European Liquid Credit: EUReka Moment[1]

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European credit is gaining investor interest as a valuable diversifier for U.S.-centric credit portfolios. Europe is often characterized as a bureaucratic region lacking the high-octane commercial exuberance of the U.S.: for credit investors, that may be no bad thing. Don't expect Magnificent Seven-level equity multiples here but instead conservatively managed corporate borrowers that pay their coupons, prudently deal with maturities, and benefit from a stable policy backdrop. In an uncertain global economy, this may be an attractive proposition.

Of course, European credit markets are smaller than those across the pond. But they're far from insignificant, with nearly €650 billion of outstanding European senior loans and high-yield bonds, and a thriving direct lending market.[2] This is split across multiple countries (the U.K., Germany and France tend to be well represented) and a wide range of industries, providing the opportunity to construct highly diversified portfolios.

European credit also has a few things in its favor right now:

- Stimulative spending in the region: Europe is set to bolster its military and industrial bases to mitigate increased detachment from the U.S.[3] This will require significant government spending: most notably, Germany has released its "debt brake" and is set to drastically increase investment. All of this is favorable for avoiding a recession.
- Robust issuers: The average quality in the European credit markets is high. Slow economic growth has constrained aggressive financings and mandated cautious balance sheet management. Together with expectations for relative insulation from tariffs, this had led to very moderate default rate predictions in Europe: only 2.5-3% in the loan market.[4]
- Limited vulnerability to creditor-on-creditor violence: We've seen signs of liability management exercises coming to Europe, but they remain difficult to execute here. European lenders continue to be relatively well protected by stringent directors' duties regimes, complex guarantee and security structures, and a collaborative creditor community.

That's not to say European issuers are invulnerable. They'll likely continue to be significant dispersion between the bulk of robust issuers and a small subset of distressed names. It's the latter which can hinder portfolio returns, and managers will have to be as diligent as ever in their credit selection. Get that right and Europe could present attractive opportunities for adding diversification and decent risk-adjusted yield to a credit portfolio.[5]

ENDNOTES

[1] Source: ***The Roundup:*** Top Takeaways from Oaktree's Quarterly Letters—June 2025 Edition. The content is derived from or inspired by ideas in recent letters, or other materials featuring or produced by Oaktree thought leaders; the text has been edited for space, updated, and expanded upon where appropriate.

[2] Combined Morningstar European Leveraged Loan Index and Morningstar Eurozone High Yield Bond par amount.

[3] EU White Paper for European Defence – Readiness 2030.

[4] Fitch, estimated 2025 European senior loan default rate.

[5] This statement is based on internal analysis of historical correlations between European and U.S. credit markets, as well as current market conditions as of June 2025. The assessment of "decent risk-adjusted yield" reflects assumptions regarding future interest rate environments, credit spreads, and default rates, which may not materialize. Actual results may differ materially due to changes in market conditions, economic factors, or issuer-specific developments.

DEFINITIONS

Magnificent Seven: The Magnificent Seven refers to Apple, Amazon, Alphabet, NVIDIA, Meta, Microsoft and Tesla.

Creditor-on-creditor violence: Aggressive liability management tactics where a subset of creditors is favored, often through restructuring or priming transactions, at the expense of others, typically without full consensus, creating conflict within the creditor group.

Liability management exercises: Strategies used by financially distressed companies to restructure existing debt, such as through buybacks, exchanges, or term changes, in order to reduce burdens and avoid insolvency.

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As an asset class, private credit is comprised of a large variety of different debt instruments. While each has its own risk and return profile, private credit assets generally have increased risk of default, due to their typical opportunistic focus on companies with limited funding options, in comparison to their public equivalents.

Because private credit usually involves lending to below investment grade or non-rated issuers, yield on private credit assets is increased in return for taking on increased risk.

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