

# Brexit fears spark credit volatility; loans recovery

In this week's credit wrap, fears of a UK exit from the European Union sparks market volatility, the Fed holds interest rates steady and leveraged loans continue to outperform.

- 10-yr US treasury yields have fallen to 1.58%, the lowest level since mid-2012
- UK's 5-yr CDS spread has widened back out to 2016 highs
- Markit iBoxx USD Leveraged Loans Index sees 4.7% total return so far this year

## Fed stays put

US Federal Reserve chair Janet Yellen cited fears around Britain leaving the EU in next week's referendum as a contributing factor in the decision to keep interest rates on hold this week. After increasing interest rates by 25bps last December, external factors have since halted any further action from the Fed. Given the credit market reaction to the growing probability of a Brexit this week, it is clear to see why the Fed chose to err on the side of caution.

### 10-yr US treasury



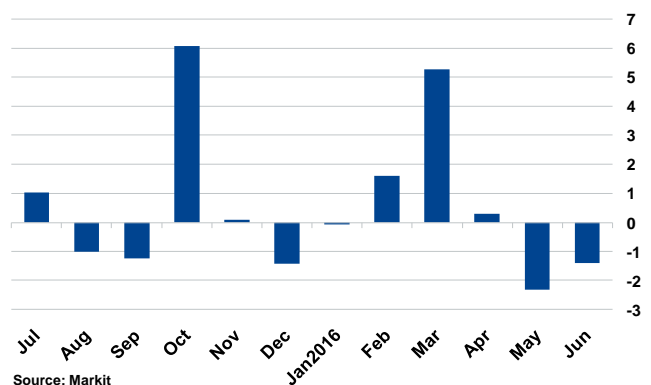
The Markit iTraxx Europe main index widened to 88bps as of June 14<sup>th</sup>, a three month high, with the banking sector taking the biggest hit. Global government bond yields have continued to fall, with 10-yr US treasury yields sinking to 1.58%; the lowest since mid-2012 according to Markit's bond pricing service.

### UK 5-yr CDS spread



Meanwhile, the cost to protect against the UK defaulting on its government debt has widened back to the highs seen in April. The UK's 5-yr CDS spread is now over double the level seen at the beginning of the year, 41bps, from 18bps.

### High yield ETFs monthly inflows/outflows (\$bn)



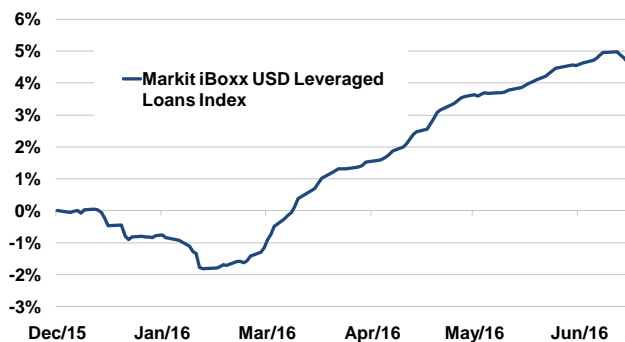
Investors have also been keen to steer clear of any volatility by de-risking. ETFs tracking high yields bonds have seen significant outflows over the past week according to Markit's ETP analytics. June's total outflow is \$1.4bn so far, on course for two consecutive

monthly outflows - similar to periods of heightened market volatility seen last December/January and last August/September.

### Loans roar on

After a tough start to the year, leveraged loans have recovered to produce consistent returns over the past few months amid a more positive economic backdrop.

**Total return so far this year**



Source: Markit

The positive sentiment around the asset class can be observed in the performance of the Markit iBoxx USD Leveraged Loans Index. The index has returned 4.7% on a total return basis so far this year and has gathered momentum. This comes in sharp contrast to the performance seen towards the second half of 2015 and the first two months of 2016, as investors dumped risky assets.

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