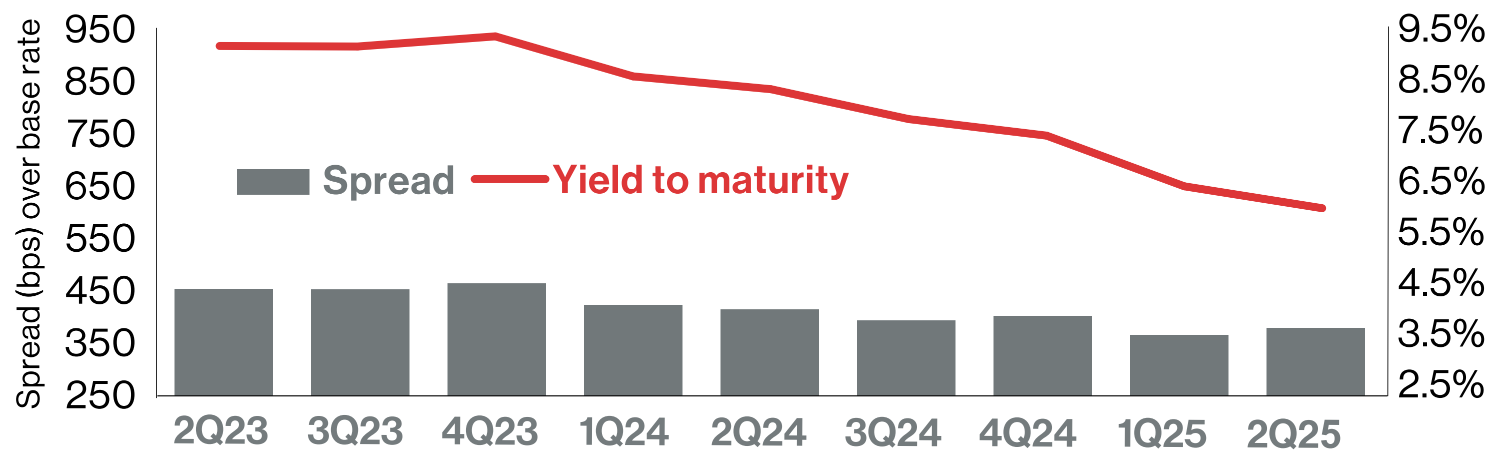
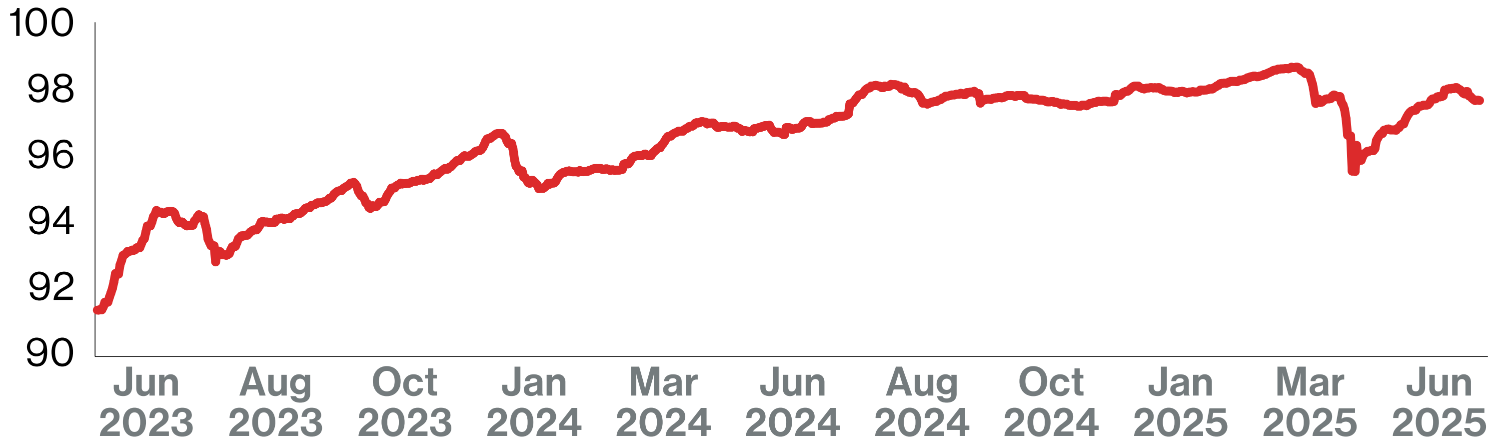
European average new-issue loan spreads and yield



European loan index (ELLI)



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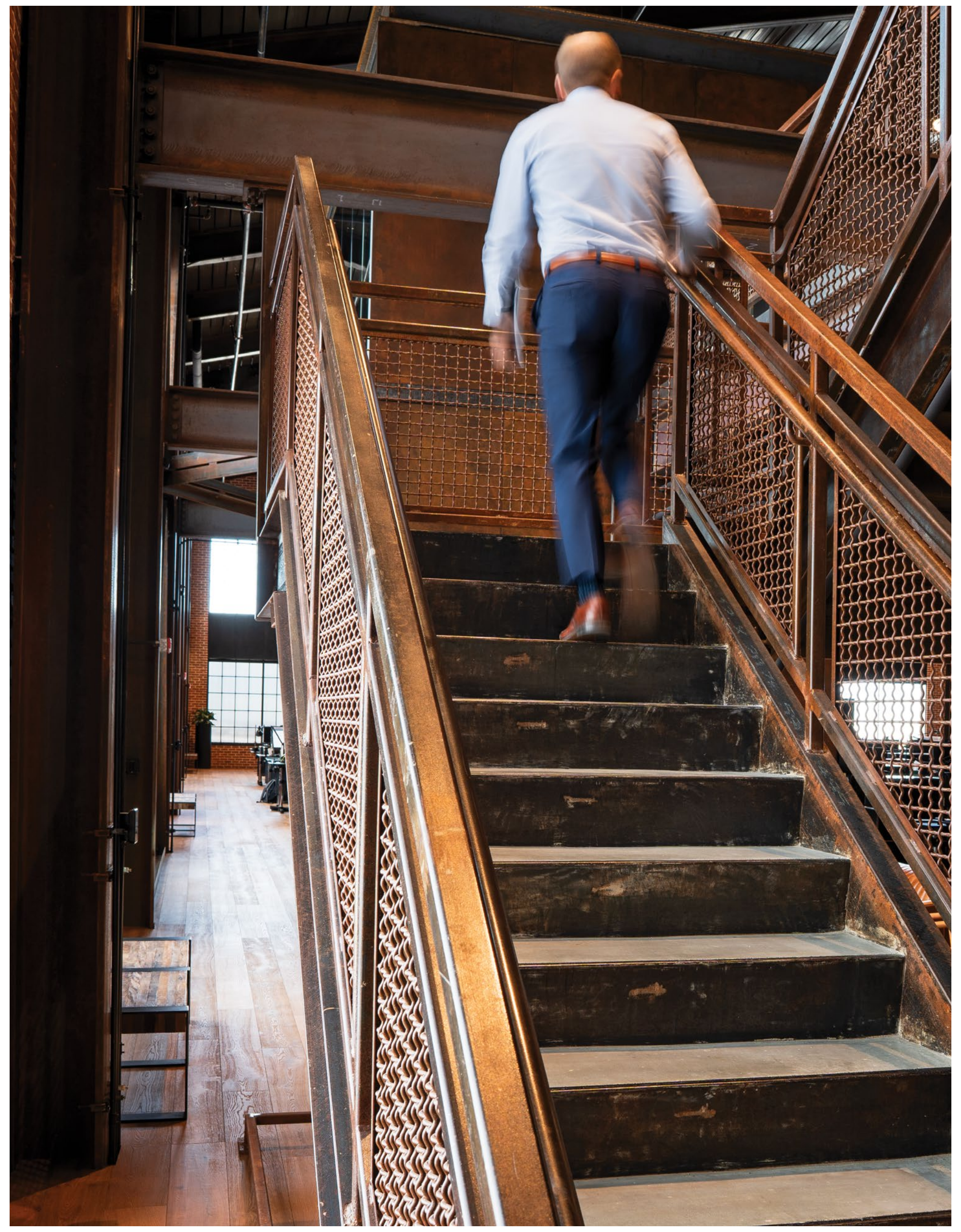
European liquid loan market overview

Following a very constructive first quarter, the promise of continued growth in loan activity was quickly derailed in April by the growing global trade tensions brought on by the "Liberation Day" trade announcements in the US. However, it was not long until market technicals took over, as pent-up investor demand for European loans as well as collateralized loan obligations (CLO) liability tranches, pushed the market quickly from neutral to overdrive. Fueling market demand in Q2 was a growing number of US credit investors seeking higher returns from both Euro loans and CLOs, pushing the supply-demand imbalance wider.



European loan activity

Fresh off record activity posted in Q1 at EUR 99.8 billion, Q2 loan activity slowed considerably (albeit back to more normalized levels) of EUR 49.4 billion, due to the sudden dislocation in the capital markets in early April. Much of the activity for Q2 occurred in the month of June, as the market sprung back to life from an earlier standstill. Looking across the various levels of activity, new-issue loans totaled EUR 20.2 billion in Q2, almost flat compared to EUR 19.0 billion for Q1. Much of the drop in Q2 activity was attributable to the decline in loan repricing amendments, which accounted for only EUR 17.3 billion in Q2 versus EUR 52.6 billion in Q1, demonstrating how important general investor sentiment is to volumes. Also contributing to the Q2 activity decline was a reduction in loan refinancing and maturity extension activity, which totaled just EUR 17.3 billion in Q2, compared to EUR 32.1 billion in Q1.

European new-issue loan spreads

After having declined in seven of the past ten quarters during the latest loan market rally, loan spreads reversed higher in Q2 in response to the April-May market dislocation. Average single B-rated loan spreads rose to 378bps in Q2, compared to 366bps in Q1, but all-in loan yield to maturity for single B-rated loans dropped to 6.07% in Q2 from 6.48% in Q1, driven by two 0.25% European Central Bank rate cuts during the quarter.

European secondary loan trading

With geopolitical news consuming the market's attention in March and April, loan trading opened Q2 on a weaker note, with the Morningstar European Leveraged Loan Index (ELLI) at 97.56% to begin the quarter and then proceeding to drop over 2.00% over nine days in early April, to bottom out at 95.54%, before investors returned to bid up loans in late April, May and much of June, with the ELLI somehow roundtripping for the quarter ending June back at 97.69%.

US collateralized loan obligations

US CLO issuance

While many markets were quieter, if not temporarily frozen during the first several weeks of Q2 as trade and tax battles ensued, US CLOs ignored this noise and continued to string together strong issuance volumes month after month. With cash continually building in both institutional and retail accounts, thanks to new investor deployment and repayments, CLO liability demand continued unabated. New issuance in Q2 rose to USD 51.3 billion from 109 CLOs, the fourth busiest issuance quarter on record. This tally was achieved despite the initial April freeze, topping Q1 activity volume of 97 CLOs and USD 48.6 billion. With continued strong investor demand across all CLO liability tranches, CLO resets and refinancings also garnered investor attention, but certainly not at the same pace as in recent quarters. For Q2, resets totaled USD 44.4 billion, compared to USD 63.9 billion in Q1. However, refinancings fell to USD 8.5 billion, compared to USD 40.9 billion. The decline in CLO reset and refinancing activity in Q2 was attributed to the wider liability spreads prevalent in April and May, which diminished the opportunistic value of these transactions.

US CLO liability spreads

US CLO average coupon and weighted average cost of capital (bps)

Time frame	AAA	AA	A	BBB	BB	WACC
2Q23 (SOFR+)	198	273	336	549	853	259
3Q23 (SOFR+)	187	260	314	495	790	245
4Q23 (SOFR+)	176	256	302	483	786	235
1Q24 (SOFR+)	156	209	254	390	687	205
2Q24 (SOFR+)	149	189	227	344	633	191
3Q24 (SOFR+)	138	172	201	309	612	176
4Q24 (SOFR+)	134	171	195	296	576	169
1Q25 (SOFR+)	119	159	184	279	509	154
2Q25 (SOFR+)	136	181	207	318	604	178
Change from 1Q25	**17**	**22**	**23**	**39**	**95**	**24**
Change from a year ago	**-13**	**-8**	**-20**	**-26**	**-29**	**-13**

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US CLO liability spreads

Q2 saw CLO liability spreads widen for the first time in two years, primarily in initial response to the uncertain trade and fiscal policies being actively negotiated in the media. The weighted average cost of capital (WACC) for US CLOs issued during Q2 increased to 178bps, levels not seen since Q3 2024, and meaningfully higher than the 154bps posted in Q1. During Q2, AAAs CLO liability spreads rose to 136bps, compared to 119bps in Q1.

Spreads on all other CLO liability tranches also widened during the quarter, rising 22bps for CLO liabilities rated AA, to as much as 95bps higher on liabilities rated BB.

US CLO secondary trading

Q2 commenced with heightened volatility, spurred by the announcement of "Liberation Day" tariffs. This development effectively stalled the primary market, while ETF-driven outflows prompted a swift widening of spreads across the capital structure. AAA-rated bonds were trading in the 140-150bps range, and BB-rated bonds were in the 750-800bps range. Volume surged by 40% both year-on-year and quarter-on-quarter, with the bulk of activity concentrated in investment-grade tranches, where most ETFs are invested. Investors and trading desks acted swiftly to capitalize on these wider levels, with demand significantly outpacing the available supply, as investors had growing cash balances from Q1 liquidations and resets.

As volatility quickly abated, the recovery was nearly as rapid as the initial widening. By Q2-end, volumes had returned to the monthly average and spreads on AAA-rated bonds in the secondary market had settled in the mid-110bps.

European collateralized loan obligations

So far 2025 has been very strong for European CLO activity, as investor demand has surged and greatly expanded in scope. The market has also seen a growing influx of US investors, drawn to mezzanine tranches in 2025, to diversify holdings, currency or spreads, even as geopolitical noise has been elevated. Despite the wider spreads, CLO managers have happily seized the opportunity, expanding new issue count, opening additional warehouses and resetting CLOs.

Euro CLO issuance

European CLO new issue volumes totaled EUR 12.7 billion from 31 CLOs in Q2, down from EUR 17.3 billion and 38 CLOs in Q1. Remarkably, almost half of this Q2 new issue volume (EUR 6 billion) was priced between May 26 and June 6, just ahead of the annual Global ABS conference in Barcelona, following the thawing of market conditions after the tariff induced market freeze. Opportunistic CLO reset and refinancing volumes also declined in Q2 to EUR 8.5 billion, compared to EUR 12.1 billion in Q1, as liability spreads widened.

Euro CLO liability spreads

With the increase in total CLO issuance supply in 2025, plus the recent market turmoil during April-May, Euro CLO liabilities spreads logically widened across all ratings classes. For Q2, WACC for new European CLOs widened to 198bps, from 184bps in Q1. CLO AAA average liability spreads increased to 131bps in Q2, from 121bps in Q1, while average spreads on other liability tranches increased by as little as 12bps for AAs, to as much as 85bps for BBs in Q2. Like in the US, the market signaled that it was open for business and ready to transact in volume, but wider liability spreads were necessary after hitting recent lows in Q1.

Euro CLO secondary trading

As the volatility from the "Liberation Day" announcement rippled through the Euro markets, bids wanted in competition (BWIC) activity in the European CLOs secondary market remained subdued, declining 8% quarter-on-quarter. In the absence of forced liquidations, whether from ETF outflows or margin calls, only a limited number of bonds changed hands. During this period, spreads widened by 25-50bps for the investment-grade parts of the structure and by 100-200bps for sub-investment-grade bonds. AAA-rated bonds saw the most activity due to their high cash prices and superior liquidity, with both real-money and fast-money investors moving down the capital structure to capture discounted prices. As volatility eased, the market rallied back swiftly, ending Q2 largely unchanged compared to the end of Q1, although still wider than year-to-date lows.

Euro CLO liability spreads

Euro CLO average coupon and weighted average cost of capital (bps)

Time frame	AAA	AA	A	BBB	BB	WACC
2Q23 (E+)	191	321	410	618	793	296
3Q23 (E+)	174	256	336	513	733	263
4Q23 (E+)	172	266	357	560	789	266
1Q24 (E+)	149	224	276	407	674	227
2Q24 (E+)	146	211	263	377	663	222
3Q24 (E+)	129	194	228	328	614	200
4Q24 (E+)	129	203	244	343	613	206
1Q25 (E+)	121	175	214	298	498	184
2Q25 (E+)	131	187	229	320	583	198
Change from 1Q25	**10**	**12**	**15**	**22**	**85**	**14**
Change from a year ago	**-15**	**-23**	**-34**	**-57**	**-79**	**-24**

Source: PitchBook | LCD • Data through 30 June 2025. For illustrative purposes only.

Spotlight topic:
It's the basic ABCs: Always Be CLOsing

With the uncertainties presented by evolving global trade battles, as well as a major US tax cut bill being passed, it remains remarkable that CLOs, as an asset class, continue to thrive and further expand their market size in the face of such headwinds. New CLO issuance is dependent on not just sufficient supply of loans as asset collateral, but enough liability investor demand to buy at the current spreads on offer, even though CLOs have a shorter issuance history and lower trading liquidity as an asset class. But as corporate credit fundamentals improved over the past 12 months, strengthening the credit risk profiles of collateral assets held by CLOs, additional institutional and retail investor cash has been deployed in this segment. The phenomenal yearly growth and returns for global CLOs can no longer be ignored by diversified investors, even in the face of challenging market conditions. It all reminds us of the adage: the heart wants what it wants. In this instance, it seems the hearts of many investors want more CLOs.

About the author

Mark Hanslin is a Managing Director & Senior Portfolio Manager who leads Partners Group's Liquid Credit team in New York. He has over three decades of liquid credit underwriting, investment and portfolio management experience for global corporate banks and investment management companies.

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