SONA
ASSET MANAGEMENT

EUROPEAN REFINANCING NEEDS MEET STRUCTURAL DEFICIENCIES

November 2025

CONTENTS

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Note: Unless otherwise stated, the source for all market information, levels, performance, supply, demand, flows, defaults etc. is Bloomberg or Sona Asset Management internal estimates.

AN EVOLVING EUROPEAN LANDSCAPE

In the era of plentiful and cheap capital that defined much of the post-GFC period prior to 2022, many European corporates overextended their borrowing capacities and, thanks to ultra-low funding costs, required little earnings growth to cover their interest expense. These dynamics, combined with a weak economic backdrop, have resulted in bloated capital structures now straining under elevated financing costs. These have included large, high-profile, and heavily indebted structures; over the past three years we have seen four of the five largest defaults ever in the European high-yield ("€-HY") market.

Unlike prior cycles, however, this one has proven to be persistent. In recent months, dispersion has risen significantly, and index-level spreads are a poor representation of the true level of credit risk in European leveraged finance markets. On the one hand, a large part of the market has remained well anchored by ferociously strong demand: record CLO creation, inflows from fixed-maturity funds, and large, long-term income streams into private credit managers from insurance tie-ups. On the other hand, though, the level of distressed credit has risen, in some cases for idiosyncratic and sectoral reasons, but in many cases due to refinancing worries related to over-levered capital structures. This is especially concerning for structures underwritten during the COVID era, which now approach a crucial maturity wall with often loose documentation.

These issues are further exacerbated by structural inefficiencies. In the European broadly syndicated loan ("€-BSL") market, 70% of debt is held by CLOs, which are structurally unsuitable for dealing with par-loss restructurings. In addition, "whitelists", common pre-approved lender lists, have also acted as a limitation by concentrating investor bases. For the high-yield market, we would argue that the evolution of liability management exercises ("LMEs") has entered a new phase. While the previous phase was characterized by early-stage co-ops, forcing companies to negotiate with all relevant creditors, the current phase also includes factors such as third-party new money to potentially layer existing creditors. This has increased the risk around co-ops; only those with scale and creative solutions are likely to benefit.

We believe this all presents a growing opportunity. As the next wave of potential restructuring candidates is priced in a structurally inefficient market, price action has been violent and gappy. Investors should be poised to take advantage of the associated dislocations.

We believe these structural deficiencies should force market participants to rethink capital management. And as part of this, we believe that there are invaluable synergies from the cross-pollination of a multi-strategy approach. This is especially the case as the lines further blur between public and private markets, which have become increasingly complementary. In our view, if you do not participate in both, you should not participate in either.

In conjunction, then, with Europe's approaching economic inflection point, the market too is undergoing what we expect to be persistent structural and fundamental transformations. We think this presents a meaningful and attractive opportunity to deploy capital across a broad range of strategies, take advantage of pricing dislocations, and provide creative solutions.

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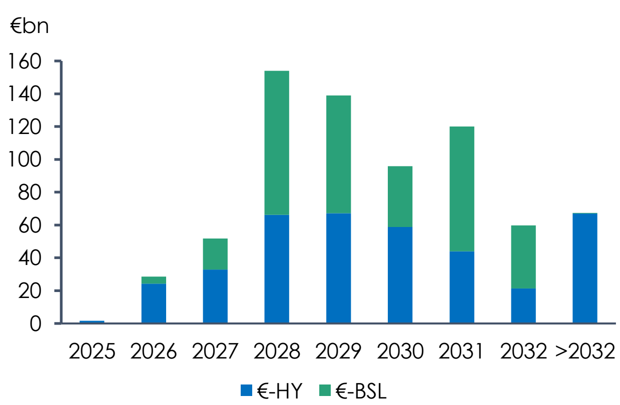
THE 2028 MATURITY WALL

Prior to 2022, access to capital markets was abundant, the cost of funding low and largely constant, and yield curves flat. Maturity walls, then, while still important, were less frequently seen as a key risk for the market. That changed quickly in 2022, however, as policy rates normalized to reflect the new macro regime, and attention turned to how corporates, especially those in leveraged finance markets, would tackle the refinancing of outstanding liabilities. At the time, the quantum of debt maturing was most acute in 2025 and 2026.

These worries proved to be vindicated. Over the last three years, European leveraged finance markets have had to deal with numerous defaults, including some of the largest on record, such as Thames Water, Altice France, Intrum, Casino, and Adler. Unlike prior cycles, there has been no sectoral common denominator. Rather, these were all examples of large capital structures, which benefited from the era of ultra-low funding costs, subsequently overextending their borrowing capacities. When funding costs normalised, these capital structures were found to be too large and over-levered, requiring restructuring.

We see the same paradigm today. While it is true that funding costs are lower today than in much of the last three years, they are still nearly double those of the pre-2022 regime.[1] And while many of the 2025/26 maturities have been dealt with, the next wave is nearing. Across the HY and BSL markets in Europe, we estimate that €154bn worth of debt is due to mature in 2028, the most of any year (and 3x the volume in 2027). Including pre-2028 maturities, €236bn of debt cumulatively matures by 2028.

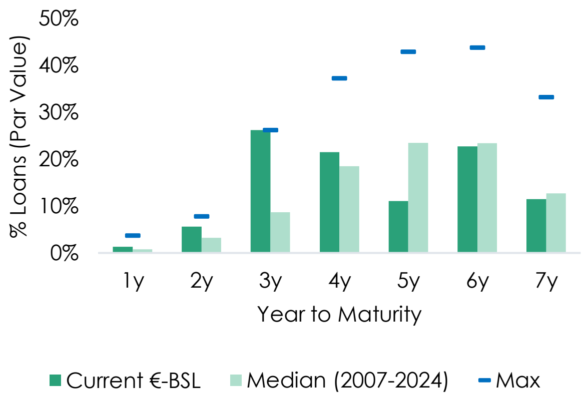
Europe is approaching a 2028 maturity wall



Source: Bloomberg, PitchBook

Admittedly, the concept of a maturity wall is not new. However, the volume of debt maturing in 2028 is very high relative to history. In the BSL market, we estimate that 26% of the entire notional face value of the market matures in 2028; the most ever. For context, since 2007, the median percentage of broadly syndicated loans maturing in 3 years' time is just 9%, while the average is just 11%.

The loan maturity wall has never been this steep



Source: PitchBook

There is also credit quality consideration, introducing some of the greatest dispersion in pricing. Of the €154bn of 2028-maturity debt, €59bn (38%) is rated B- or below (including non-rated). For these 2028 maturities, the average pricing of BBs and higher quality single-Bs is in the range of 98 to par. However, this quickly falls to 95 for B- debt and then to 55-75 for CCCs.

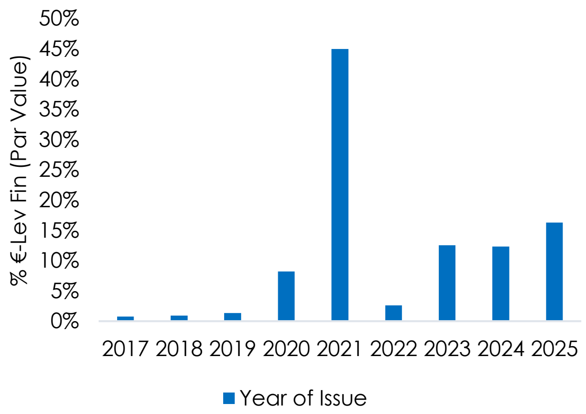
As price action in recent months has shown, refinancing risks are priced early. The 2028 wall is not an issue for 2027 or 2026 – it is an issue for today and will persist over the next 12-24 months.

THE 2021 VINTAGE

There are important lessons to be learned from the restructurings of the last few years, as they often reflect the large, indebted capital structures of today. Not to mention, of course, that nearly half of today's 2028 cohort was borne out of the 2021 underwriting vintage – a year in which capital was abundant, pricing tight, and supply robust, marking the largest ever year for European leveraged finance markets with €237bn issued across €-HY and €-BSL.

[1] Source: Bloomberg, Oct-25

Many of the 2028s are from the 2021 vintage



Source: Bloomberg, PitchBook

We contend, perhaps uncontroversially, that much of the 2021 vintage was characterized by questionable underwriting standards, particularly in relation to documentation and the ability for management or sponsors to extract value from creditors. In addition, this cohort had both the largest ever portion of LBOs underwritten with leverage of at least 6.0x (45%) and the highest average purchase price (outside of the small sample size in 2020) at 11.5x.[2]

Accordingly, private equity exits over the past several years have been challenged, with sponsors occasionally walking away from assets that have been irreparably scarred. While there is reason for greater optimism today in light of the re-opening of the European IPO market, the return of M&A/LBOs, further allocation to private assets, and an improved 2026 macro backdrop, we will undoubtedly continue to see some sponsors choosing against the extension option – a symptom of the elevated multiples paid in an environment of abundant capital.

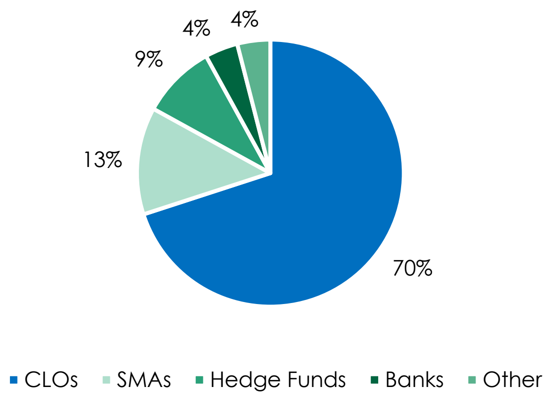
STRUCTURAL DEFICIENCIES

We think that concerns around the maturity wall, specifically as they relate to price action, are exacerbated by the structural inefficiencies of the European investor base. Specifically, we highlight dynamics around the deployment of capital, the tolerance of risk, and the transfer of risk across investor bases, both in public and private markets, as key drivers of potential dislocation.

CLOs - THE DOMINANT BUYER OF LOANS IN EUROPE

In Europe, CLOs account for ~70% of the broadly syndicated loan market[3], a percentage which has increased in recent years with CLO supply outstripping net loan supply. This is a slightly higher percentage than in the US, given the greater retail presence in the US BSL market. Accordingly, European CLOs exert significant influence over loan market pricing.

CLOs account for ~70% of the BSL market in Europe



Source: Bloomberg, Barclays

While CLOs are inherently long-term providers of sticky capital, contributing to sustained periods of calm (even when broader markets endure more elevated volatility), structural inefficiencies arise from this dynamic. This is especially the case in an environment like today's, beset by increasing dispersion and distress.

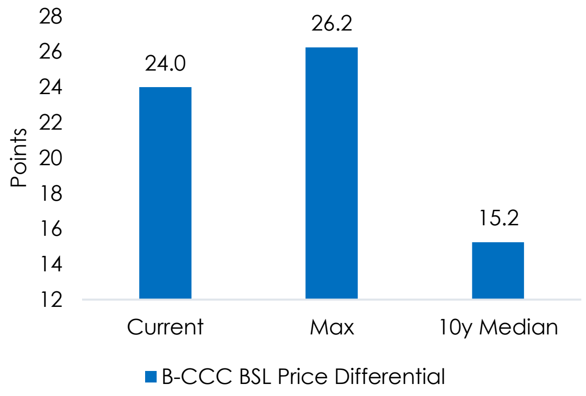
In our view, this is because CLOs are not the natural investor base or vehicle to deal with par-loss restructurings. Why? Among other things, CLOs are characterized by an outsized aversion to defaults, lack of flexibility, need to protect equity holders, structural constraints including CCC limits, and the inability (in some cases) to participate in new-money opportunities. Additionally, CLOs must mark equity at zero, a significant constraint versus, for example, traditional credit funds.

As such, any questions around the viability or outlook of a performing credit can often lead to sharp price action and heightened levels of gap risk. This has been particularly evident of late, for example, in the price differential between CCC-rated and B-rated loans, which is now close to the largest on record.

[2] Source: PitchBook, Sep-25

[3] Source: Barclays, Oct-25

Gap risk has been common in the BSL market lately



Source: Bloomberg, PitchBook

Another limitation stems from whitelists. A norm in European markets (and unique to Europe – so-called blacklists in the US are common but less restrictive), whitelists effectively act as a pre-approved list of lenders who can trade loans without the borrower's permission. The aim is to prevent institutions from acquiring large enough stakes in a company's debt to effectuate a control change ("Loan-to-Own").

These lists can have an adverse impact on market liquidity in the broadly syndicated loan market. In a stressed situation, lenders who wish to sell are unable to find buyers, and those who perhaps would buy are unable to do so if not party to the whitelist.

This has undoubtedly contributed to some of the volatile price action of late. Without a deep, natural buyer base, the price at which a loan transitions from performing to non-performing can be considerably lower, exacerbating some of the structural inefficiencies in the BSL market discussed above.

EVOLUTION OF LMEs

Liability management exercises in Europe have increased in frequency over the last few years, although they remain a relatively new concept when compared to the US market. Nevertheless, despite a shorter history, we think European LMEs have evolved quickly. While there are many nuances unique to each single LME, we would argue that the following general phases describe the progression:

(1) The first phase was somewhat disorderly, with no structured co-op groups leading to unfriendly creditor behaviour and poor recoveries for all.

(2) The second phase was more organized insofar as co-ops were signed as soon as possible, creditors locked arms, and companies were forced to negotiate with all. Transactions involving up-tiering were also common, where lenders exchanged loans for higher-seniority debt instruments.

(3) In the third phase, more recent examples have continued to include early-stage co-ops but have also introduced third-party new money to influence pricing of the existing structure and capture discounts. Existing creditors may be layered or lose access to assets from which they could have previously extracted value.

Today's environment for LMEs is intense and includes competition among borrowers, sponsors, holdouts, third parties, and ad-hoc groups. In our view, creditors who lack the size and scale to exert significant influence during a process risk enormous disadvantage.

In fact, the attractiveness of co-op membership is an open question in this current phase. We believe creditors who were once happy to participate in LMEs are now less likely to do so, preferring to exit positions early, further contributing to volatile and gappy price action.

REPEAT OFFENDERS

We also note the emergence of repeat defaults of the same issuer. While more commonplace in the US, Europe has seen the likes of debt collector Lowell hire advisers only months after emerging from a restructuring. In general, these situations have demonstrated that the volume of debt written down through an initial restructuring was insufficient to create a sustainable capital structure going forward, ultimately leading to yet further restructuring efforts.

ABUNDANT CAPITAL STREAMS

We have discussed concerns around the maturity wall and the structural inefficiencies that may explain some of the pricing dislocations and volatility in recent months. However, it is just as important to acknowledge the abundance of capital that has flowed into European leveraged finance markets.

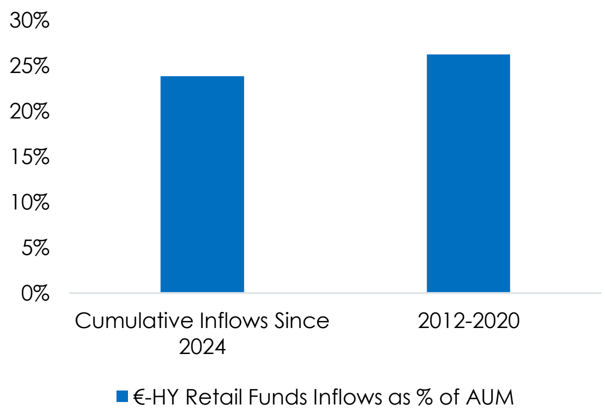
Year-to-date CLO creation in Europe has already set a new annual record in 2025, with €50bn of supply through October versus €48bn for the entirety of 2024. More importantly, CLO creation has also eclipsed the growth of the BSL market. While the BSL market has grown ~9% in notional terms this year[4], this is worth only €27bn in absolute terms; CLO creation has covered this ~2x. Notably, this is the fourth successive year in which CLO creation has comfortably eclipsed the growth of the BSL market, and, in cumulative terms, represents the equivalent of €83bn of incremental net demand.

CLO creation has comfortably eclipsed BSL market growth for the last four years

Source: Bloomberg, PitchBook

For the €-HY market, retail inflows have been relentless since the end of 2023, totaling 24% of AUM.[5] For comparison, the entirety of inflows from 2012 to the start of 2020 was equivalent to 26%. Put another way, €-HY has seen an almost equivalent magnitude of inflows in the last two years as it did for the entire eight-year period leading into the pandemic.

€-HY inflows since 2024 match the 2012-20 period



Source: Bloomberg, EPFR

Behind these inflows, and especially so for €-IG, is the exponential growth of fixed-maturity funds. From 2023 to August 2025, fixed-maturity funds' AUM increased from $30bn to nearly $120bn.[6] This has come at a time when the ECB's holdings of corporate bonds have fallen nearly $100bn over the same period, helping to ease some of the concern around corporate quantitative tightening. In fact, we would argue that the increase in AUM of fixed-maturity funds over the last two years has had a QE-like impact similar to that of CSPP over the last decade.

Last, but by no means least, annuity streams to private credit managers from linkups with insurance companies have had a significant impact on pricing in the direct-lending market. While it is difficult to accurately measure the volume of capital that has been deployed (or is received in a regular fashion), anecdotal evidence would suggest that it is large and influential. Subsequently, direct-lending spreads trade at compressed levels on a ratings-adjusted basis versus equivalent public-market spreads.

We do see risk arising from this. This stream of capital is beneficial when capital is abundant and underwriting opportunities are vast. However, when the need to deploy capital does not align with the "want" to deploy capital – whether for valuation reasons, the broader macro environment, or the opportunity set – it can pose a meaningful headwind.

While the ability to diversify across different pools of assets helps to reduce deployment pressure, the limits of this have arguably not been fully tested. The risks emerge when inflows of capital accumulate, deployment pressure increases, and the opportunities to deploy do not keep pace. And it should be noted that many of these trends are also consistent in the US market.

Importantly, much of these flows have been targeted at the higher quality and performing parts of the market. We think that it is fair to assume demand remains strong given the prevailing yield environment. However, in the context of Europe's maturity wall issue, this distribution of capital, or inflows from CLOs and traditional €-HY funds, is unlikely to reach the lowest quality names. Where there are concerns about credit quality and stress, the availability of capital inevitably becomes more concentrated, and, in some cases, specialized. In our view, capital is, and will remain,

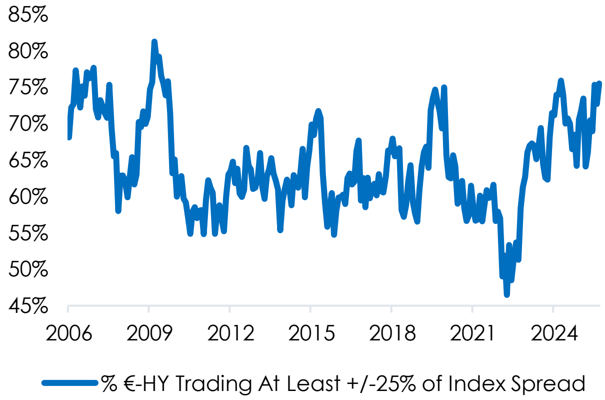
[4] Source: PitchBook, Oct-25
[5] Source: EPFR, Oct-25
[6] Source: Bank of America, Aug-25

abundant, but will not be linearly or uniformly distributed across the universe.

ELEVATED DISPERSION

The combination of the aforementioned factors has contributed to elevated dispersion. For example, the percentage of bonds in €-HY trading in a band at least +/-25% away from the index-level spread is currently 75% and in line with the highest levels outside of the GFC.

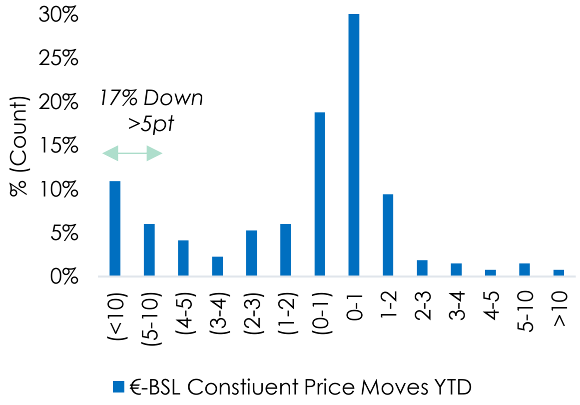
Dispersion in €-HY is near historical highs



Source: JP Morgan

What this fails to show, however, is just how aggressive some of the price moves have been. This has particularly been the case in the BSL market, where we estimate that, year to date, 35% of the market is down at least 1pt, 17% is down at least 5pts, and 11% is down at least 10pts. To illustrate how asymmetrical this price action has been, note that only 3% of the market is at least 5pts higher. Put another way, the ratio of loans that are down at least 5pts to those up at least 5pts is a staggering 8.0x, resulting in a long left-tail distribution.

The €-BSL has seen particularly aggressive price moves



Source: Bloomberg

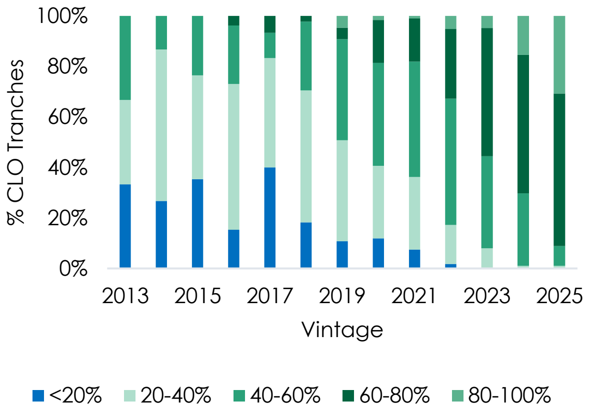
As a result, the €-BSL distress rate – measured as the percentage of loans trading below a cash price of 80 – has risen to slightly more than 5.0% today.[7] This is higher than the 3.7% peak in April and up from 1.2% at the start of the year, reaching the highest level since early 2023. By contrast, the US distress rate has been both lower and more stable this year at a current 3.4%, a stark departure from the trend of the last decade in which the US rate was higher than Europe's 96% of the time. For the €-HY market, the distress rate (calculated as the percentage of bonds trading with a spread wider than 1,000bps) is 6.4%, a more moderate rise relative to the 5.5% distress rate at the start of the year.

This rise in distress in the €-BSL market has further led to increased dispersion in the CLO market. Specifically, the share of CLO equity tranches with low (or in some cases negative) equity NAV has picked up considerably. For pre-2018 vintages, as much as 40% of tranches have an equity NAV of less than 20%[8]; (though, there are also instances of 2020 to 2022 vintages with <20% equity NAVs).

[7] Source: PitchBook, Oct-25

[8] Source: Bank of America, Oct-25

CLO equity NAVs also show dispersion between vintages



Source: Bank of America

Overall, just under 5% of equity tranches have a negative NAV today, a number which increased significantly through October and is only slightly below the peak in April. This is important as a negative equity NAV implies single-B MVOC (Market Value Over-Collateralization) ratios below 100%. In other words, for impacted deals, single-Bs are not fully covered.

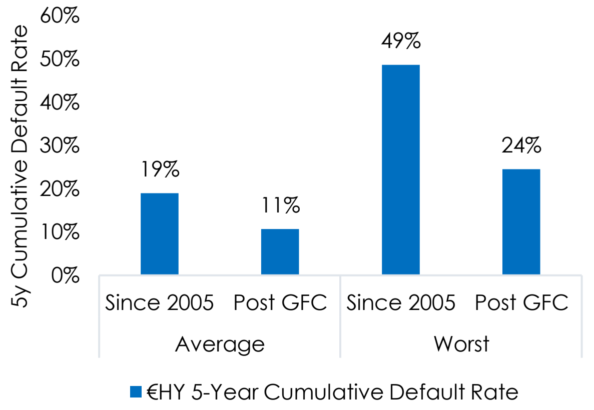
WE SEE €100BN OF DEBT AT RISK

Across the €-HY and €-BSL markets, we think that there could be as much as €100bn of debt at some risk of a future restructuring in the next five years, with the 2021 vintage being the largest contributor.

While current distress in both markets is helpful in guiding to which names are potentially at risk now, it is less helpful in guiding to which names might be at risk in twelve months' time (or beyond). Rather, our preferred method is using a range of future default rate assumptions.

Over the past twenty years, the average cumulative 5-year default rate for €-HY has been 19%. However, that number is heavily impacted by the 2008-09 period, when the rolling twelve-month default rate exceeded 10%, far eclipsing any other cycle seen in history. Excluding that period, then, or looking at the period since the GFC, we have had an average 5-year cumulative default rate of 11%. For context, at its worst this metric was 24% in the early part of the last decade.

Defaults have averaged 11% on a 5-year cumulative basis in €HY since 2010



Source: Bloomberg, S&P

We think it is reasonable to assume a higher-than-average default rate over the next 5 years. For one, the recent trend has been for the default rate to steadily rise. For example, the current 5-year cumulative default rate of 10% represents an increase of four percentage points since 2021. That largely reflects the fundamentally different interest rate environment today versus that of pre-2021. In addition, the high quantum of 2021-vintage bonds and loans is another reason for caution, given our concerns around the overall standard of underwriting and documentation protection. Last, of course, is the record amount of debt over the next 5 years that will be hitting its 3-year maturity window.

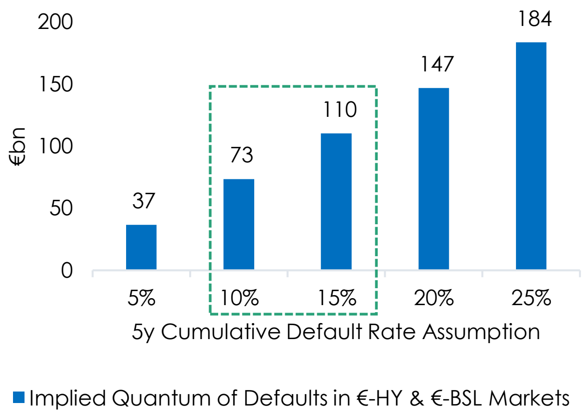
Importantly, our universe also includes the €-BSL market. There is an important fundamental difference between the €-BSL market and the €-HY market, which is average credit quality. In the €-BSL market, around 80% of the market is rated single-B, with an average rating of single-B flat. By contrast, more than 60% of the €-HY market is rated BB and the average rating is BB-, or two notches higher. Put simply, the €-BSL market is considerably lower quality than the €-HY market.

Assuming a default rate of 10% over the next 5 years across the €-HY and €-BSL universe implies €73bn of debt defaulting. At 15%, that increases to €110bn. In our view, a default rate between 10% and 15% is a fair assumption for the next 5 years given our previous observations. If, for example, defaults amounted to €100bn (or a default rate of 14%), that would be the most ever, in absolute terms, over a five-year period (a function of the fact that the market has grown significantly over the past two decades).

More important than forecasting the exact quantum, however, is our belief that this underscores a large and growing opportunity set from which to source opportunities. While there will invariably be considerable dispersion in terms of recovery rates within these future defaults (including the split between "hard" defaults and LMEs, for example), this opportunity set is exciting not only from a trading perspective, but also from that of providing capital for creative solutions.

Specifically, in contemplating the capital solutions opportunity, we suspect this will most likely involve the provision of private capital into public structures, further emphasizing the importance of these blurring market lines.

We think ~€100bn of debt is at risk of default in the next 5 years



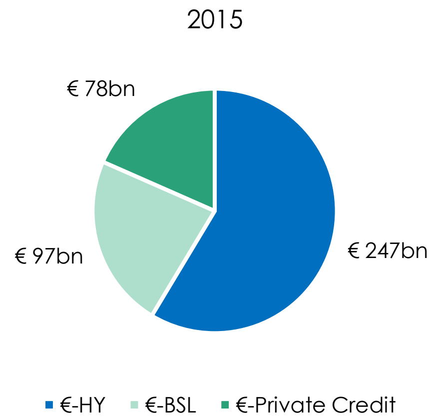
Source: Bloomberg, S&P

PERSISTENCE OF OPPORTUNITY

The window to deploy capital into a large opportunity set can often be short-lived. This cycle, however, is unique. We are presented with the next wave of refinancing concerns in a market of pronounced structural deficiencies, which will not be rectified, or disappear, overnight. This opportunity set is likely to be more persistent than those seen previously, and, therefore, the opportunity to deploy capital too will be persistent.

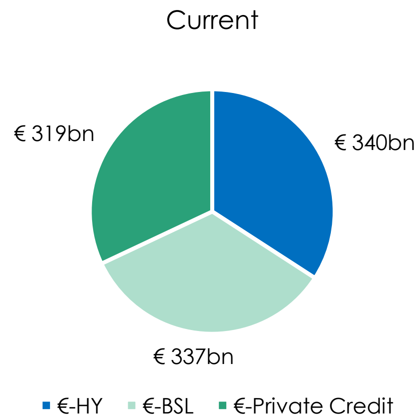
When evaluating the opportunity set, it is important to consider the overlap between different pockets of the European leveraged finance market. A decade ago, the high-yield market was 60% of the universe in par value terms. Today, each of the high-yield, broadly syndicated loan, and direct-lending markets is roughly equal in size. No longer does the high-yield market dominate. And more importantly than ever, what happens in one market can have a bearing or read across to others.

From a landscape which was €-HY dominant…



Source: Bloomberg, PitchBook, Preqin

…to three markets which are comparable in size



Source: Bloomberg, PitchBook, Preqin

CONCLUSION

There is something of a perfect storm brewing in European leveraged finance markets right now. The next wave of potential restructuring candidates is being priced into a market with persistent structural deficiencies.

This is giving rise to heightened dispersion and pricing dislocations, all emerging as Europe approaches a crucial economic inflection point. We expect this to be met by abundant capital – both fiscal capital from governments and, increasingly, private capital solutions for stressed public structures.

Most importantly, however, we believe the degree of success for managers in this credit cycle will be defined by their ability to be flexible and leverage synergies across strategies. More so than ever, the lines are crisscrossing between the various pockets of leveraged finance. Where once the differentiation between public and private, loan and bond, was clear, the Venn diagram today overlaps substantially. Events in one market can have a clear bearing on others, as we have seen recently in First Brands and Tricolor. We think managers who are unable to leverage information from one market in the context of another are at a competitive disadvantage.

The opportunity set is growing and will be met with abundant sources of capital, but the deployment of this capital must be increasingly dynamic, overlapping, and flexible across strategies. And trading strategies must be dynamic as well. We see compelling opportunities not only from the long side and through the provision of capital solutions, but from the short side as well. The frequency of problematic credits is increasing, and the speed with which prices move can be significant – managers would be well served in remaining vigilant, nimble, and humble.

ABOUT SONA

Sona Asset Management is a London-based credit platform that aims to extract alpha, through the cycle, primarily from the European credit markets. Sona has been investing in Europe since its inception in 2016, with a total AUM of over $15bn.

The team is large, diverse, and experienced. With 143 team members,[9] including 80 dedicated investment professionals, Sona's reach covers public and private markets, corporate credit, structured credit, and equities.

[9] Source: Sona, Oct-25

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