Report | 5 June 2023

CREDIT

Euro Credit Supply: Large supply played a role in weaker spreads

Weakness in credit markets is partially due to the supply indigestion from the large supply seen in May. We expect spreads will continue to be plentiful in June

Executive summary

Expect supply in June to be decent, although below the large levels seen in May

There was substantial corporate supply in May, totalling €48bn, the highest monthly supply so far this year. Supply was heavier after limited windows of opportunity in March and April. The macro environment has become ever so important for credit and rates, and thus primary markets remain closed during economic data publications, central bank meetings and holidays. Therefore, when an issuance window is open, there is a big rush of new deals – from corporates, financials and SSAs. Saturated primary markets therefore results in very heavy days of supply indigestion. As such, primary markets will continue to drive secondary spreads by pushing secondary spreads wider to match the primary levels, which is the true place where substantial supply meets substantial demand. This is one of the many factors that combined to pressure credit, as outlined in our report Small factors combine to pressure credit.

YTD supply is at €161bn, currently running 13% ahead of last year. We continue to forecast supply to total €270bn, up 10% on last year. As such, we are likely to see a decent level of supply come to the market in June, and then slightly slower supply in the

second half of this year.

Reverse Yankee supply is adding to the barrage. Reverse Yankee supply was also plentiful in May, with €12bn issued. The calculation was favourable for a cost saving advantage for US issuers to bring a EUR bond to the market, namely on the back of USD spread underperformance versus EUR. This differential is now narrowing, particularly in the 5yr. Thus, we may not see too many more Reverse Yankee deals this month, unless the differential widens again.

Financial supply to remain at elevated levels in June

Financials supply was also substantial in May, totalling €33bn, although not to the same levels as corporates. The last week of May, however, saw a skew towards more financials supply. We expect financials supply will continue to come at significant levels over the coming few of weeks. YTD supply is still running ahead of previous years, now sitting at €163bn.

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