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S&P GLOBAL
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(EUR) Topical: Europe's need for liquidity opens up new opportunity

Companies across Europe are tapping investors for liquidity support, either through privately placed or more widely syndicated term loans and bonds. For some, this is prudent balance sheet management, while for others this cash provides the bridge needed to traverse the revenue collapse from the coronavirus pandemic. For investors, the sheer scale of disruption is bringing an entirely different set of credit skills into play.

By any measure, risk assets across equity and debt have enjoyed a remarkable rally since their deep and sudden collapse in March. The technology-heavy Nasdaq index, for example, is trading at close to all-time highs after falling to 15-month lows in March.

High-yield has led the way in leveraged assets, as it more directly benefits from the far more massive injection of central bank liquidity than was even seen in the aftermath of the Global Financial Crisis. Loans have also rallied, with the average bid on the S&P European Leveraged Loan Index (ELLI) rising to 92.97 yesterday, from a low of 78.92 on March 24, which was the lowest level since September 2009. The ELLI bid is now just under six points away from its 2020 high of 98.58 on Jan. 1, 2020.

Weighted average bid of European loans

Data through June 4 2020
Sources LCD, an offering of S&P Global Market Intelligence; S&P European Leveraged Loan Index (ELLI)

But this crisis hides considerable bifurcation between individual credits. “Within the equity indices you have winners and losers and so it is the same with debt,” said David Allen, CIO of AlbaCore Capital Group. “Post lockdown there are going to be big winners and losers. Some business models have proven to be very resilient, flexible, and buoyant. At the same time, we will see a large increase in the default rate from companies who didn’t make it through this period due to liquidity, poor business models, or changing lifestyles.”

Indeed, for every stock like **Amazon** in the S&P 500 trading at or close to all-time highs, there is a **Norwegian Cruise Line**, which has lost around 70% of its value this year. As an aside, Amazon took full advantage of its success through global lockdown this week to place a $10 billion debt refinancing at a historically low yield.

Leveraged credit has also bifurcated, with the market splitting between the more resilient names now firmly in the mid-90s or higher, and the COVID-exposed names trading in the 80s or well below.

For those in the resilient category, the market – though at a higher cost – is not that much different than it was prior to the pandemic. In one of the first deals to reopen high-yield in Europe, Sweden-based alarm monitoring group **Verisure** placed a €200 million FRN at E+500 with 0% floor at 99.5, suggesting a yield of 5.3% to the five-year maturity or a decent premium against the firm’s pre-COVID loan margins that paid E+300 and E+350. The deal has subsequently tightened in secondary to a 101.625 mid-quote, suggesting a yield of 4.71% on the same basis. “If you were happy to buy Verisure at 3% or 3.5% prior to the crash, then you’ll buy it all day at 5%,” said one manager.

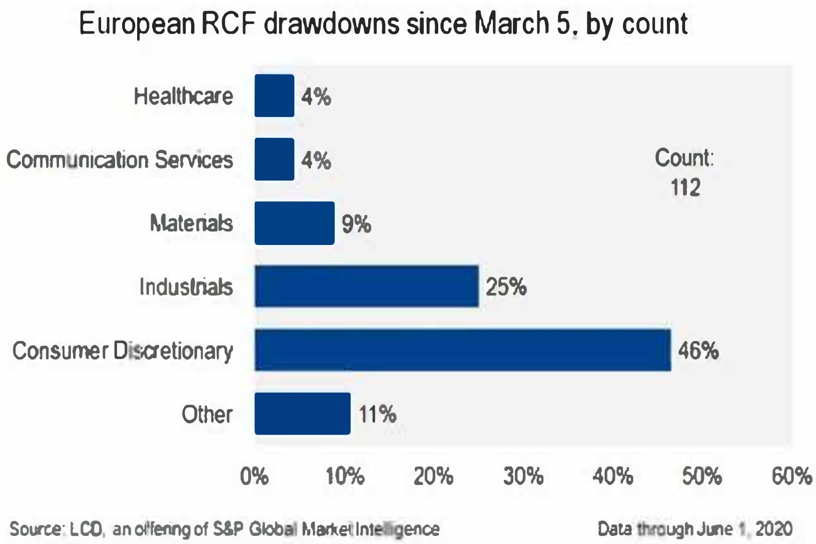
Recent European revolver drawdowns

Announced	Company	Borrowing amount (€M)	Capacity (€M)	Issuer rating (S&P/Moodys)	Status	Sector—broad
4/16/2020	Carlson Travel	150.00	150.00	B- / B3	Fully drawn	Consumer Discretionary
4/16/2020	Schoeller Allibert	30.00	30.00	B / B2	Fully drawn	Materials
4/16/2020	Cobham	321.40	321.40	B / B2	Fully drawn	Industrials
4/16/2020	Rubix Group	135.00	135.00	B- / B3	Fully drawn	Industrials
4/16/2020	McLaren Group	149.15	149.15	CCC / B3	Fully drawn	Consumer Discretionary
4/16/2020	Laird	122.38	122.38	B / B3	Fully drawn	Industrials
4/17/2020	Armacell	70.00	100.00	B / NR	Partially drawn	Materials
4/21/2020	Ediliians	90.00	90.00	B / B2	Fully drawn	Industrials
4/21/2020	Stella Group	60.00	60.00	B / B2	Fully drawn	Industrials
4/21/2020	Esmalglass	60.00	60.00	B / B2	Fully drawn	Materials
4/21/2020	Premier Foods	97.40	202.50	B / B2	Partially drawn	Consumer Staples
4/22/2020	Grupo Antolin	100.00	100.00	B- / B3	Partially drawn	Consumer Discretionary
4/22/2020	FiatChrysler	6250.00	6250.00	BB+ / Ba1	Fully drawn	Consumer Discretionary
4/22/2020	Breitling	69.28	75.93	B- / B3	Partially drawn	Consumer Discretionary
4/22/2020	Rekeep	40.00	50.00	B / B2	Partially drawn	Industrials
4/23/2020	Paprec	200.00	200.00	B / B	Fully drawn	Industrials
4/23/2020	Nets	240.00	240.00	B- / B2	Fully drawn	Information Technology
4/23/2020	Novafives	75.00	115.00	B- / Caa1	Partially drawn	Industrials
4/24/2020	Hurtigruten	85.00	85.00	CCC+ / B3	Fully drawn	Industrials
4/24/2020	Rohm (Madrid)	95.00	300.00	B- / B3	Partially drawn	Materials
4/27/2020	GHD	80.00	80.00	B- / B2	Fully drawn	Health Care
4/28/2020	Marcolin S.p.A.	40.00	40.00	B- / B3	Fully drawn	Consumer Discretionary
4/28/2020	Rodenstock	20.00	20.00	B- / B2	Fully drawn	Health care
4/30/2020	Ahsell	81.34	189.79	B / B2	Partially drawn	Industrials
5/5/2020	Haya Real Estate	15.00	15.00	B- / B3	Fully drawn	Real Estate
5/8/2020	APCOA	35.00	35.00	B / B2	Fully drawn	Industrials
5/12/2020	New Look	136.90	136.90	CCC / Caa3	Fully drawn	Consumer Discretionary
5/13/2020	Telepizza	45.00	45.00	CCC+ / B3	Fully drawn	Consumer Discretionary
5/13/2020	Proxiserve	43.50	60.00	B / B2	Partially drawn	Utilities
5/13/2020	Delachaux	75.00	75.00	B+ / B2	Fully drawn	Industrials
5/14/2020	Empark	100.00	100.00	BB- / B1	Fully drawn	Consumer Discretionary
5/15/2020	Boels	190.00	200.00	BB- / NR	Partially drawn	Industrials
5/15/2020	Q-Park	250.00	250.00	BB- / Ba3	Fully drawn	Real Estate
5/19/2020	Vermaat	35.00	110.00	B- / B3	Partially drawn	Consumer Discretionary
5/22/2020	Olympic Entertainment	25.00	25.00	CCC+ / B2	Fully drawn	Consumer Discretionary
5/21/2020	Gerflor	125.00	125.00	B / B2	Fully drawn	Industrials
5/29/2020	Atalian	103.00	103.00	B / Caa1	Fully drawn	Industrials
5/30/2020	BGIS	13.07	65.36	B / B3	Partially drawn	Real Estate

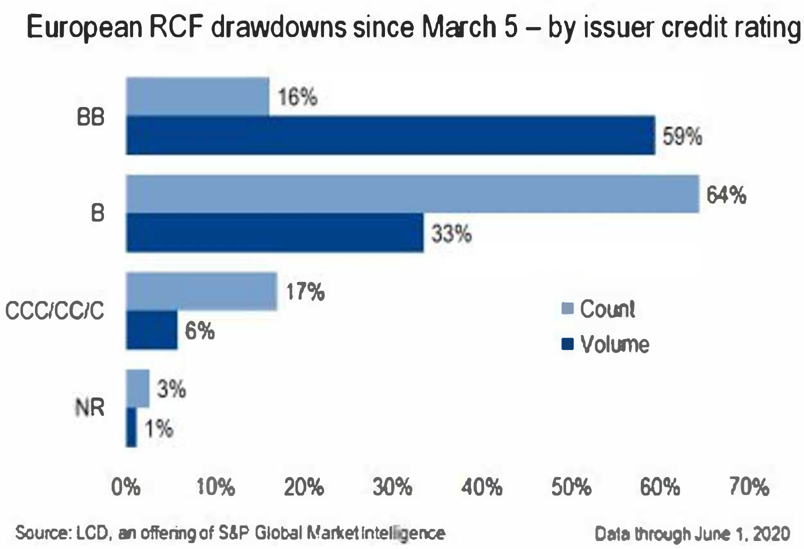
Source: LCD, an offering of S&P Global Market Intelligence; S&P Global Ratings; Moody's; press releases

But there is another section of the market for whom the crisis remains existential and far from over. "The markets are up, but downgrade volumes are already through 2009 and banks are predicting defaults to exceed that year as well," said one manager. Indeed, for the worst affected it's hard to overstate the impact of lockdowns that wipe out revenues in areas such as travel, leisure, and retail.

For these names an ability to demonstrate access to sufficient liquidity to see them through the lockdown and on to recovery has become key. In the first instance borrowers turned to their revolvers, which were drawn across the market often as a precautionary measure. According to data tracked by LCD, since March 5, European companies have drawn €23.15 billion from 112 facilities through June 1.



The swift action from Central Banks to prop up the financial system in efforts to avoid the mistakes of the GFC have helped here, sources note. “Central banks provided the liquidity insurance we all needed,” said one manager who nevertheless added it was leading to some artificially high prices.



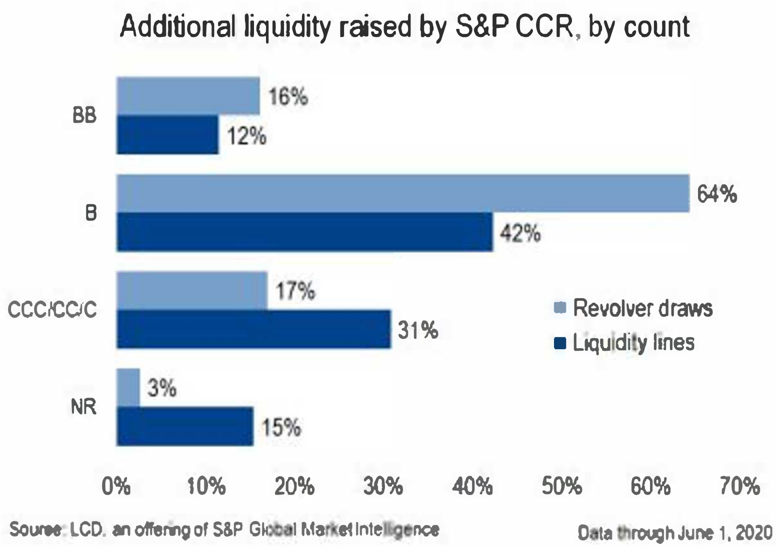
The further reopening of the market allowed borrowers to start to build their liquidity bridges. U.K.-based attraction group **Merlin** enlivened the European high-yield market in April when it placed a €500 million offer of 7% notes to support its business that was, at the time, largely shut and burning around £50 million of cash a month. The secured notes were pari-passu to loans that had priced at E+300 at the time of its KIRKBI- and Blackstone-backed take-private in 2019, but had been trading as low as 73 in March.

Merlin had the support of a cash-rich family-owned sponsor and was in part able to tap high-yield as it was an existing issuer and so had all the documents ready to go. For previous loan-only borrowers, high-yield is not as accessible. Sticking with loans, British used-car marketplace **BCA** opened proceedings with a €67 million three-year trade at the end of April, followed by **Parques Reunidos**, which placed a €200 million tranche in May, and German car parking group **Apcoa** attempted a more public process with a €68 million add-on. Among more recent names, Danish hearing aid group **WS Audiology** said it had secured a €100 million privately placed two-year term loan alongside an agreement with revolver lenders to amend covenants last week. Spanish sporting rights group **Imagina** is also said to have tapped existing investors for cash support.

Recent add-ons					
Name	Purpose	New-money amount (€M)	S&P/Moody's Issuer Rating	TLB spread	TLB OID/Floor/YTM
Inspired Education (Add-on 4/20)	Refinancing	100.0	B/B2	E+325	98.5 / 0% / 3.57%
IQ-EQ (Add-on 3/20)	Acquisition	50.0	B-/B3	E+375	98.5 / 0% / 4.14%
Synlab (Add-on amend TL 6/20)	Refinancing	94.7	B+/B2	E+400	100 / 0% / 4.53%
Parques Reunidos (Add-on 6/20)	GCP	183.5	B-/B2	E+750	- / 0% / -
Cognita (Add-on 6/20)	GCP	81.0	B-/B3	E+425	- / 0% / -
Galileo (Add-on 1L 6/20)	LBO	90.0	B/B2	E+325	94.5 / 0% / 4.32%
Apcoa (Add-on 6/20)	GCP	68.0	B/B2	E+725	94 / 0% / 9.88%

Source: LCD, an offering of S&P Global Market Intelligence

The private and limited syndication for most of these deals reflects highly disrupted credit stories that are primarily targeted at a small group of core existing lenders that might include special situation or other similar credit strategies. “These are strategic privately placed situations that are not targeted at typical flow buyers,” said one banker at an international firm. Indeed, many of these borrowers remain firmly in the cross-hairs of the crisis and so may still be on a downward rating trajectory, which is not attractive to structured investors such as CLOs, who are currently managing record downgrades to their portfolios.



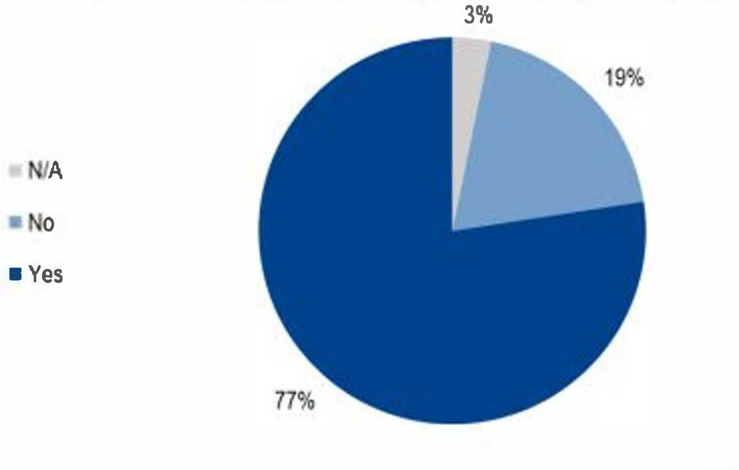
The sheer severity of the crisis on company earnings further raises questions that challenge long-held market tenets. “The leverage multiple calculation was not made for this world,” said one long-standing market manager. AlbaCore’s Allen agrees, and thinks the market can no longer look at just LTM EBITDA or ratings. “Credit analysis is much more complicated now with more factors to be considered. Factors like liquidity sources, access to capital, hard asset base valuations, detailed working capital analysis, and changing consumer behaviours need to be considered more than before. We have to be more dynamic and forward looking,” he said.

"People are going to have to get away from just considering LTM EBITDA."

Sponsors and bankers are slowly trying to work their way through these questions though moves to develop COVID-adjusted measures such as EBITDAC have drawn mixed responses. Blackstone-backed **Schenck** used this technique in its first-quarter results published last month but soon drew the ire of buyside trade grouping ELFA, which called the move “inappropriate”. Others are more sanguine. “If a sponsor has spent ten million euros to counteract the effect of COVID, then there is value in a one-off adjustment in EBITDA. But it has to be just that – a one off,” said one account at a global firm this week, adding that managers have to take a view on likely results come 2021.

These too are questions for revolving credit lenders that are dealing with a steady flow of covenant wavier and amendment requests as tests spring on drawing. According to data tracked by LCD, of revolver drawings since March 5, 77% that have springing covenants have had this feature triggered due to the drawdown.

European RCF drawdowns since March 5, springing covenants



Source: LCD, an offering of S&P Global Market Intelligence Data through June 1, 2020

These are questions that will no doubt bring far more debate in the coming months. But in the meantime it is clear that for those investors able to get comfortable with the numbers there is a potential rich investment offering available. “There are obvious areas of weakness but there are sectors that would normally be expected to do badly in a recession but are now not as vulnerable,” adds Allen. “If you can predict an improving credit you are going to make a lot of money,” he said.

Given that the deals are private, OIDs are typically not disclosed on most of these liquidity lines, which makes yield comparisons impossible, but margins tend to be rich when compared with those paid just a few months ago. Parques Reunidos paid E+750 on its deal, compared with E+375 on its €970 million term loan put in place in September last year, for example. For Apcoa, a more public process appeared to make little difference to pricing, and the group allocated its add-on at E+725 with a 0% floor at 93 to give a yield of 9.8%. In February the group placed a €514 million repricing and add-on at E+325.

Sources say yield can come through margin, OID, or a mixture of the two, though facilities allocated closer to par require stronger call-protection as insurance against quick repricings. Apcoa, for instance, came with a NC1/101 call structure. Others have looked to increase yield though shorter-dated facilities, such as two years from WS Audiology or three from BCA. Investors add that most deals also require some form of new-issue premium and that secondary is an imperfect guide to likely yields. “Loans can be illiquid and the price you see on the screen is not necessarily a real gauge of demand so a lot of price discovery needed for these deals,” said one banker who stressed a fully operational secondary capability certainly helped in these cases.

For sponsors, these are clearly terms a distance away from norms just a couple of months ago. But the benefits are real and these runways are frequently the difference between failure and survival for their holdings. This in turn increases equity values and the benefit is seen in secondary prices. WS Audiology, for one, is up by five points or so following news of its fund raising that also came with a fresh equity contribution of €50 million. Of course, this may beg the question of why more companies are not taking advantage of this liquidity, and it is clear that activity in the U.S. continues to far outrun Europe, where overall volume continues to disappoint.

In part, sources say, many companies in Europe continue look to their commercial banks for support often in conjunction with government guarantee schemes. Just last week for instance, U.K.-based cinema chain **Cineworld** said it had agreed to a $100 million revolver increase alongside a further $45 million in British Government–guaranteed funding. The firm also expects to start a process for a further $25 million through the U.S. Government CARES Act. The total package provides it enough liquidity to last to the end of the year, even if all of its cinemas remain closed. LCD has now tracked 26 borrowers who have previously tapped the broadly syndicated loan market, but have now turned to government-backed loans, equity, or privately placed debt for €10.31 billion.

Recent European additional liquidity lines						
Announced	Company	Currency	Borrowing amount (€M)	Current issuer rating (S&P/Moody's)	Type	Lenders
3/18/2020	Pizza Express	GBP	84.1	CC / Ca	Super senior term loan	HPS Investment Partners
3/23/2020	Officine Maccaferri	EUR	60.0	NR / Ca	Super senior bridge	Holders of ~54% of the firm's outstanding 5.75% senior notes due 2021
3/23/2020	Fiat Chrysler	EUR	3500.0	BB+/Ba1	Bridge facility	2 banks
3/26/2020	Selecta	EUR	50.0	B- / Caa1	Term loan	KKR
3/27/2020	Hotelbeds	EUR	400.0	CCC+ / Caa1	Term loan	Cinven, CPPIB, EQT
3/27/2020	Kloeckner Pentaplast	-	NA	B- / B3	Factoring Line	-
3/31/2020	Aston Martin	USD	90.4	CCC- / Caa1	Inventory finance facility	-
4/6/2020	OHL	EUR	140.0	NR / Caa1	Term loan	SANT, BBVA, CaixaBank, Bankia, Sabadell, SG
4/8/2020	Tui	EUR	1800.0	B- / B2	RCF	German Federal Government state-aid loan
4/15/2020	Faurecia	EUR	800.0	BB+ / Ba1	Unsecured Loan	BNPP, CACIB, SG, NAT
4/20/2020	Fnac Darty	EUR	500.0	BB / Ba2	State backed credit agreement	Arkéa Banque, Bred, BNPPs, CIC, CA, La Banque Postale, LCL, NAT, SG
4/24/2020	Hurtigruten	NOK	15.6–24.3	CCC+ / B3	State backed loan	Norwegian Government
4/16/2020	Europcar	EUR	307.0	B- / B2	State backed loan	BofA, Banque Européenne du Crédit Mutuel, BNPP, CACIB, Crédit du Nord, CIC, DB, GS, HSBC, ING, NAT, SG
4/30/2020	Loxam	EUR	230.0	B / NR	State backed loan	-
5/5/2020	Rodenstock	EUR	75.0	NR / B3	Equity	Compass Partners
5/7/2020	Naviera Armas	EUR	40.0	B- / Caa2	State backed loan	-
5/11/2020	Lecta	EUR	150.0	NR / NR	Equity, snr sec notes, state backed loan	Shareholders, Spanish banks
5/13/2020	CMA CGM	EUR	1050.0	B- / B2	State backed loan	BNPP, HSBC, SG
5/19/2020	CBR Fashion	EUR	40.0	B / B2	Super senior loan facility agreement	Existing lenders
5/27/2020	Fives	EUR	200.0	B- / Caa1	State backed loan	France Government
5/27/2020	Technicolour	EUR	400.0	B- / Caa2	Additional financing	Existing lenders
5/28/2020	Cineworld	USD	41.0	CCC+ / B3	State backed loan	UK Government
5/28/2020	Codere	EUR	105.0	CCC / Caa3	Secured facilities	-
5/29/2020	Matalan	GBP	55.7	CCC / Caa1	State backed RCF, notes	UK Government, existing noteholders
6/1/2020	Telepizza	EUR	20.0	CCC+ / B3	State backed loan	Spanish Government
6/3/2020	WS Audiology	EUR	150.0	B / B3	Term loan, equity	Shareholders, Spanish banks

Sources: LCD an offering of S&P Global Market Intelligence; S&P Global Ratings; Moody's; press releases

Moreover, these are not risk-free trades. Investors warn that even in deals with new equity, there is still a net increase in debt that will have to be paid back, meaning that these liquidity runways could be a bridge for a new generation of zombie companies that will have to be restructured at some point. “In January we as investors said companies had too much leverage, now we cheer when they add more debt with lower earnings,” said one investor who stated that even cases of relatively minor underperformance could have a meaningful longer impact on financial health given extra debt loads. — David Cox