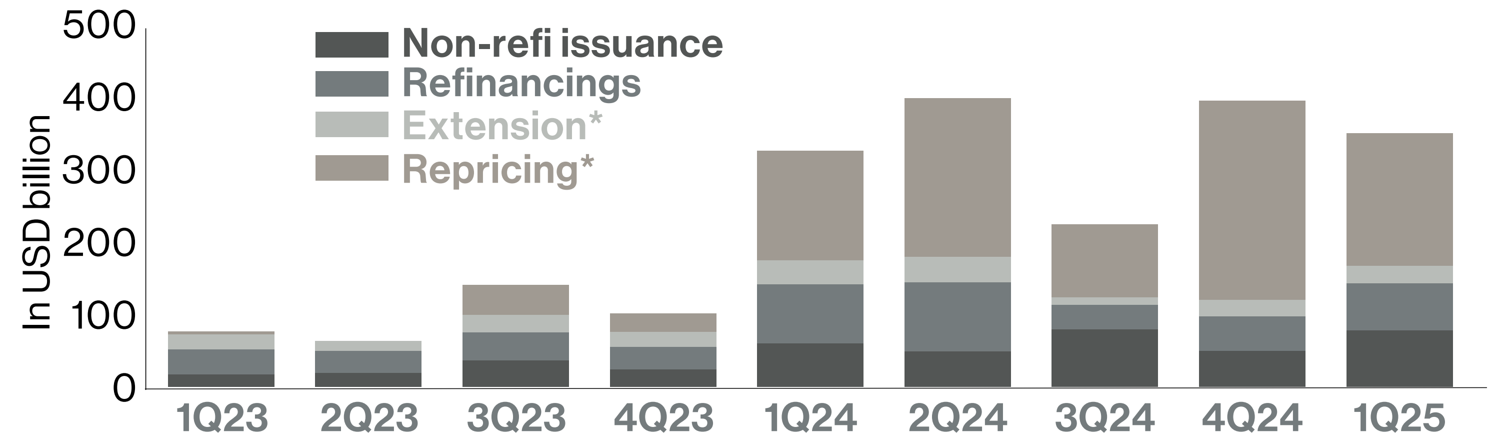
PARTNERS GROUP

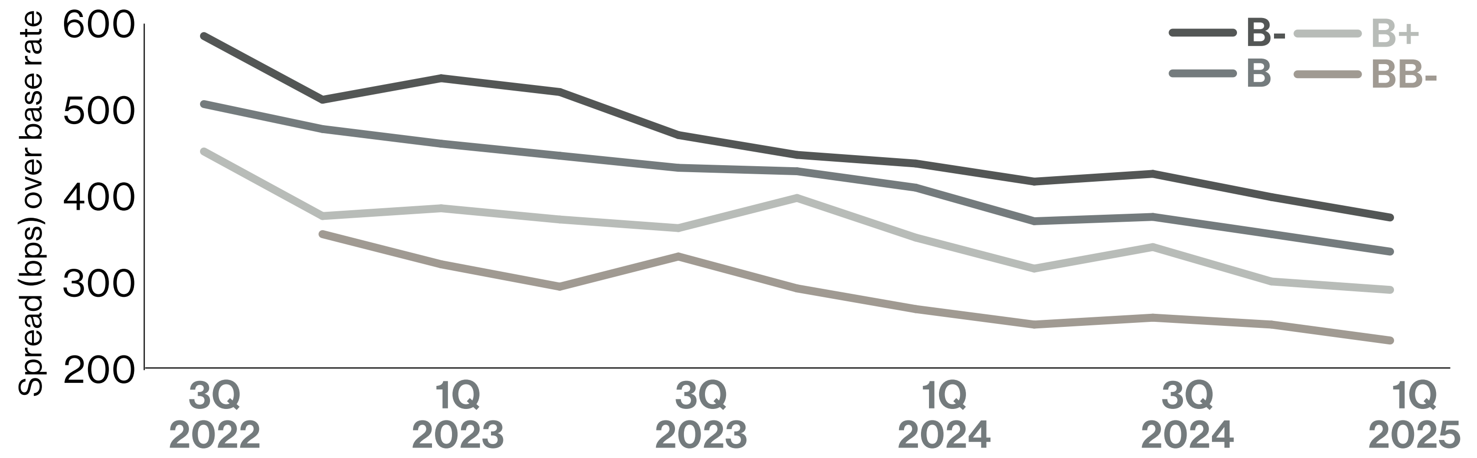
Quarterly Liquid Credit Market Commentary Q1 2025 Issue 23

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 31 March 2025. For illustrative purposes only.

US liquid loan market overview

Q1 2025 began right where Q4 2024 left off: unrelenting demand for loan assets by both institutional and retail investors keeping secondary pricing levels strong and new-issue loan syndications oversubscribed. And despite higher new-issue volumes creating more loan supply, investors were confronted with another wave of loan repricing amendments during January and February. But unlike recent quarters in 2024, this latest loan repricing surge lost steam in mid-February, as investors became increasingly concerned about the adverse impacts of potential US trade and fiscal policy changes being discussed in Washington, resulting in a sudden risk-off investor response in March.

Several loan repricing attempts were then withdrawn, while other new loan syndications had to flex spreads higher to lock in full subscription. At the same time, the long run of active collateralized loan obligations (CLO) new issuance and resets coming at tighter liability spreads came to a halt towards March-end, and liability spreads began widening quickly for each following issuance. Just like that, the 18-month long US loan and CLO rally ended.

US loan activity

Despite the market shifting to a lower gear by quarter-end, Q1 2025 was still busy with new-issue loan activity, thanks to the strong monthly volumes posted during January – the busiest month of loan activity on record, easily topping the recent high mark from December 2024. Q1 delivered USD 354.6 billion of loan transaction volumes when including repricings, not far from the impressive USD 400.5 billion posted in Q4 2024 or USD 403.8 billion from Q2 2024. The biggest story for the quarter was loan repricing activity, which totaled USD 185.6 billion, compared to USD 278.8 billion in Q4. When aggregating the repricing activity since January 2024, the market has seen an incredible USD 788 billion of loans repriced during a 15-month window, effectively half of the total institutional loan market outstandings of USD 1.45 trillion.

Away from these impressive repricing volumes, loan refinancings, maturity extensions and new issuance contributed USD 65.4 billion, USD 24.6 billion, and USD 79.1 billion to Q1 2025, respectively. This was a notable increase from the USD 48.5 billion, USD 23.3 billion and USD 49.9 billion, respectively, in Q4 2024. The clear takeaway from Q1 was that the US loan market had just experienced its greatest 12-18-month period of total loan activity on record before the reversal in mid-March.

Upon focusing on new loan issuance activity, Q1 2025 saw speculative-grade borrowers issue USD 52 billion of institutional term loans, led by USD 24.9 billion of LBOs, USD 13.7 billion from private equity-led term loan add-ons, and USD 13.3 billion of corporate M&A loans. This total compared quite favorably to the USD 28 billion tally in Q4 2024, where LBOs added just USD 8 billion, term loan add-ons were USD 14.4 billion and corporate M&A was USD 5.7 billion. While not close to what the US market enjoyed back in 2018, 2019 or 2021, the Q1 2025 increase in new-issue loan volumes was a positive development for a market starved for loan supply.

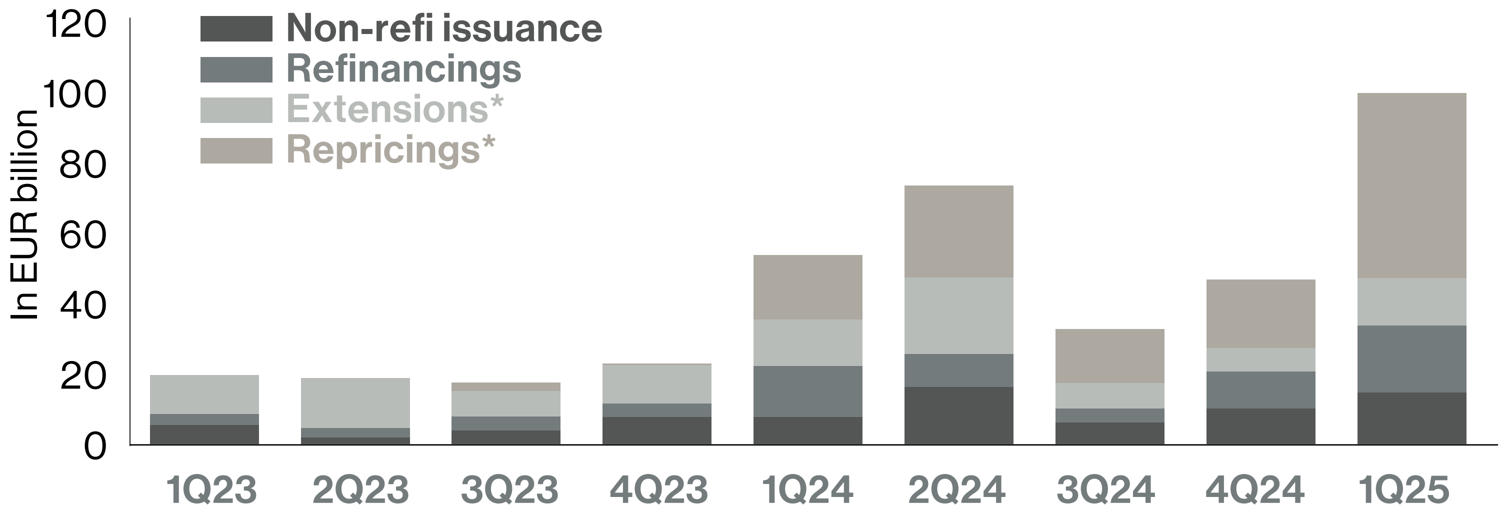
US new-issue loan spreads

Strong US investor demand for loan assets at the start of the year led spreads of new-issue loans rated B and B- to touch a five-year low in January at SOFR+313bps and SOFR+363bps, respectively. For the full quarter, Q1 spreads for new-issue loans rated B and B- averaged S+333bps and S+373bps, respectively, compared to S+354bps and S+397bps in Q4 2024. Meanwhile issuers rated BB- and B+ dipped to S+231bps and S+289bps in Q1, compared to S+249bps and S+299bps in Q4, as certain investors also bid up for credit quality. However, with loan activity slowing at quarter-end, spread tightening trends reversed for all ratings categories, as investors became more risk-averse.

US secondary loan trading

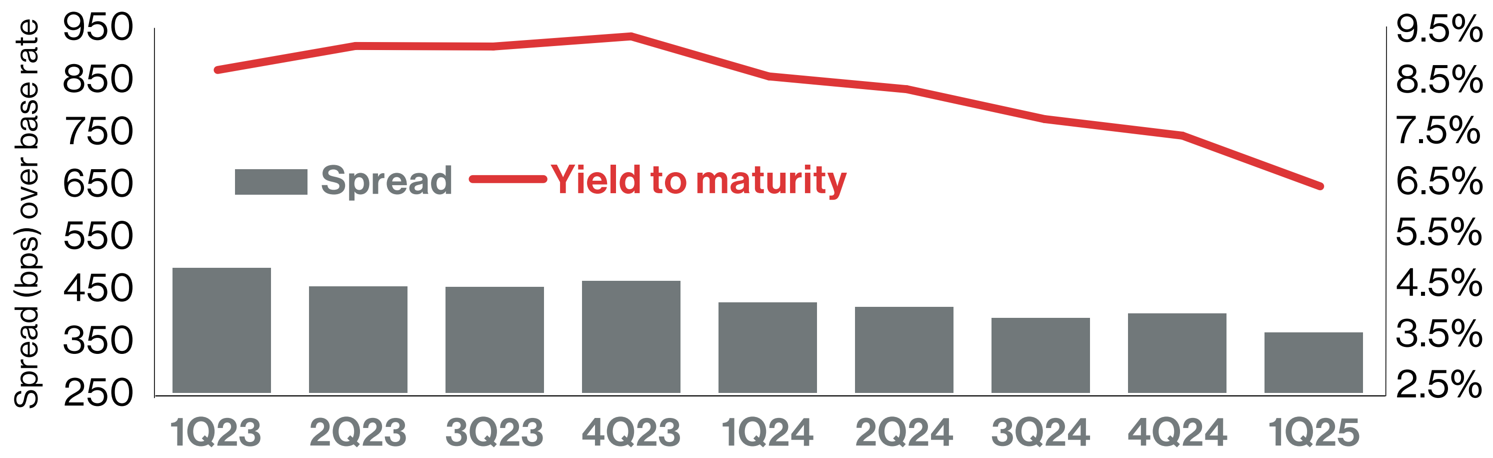
Following a steady rise in US secondary loan trading levels over the past 18 months, Q1 2025 finally saw bids slip starting in late March. The Morningstar LSTA US Leveraged Loan Index (LLI) opened the quarter at 97.33%, peaked in late January at 97.70%, and slowly declined throughout February and March, ending Q1 down at 96.31%. This price decline reduced loan returns for Q1 2025 down to 0.48%, the weakest quarter posted in the US since 2022.

European new-issue institutional loan volume

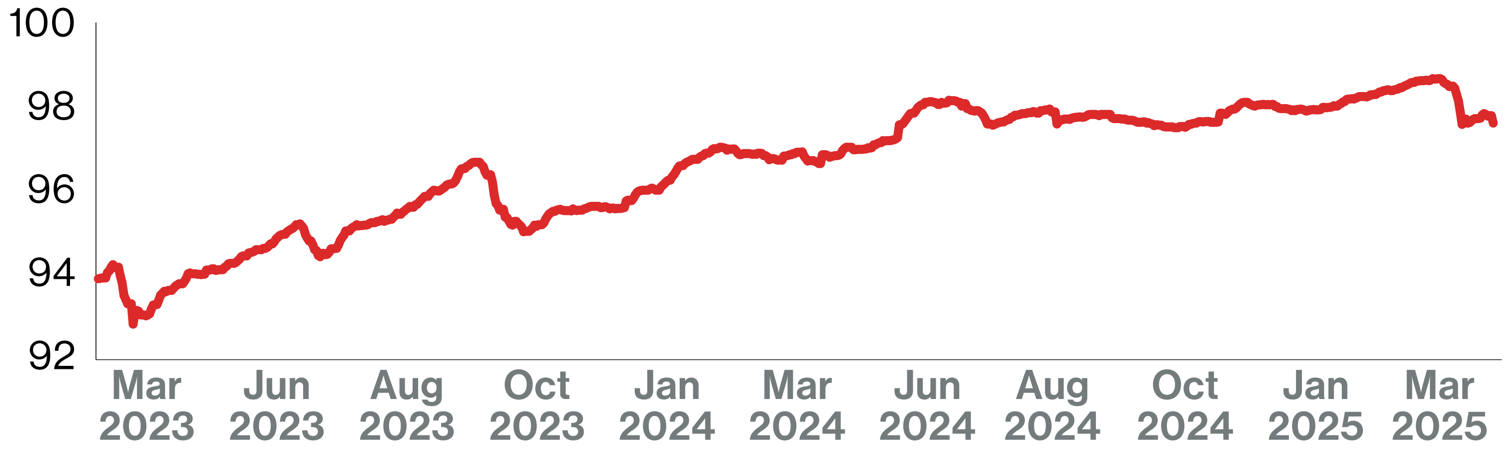


**Reflects extensions and repricings done via amendment process only.*

European average new-issue loan spreads and yield



European loan index (ELLI)



Source: PitchBook | LCD • Data through 31 March 2025. For illustrative purposes only.

European liquid loan market overview

While the European loan market typically takes time to ramp up activity at the new year, Q1 2025 proved to be an exception. The continuation of the strong loan investor demand from Q4 carried into 2025. New CLOs continued to issue, institutional investment vehicles raised cash and the M&A market once again failed to fuel new loan supply, all driving market bids during January. This environment also helped accelerate the pace of loan repricings and maturity extension requests, creating one of the strongest quarters of loan activity seen in Europe since 2007 (pre-GFC). But as in the US, European sentiment began to weaken in March as investors turned focus onto global economic conditions and evolving global trade policies. Loan bids receded, CLO issuance declined, and like in the US, the loan and CLO rally in Europe was over by quarter-end.

European loan activity

European loan activity for Q1 2025 surprised many, totaling a record-breaking EUR 99.8 billion, nearly double the Q4 2024 levels of EUR 46.7 billion. Much of this activity was attributable to a constant string of loan repricings during the first half of Q1, totaling EUR 52.6 billion. This amount was more than double the highest loan repricing volume previously observed in any quarter and well above the EUR 19.4 billion of loans repriced during a busy Q4 2024. The average loan spread reduction from these loan repricings was 65bps during Q1. Loan maturity extensions also contributed EUR 13.4 billion, while refinancings added EUR 19 billion. New-loan issue volumes for Q1 were at EUR 14.7 billion, resulting mostly from a pickup in LBO and dividend recapitalization activity. This led to the second highest quarterly volumes posted since the COVID rebound year 2021.

European new-issue loan spreads

With persistent investor demand for new-issue loans in Q1, combined with a slow M&A environment which did not generate sufficient new loans, investors reluctantly accepted tightening loan spreads for both new-issue and repricing requests in order to keep funds invested.

The average loan spread for a typical loan with a B rating dropped to 366bps in Q1, from 401bps in Q4 2024. This loan spread level in Q1 was the lowest observed in the European market since 2007. On a yield-to-maturity basis, loans with a B rating were now paying 6.48% in Q1, compared to 7.43% in Q4, reflecting both a decline in loan spreads, as well as falling Euribor base rates over the quarter.

European secondary loan trading

European loan trading started off Q1 2025 quite strong, reflecting continued pent-up investor demand and a weak supply of new loans. This rally persisted into March, when investors became preoccupied by rising global trade tensions and policy uncertainties. Rattled by this market noise, investors began retreating to re-assess and reposition. The Morningstar European Leveraged Loan Index (ELLI), which had opened Q1 at 98.01%, advanced consistently week after week peaking in early March at 98.70% (with 69% of ELLI loans bid above par). But from that point on, trading weakness took over dropping the ELLI over 1.00% (the largest two-week price decline recorded in the past 20 years) leaving the ELLI to finish Q1 at 97.63%. The total year-to-date 2025 return for the ELLI slipped to 1.08%, falling well behind the returns posted in 2023 and 2024.

US collateralized loan obligations

US CLO issuance

Following record-breaking CLO activity in 2024, investors would not have been surprised if the market took a pause at the start of the new year. But like loans, US CLO activity started 2025 without missing a beat, resulting in an impressive USD 48.6 billion of new-issue volume from 97 CLOs. Despite being behind the Q4 2024 issuance levels of USD 59.5 billion and 123 transactions, this Q1 volume matched CLO issuance in Q1 2024 of USD 48.8 billion. The drivers for the Q1 CLO issuance volume continued to be: i) a steady balance of cash to invest or redeploy into CLO liabilities by both institutional and retail (ETFs) investors; ii) appealing secondary loan prices for loan collateral, which help achieve sufficient CLO equity arbitrage; and iii) CLO-liability spreads, which touched recent market lows during the quarter. CLO managers were keen to lock in these low liability spreads, knowing that spreads could quickly widen out on short notice. Beyond this new-issuance activity, CLO reset and refinancings also posted healthy volumes during Q1, with resets totaling USD 63 billion and refinancings adding USD 41 billion, comparable to the USD 80 billion and USD 24 billion, respectively, realized in Q4 2024.

US CLO liability spreads

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

Time frame	AAA	AA	A	BBB	BB	WACC
1Q23 (SOFR+)	196	261	335	541	825	261
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	577	169
1Q25 (SOFR+)	119	159	185	281	511	154
Change from 4Q24	-15	-12	-10	-15	-67	-15
Change from a year ago	-37	-50	-69	-108	-177	-51

Source: PitchBook | LCD • Data through 31 March 2025. For illustrative purposes only.

US CLO liability spreads

CLO liability spreads tightened for the seventh consecutive quarter in Q1, as investor demand for CLO liabilities from both repayments and new cash deployment remained the catalyst. The weighted average cost of capital (WACC) for US CLOs during Q1 dropped to 154bps, compared to 169bps in Q4, and was a remarkable 51bps lower than the 205bps WACC observed a year ago in Q1 2024, highlighting the magnitude of spread tightening in the past year. During Q1, AAA CLO-liability spreads tightened to 119bps, compared to 134bps in Q4, and 156bps a year previous in Q1 2024. Spreads on other CLO-liability tranches also saw further tightening in the quarter, from 10bps lower for CLO-liabilities rated A, to 67bps lower for liabilities rated BB.

US CLO secondary trading

The year began with an exceptionally busy primary CLO issuance pipeline, capturing the market participants' attention. The limited activity in the secondary market, coupled with increasing demand from CLO ETFs, led to a further decrease in the already negative spreads between primary and secondary bonds. However, sentiment shifted dramatically as increased volatility crept into the market by the end of March, resulting in heightened activity in secondary trading and a rapid widening of spreads. By the end of the quarter, volumes were up 22% year-on-year and 27% quarter-on-quarter, with spreads widening by 20bps for AAA-rated bonds and 125bps for BB-rated bonds. Trades were focused on the higher rated part of the liability structure, given the higher dollar price, leading to a widening relative to the primary market. Despite the rising volatility and concerns around CLO ETF flows, the secondary trading market continued to function well, with strong demand at the wider levels from both real money and fast money investors.

European collateralized loan obligations

Following record-setting volumes in 2024, expectations of an equally strong 2025 for CLO issuance were widely held. With growing investor cash balances from repayments, as well as new cash for deployment (especially from ETFs), market participants did not wait long for the European CLO market to resume issuance activity in Q1. New-issue volumes were brisk out of the box in early January and during much of the quarter, although resets fell slightly behind a busy Q4.

Euro CLO issuance

New issue delivered EUR 17.3 billion of volume from 38 CLOs in Q1, besting the EUR 13.1 billion from 31 CLOs in Q4. This Q1 2025 volume is the largest the European market has recorded during any first quarter and has already delivered over one-third of the market's estimated EUR 50 billion of annual CLO volumes for 2025. While CLO reset activity also continued in Q1, volumes came in slightly lower, at EUR 11 billion versus EUR 13.6 billion posted in Q4. Lastly, CLO refinancings contributed EUR 1.2 billion to Q1 activity, improving on the EUR 0.7 billion delivered in Q4.

Euro CLO liability spreads

With the active flow of issuance in Q1, especially in January and February before both loan and CLO investment demand slipped, CLO liability spreads tightened from the already recent lows posted in Q4. European CLO WACC in Q1 tightened to 184bps, from 206bps in Q4. Q1 saw AAA spreads drop to 121bps, compared to 129bps in Q4. Spreads for liability tranches rated between AA and B all tightened during Q1, from 27bps for AA-rated tranches, to as much as 114bps for BB-rated tranches. Even as strong as Q1 was, there was eventually a widening of spreads in the last several weeks of March, consistent with the softer investor conviction for loans (and other credit products), as the quarter came to a close.

Euro CLO secondary trading

The first two months of 2025 were marked by the busiest primary CLO issuance volume on record, accompanied by a busy secondary market. Despite the high volumes, liability spreads continued to tighten, following the broader credit markets. The relatively high yields attracted new accounts to the market, pushing lower-rated CLO bonds routinely above par and spreads into the mid-400s.

As volatility began to rise in March, the secondary market remained active, with volumes ending Q1 up 54% quarter-on-quarter and down 15% year-on-year, and spreads 15-20bps wider at the top of the stack and 175-200bps wider at the bottom.

Euro CLO liability spreads

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

Time frame	AAA	AA	A	BBB	BB	WACC
1Q23 (E+)	180	297	394	577	728	275
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	176	214	298	498	184
Change from 4Q24	-8	-27	-29	-45	-114	-23
Change from a year ago	-28	-48	-62	-109	-176	-43

Source: PitchBook | LCD • Data through 31 March 2025. For illustrative purposes only.

Spotlight topic:

M&A activity – Green shoots or more of the same?

Following the start of the US rate-cut cycle, the taming of inflation and improved economic conditions in the second half of 2024, loan market participants have anxiously sought signs that the long dormant M&A and LBO cycle could finally pick up during 2025. After all, private equity sponsors have been sitting on many portfolio companies which they wish to sell and realize gains for their investors, while also possessing significant amounts of investible capital (i.e., 'dry powder') ready to be deployed into new investment opportunities. For the loan market, M&A and LBO activity is the lifeblood of new-issue loan supply, and this activity has been woefully inadequate for years. With Q1 now in the books, how has M&A responded so far? The first quarter of 2025 saw a near 50% pickup in M&A-related US loan volume, with activity spread across LBOs, private equity-sponsored term loan add-ons and corporate M&A bolstering investor sentiment and expectations. But even with this pickup in volume, the evolving macroeconomic conditions, uncertainties related to global trade, fiscal policies, interest rates, and investor conviction will ultimately determine how sustainable M&A growth can be this year.

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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