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Recorded 30 September 2025

Fixed Income

Euro Credit Market Update

Boutain Deixonne, Head of Euro IG & HY Credit

What have we seen since our last quarterly update?

Euro credit spreads continued to tighten during the summer period, supported by robust inflows, decent Q2 earnings and the expected easing cycle from the Federal Reserve (Fed). The uncertainty around tariffs is now behind us, and for now, there has not been a large impact on companies' fundamentals.

In the second half of August, spreads widened modestly on the back of expectations of a dynamic primary market, some concerns about the Fed's independence, and some political tension in European countries. But this trend has already reversed due to an underwhelming primary market while the flows momentum continue to be strong.

Recent economic data has been mixed, notably in the labour market in the US. However, this implies that the economy and labour markets will potentially cool in an orderly manner, and with earlier cuts, the odds for a recession have gone down. This context bodes well for spreads in the coming months.

Will this positive momentum continue ?

One of the main drivers of credit spread tightening has been the robust inflows we have seen into the credit asset class. This can be explained by the high level of savings rates we benefit from in Europe. With central banks expected to continue to cut in the coming months, credit markets should continue to benefit from this trend as it may offer an extra pick-up versus risk free rate and cash instruments.

As yields remain attractive, this should also support inflows and at this stage, we don't see any imminent catalyst for outflows. Primary issuance has provided additional supports. Year to date supply in the euro investment grade has risen by 10%, exceeding €600 billion¹. We do not anticipate a significant acceleration of issuance over the coming months, suggesting that technical pressure on spreads could persist, particularly if inflows remain strong.

Finally, fundamentals of the euro credit remain sound. Q2 earnings have been in line with expectations overall, with corporates and financials reporting strong credit metrics, solid capitalisation and still positive rating trajectory. On the other hand, M&A (merger and acquisitions) has been rather underwhelming in Europe, implying lower idiosyncratic risk.

Taken together, those factors should continue to provide a support for the credit asset class.

What are the potential risks and how are we positioned ?

Growth remains positive overall, although risks are tilted to the downside. In Europe, inflation is decelerating broadly in line with expectations, while in the US it has proven stickier than expected. The impact of tariffs has been relatively benign so far, with companies benefiting from front-loading. However, Q3 and Q4 earnings will be critical to monitor as the additional 15% tax could eventually weigh on volumes, on demand or corporate margins. While valuation alone might not be the primary driver of spread widening, a combination of weaker growth and stretched valuation could put pressure on credit spreads.

¹ Source: Bloomberg, as of 30 September 2025

This dynamic may also influence central bank policy decisions in the coming months.

Another key factor to monitor is the potential for a prolonged period of volatility in the rates market. Given the historical correlation between rates and credit volatility, a sustained episode could spill over into credit markets.

In conclusion, we continue to be defensively positioned with selective allocation to high-yield and subordinated debt. We have a preference for the 5 to 10 Year exposure, notably for banks, utilities and telecoms, and remain underweight on cyclical. Nevertheless, we would be inclined to increase risk if we see higher spreads in the coming months.

Thank you for watching this video and see you soon.

Source : AXA IM as of September 2025

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