Debt Funds in Europe
– Stuck Between Ultra-loose Monetary Policy and the Cyclical Downturn

Financial Research
September 2019

Management Summary

1.

The European debt fund market as a whole has once again experienced a strong year. The cumulative fund volume grew by 43.8bn euros to 197.2bn euros in 2018. This performance was largely driven by strong growth of the direct lending segment. In 2018, European direct lending funds recorded a capital inflow of 27.7bn euros. After 14.2 and 24.6bn euros in 2016 and 2017 respectively, inflows in this segment grew for the third consecutive year. European real estate debt funds also posted sustained growth, albeit somewhat weaker than in the previous year (9.8bn euros). Meanwhile, the market for infrastructure debt funds, the smallest segment in terms of volume, picked up noticeably in 2018. After the aggregate fund volume had fluctuated between 3 and 4bn euros per year in 2015-17, a new high of 6.3bn euros was reached. Overall, direct lending funds were thus able to further consolidate their leading position in the European debt fund market.

2.

The US debt fund market also remained on its upward trajectory in 2018. However, both the fund volume and the number of newly established funds were lower than in the previous year. After the record year of 2017, when 146 new funds with a volume of 72.3bn euros were recorded, the number of new funds in 2018 totaled 117, the corresponding volume across all asset classes was 62.2bn euros. This was mainly due to the more moderate growth momentum in the direct lending segment.

3.

The steadily growing number of European debt fund managers is a further indication of the increasing attractiveness of debt funds. In addition to the 209 investment companies that launched their debt funds in 2008, a further 100 companies were added by 2012 alone, and in 2016 388 financial market players were already managing debt funds. In the past two years, however, the number of new fund managers has grown only modestly to now 407. What is striking in this context is a strong geographical concentration with regard to the origin of the fund managers. Two thirds of the investment companies are based in only three European countries, with the United Kingdom accounting for around half of them.

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As regards the composition of the investor base of European debt funds, European investors are not of paramount importance on their domestic market. As measured by the number of investors, all segments of the European debt fund market are dominated by North American investors, primarily from the United States. That said, the European investor base is comparatively strong in the direct lending asset class.

Public and private pension funds are by far the most important investors, followed by insurance companies. Moreover, institutional investors appear to view alternative assets more as an admixture than as a main component of the portfolio. However, there are clear differences in the investment behavior of North American and European investors, as the latter appear to be more reluctant to invest in alternative assets than their American counterparts.

5.

The European debt fund industry must prepare itself for a challenging macroeconomic environment in the short to medium term. On the one hand, we expect an economic downturn in the euro area that will be accompanied by significantly lower growth rates than we have observed in recent years. On the other hand, we believe that we will not see an abrupt end to the ultra-loose monetary policy witnessed over the last couple of years. To the contrary, the current interest rate environment in the euro area is likely to remain in place in the medium term.

In the context of a weakening economic environment, we see downside risks, especially for debt funds that focus on direct lending. On the one hand, existing direct lending debt funds are likely to be increasingly confronted with a deterioration in firm-specific risk against the weaker backdrop in the general economic situation. In the case of new direct lending funds, we expect that the effects of the generally weaker economic situation on credit quality and company valuations will tend to lead to a widening of spreads. In principle, there is also the danger of an oversupply of financing, which in the worst case could result in excessive risk-taking and adverse effects on the underwriting quality.

Furthermore, we assume that politics and the banking sector will remain intact as structural drivers. While policymakers in Europe welcome and support instruments that are conducive to facilitating a market-based finance system, banks will continue to be increasingly cautious in the high-yield segment amidst stricter regulatory risk requirements, or are divesting themselves of business segments that could then fall to debt funds going forward.

1. The Interest Rate Environment – Lower for Longer

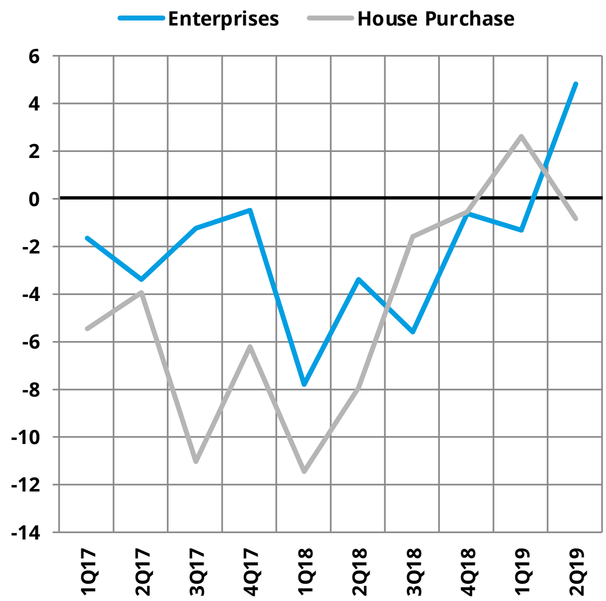
Institutional investors or other funds use debt funds to invest in loans to companies, real estate or infrastructure projects. As already elaborated in our previous analyses of the European debt fund market, a debt fund is an investment vehicle that invests in largely illiquid and non-tradable loans or grants loans directly. A debt fund is financed by equity in the form of shares or by issuing debt instruments (see e.g. Debt Funds in Europe – Buoyant Growth in a Nascent Market, August 2015). Essentially, there are two characteristics that distinguish debt funds from fundamentally similar product alternatives such as securitizations: (i) the number of assets in which a debt fund invests tends to be generally substantially lower than in an ABS pool, and (ii) there is no slicing into tranches in a debt fund structure, i.e. there is no waterfall.

Looking back over the past year, it should be noted that the market environment for debt funds has become more complex both in Europe and in the United States. Economic activity on both sides of the Atlantic thus peaked in 2018 (United States) or has already passed its peak (euro area).

Deteriorating economic prospects are reflected, inter alia, in the lending practices of European banks. According to the latest Bank Lending Survey conducted by the European Central Bank (ECB), banks in the euro area became increasingly cautious about lending over the course of last year. Largely driven by declining risk tolerance and a simultaneous increase in risk perception with regard to macroeconomic and company-specific risks, banks in the euro area have tightened their credit standards for companies and households since the first quarter of 2018 (see Fig. 1).

Figure 1: Changes in Credit Standards in the Euro Area

Net percentages of banks reporting tighter credit standards (>0: more restrictive credit standards)



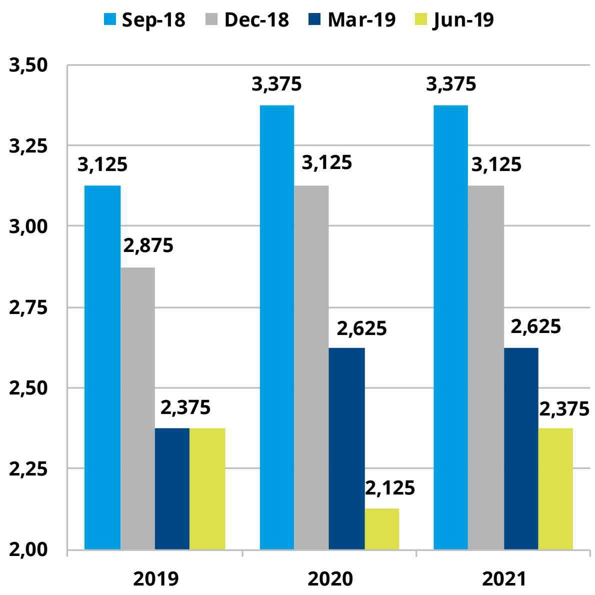
Sources: ECB, Creditreform Rating

Against this background, the major central banks' monetary policy normalization came to a halt. In the euro area, the ECB has repeatedly postponed the tightening of its monetary policy since last summer. Although the asset purchase program (AAP) was terminated on schedule in December, a first rate hike will come much later than previously envisioned. While in June 2018 a first interest rate increase had been envisaged for 2019, the ECB adapted its forward guidance several times, to signal a later start of policy rate normalization and a flatter projected interest rate path. Following its meeting in March 2019, the ECB Council had announced that it would maintain the main refinancing rate at the current record low of 0.0% at least beyond the end of 2019, before deciding to postpone it again in June. According to the latest decision back in July, key interest rates in the euro area will now remain at the current level at least beyond the summer of 2020.

The Federal Reserve also recently took account of the gradual cooling of the US economy and the gloomy global economic environment. After four key interest rate hikes in 2018, the Fed has now initiated a change in its monetary policy stance. Since the fourth quarter of 2018, FOMC members thus have continuously revised their expectations for the future interest rate path downwards (see Fig. 2).

Figure 2: FOMC Forecasts for the Fed Funds Rate

Fed Funds Rate in %, median forecast for the end of the year at the respective FOMC meetings



Sources: Federal Reserve Board, Creditreform Rating

Instead of three, as in September 2018, they only expected two further interest rate hikes in 2019 last December. At its meeting this March, the Fed finally decided to completely give up plans to further tighten monetary policy. The June FOMC minutes revealed that monetary policy was even expected to become more expansionary in the near term. While one FOMC member expected an interest rate cut by the end of 2019, seven of the 17 voting FOMC members announced that they expected two cuts in the Fed Funds Rate in 2019. Eventually, the Fed lowered interest rates in July for the first time since December 2008, cutting the Fed Funds Rate target range by 25 basis points to 2.00-2.25%. In view of the escalating US-Chinese trade conflict and slower global economic growth, the Fed has also signaled the possibility of further rate cuts.

How did European debt funds perform in this environment? In what follows, we continue our analysis of the market development of debt funds in Europe. In general, Creditreform Rating monitors market developments on an ongoing basis, analyzing existing, future, and potential risks at the various levels of debt fund structures, and assessing a wide range of financial instruments related to debt funds.

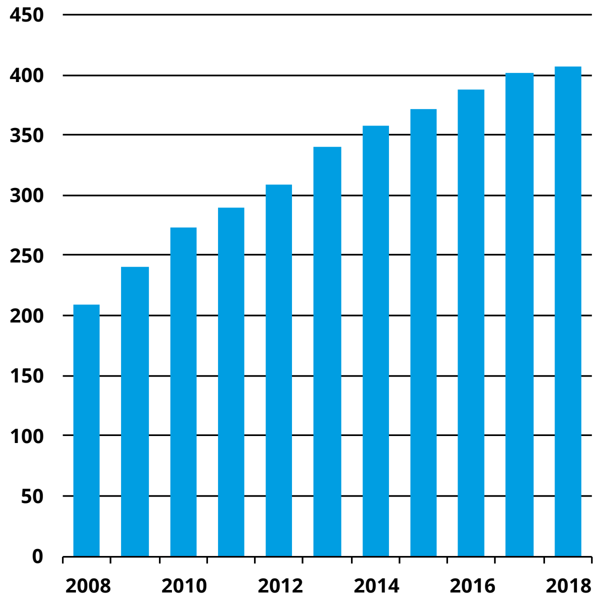
Published for the first time in 2014, we provide an overview of the trends in the asset classes real estate, infrastructure and direct lending (corporate), and compare them with the development of the US market. We follow an inductive and explorative approach by compiling the available data on the European debt fund market in order to highlight the most exciting developments. Our calculations are based on data from Preqin and our own market data. This year we will take a closer look at the investor side of the debt fund market for the first time.

2. The Debt Fund Market in Europe and the United States

One indication of the increasing attractiveness of debt funds as a form of investment is the steadily growing number of debt fund managers who have entered the European market in recent years. In addition to the 209 investment companies that launched debt funds in 2008, a further 100 companies were added by 2012 alone; in 2016, 388 financial market players were already managing debt funds. In the past two years, however, the number of new fund managers has grown only moderately. Whereas in 2016 17 fund managers discovered the debt fund market, in 2017 and 2018 only 14 and 5 market entries were observed (see Fig. 3).

Figure 3: Fund Managers in Europe

Number of European debt fund managers

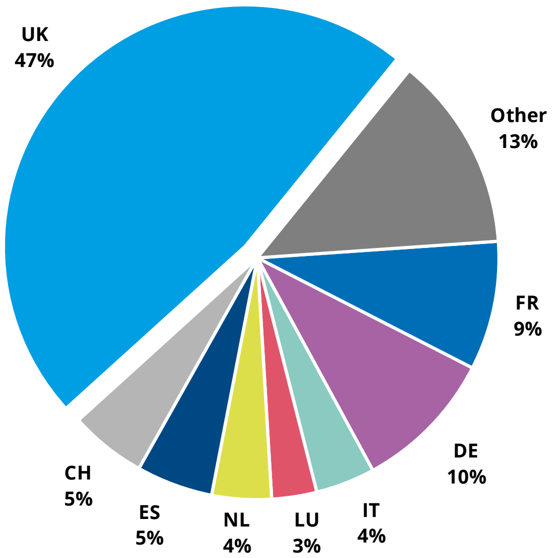


Sources: Preqin, Creditreform Rating

In this context, we assess a strong geographical concentration with regard to the origin of the European fund managers. Two thirds (65.7%) of the investment companies are based in only three European countries (see Fig. 4). The ranking of the most important countries of domicile is clearly led by the United Kingdom. Almost half (47%) of all European debt funds are managed from the British Isles. Germany (10%) and France (9%) follow in second and third place. Barring these three economies, however, the European market is relatively fragmented. Measured by the share of the total number of European fund managers, none of the other European countries reaches a market share larger than 5%.

Figure 4: Fund Managers by Country of Origin

Share of total number of European fund managers



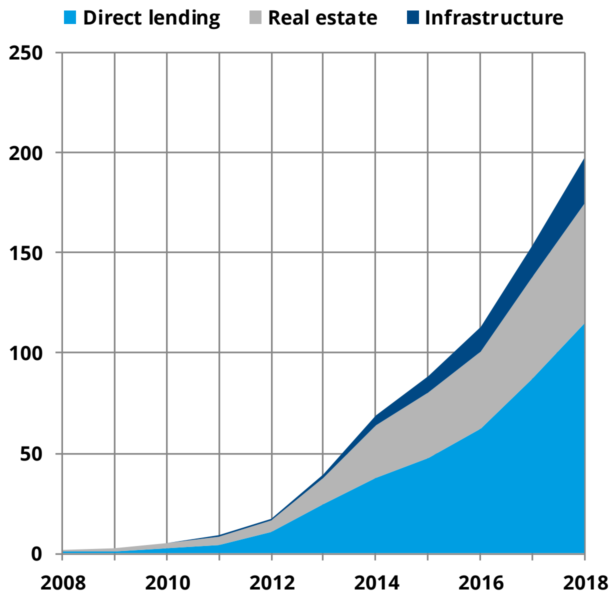
Sources: Preqin, Creditreform Rating

Turning to market activity, the available data confirms that the European debt fund market has been extremely buoyant over the last decade and has increasingly established itself as an alternative to traditional forms of financing such as bank loans and bonds.

While the cumulative debt fund volume in Europe, which in our analysis comprises the asset classes private debt (direct lending), real estate, and infrastructure, came in at only 1.9bn euros in 2008, five years later it was 20.2bn euros (2012), before the threshold of 150bn euros was crossed for the first time in 2017 (see Fig. 5). The long-term upward trend continued more recently, as the European debt fund market experienced another strong year in 2018. The cumulative fund volume, including debt funds which are still raising, thus grew by 43.8bn euros to 197.2bn euros in 2018.

Figure 5: Development of the Total Volume of European Debt Funds

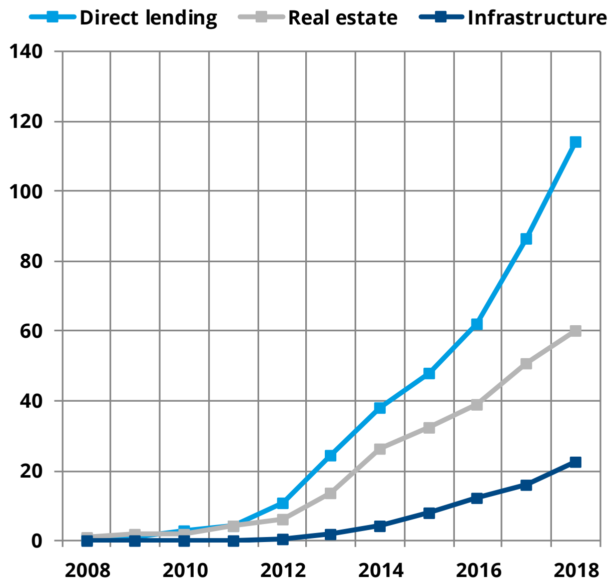
Total cumulative volume in billion euros, including raising debt funds



Sources: Preqin, Creditreform Rating

Figure 6: Volumes of European Debt Funds in the Various Asset Classes

Total cumulative volume in billion euros, including raising debt funds



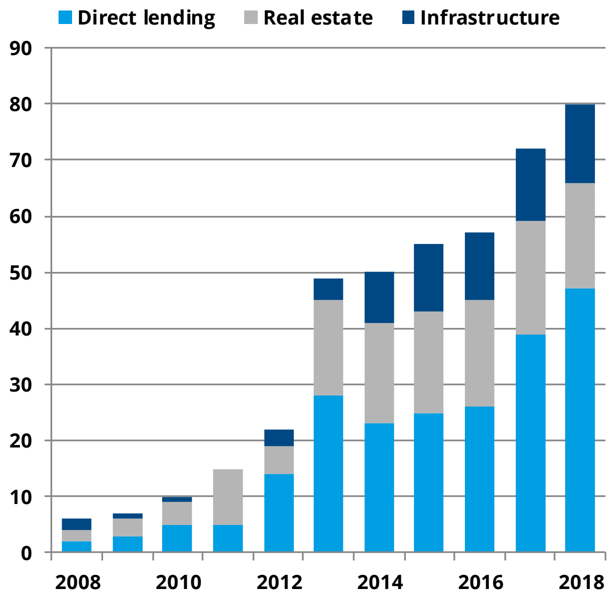
Sources: Preqin, Creditreform Rating

The debt fund market performance was largely driven by the strong growth in the newly registered fund volume in the private debt segment. In 2018, European direct lending funds recorded a capital inflow of 27.7bn euros within a year (see Fig. 6). After 14.2bn and 24.6bn euros in 2016 and 2017 respectively, inflows in this segment grew for the third consecutive year. Direct lending was also the most dynamic debt fund segment last year in terms of the number of new funds launched. While the number of new funds registered in the asset classes real estate (19) and infrastructure (14) in 2018 was similar to that of the previous year (20 and 13 respectively), the number of direct lending funds grew significantly from 39 to 47 in 2017-18 – doubling the number of funds since 2014, when 23 funds from this asset class were registered (see Fig. 7). Overall, direct lending funds were thus able to further consolidate their leading position in the European debt fund market.

European real estate debt funds also recorded sustained, albeit somewhat weaker growth, than in the previous year. While the newly registered fund volume in the market almost doubled in 2017 to 11.6bn euros (2016: 6.3bn), growth in 2018 was more moderate at 9.8bn euros. Nevertheless, the capital raised last year was still well above the level of 2015 and 2016. Despite the robust growth in the recent past, European real estate funds are increasingly losing ground compared to the direct lending segment. While both asset classes were still at the same level (EUR 4.4bn) in terms of cumulative fund volume in 2011, the gap gradually widened in subsequent years. In 2018, the cumulative fund volume in the real estate segment amounted to 60.3bn euros, well below the corresponding value for direct lending funds (114.3bn euros).

Figure 7: Number of European Debt Funds in the Various Asset Classes

Number of debt funds per year, including raising debt funds



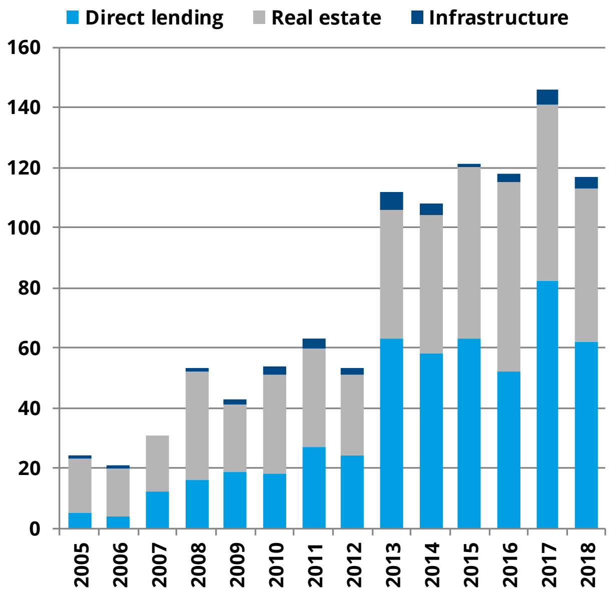
Sources: Preqin, Creditreform Rating

Meanwhile, the market for European infrastructure funds, the smallest debt fund segment in terms of volume, picked up considerably in 2018. After the capital collected by newly established funds fluctuated between 3 and 4bn euros per year in 2015-17, the segment gathered some steam more recently. At 6.3bn euros, the aggregate volume of new European infrastructure funds marked a new high within the period covered by our analysis. Nonetheless, despite persistently strong growth, the infrastructure sector continues to be kind of a niche in the European debt fund market. Recently, the cumulative fund volume of the infrastructure asset class climbed to 22.5bn euros, thus amounting to only one-third and one-fifth of the market size of European real estate and direct lending funds respectively.

As a result of the growing importance of direct lending funds over the past decade, there has been a structural shift in market shares within the European debt fund market. In 2018, just under a third (30.6%) of the cumulative debt fund volume was attributable to the asset class real estate, while infrastructure and in particular, direct lending funds were able to significantly expand their respective market shares to 11.4% and 58.0% respectively. To put things into perspective: in 2008, the real estate fund segment (60.5%) dominated the market by a wide margin, followed by direct lending (35.3%) and infrastructure funds (4.2%).

Figure 8: Number of US Debt Funds in the Various Asset Classes

Number of debt funds per year, including raising debt funds

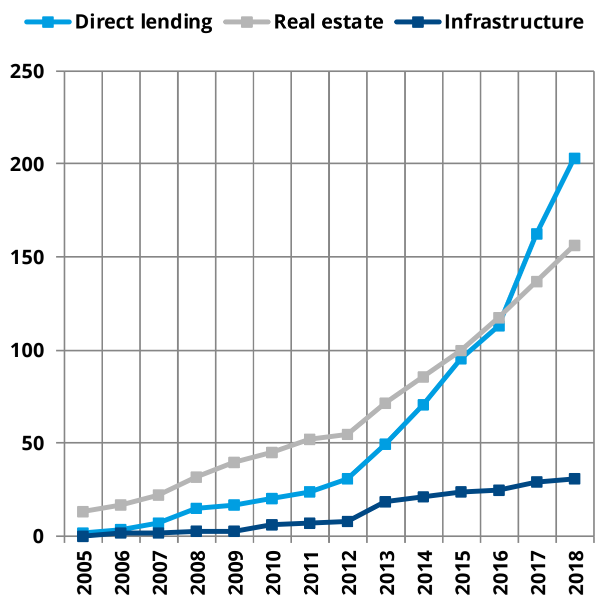


Sources: Preqin, Creditreform Rating

Looking at debt fund markets on the other side of the Atlantic, we see that the US debt fund market also remained on its expansion course in 2018, although both the capital raked in and the number of newly established debt funds stood below the previous year's level. After the record year of 2017, when 146 new funds with a volume of 72.3bn euros were registered, the number of funds in 2018 totaled 117 (see Fig. 8), the corresponding volume across all asset classes was 62.2bn euros.

Figure 9: Volumes of US Debt Funds in the Various Asset Classes

Total cumulative volume in billion euros, including raising debt funds



Sources: Preqin, Creditreform Rating

This was mainly due to the more moderate growth momentum in the direct lending segment. While 82 new direct lending funds were counted in the market in 2017, their number recently fell to 62, roughly the same level as in 2015 (63). The associated fund volume also declined slightly, falling from 49 (2017) to 40.6bn euros within a year (see Fig. 9). Although at a significantly lower level, the US infrastructure funds have recently experienced a similar development. While the number of newly established funds fell only slightly from 5 (2017) to 4 in 2018, the corresponding volume fell significantly from 4.7 to 1.8bn euros.

At the same time, the US real estate debt fund segment remained relatively stable. Although only 51 new funds entered the market last year (2017: 59), as few as in 2014 (46), this was not reflected in a decline in the corresponding fund volume. On the contrary, equaling 19.8bn euros, slightly more fresh capital flowed into US real estate debt funds in 2018 than in the previous year (19.6bn euros). Overall, last year's growth was not yet sufficient to regain the top position held by direct lending funds. After the US debt fund market had been dominated by real estate debt funds for many years, this asset class was outperformed by direct lending funds for the first time in 2017. Most recently, the cumulative real estate fund volume amounted to EUR 156.4bn and was thus well behind the direct lending segment (EUR 202.7bn).

A comparison with Europe shows that debt funds played a more relevant role on the US capital market relatively early on. Ten years ago, the United States already had a debt fund market of considerable size at a time when the European market was still in its infancy. While the volume of US real estate debt funds alone already amounted to 31.9bn euros in 2008, the European market achieved a cumulative volume of just 1.9bn euros across all asset classes. It is therefore not surprising that the US market is now at a much more mature stage. There is no doubt, that Europe has been able to gain ground in recent years. Still, the US debt fund market, with a cumulative volume of 389.5bn euros in 2018, remains significantly larger than its European counterpart (197.2bn euros).

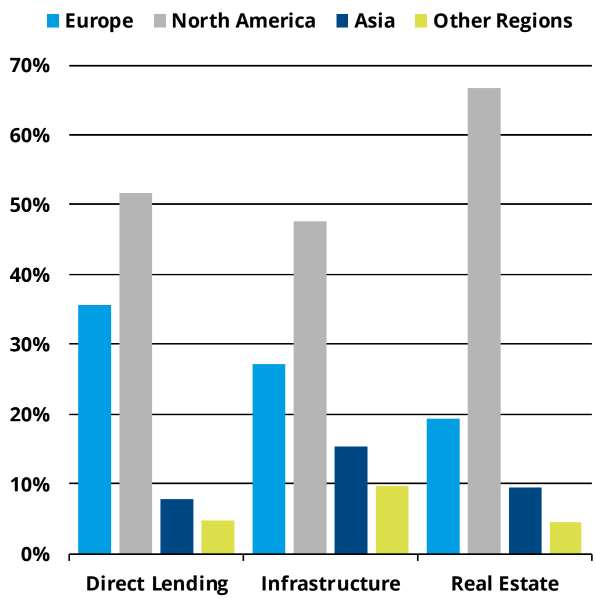
3. The Investor Base of European Debt Funds

Having already examined the sector focus (2017) and risk/return profile (2018) of European debt funds in detail in recent years, we would like to highlight the structural composition of the financing side for the first time in this year's analysis. So what kind of financial market participants invest in European debt funds?

Contrary to what might be expected, European investors are not of paramount importance on their domestic market. Measured by the number of investors, all segments of the European debt fund market are dominated by North American investors (see Fig. 10). The lead in European real estate debt funds is particularly pronounced. Two out of three investors (67%) who cited this segment as their preferred investment target were based in North America. By contrast, only every fifth company (19%) was a European-based investor. The same pattern can be observed in the infrastructure segment, although the discrepancy between American and European investors is not quite as pronounced.

Figure 10: Investor Base of European Debt Funds by Asset Class

Regional share of total number of investors with primary focus Europe, in %



Sources: Preqin, Creditreform Rating

Meanwhile, the European investor base is comparatively strong in the direct lending asset class. European investors accounted for 36% of the players investing primarily in this segment. In the infrastructure and real estate segments, the respective share of European investors is significantly lower at 27% and 19% respectively.

If we take a look at the level of individual countries, the dominance of North American investors is essentially a result of the strong engagement of US investors. Investors from the United States are by far the most important investors in all asset classes. While 44% of infrastructure investors come from the United States, the respective shares in the direct lending and real estate segments are significantly higher at 48% and 64% respectively. With a view to Europe, it is primarily investors from the United Kingdom who are showing strong interest in debt funds: About every tenth investor in European direct lending (10.0%) and infrastructure funds (11.3%) is based in the UK, while the UK share of real estate funds is 6.6%.

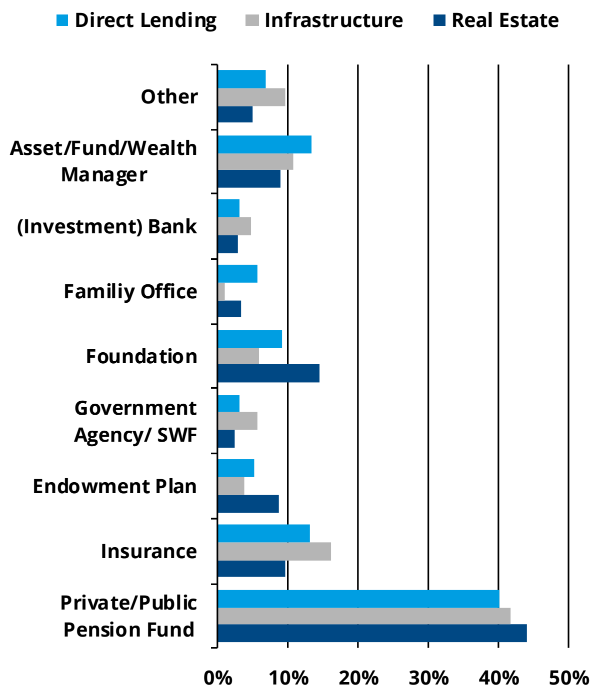
On the whole, the investor base of European debt funds is relatively strongly concentrated in only a few countries. Depending on the asset class, the top three countries by origin of the investors cover between 62.3% (direct lending) and 75.7% (real estate) of the respective market. From a geographical point of view, the investor base of European infrastructure funds is the most diversified. In addition to the USA and UK, which also lead the ranking here, a striking number of countries from the Asia-Pacific region are represented in the top 10. With an investor share of 8.3%, Australia ranks third, followed by South Korea (7.5%) and Japan (4.1%). In addition, infrastructure is the only asset class in which Chinese investors play a significant role: with 1.5%, China ranks tenth in the infrastructure ranking.

Similar to the analysis by geographical origin, the typology of institutional players investing in European debt funds shows a high degree of concentration.

Not surprisingly, public and private pension funds are by far the most important investors, followed by insurance companies. In the direct lending segment, pension funds recently accounted for 40% of investors, followed by insurance companies and asset managers with 13% each. There were only slight differences in the investor ranking of infrastructure funds, with values in the corresponding asset classes of 42%, 16%, and 11%. Only the European real estate funds have a slightly different composition of the top-3 investors. Although pension funds (44%) have the greatest weight here as well, with a share of 15%, foundations are pushed past insurance companies (10%) to second place (see Fig. 11).

Figure 11: Investors by Firm Type

Share of total number of investors with primary focus Europe in the respective assets class

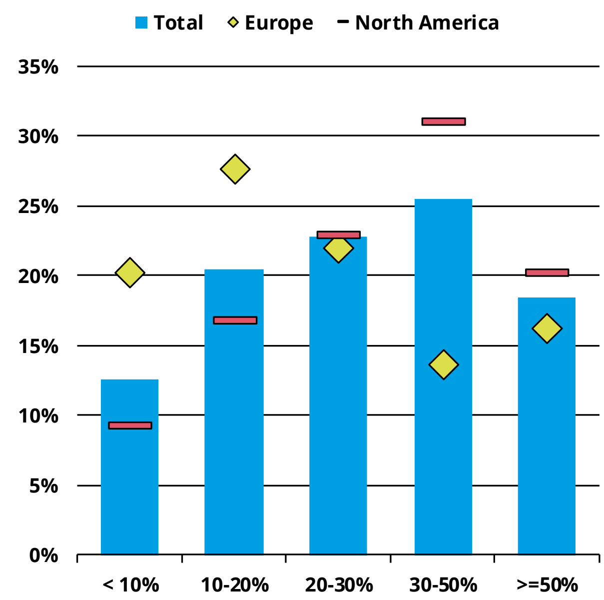


Sources: Preqin, Creditreform Rating

Finally, institutional investors appear to view alternative assets, which also include debt funds in this analysis, more as an admixture than as a main component of the portfolio. Slightly more than half of investors with an investment focus on Europe (56%) state that they invest a maximum of 30% in alternative assets in their portfolio (see Fig. 12).

Figure 12: Fund Allocation to Alternatives

x-axis: Share of AUM allocated in alternatives,
y-axis: Share of investors with primary focus Europe falling into respective classes of alternatives allocation



Sources: Preqin, Creditreform Rating

However, there appear to be significant differences in the investment behavior of North American and European investors. The results of our analysis suggest that European investors are more reluctant to invest in alternatives than their American counterparts. For example, one-fifth (20%) of European investors say they invest less than 10% of the fund's assets in alternative assets, a further 28% state their limit as 20%. For comparison: Among North American investors, the respective shares are significantly lower at 9% and 17% respectively. In contrast, American investors are disproportionately represented at the opposite end of the spectrum. Almost a third (31%) of North Americans allocate 30-50% of their assets under management to alternative assets, every fifth American investor (20%) even invests more than half of the available funds in alternative assets (Europe: 20 and 16% respectively). A potential explanation for the greater openness of North American investors may be found in the advanced maturity of the domestic alternative asset market, which may favor a higher degree of specialization among investors, and the fact that the US financial system tends to be more market based.

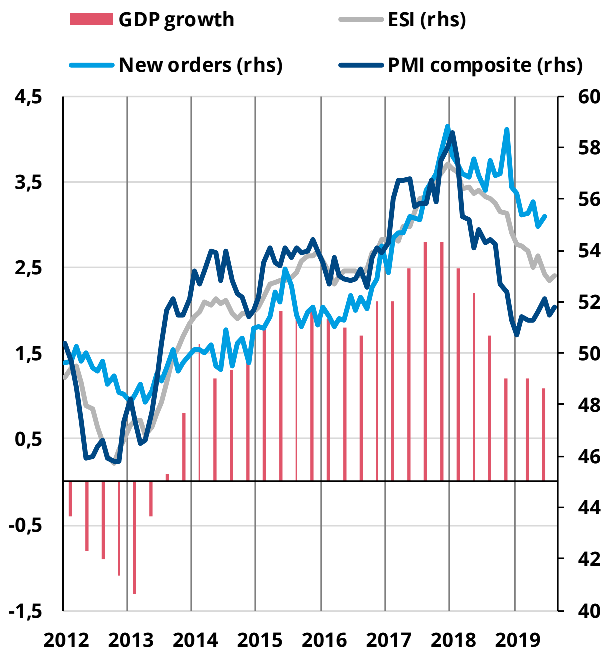
4. Outlook

The European debt fund industry must prepare itself for a challenging macroeconomic environment in the short to medium term. On the one hand, we expect the euro area to experience an economic downturn, not a recession, accompanied by significantly lower growth rates than we have observed in recent years. On the other hand, we believe that we will not see an abrupt end to the ultra-loose monetary policy witnessed over the last couple of years. On the contrary, the current interest rate environment in the euro area is likely to be maintained in the medium term.

In the first half of the year, growth rates of 1.2% (Q1-19) and 1.1% y-o-y (Q2-19) respectively were recorded, well below the level of the previous year (2.5% and 2.2%). The available leading indicators currently do not point to a noticeable recovery in the second half of the year (see Fig. 13). Incoming orders in the industry sector as well as the Economic Sentiment Index of the EU Commission have tended to continue their downward trend recently. Since the beginning of the year, the Purchasing Managers' Index (PMI) for the euro area has shown only signs of stabilization, not recovery, after a significant decline throughout 2018. In August, the composite PMI remained above the 50 point mark, indicating that the euro area economy should maintain its current growth rate in the coming months. For the year as a whole, however, the economy in the euro area will prospectively lose considerable momentum.

Figure 13: Growth Prospects for the Euro Area

LHS: y-o-y change in real GDP in %
RHS: Diffusion indices. Economic Sentiment Indicator (ESI) and New Industry Orders have been standardized and rescaled to display the same standard deviation and mean values as the Purchasing Managers' Index (PMI)



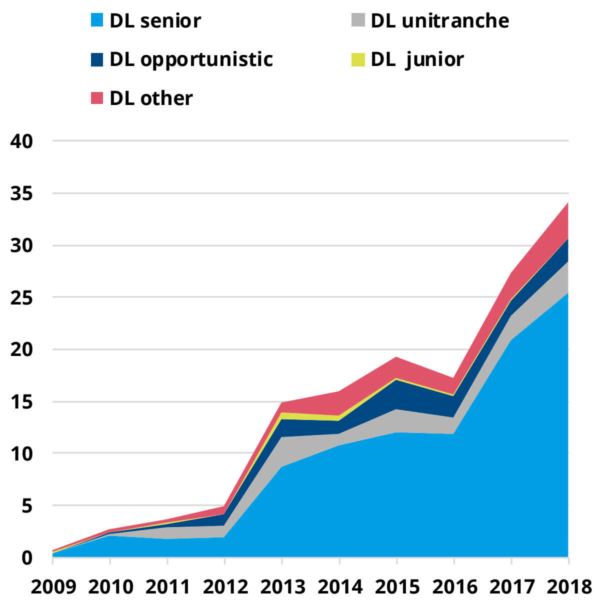
Sources: Eurostat, Refinitiv, Creditreform Rating

In the context of the weakening economic environment, we see downside risks for debt funds, in particular for direct lending debt funds. On the one hand, existing direct lending debt funds are likely to be increasingly confronted with a deterioration in firm-specific risk against the weaker backdrop in the general economic situation. Corporates are struggling with recessionary trends in the industrial sector, US-China trade disputes as well as concerns about a disorderly Brexit and an abrupt slowdown in Chinese economic growth. In view of the fact that direct lending funds are primarily invested in the sub-investment grade corporate sector, difficulties are to be expected here rather than in segments with higher credit quality. Obviously, a distinction must be made here between debt funds that are already fully invested, and those that are still fundraising and can diversify their portfolios from a risk perspective to some extent.

Looking ahead, i.e. with direct lending funds that are awaiting to be launched, we expect that the effects of the generally poorer economic situation on credit quality and company valuations will lead to some adjustment in pricing, and we may see spreads that tend to widen.

Figure 14: Dry Powder of European Direct Lending Debt Funds

In billion euros



Sources: Preqin, Creditreform Rating

From a risk perspective, direct lending funds should also be monitored closely as we believe that financing targets are becoming increasingly scarce ("chasing for opportunities"). At the same time, more and more capital is being secured that can be used to finance the corporate sector, as illustrated, e.g. by Preqin's direct lending dry powder data. Dry powder of direct lending debt funds in 2018 rose by around 25% on the year to around EUR 34bn, a quarter of which was non-senior debt (see Fig. 14). Compared to the level ten years ago, dry powder has almost risen by a factor of 60. In principle, there is a danger of an oversupply of financing, which in the worst case could result in excessive risk-taking and adverse effects on the underwriting quality.

Finally, it must be mentioned that, especially in the direct lending segment, we perceive a number of new fund managers in the market who do not have the experience and track record of several financial cycles as is the case in the infrastructure segment, for instance.

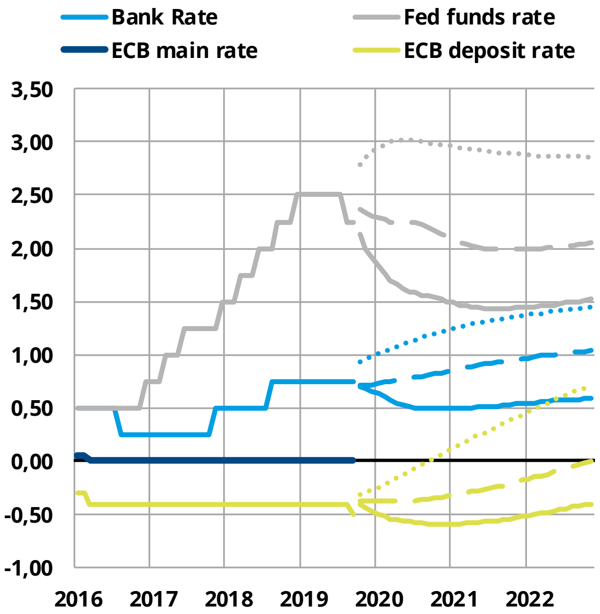
As regards the second major macro driver, interest rates should remain low in the short to medium term in the light of recent monetary policy decisions.

A third round of longer-term refinancing transactions (TLTRO III) has already been concluded in spring 2019, which is intended to provide euro area banks with sufficient liquidity, and to boost corporate and consumer lending. In the wake of increasing economic downside risks and declining inflation expectations, the ECB took additional expansive measures at the latest meeting of the Governing Council on 12 September. As expected, the interest rate for the deposit facility was decreased by 10 basis points to -0.5%. In addition, it was decided to resume net purchases under the APP in a monthly amount of 20bn euros as from 1 November.

The net purchases will not end until shortly before the ECB raises its key interest rates. As can be seen in Fig. 15, however, the first increase in key interest rates should not be expected before 2021 - not only in the euro area, but also in the United States and the UK.

Figure 15: Key interest rates and market expectations regarding interest rate paths

Nominal policy rates, forward overnight index swap rates as of 24-Jul-19 (solid lines), 24-Apr-19 (dashed lines), 24-Oct-18 (dotted lines)



Sources: Bank of England, Creditreform Rating

We are somewhat skeptical about the effectiveness of the ECB war chest. From our point of view, recent and possible further monetary policy measures should have a limited impact on economic activity and consumer prices. It seems too tempting to assume that the mere announcement of further measures alone will increase the confidence of households and companies going forward. Rather, we believe that the hope that the ECB will revive growth in the euro area is likely to be disappointed as it has fought for so long for a sustained recovery of the euro area economy, and is nearing the limit for government bond purchases, which is limited to one third of each member state's debt. Indeed, it is much more up to national authorities to step up the urgently needed structural reforms in order to boost the growth potential of their economies and reduce structural unemployment.

That being said, we believe that in an economic environment in which safe-haven government bonds often only display negative yields, the asset class of debt funds will continue to benefit from a continued search-for-yield momentum. The demand for riskier forms of investment promising higher yields, such as debt funds, should remain brisk in the current monetary policy environment.

Furthermore, we assume that politics and the banking sector will also remain intact as structural drivers. While policymakers in Europe welcome and support instruments that are conducive to facilitate a market-based finance system, banks will continue to be cautious in the high-yield segment amidst stricter regulatory risk requirements, or are divesting themselves of business segments that could then fall to debt funds going forward.

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