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2025: Positive returns, yet below expectations as asset dispersion widens and coupons reprice – Coupon carry holds, credit selection poised to drive 2026 outside market tail risks

MANDATUM

Another year of repricings and extensions

European leveraged finance issuance continued to strengthen in 2025, following the strong recovery in 2024. Leveraged loan and high-yield (HY) issuance grew by 16% and 27%, respectively, with both markets contributing half of the €250bn total volume – just shy of the €255bn record set in 2021. The €125bn of new loan issuance was split quite similarly to 2024: 46% refinancings, 34% new M&A, and 20% recapitalisations. Notably the latter – dividend transactions – accelerated as anticipated, with both the relative share and absolute volume reaching recent highs, underscoring supportive market conditions and heightened sponsor focus on returning capital.

2025 marked another year of repricings and extensions, adding significantly to overall volumes noted above. Repricings, unfortunately, reached a new record at €109bn, up from €79bn in 2024, covering nearly one-third of the index, and combined with last year, almost 60%. After two hectic years of maturity extensions (>€40bn p.a.), amend-and-extend transactions (A&Es) printed another €45bn, meaning A&Es have reset over 40% of the index during the last three years.

New LBOs, the key driver of new loan supply, continued to recover, and with €25bn printed, buyouts are now at least a bit closer to past averages. However, relatively speaking contribution remains subdued: In 2023-2025 LBOs accounted for only 15-20% of annual loan issuance, or 3-7% of the ELLI index* volume, well below 2016-2022 averages (34% and 16% respectively). Combined with record high CLO issuance, market continues to face a persistent undersupply of new assets.

2025 gross return softer than expected

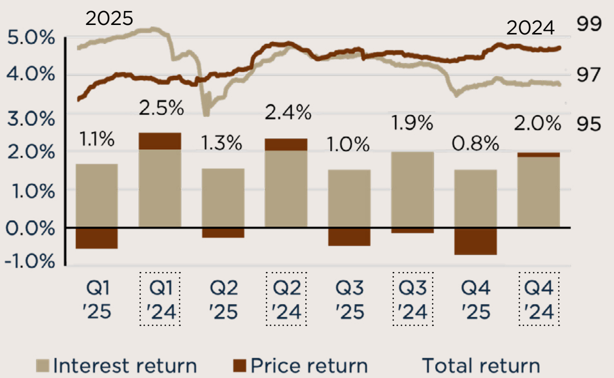
In our last year's white paper[1], we projected favourable conditions for EUR leveraged loans in 2025, supported by an estimated >6% coupon carry at an average base rate of 2.2% and a margin of around 4%. The year ultimately delivered a total return of 4.1%, driven by an interest carry of 6.4% at an average 2.2% base rate, but offset by meaningful price consolidation of -2.0%. Unlike 2024, which posted uninterrupted positive monthly gross returns and a price gain of 0.7%, 2025 saw a few periods of weakness – most notably in March-April around Liberation Day, and to a lesser extent, in October. Ultimately, each quarter ended in slightly negative price return (Table 1), which combined with relentless repricing and consequent spread erosion, contributed to the shortfall relative to our expectations.

After four consecutive years of EUR loans outperforming EUR HY** by a cumulative 14.5ppts, EUR HY narrowed the gap to 13.9ppts in 2025, grossing 5.1% for the year (see Table 8).

Aside from brief uncertainty and some spread decompression in March-April, risk compensation remained tight throughout 2025. This was a possibility given the persistent supply-demand imbalances. Primary spreads compressed to an average of 377bps for the year (vs 467 bps average in 2019-2025, excluding the Euribor floor benefit). For the broader market, favourable conditions and repricing activity reduced the index composite margin by c 30bps to ~370bps. However, on discount margin basis, aggregate price softness left the year roughly flat at c 450bps (Table 2).

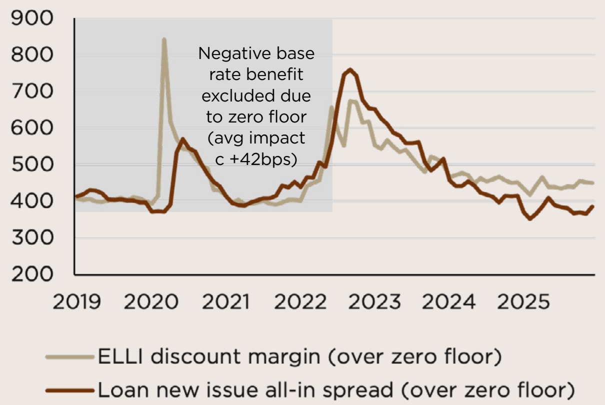
1. Return by component (2025 vs 2024)

ELLI index quarterly return (%) and average price



2. Loan credit spreads (2019-2025)

Credit spreads, basis points over zero floor



1) https://www.mandatumam.com/48e6ba/globalassets/mam/pdf/mam_leveraged_finance_whitepaper_0125_eng.pdf
*) Morningstar European Leveraged Loan Index "ELLI"). Source: Bloomberg, PitchBook Data Inc, ICE BofA. **) ICE BofA bond indices

Underlying fundamentals seem solid but increasingly bifurcated

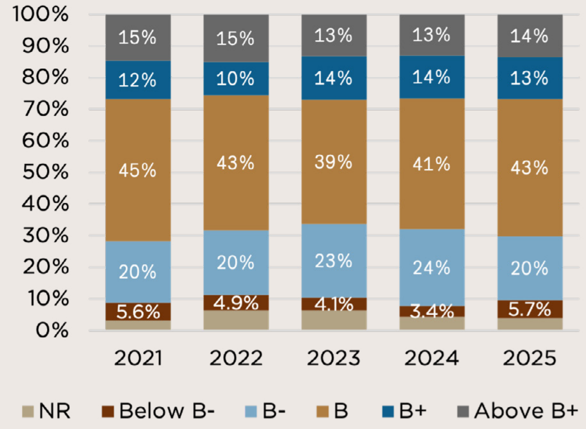
One of the themes in 2025 was the growing dispersion between performing and underperforming assets. Below, we review select fundamentals of market "health": ratings, price dispersion, maturity wall and default rates. Assets with varying combinations of weaker financial metrics, CCC and B3/B- ratings with negative outlook, challenging sector conditions, shorter refinancing runways, or more uncertain sponsor exit valuations and possibilities, have faced notable secondary pressures and widening spreads, as investors seek to avoid increased mark-to-market par losses and, ultimately, potential credit losses. Notably, CCC spreads in EUR HY space have not compressed comparably to the rest of the ratings stack, diverging from historical patterns.

Table 3 illustrates changes in ratings cohorts over the past five years and table 4 the upgrade-downgrade trend. Comparing year-end 2025 to prior years, trends appear overall healthy: the share of B+ and B-flat rated cohorts has increased, particularly at the expense of B-. During 2025, the share of CCC+ and below has, however, seen a modest increase from 3.4% to 5.7%. As outlined in this commentary, the CCC cohort has drawn increased attention from creditors, reflecting both the significant spread pickup and the range of possible outcomes for these credits. Lastly the trend in ratings changes (Table 4) does not suggest any material weakening relative to historical norms, but rather appears range-bound, with a skew towards downgrades.

With regards to asset dispersion or bifurcation, the lower cohort of stressed assets priced below 80, has risen from under 2% to 5% (for comparison, 2022 briefly peaked at c 7% in a risk-off market), explaining some of the negative price development in the index. Conversely, performing assets maintained strong momentum, pricing at par and above. Outside of the brief dip following Liberation Day, share of above-par loans averaged over 50% for the year, peaking at 70% in February and closing the year at 64% (≥101 at 8%, highest since 2017 when it peaked at 50%). This reflects robust demand for high-quality assets and sustained repricing pressures, with spreads tightening – E+325-350bps becoming almost standard for strong names. This again is partly an outcome of the imbalance between strong CLO demand and limited supply of new-money LBOs, with the latter perhaps finally shaping up as a potential driver for 2026, particularly in light of the sizable inventory of assets slated for exit.

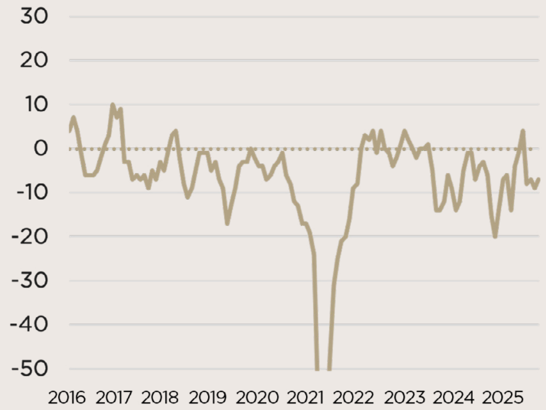
3. ELLI Index ratings (2021-2025)

ELLI index rating cohorts, % of total



4. Ratings changes (2016-2025)

Net ratings changes (positive-negative, 3m rolling)



5. ELLI Index prices (2021-2025)

ELLI-index price cohorts, of total index

Source: Bloomberg, PitchBook Data Inc, ICE BofA.

Underlying fundamentals seem solid but increasingly bifurcated (continued)

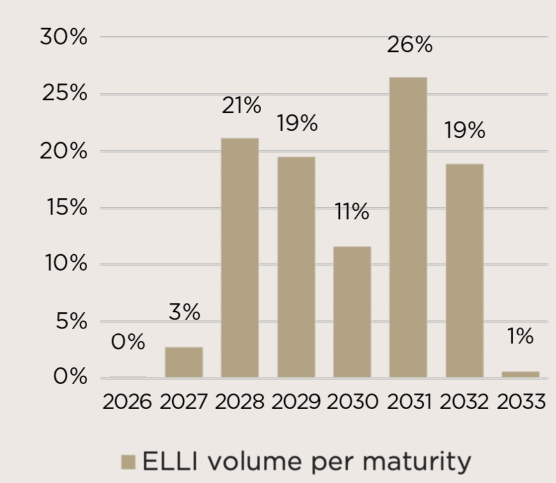
Briefly on the maturity profile: thanks to the steady flow of A&Es over the past three years, the ELLI index remains well-addressed. Only 3% of the ELLI index now falls due in 2026-2027 (down from 12% a year ago), while the 2028 maturity balloon has been reduced to 21%.

Loan default rates (ELLI index) remained low and credit conditions broadly benign in 2025, averaging just 0.7%, although monthly rates picked up to 1.4-1.5% by year-end. A notable statistical development was PitchBook's introduction of liability management exercise ("LME")-adjusted EUR loan default rate covering the past three years. The average default rate in 2025 was 2.0%, and 2.4% over the past three years, compared with the index-level "hard" defaults averaging 1.3% over the same period, thus adding roughly 1ppt from LME-driven situations. Despite this statistical adjustment, absolute levels remain relatively low although the data may still fail to capture all comparable cases in the market. For perspective, the US loans* LME-adjusted default rate averaged 4.2% in 2025 and 3.8% since 2023, while index-level average all-in spreads were roughly 40bps tighter than European comparables both in 2025 and over the 2023-2025 period.

For long-term investors, current market conditions present challenges at the higher end of the credit quality spectrum due to continued spread compression and opportunistic issuance, underscoring the need for selective capital deployment. Conversely, weaker assets require careful underwriting while technical drivers such as CCC downgrades and deeper discounts they trigger, can present compelling credit-picking opportunities, offering yields in the 10-15% range.

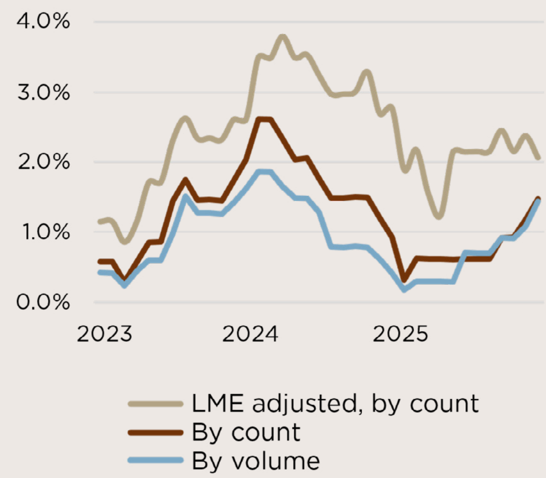
6. ELLI maturity wall (2025)

ELLI Index loan maturity distribution, % of total



7. ELLI default rates (2023-2025)

Default rate % by three different measures



Outlook for 2026

We reiterate our constructive outlook for 2026, with 2025 year-end ELLI loan index yield of 6.6%, supported by still-attractive coupon carry of 5.7% (excluding curve) and some potential upside value in oversold assets. Regarding coupon potential, Euribor has now turned flat to slightly upward-sloping, while spreads remain somewhat constrained by tight market conditions, with the well-liked names trading at the more expensive end.

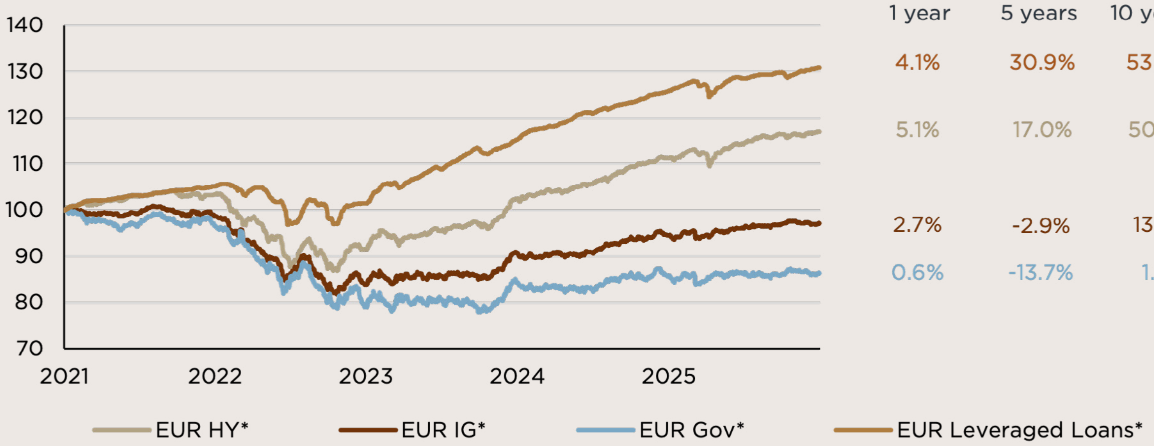
Secondary market looks to remain two-fold for now, favoring selective credit-picking. For agile and flexible mandates and managers, some of these oversold assets will, in our view, be one of the essential drivers of potential future relative overperformance. Barring significant sell-offs and pronounced mark-to-market volatility, 2026 should have grounds for around or above long-term average gross returns (5-6%).

Source: Bloomberg, PitchBook Data Inc, ICE BofA. *Morningstar US Leveraged loan index.

Appendix (select updated tables)

8. European leveraged loans total return vs. European HY, IG and Government bonds

Total return in %, indexed to 100 (01/2021 - 12/2025)



Total return as of 12/2025

1 year	5 years	10 years
4.1%	30.9%	53.2%
5.1%	17.0%	50.2%
2.7%	-2.9%	13.2%
0.6%	-13.7%	1.1%

		2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
EUR HY	YTM*	5.8%	3.9%	3.1%	4.9%	3.3%	3.2%	3.2%	7.7%	6.5%	5.9%	5.6%
	Gross return	9.1%	6.7%	-3.6%	11.3%	2.8%	3.3%	-11.5%	12.0%	8.6%	5.1%	
EUR IG	YTM*	1.5%	0.9%	0.9%	1.3%	0.6%	0.3%	0.6%	4.2%	3.5%	3.2%	3.3%
	Gross return	5.4%	2.0%	-1.1%	6.5%	2.9%	-1.2%	-15.1%	8.2%	4.3%	2.7%	
EUR GOV	YTM*	0.7%	0.4%	0.6%	0.8%	0.2%	-0.2%	0.1%	3.2%	2.7%	2.7%	2.9%
	Gross return	3.3%	0.1%	1.0%	6.8%	4.9%	-3.4%	-18.2%	6.7%	1.8%	0.6%	
EUR Loans	YTM*	5.1%	4.6%	3.8%	4.2%	4.0%	4.3%	4.0%	8.6%	9.1%	7.3%	6.6%
	Gross return	3.8%	3.6%	1.3%	4.9%	2.4%	5.2%	-3.5%	13.5%	9.2%	4.1%	

*) Yield prior year-end

The first table summarizes annual gross returns for the selected credit segments alongside their starting yields for each year. The second table presents mid-term EUR loan performance under varying levels of accumulated credit losses, excluding market price volatility. As expected, annual returns often diverge from initial yield expectations due to fluctuations in market prices driven by spread movements, interest-rate changes and duration impact, as well as realized credit losses. In other words, yields rarely materialize in a smooth, linear fashion over time. The second table therefore takes a simplified approach by stripping out price volatility and focusing solely on accumulated losses and the resulting net returns.

9. Three-year annualised return scenarios** as a function of default and recovery rates (with forward curve)

Annual default rate 2026-2028

Recovery rate 2026-2028	0.0%	1.0%	2.0%	3.0%	4.0%
90%	6.9%	6.7%	6.6%	6.5%	6.4%
80%	6.9%	6.6%	6.4%	6.2%	6.0%
70%	6.9%	6.5%	6.2%	5.9%	5.6%
60%	6.9%	6.4%	6.0%	5.6%	5.2%
50%	6.9%	6.3%	5.8%	5.3%	4.8%

**) Illustrative return for an investment into a loan portfolio with ELLI's price (96.7), margin (368bps) and maturity (4.5 years). Assuming par repayment and a linear price increase towards maturity excluding defaults that are exited at recovery value. Assuming forward curve for 3m Euribor as of 12/2025.

*) ICE BofA bond indices, Morningstar European Leveraged Loan Index "ELLI"
Source: Bloomberg, PitchBook Data Inc, ICE BofA.

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