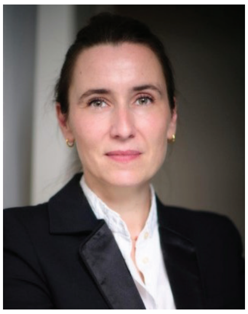
EDMOND DE ROTHSCHILD

MARKETING COMMUNICATION

THE HIGH YIELD MARKET: TOWARDS A RESUMPTION IN M&A AND LBO TRANSACTIONS IN 2025

INTERVIEW



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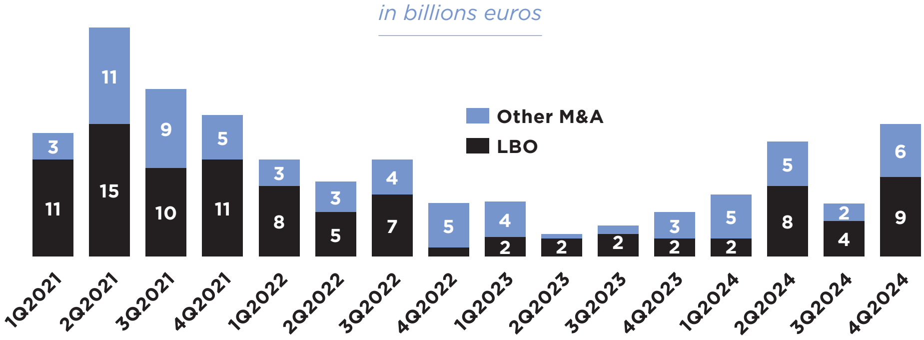
A DRYING-UP OF THE MARKET SINCE 2022

The restrictive monetary policies introduced by central banks in 2022 considerably increased the cost of financing for companies, leading to a sharp drop in primary issues on the credit market. This contraction was particularly marked in the High Yield segment, where the volume of new issues fell by almost 80% between the peak of 2021 and 2022[1]. The gradual recovery observed in 2023 and 2024 was mainly concentrated on refinancing transactions.

Historically, growth in the High Yield market has been fuelled by the financing of M&A (mergers & acquisitions) and LBOs (leveraged buyouts), as well as by dividend payouts. These operations used to account for an average of 35% to 40% of annual issues, but their share has fallen to between 10% and 15% over the last two years[2]. Nevertheless, recent momentum has been positive, with transaction volumes in recent months reaching their highest level since 2022.

LBO and M&A transaction volumes in Europe

in billions euros



Source: JP Morgan, data as of 31 December 2024.

TOWARDS A RECOVERY IN 2025

Several factors suggest that M&A, LBO and recapitalization transactions will pick up again this year, marking a return to market normalization:

▸ **More favourable market conditions:** The stabilization of risk premiums and the gradual easing of financing conditions, particularly in Europe where the fall in interest rates is well underway, should facilitate the return of leverage operations.

▸ **A low-growth environment in Europe:** In a context of limited economic growth, some major groups may be encouraged to optimize their portfolios by disposing of non-strategic assets, thus creating opportunities for private equity funds.

▸ **High levels of "Dry Powder" (undeployed capital):** With nearly $1.3 trillion not deployed in private equity funds following two years of low M&A activity, the pressure to invest this cash and generate returns for investors will increase this year.

▸ **Increased capacity of the bond and syndicated loan markets to finance these transactions,** with the creation of a record number of corporate securitization funds (CLO) and the positive flows captured by the fixed-income market.

EMERGING OPPORTUNITIES IN 2025

Several key trends should shape the High Yield market this year[3]:

***1.* LBO activity with new transactions and therefore new issuers of bond debt**

a. The Clayton Dubilier & Rice (CD&R) fund's acquisition of Opella, Sanofi's OTC subsidiary, will be financed on the bond markets this year.

b. The Anglo-Dutch consumer goods company Reckitt Benckiser is considering the sale of certain brands in its product portfolio, which is attracting the interest of private equity funds such as Advent, CD&R and Apollo.

***2.* IPOs of High Yield companies** such as EG Group, Verisure and Cirsa. Raising capital on the equity markets will strengthen the liquidity and credit profile of these companies.

***3.* Companies already listed on the stock exchange, which may be the object of a partial or total takeover by private equity funds or industrialists**, influenced by current low valuations. Groups such as Telecom Italia, Metro, Worldline, Ubisoft and Ipsos could be part of this trend.

***4.* More traditional dividend payouts will certainly be more significant this year.**

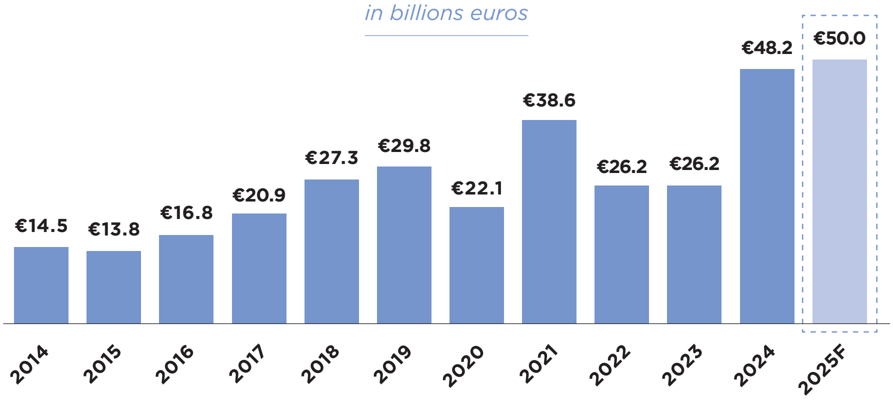
PERFORMANCE DRIVER FOR THE HIGH YIELD MARKET

The financing of LBOs and dividend payouts is often considered as an increased risk factor for High Yield bonds, as these transactions generally involve higher levels of debt. However, they also offer attractive opportunities, since the yield on issue tends to be higher, offsetting the risk associated with these more aggressive transactions. What's more, if the issuer manages to generate positive cash flows and rapidly reduce its debt, the potential for risk premium compression, and hence bond price appreciation, is significantly increased. This also contributes to greater market diversification in terms of sectors and issuers.

High Yield bonds rarely follow a linear path, due to their structure, which includes a number of early redemption clauses at prices defined at the time of issue. The bond's performance potential in the event of an IPO or takeover by a private equity fund or industrial company is therefore assessed in the light of the price at which the bond trades on the secondary market, compared with the redemption price specified in the documentation, if such an event occurs.

Trends in inflows to the syndicated loan markets (CLO)

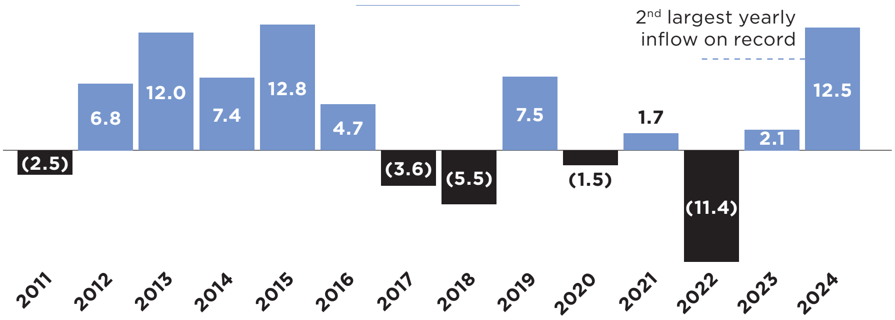
in billions euros



Source: Citi.

Trends in inflows to the High Yield credit markets

in billions euros



Source: JP Morgan, data as of 31 December 2024.

1. Source: Edmond de Rothschild Asset Management, Bloomberg. Data as of 31 January 2025.
2. Source: Edmond de Rothschild Asset Management, Bloomberg. Data as of 31 January 2025.
3. The information on companies should not be considered as an opinion of the Edmond de Rothschild Group on the foreseeable development of these securities and, where applicable, on the foreseeable development of the price of the financial instruments they issue. This information does not constitute a recommendation to buy or sell these securities.

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