

Corporate Credit Monthly Update

August 2023

Europe

In July, the eurozone saw its PMI indices – the manufacturing PMI in particular – fall further. Economic activity, however, is holding up better than predicted by the dire forecasts made at the height of last year’s energy crisis. Nevertheless, the tightening of financial conditions is now affecting outlooks. Inflation continued to decline but remains well above the ECB’s target and core inflation stayed the same. The latter is fuelled by upward wage pressures and full employment, and is concerning because it could have a knock-on effect on other components such as services. According to the most recent data, wages in the eurozone increased by more than 5% year on year. As a result, the ECB continued its hiking cycle and raised interest rates by 25 basis points in July. However, at its last meeting it adopted a less restrictive tone than expected, and did not come out explicitly in favour of another increase in September. In terms of currencies, the euro and the pound sterling rose against a weaker dollar overall.

On the credit markets, the German 10-year Bund yield ended the month at 2.49%, up 10 basis points from the previous month. The 2- and 10-year Bund yield curve is the most sharply inverted it has been since 1992, reflecting the strong tightening policy in the eurozone. Corporate bonds recorded positive performance in July. Credit spreads narrowed as investors’ appetite for risk increased. The volume of new issues, in both Europe and the United States, decreased during the summer months, in the context of a normal summer period. The European corporate index yield ended the month at 7.24%.

In the United States, after a brief pause in June, the Fed raised interest rates by 25 basis points in July, in line with expectations. Its position is similar to that of last month: progress on the inflation front is satisfactory, but the risks are still high. Fitch’s downgrade of the US credit rating has brought the country’s budgetary situation into the spotlight. On the macro data front, the indicators paint a more resilient picture than expected of the US economy, supported by low unemployment and stable consumer spending. Headline inflation has stabilised, but core inflation is also persistent in this zone. Oil prices rose sharply in July, by almost 16%, due to pressures on supply and demand. Announcements from Saudi Arabia and Russia of further production cuts, as well as growth that surpassed expectations in major economies, exerted upward pressure.

Rising interest rates on both sides of the Atlantic in the last week of the month drove down US Treasuries. Strong macro data, along with heightened risk appetite, dampened demand for long-dated bonds. US 10-year Treasury yields ended the month up 12 bps at 3.96%. The yield curve remains inverted in the US and in most developed markets with the exception of Japan. July was a positive month for US risk assets. Upward revisions to growth and the Fed’s less aggressive stance on inflation led to a tightening of credit spreads, reflected by solid corporate bond performance. High yield in particular outperformed the investment grade segment. The yield on the US corporate index stood at 7.67% at the end of the month.

United States

Emerging

In emerging markets, hope for a soft landing across economies dominated investor sentiment in July. Fears of a global recession have eased thanks to favourable employment figures and the start of earnings season for the second quarter, which exceeded expectations. Inflation continued to trend downwards in many emerging countries. Chinese macroeconomic data were disappointing, however. The long-awaited recovery is still being held back by the slowdown in GDP in the second quarter, the struggling real estate sector and record youth unemployment. However, the Chinese authorities signalled their intention to further support the economy, and gave some reasons for investors to remain optimistic.

The performance of risk assets in emerging markets, both in equities and credit, reflects this growing optimism. Corporate bonds had a positive month. Credit spreads tightened across all rating segments, with outperformance and a more marked tightening in high yield compared with investment grade. The strong market trend is supported by sound foreign capital inflows and limited new issues. The yield on the emerging market corporate index closed the month at 10.51%.

Edited: 09/08/2023

Forvia (EU)

The French automotive supplier Forvia published its first half-year results, which proved to be satisfactory. The group reported good organic growth (+19%) on the back of the easing of supply chain disruptions and solid outperformance versus the automotive industry (+740 bps). It also upgraded its sales and operating income margin guidance for the fiscal year 2023, after having revised upwards its car production assumptions for the year like many players in the automotive sector.

Vici Properties (US)

The US company, which owns gaming, hospitality and entertainment destinations, continues to be active with business development, both on the gaming and non-gaming side. This was recently demonstrated by their USD 165m announced acquisition of four Canadian casino properties, while in July they announced their plans to expand their investment partnership with Canyon Ranch (provider of luxury health and wellness experiences). Despite a healthy appetite for business development, leverage remains within the target range as management remains focused on improving their credit profile, notably via the use of equity to fund some acquisitions.

Asea (EM)

Asea, the leading restaurant operator in Latin America and Spain, reported a good set of results for the second quarter. Its top line increased by 12%, driven by growth across all regions, highlighting a double-digit growth in Mexico on the back of strong Starbucks performance. The EBITDA continued to show improving trends (+6% year-on-year) even though higher energy costs, inflation pressures in Europe, and labour costs led to some margin contraction (-100 bps to 20%). FCF generation was solidly in the green (+USD 123m) and net leverage improved to 2.8x versus 3.1x one year ago.

Rating moves

Adevinta	Fitch	➔	BB+
Birkenstock	S&P	➔	B+
Cirsa	Moody's	➔	B2
Digi Communications	Moody's	➔	B1
Dufry	S&P	➔	BB
Eutelstat	Fitch	➔	BBB-
Goldstory	S&P	➔	B+
Matterhorn	S&P	➔	BB-
Nexi	Fitch	➔	BB+
Stellantis	Fitch	➔	BBB+

Significant Primary Issues

Europe

Issuer	Yield	Maturity	Amount	Rating
Iceland Foods	11.125%	2027	£265M	B
Profine	9.375%	2028	€380M	B

United States

Issuer	Yield	Maturity	Amount	Rating
Coty	6.625%	2030	\$750M	BB
LifePoint Health	9.875%	2030	\$800M	B

Emerging

Issuer	Yield	Maturity	Amount	Rating
No new issues in July				

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Macro Economic Events

Europe

Eurozone: the economic sentiment indicator was down for the third month in a row, reaching 94.5 in July, its lowest level since last October. The effects of the ECB's aggressive policy tightening, at a time of persistently high inflation, have started to be felt. Eurozone inflation fell to 5.3% in July, in line with expectations, but it remains well above the ECB's 2% target. Core consumer prices haven't slowed much. Eurozone GDP grew by 0.3% in the second quarter.

Germany: the unemployment rate dipped to 5.6% in July, lower than the market's forecast of 5.7%. However, the economy's weakness still presents a risk of more people being out of work.

United Kingdom: the house price index was down 3.8% in the 12 months to July, steepening its descent (-3.5% y/y in June). This reflects the biggest drop in house prices since July 2009. It's becoming increasingly difficult for first-time-buyers to get a foot on the property ladder, especially if they need a mortgage given the unprecedented rise in interest rates.

US & EM

United States: Fitch downgraded its long-term credit rating from AAA to AA+ due to a deterioration in US governance and uncertainty over taxation. The agency highlighted the wider budget deficit, which is likely to hit 6.3% of GDP in 2023, as well as the combination of tighter lending conditions, lower capital expenditure and slower consumer spending.

China: the composite PMI output index was down to 51.1 in July from 52.3 the previous month. This is the lowest figure since December 2022 as the economy is proving slow to pick up. Industrial activity contracted for the fourth month in a row, reflecting weak demand. The real estate industry is still idling, while the services sector recorded its weakest expansion for seven months.

Brazil: the country posted a trade surplus of \$9 billion in July, up 68% from \$5.3 billion a year earlier. This figure remains close to the record surplus of \$11.3 billion in May.

Mexico: the manufacturing PMI increased from 50.9 in June to 53.2 in July, its highest level since May 2016. New orders posted their sharpest rise since February 2019 due to lighter inflation pressures, clement weather and firm demand from customers. The upturn in sales matched that of exports, with international orders up for the first time in five months.

Market Data Indices

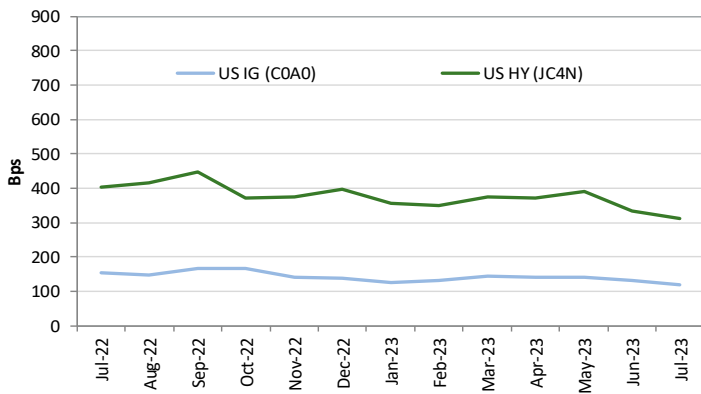
Indices (end of July)		Performance		Duration	Yield
		MTD	YTD	DTW	YTW
High Yield					
HE00	High Yield Europe	1.10%	5.50%	3.10	7.31%
JOA0	High Yield United States	1.43%	6.84%	3.91	8.32%
H7PC	High Yield Europe BB/B Excluding Financials	1.26%	6.16%	2.99	7.24%
JC4N	High Yield United States BB/B Excluding Financials	1.23%	6.16%	3.98	7.67%
HYEF	High Yield Emerging Countries Excluding Financials	1.23%	3.45%	3.58	10.51%
Investment Grade					
ER00	Investment Grade Europe	1.00%	3.06%	4.54	4.22%
COA0	Investment Grade United States	0.43%	3.68%	6.88	5.53%
EMIC	Investment Grade Emerging Countries	0.51%	3.41%	5.34	5.75%
Governments					
G4D0	10-Year German Bond	-0.14%	1.76%		2.49%
G402	10-Year US Bond	-0.59%	1.01%		3.96%

Inflation (end of July)		July	June	May	6M	12M
Realized inflation						
EUR CPI	Realized inflation in Europe (rolling 12-month)	5.30%	5.50%	6.10%	8.60%	8.90%
US CPI	Realized inflation in the United States (rolling 12-month)		3.00%	4.00%	6.40%	8.50%

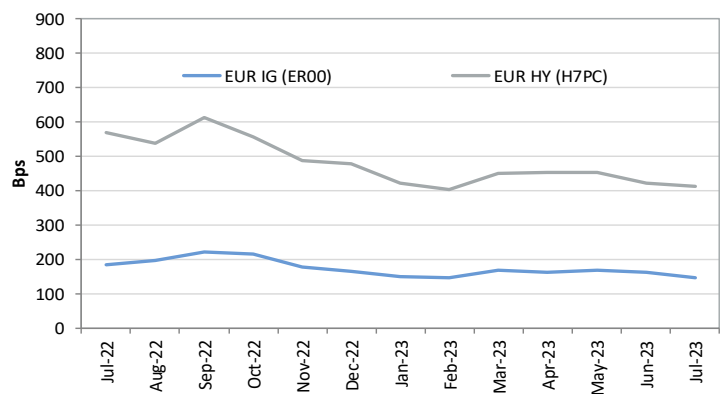
Month-to-date = MTD Duration-to-worst = DTW
Year-to-date = YTD Yield-to-worst = YTW

Source: Merrill Lynch
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US Corporate Bond Spreads (OAS) by Index



EUR Corporate Bond Spreads (OAS) by Index



Corporate Bond Spreads

		July	June	May	12 months
Europe					
ER00	Investment Grade Europe	150	164	172	181
HE00	High Yield Europe	451	464	498	580
H7PC	High Yield Europe BB/B Excluding Financials	426	440	469	561
ER30	Bonds rated A Europe	132	145	150	150
ER40	Bonds rated BBB Europe	176	193	202	220
HE10	Bonds rated BB Europe	346	365	389	462
HE20	Bonds rated B Europe	528	539	574	752
United States					
COA0	Investment Grade United States	121	134	145	154
JOA0	High Yield United States	395	422	483	480
JC4N	High Yield United States BB/B Excluding Financials	331	356	409	420
COA3	Bonds rated A United States	102	113	122	123
COA4	Bonds rated BBB United States	151	165	180	193
JUC1	Bonds rated BB United States	265	285	330	339
JUC2	Bonds rated B United States	419	448	513	551
Emerging Countries					
EMIC	Investment Grade Emerging Countries	145	154	166	210
HYEF	High Yield Emerging Countries	615	672	761	909
EMAQ	Bonds rated A Emerging Countries	109	114	118	134
EM2B	Bonds rated BBB Emerging Countries	204	215	235	305
EM3C	Bonds rated BB Emerging Countries	369	392	448	559
EM6B	Bonds rated B Emerging Countries	652	694	836	1093

Source: Merrill Lynch

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Anaxis specialises in corporate credit for investors who firmly believe in fundamental investing based on in-depth knowledge of issuers. For more than 10 years, Anaxis has focused on corporate credit strategies and has developed comprehensive expertise and methods renowned for their reliability by its clients.

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