

Morningstar Leveraged Loan Index Monitor: Q4 2025

Leveraged loans wrap up the year with positive returns.

Morningstar

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Executive Summary

This is the latest installment of the Morningstar Leveraged Loan Index Monitor, which is designed to help investors stay on top of the latest trends in the leveraged loan market through the lens of three Morningstar Leveraged Loan Indexes: Morningstar LSTA US Leveraged Loan Index, Morningstar European Leveraged Loan Index, and Morningstar Global Leveraged Loan Index.

Key Takeaways

- ▶ In the last quarter of 2025, the Federal Reserve reduced the federal-funds rate by 50 basis points through consecutive rate cuts in October and December.
- ▶ The Bank of England implemented a 25-basis-point cut, bringing the policy rate to 3.75% at the December 2025 Monetary Policy Committee meeting. In comparison, the European Central Bank kept the key ECB rates unchanged, maintaining the deposit facility rate at 2%.
- ▶ Shorter-maturity Treasury yields declined by an average of 35 basis points, while longer-maturity yields increased modestly, rising only 8 basis points.
- ▶ The Morningstar LSTA US Leveraged Loan Index provided the best risk/return characteristics relative to the Morningstar Global Leveraged Loan Index and Morningstar European Leveraged Loan Index over the fourth quarter amid increased market volatility and secondary market weakness.
- ▶ US leveraged loan spreads edged wider by 14 basis points in the fourth quarter, while European leveraged loan spreads tightened by 10 basis points and remained near long-term lows.
- ▶ Leveraged loan issuance lost momentum throughout the quarter. In the US, issuance reached USD 207 billion, a decrease from USD 347 billion in the previous quarter. Similarly, European new issuances fell to EUR 54 billion, down from EUR 72 billion in the previous quarter.
- ▶ BB rated credits outperformed in the US leveraged loan market, while CCC credits delivered negative returns. In Europe, only B rated loans generated positive returns for the quarter, as BB and CCC cohorts declined.

Market Update

Federal Reserve Cuts Rates to Spur Economic Growth

The Fed reduced the target federal-funds rate by 25 basis points in both the October and December Federal Open Market Committee meetings, bringing the target rate to 3.50% to 3.75%.

Real gross domestic product grew in the second quarter of 2025 by an annual rate of 4.3%, a 50-basis points improvement over the 3.8% annual growth in the second quarter¹. The projections for annual real GDP growth in 2025 increased to 1.7% from an earlier projection of 1.6%. Personal consumption expenditures inflation projection was reduced to 2.9%, a 10-basis-point reduction from the previous projection².

The job market showed signs of a slowdown with the slightly elevated unemployment rate in September playing a significant role in the Fed's decision to reduce interest rates. Despite inflation remaining slightly elevated, the Fed made the decision to pivot toward supporting economic growth and maintaining stable employment.

Bank of England Cuts Rates, With Eye on Inflation

The Bank of England cut interest rates by 25 basis points to 3.75% at the Monetary Policy Committee meeting in December 2025, after holding rates steady in November.

The UK's real GDP witnessed an increase of only 0.1% in the third quarter of 2025, compared with the 0.2% growth recorded in the previous quarter.

The third quarter of 2025 reflected stagnated economic growth but a slight drop in CPI inflation to 3.2% in November compared with 3.8% in September.³ CPI inflation is projected to ease to 3% by first-quarter 2026. Reduced inflationary pressures allowed the Bank of England to continue on the downward trajectory for interest rates.

European Central Bank Keeps Rates Unchanged

The European Central Bank decided to keep the three key ECB rates unchanged in the October and December Monetary Policy Committee meetings. The deposit facility rate stands at 2%, the main refinancing operations rate at 2.15%, and the marginal lending facility rate at 2.4%.

The euro area's real GDP grew by 0.3% in third-quarter 2025 against the backdrop of stronger consumption and investments. The unemployment rate stood close to historical lows at 6.4% in October, showing robustness in the European labor market.

Inflation remained within the ECB's 2% target, with the headline Consumer Price Index holding steady at 2.1% in November. European Central Bank projections see inflation averaging 2.1% in 2025 and 1.9% in

¹ Data source for GDP growth rates: Bureau of Economic Analysis, US Department of Commerce, released on Dec. 23, 2025.

² Real GDP growth rates projections data source: FOMC Projection Material, Federal Reserve.

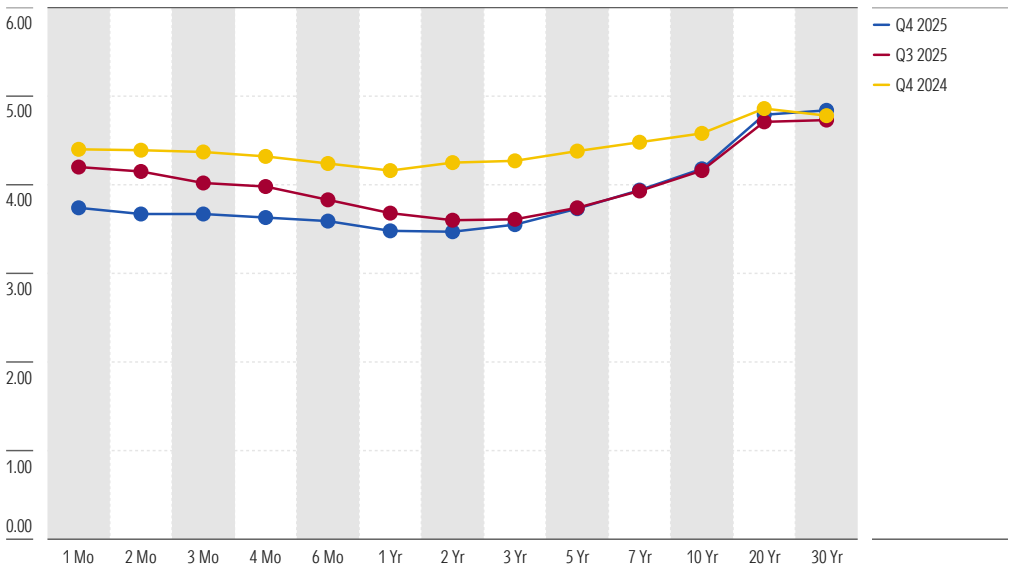
³ Real GDP growth rates and inflation projections data source: Bank of England December Monetary Policy Statement.

2026, while GDP growth projection for 2025 is expected to be 1.4%, up from the previous projection of 1.2%.⁴

US Yield Curve and Interest Rate Movement Summary

In the fourth quarter, short-term interest rates declined sharply following the Fed's rate cuts, with Treasury yields up to one year falling by an average of 35 basis points. Longer-maturity-term yields beyond 10 years saw a more modest rise of 8 basis points, while medium-term maturities between two and seven years remained unchanged. The yield curve witnessed marginal steepening, specifically in the shorter end of the curve over the quarter. However, a more pronounced steepening trend has occurred over the past 12 months.

Exhibit 1 Yield Curve (%)



Source: US Department of Treasury. Data as of Dec. 31, 2025.

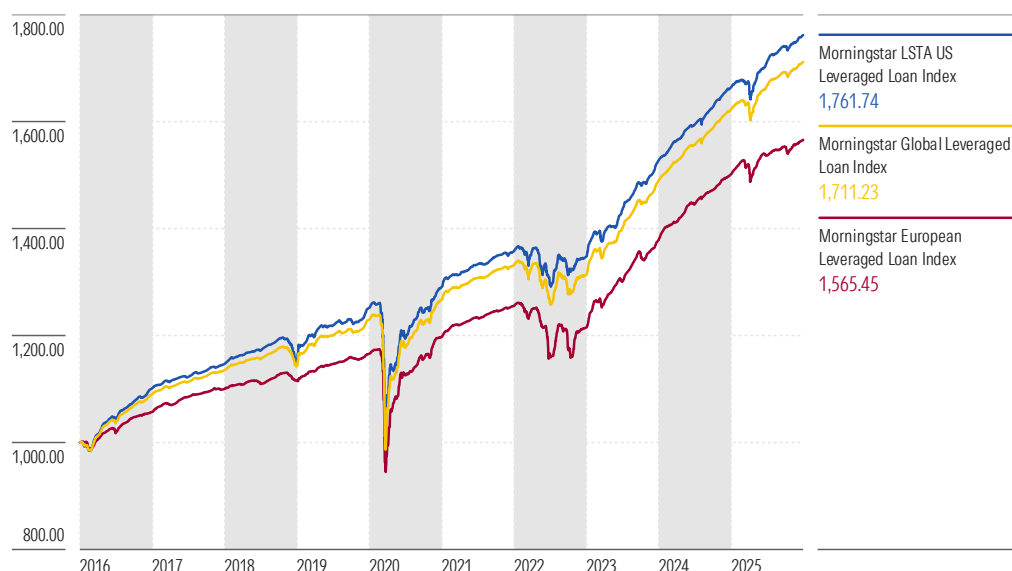
⁴ Growth, unemployment rate, and inflation data source: ECB December Monetary Policy Statement.

Leveraged Loans Insights

Morningstar Leveraged Loan Indexes Performance Summary

Over the past 10 years, the Morningstar LSTA US Leveraged Loan Index has delivered the strongest overall returns, coupled with lower risk, as illustrated in Exhibits 2 and 3. The Morningstar Global Leveraged Loan Index, a fixed-weight composite comprising 75% from the Morningstar LSTA US Leveraged Loan Index and 25% from the Morningstar European Leveraged Loan Index, exhibits risk/return characteristics that closely mirror those of its primary contributor.

Exhibit 2 Performance Chart of Morningstar Leveraged Loan Indexes



Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

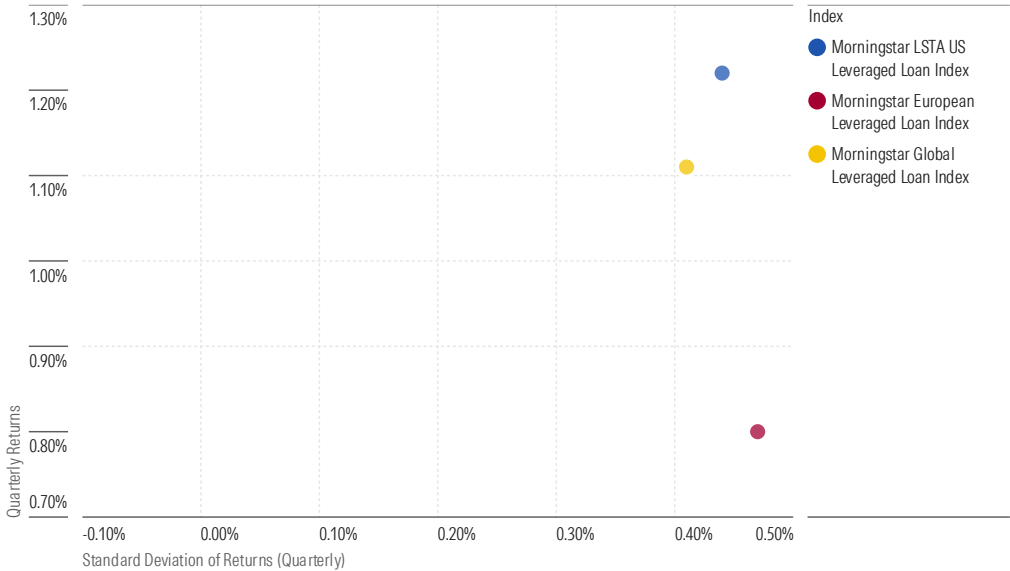
Exhibit 3 Risk/Return Characteristics

Parameters	Morningstar LSTA US Leveraged Loan Index	Morningstar European Leveraged Loan Index	Morningstar Global Leveraged Loan Index
Start Date	12-31-2015	12-31-2015	12-31-2015
End Date	12-31-2025	12-31-2025	12-31-2025
Return (%)	5.83	4.58	5.52
Risk (%)	5.37	6.37	5.54

Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

The comparative risk/return performance of the Morningstar Indexes over the fourth quarter is shown in Exhibit 4. In the fourth quarter, market volatility increased compared with the third quarter, driven by ongoing secondary market weakness and a diminishing floating-rate advantage following subsequent rate cuts. Despite these challenges, leveraged loans extended their positive trajectory into 2025's final quarter, with the Morningstar LSTA US Leveraged Loan Index leading the performance with a 1.2% return, followed by the Morningstar Global Leveraged Loan Index, which gained 1.1%.

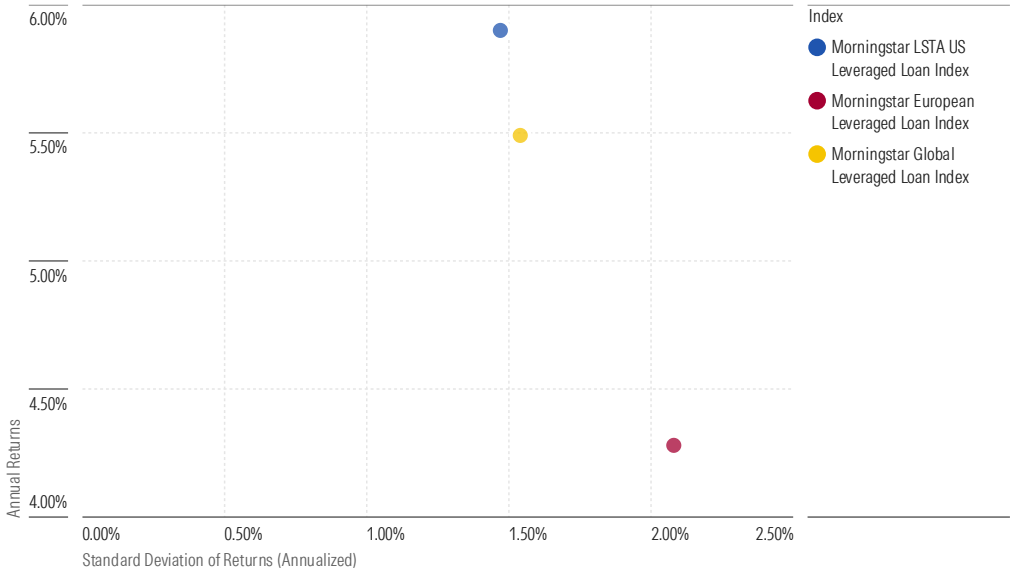
Exhibit 4 Fourth-Quarter 2025 Performance



Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

Exhibit 5 highlights the comparative performance over the previous 12 months. The Morningstar LSTA US Leveraged Loan Index provided the best risk/return characteristics because comparatively higher base rates prevailed in the US. Over the past 12 months, European leveraged loans experienced greater volatility, reflected in the higher risk and weaker returns of the Morningstar European Leveraged Loan Index. Meanwhile, returns of the Morningstar Global Leveraged Loan Index trailed the US, while exhibiting marginally higher volatility, largely due to the influence of European loans.

Exhibit 5 12-Month Performance Ended Dec. 31, 2025

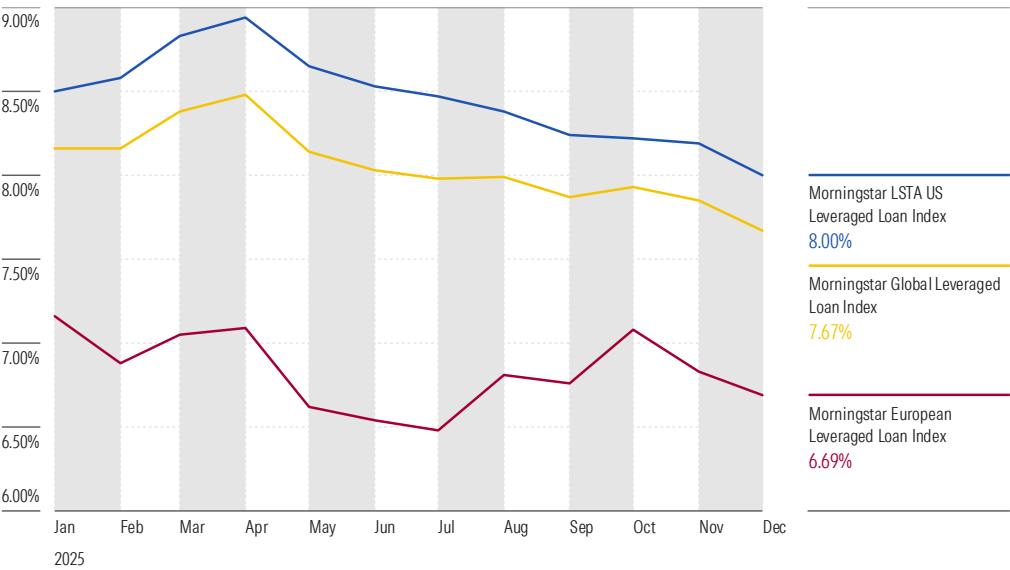


Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

Leveraged Loan Yields Ease Amid Fed Rate Cuts in Late 2025

As seen in Exhibit 6, the yield to maturity for leveraged loans continued to decline from record highs in April 2025. The yield to maturity of the Morningstar LSTA US Leveraged Loan Index ended the fourth quarter at 8%, which represents a decline of 40 basis points in the third quarter, followed by an additional decline of 25 basis points in the fourth quarter. This reduction in yield was primarily driven by the Federal Reserve’s rate cuts in October and December 2025. In contrast, the Morningstar European Leveraged Loan Index experienced an increase in yield to maturity, peaking at 7.08% in October 2025, before easing by 39 basis points to end the year at 6.69%.

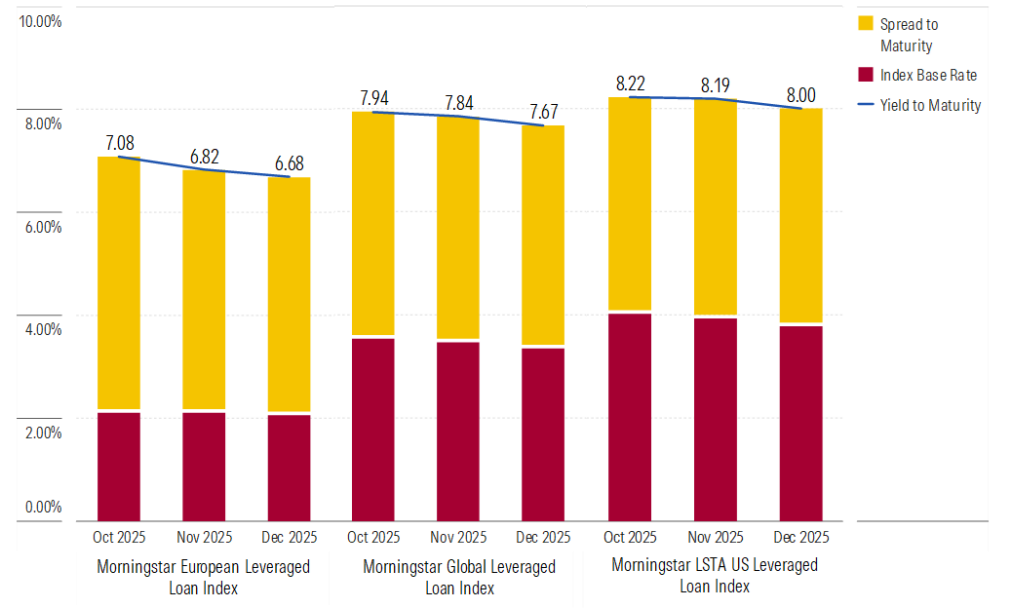
Exhibit 6 Yield to Maturity



Source: Morningstar Indexes. Data as of Dec. 31, 2025.

Exhibit 7 illustrates the impact of the Fed's rate cuts in October and December 2025, which led to a 38 basis points decline in base rates for US leveraged loans and contributed to a lower yield to maturity for the index. During the quarter, the spread to maturity increased by 14 basis points in the US and 8 basis points for the Morningstar Global Leveraged Loan Index because of a fall in the secondary market prices. In contrast, base rates for the Morningstar European Leveraged Loan Index remained flat and the spread to maturity declined by 10 basis points, resulting in lower yields for European loans.

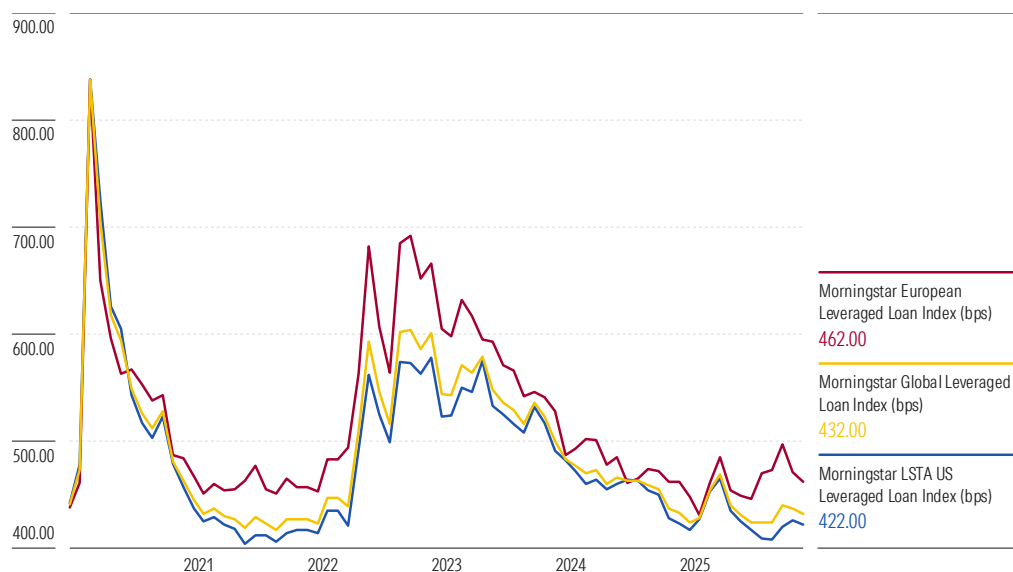
Exhibit 7 Fourth-Quarter 2025, Yield to Maturity, Spread to Maturity, Index Base Rate



Source: Morningstar Indexes. Data as of Dec. 31, 2025.

As shown in Exhibit 8, the spread to maturity widened by 14 basis points in the US and 8 basis points for the Morningstar Global Leveraged Loan Index during the quarter, driven by declines in secondary market prices. In contrast, European leveraged loan spreads rose by 24 basis points in October 2025 but subsequently narrowed by 34 basis points in November and December, ending the quarter 10 basis points lower than the previous quarter. The Morningstar European Leveraged Loan Index's spread of 462 basis points remains near historically compressed levels.

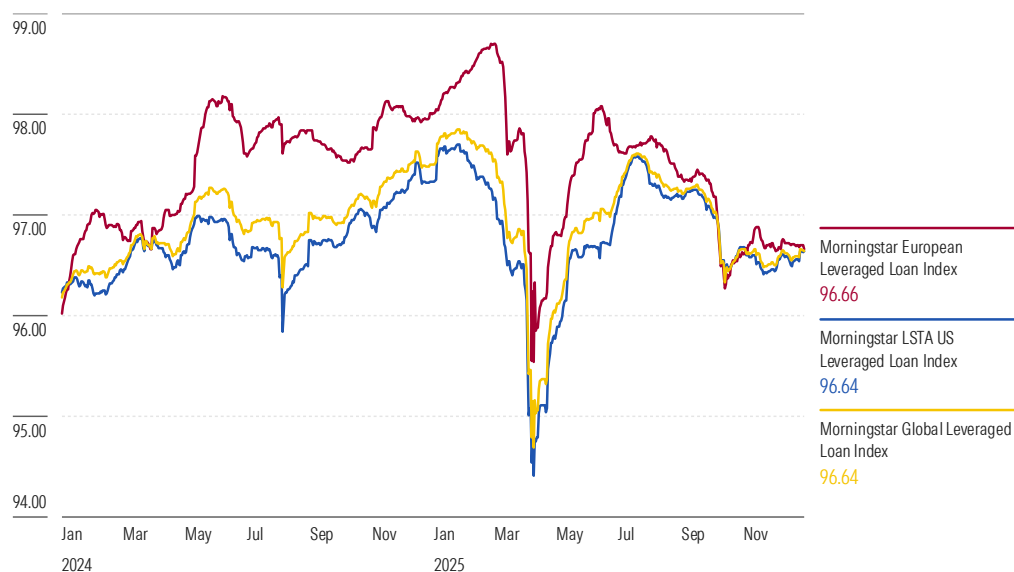
Exhibit 8 Spread to Maturity for Morningstar Leveraged Loan Indexes



Source: Morningstar Indexes. Data as of Dec. 31, 2025.

Secondary Market Volatility Drives Leveraged Loan Prices Lower in Fourth-Quarter 2025

Across both the US and European markets, leveraged loan prices declined in the fourth quarter, as seen in Exhibit 9. By the end of the quarter, prices had fallen by 0.42 points in the US and 0.65 points in Europe. Despite this, prices have still rebounded significantly from their April lows, rising more than 2.0 points to close the year at 96.64 for both the Morningstar LSTA US Leveraged Loan Index and the Morningstar Global Leveraged Loan Index. The Morningstar European Leveraged Loan Index also recovered, ending the year at 96.66, up 1.7 points from its April trough.

Exhibit 9 Weighted Average Bid Price

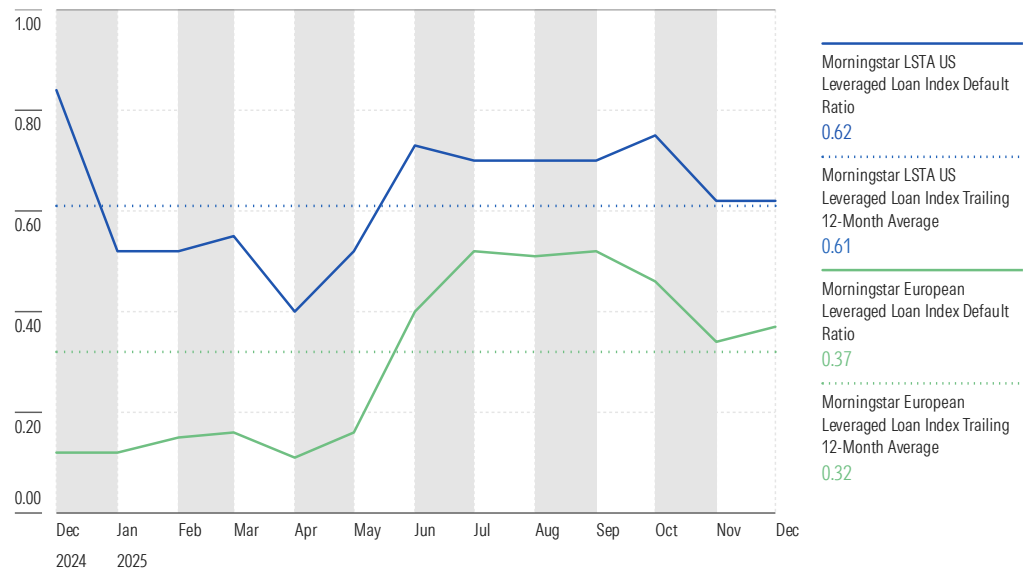
Source: Morningstar Indexes. Data as of Dec. 31, 2025. In USD.

Altice France Restructuring Drives Default Ratio Lower

Exhibit 10 shows the default ratio⁵ for both the Morningstar LSTA US Leveraged Loan Index and the Morningstar European Leveraged Loan Index declined in the fourth quarter. This improvement was primarily driven by the restructuring of Altice France loans, which brought the ratios closer to their respective trailing 12-month averages.

⁵ The default ratio is calculated as the total amount outstanding of defaulted loans divided by the total amount outstanding of all the loans in the index on each effective date. Monthly default ratios are obtained by averaging the daily default ratios within each calendar month. The 12-month average default ratio is computed as the trailing 12-month average of these monthly ratios.

Exhibit 10 Default Ratio: Morningstar Leveraged Loan Indexes

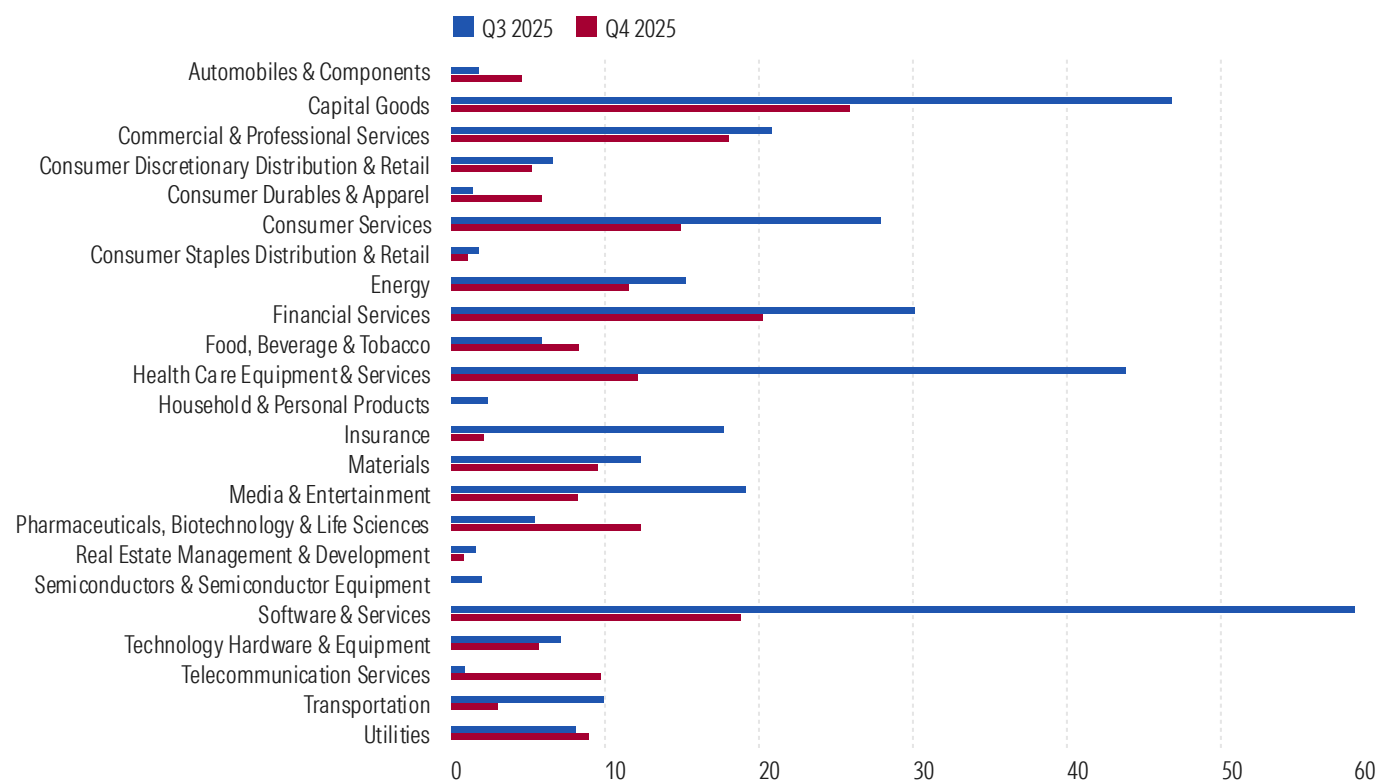


Source: Morningstar Indexes. Data as of Dec. 31, 2025.

Sector Spotlight

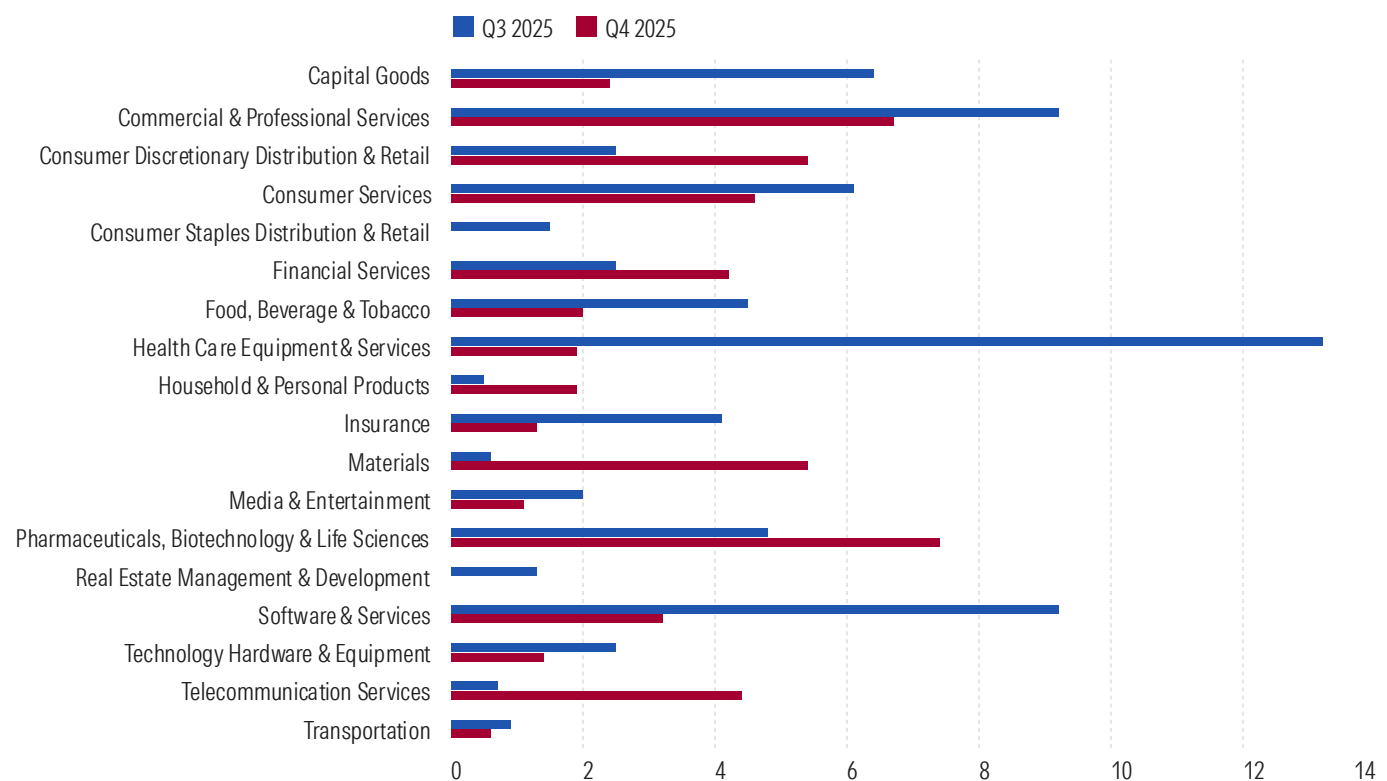
Capital Goods Tops US Leveraged Loan Issuance; Pharmaceuticals Leads in Europe for the Quarter

New loan activity lost momentum in the last quarter of 2025. According to the Morningstar LSTA US Leveraged Loan Index, USD 207 billion in new loan issuances was added as compared with USD 347 billion recorded in the third quarter. The most active sectors included capital goods and financial services, as shown in Exhibit 11. Among the leading issuers were Focus Financial Partners LLC and ARG IH Corp, issuing USD 4.4 billion and USD 4.1 billion, respectively.

Exhibit 11 New Issuances: Morningstar LSTA US Leveraged Index (USD Billion)

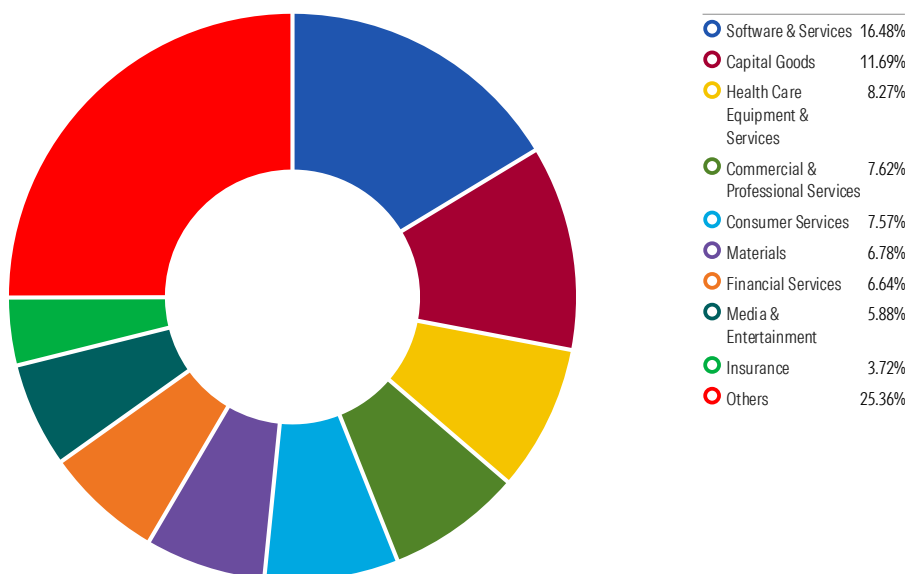
Source: Morningstar Indexes. Data as of Dec. 31, 2025.

The European leveraged loan market also experienced a slowdown in issuance activity. According to the Morningstar European Leveraged Loan Index, new loan issuances in the fourth quarter totaled EUR 54 billion as compared with EUR 72 billion in the third quarter. The pharmaceuticals and commercial and professional services sectors led the activity, as illustrated in Exhibit 12. Leading the momentum were Action Nederland BV and Zentiva, issuing EUR 3.6 billion and EUR 2.6 billion, respectively.

Exhibit 12 New Issuances: Morningstar European Leveraged Index (EUR Billion)

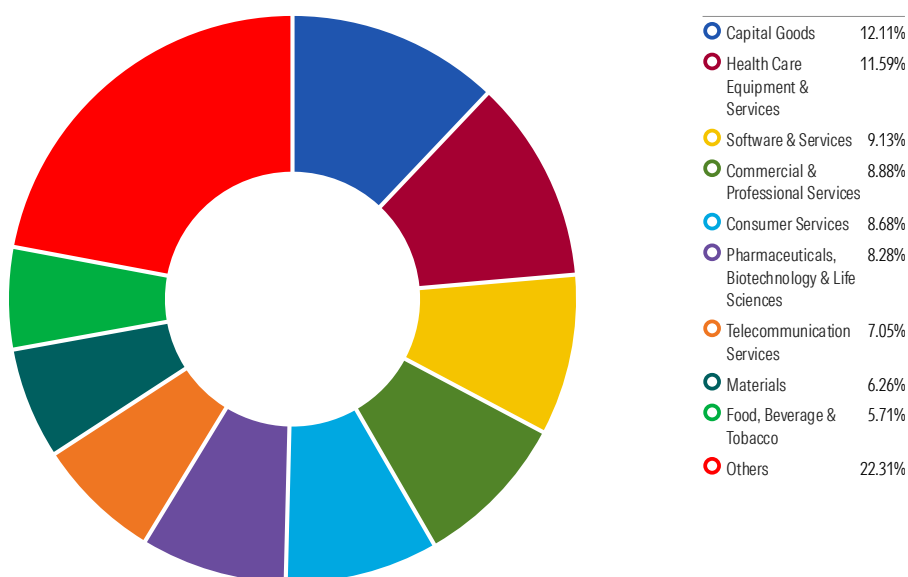
Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

As shown in Exhibit 13, the largest sector exposures within the Morningstar LSTA US Leveraged Loan Index include software & services, capital goods, healthcare, and commercial & professional services, which collectively account for approximately 44% of the index's total market value.

Exhibit 13 Morningstar LSTA US Leveraged Loan Index Sector Distribution

Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

A similar sector concentration is observed in Europe, as illustrated in Exhibit 14, where capital goods, healthcare, software & services, and consumer services sectors represent the largest exposures within the Morningstar European Leveraged Loan Index, encompassing approximately 42% of the index's total market value.

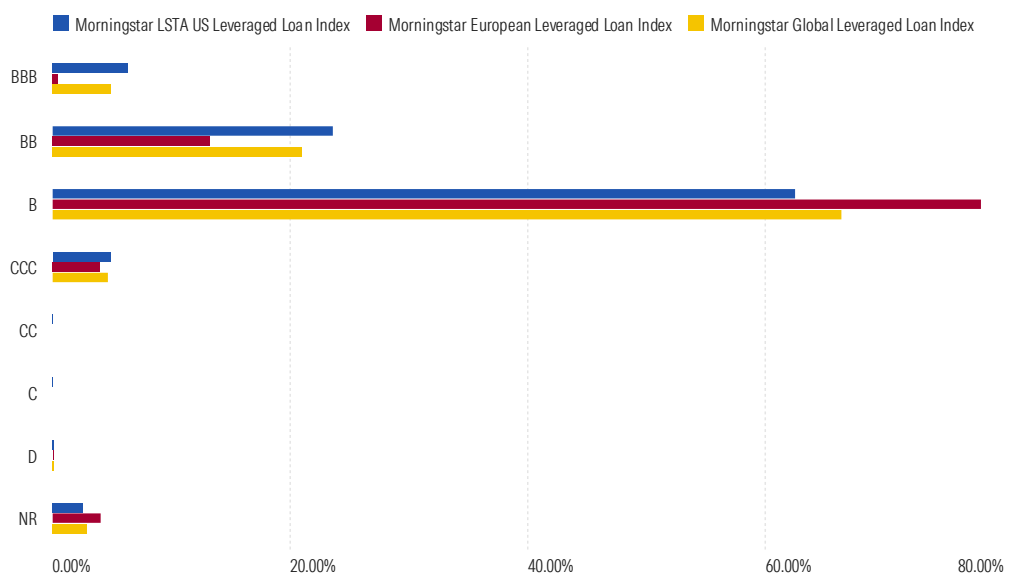
Exhibit 14 Morningstar European Leveraged Loan Index Sector Distribution

Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

Credit Ratings Radar

Exhibit 15 breaks down the credit-quality composition of the loan market, highlighting that B rated loans constitute the largest share across the Morningstar Leveraged Loan Indexes. This ratings cohort comprises 63% of the Morningstar LSTA US Leveraged Loan Index, 78% of the Morningstar European Leveraged Loan Index, and 66% of the Morningstar Global Leveraged Loan Index.

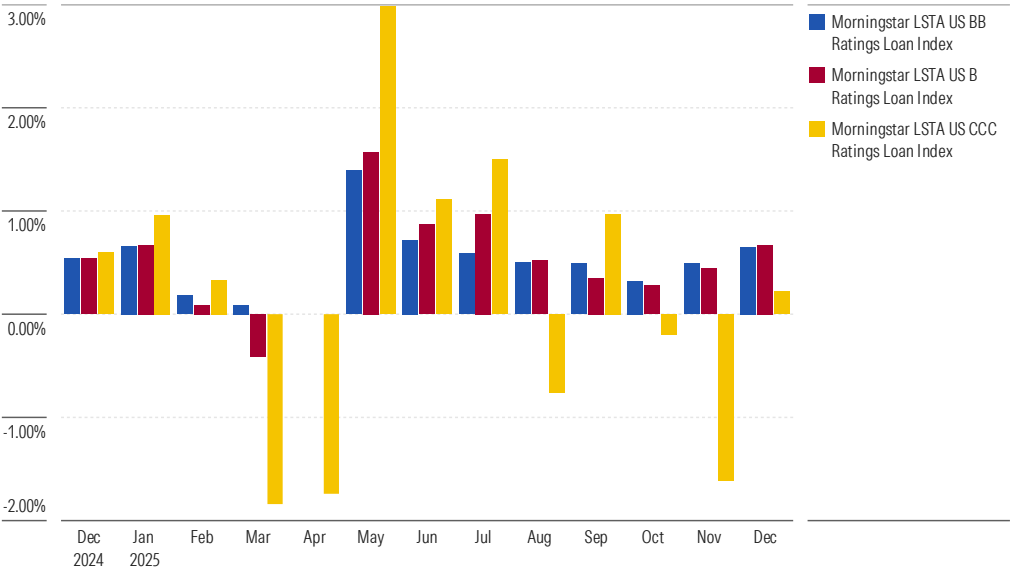
Exhibit 15 Morningstar Leveraged Loan Indexes Rating Distribution



Source: Morningstar Indexes. Data as of Dec. 31, 2025. TR LCL Variant.

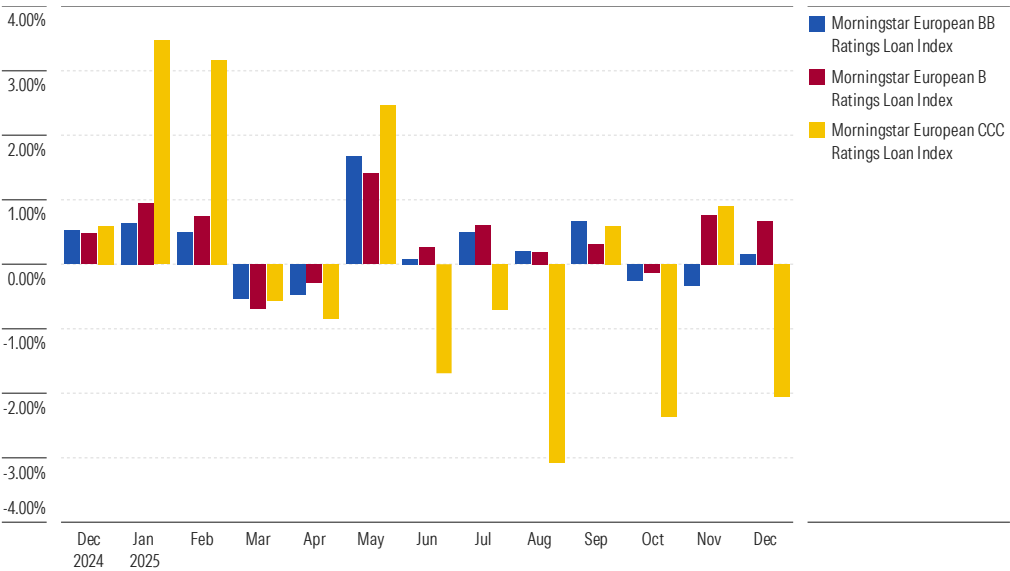
As observed in Exhibit 16, the risk-off environment prompted a shift in investor focus toward higher-quality loans. The Morningstar LSTA US BB Ratings Loan Index, which tracks loans rated BB- to BB+, outperformed, with a return of 1.47%. B rated loans, as measured by the Morningstar LSTA US B Ratings Loan Index, followed closely, with a return of 1.40%. In contrast, CCC rated credits, tracked by the Morningstar LSTA US CCC Ratings Loan Index, underperformed, with a negative return of 1.59% for the quarter.

Exhibit 16 Morningstar LSTA US Leveraged Loan Index Monthly Returns by Loan Rating



Performance in the European leveraged loan market was notably different when looking across the credit quality spectrum. As observed in Exhibit 17, only B rated credits, tracked by the Morningstar European B Ratings Loan Index, delivered positive results, posting a return of 1.3%. In contrast, BB rated loans, measured by the Morningstar European BB Ratings Loan Index, and CCC rated loans, according to the Morningstar European CCC Ratings Loan Index, with negative returns of 0.44% and 3.5%, respectively.

Exhibit 17 Morningstar European Leveraged Loan Index Monthly Returns by Loan Rating



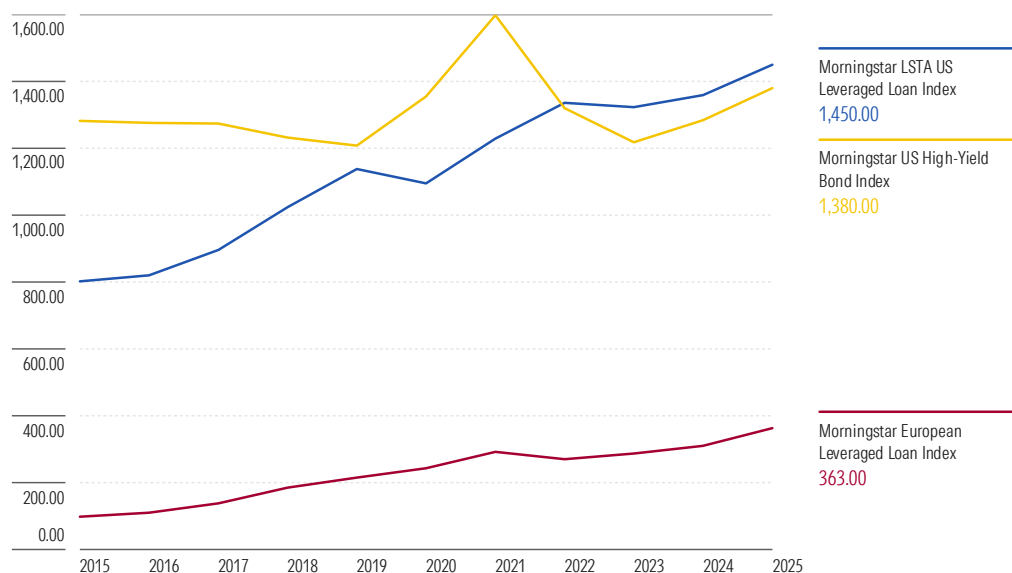
Comparison with Traditional Fixed-Income Benchmarks

Decadelong Evolution of Leveraged Loans and High-Yield Bonds

Exhibit 18 highlights market value trends for the US leveraged loan, US high-yield bond, and European leveraged loan markets from 2015 to 2025. The US leveraged loan market represented by the Morningstar LSTA US Leveraged Loan Index has shown consistent growth, reaching a market value of USD 1.45 trillion as of December 2025. In contrast, the US high-yield bond market, according to the Morningstar US High Yield Bond Index, experienced a sharp rise, peaking at USD 1.62 trillion in 2021, followed by a notable contraction and eventual stabilization at USD 1.38 trillion by the end of 2025. The European leveraged loan market, while much smaller in scale at USD 363 billion (EUR 321 billion), demonstrated steady growth since 2014.

These trends showcase the relative resilience of the US loan market compared with the more cyclical nature of high-yield bonds, while also underscoring the steady development of the European loan market.

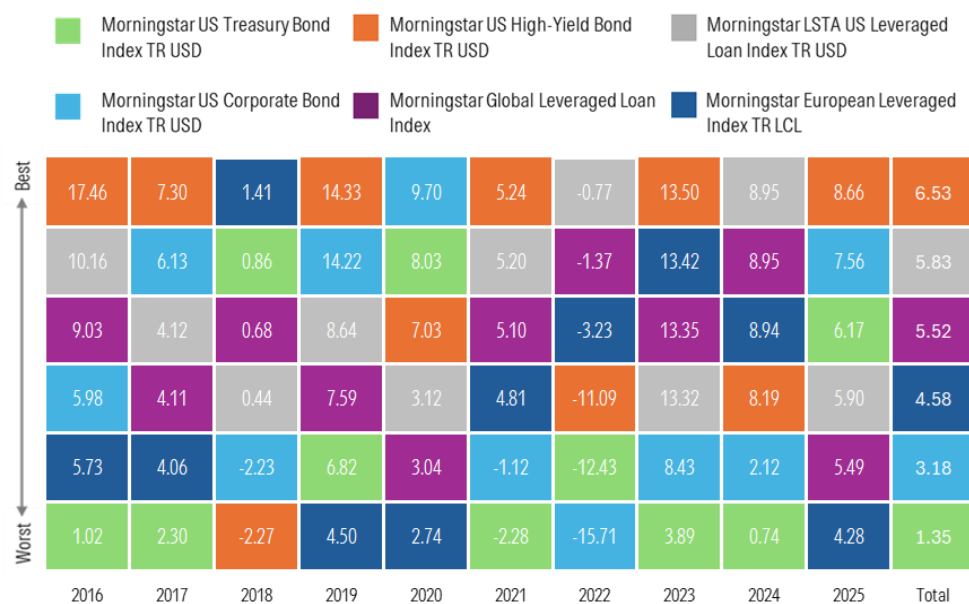
Exhibit 18 Market Value in USD Billion



Source: Morningstar Indexes. Average daily market value for the year. Data as of Dec. 31, 2025. USD.

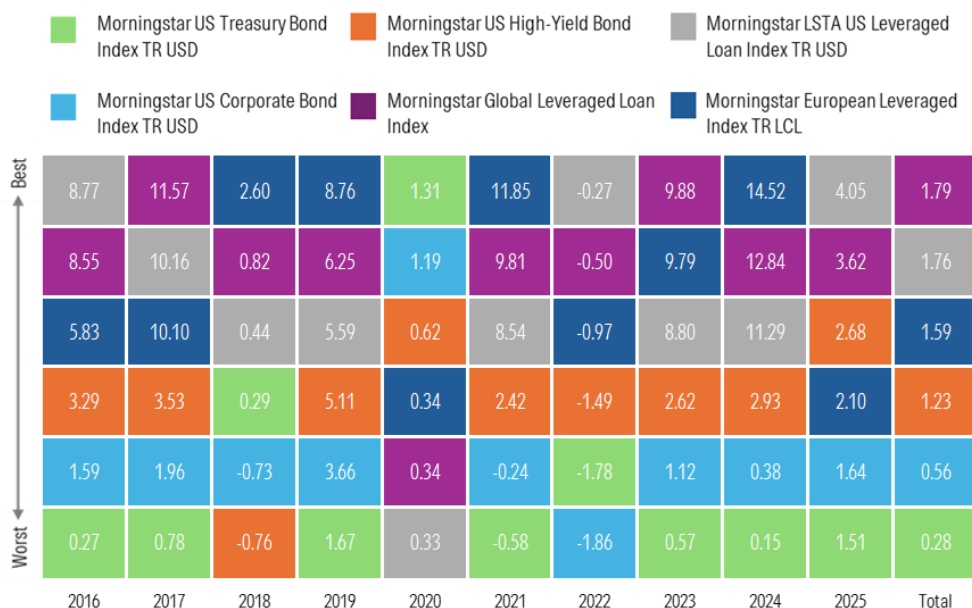
Horizon Returns

Exhibit 19 compares the performance of traditional fixed-income asset classes with leveraged loans over the past decade. As base rates declined and credit spreads tightened in 2025, leveraged loans have lost some of the floating-rate advantage the asset class experienced in previous years. Consequently, US leveraged loans delivered a return of 5.9%, underperforming both US high-yield bonds (8.66%) and US investment-grade bonds (7.56%) in 2025. While the Morningstar US High-Yield Bond Index delivered the highest overall returns, the Morningstar LSTA US Leveraged Loan Index, the Morningstar Global Leveraged Loan Index, and the Morningstar European Leveraged Loan Index closely followed.

Exhibit 19 Horizon Returns (%)

Source: Morningstar Indexes. Data as of Dec. 31, 2025.
 Period for Total - Dec. 31, 2015, to Dec. 31, 2025.

Although the Morningstar US High-Yield Bond Index demonstrates strong absolute returns, its performance is less compelling when volatility is considered. Exhibit 20 provides a risk-adjusted performance comparison between traditional fixed-income indexes and leveraged loans. Notably, the Morningstar Global Leveraged Loan Index emerges as one of the top performers, supported by its stable return profile and lower volatility because of the floating-coupon payment structure. The US and European Leveraged Loan Indexes also show favorable risk-adjusted results, outperforming traditional fixed-income benchmarks and reinforcing the relative resilience of the loan market.

Exhibit 20 Return/Risk Performance (%)

Source: Morningstar Indexes. Data as of Dec. 31, 2025.

Period for Total - Dec. 31, 2015, to Dec. 31, 2025

Reliable Benchmarks in a Dynamic Credit Market

Amid shifting interest rate cycles and evolving credit conditions, the Morningstar Leveraged Loans Indexes continue to serve as a reliable benchmark for tracking performance across US, European, and global loan markets, now a significant component of the broader fixed-income universe. The indexes capture the nuances of credit quality, sector allocation, and regional risk premiums, enabling investors to analyze trends and manage exposures effectively. By providing consistent, transparent coverage, the index suite supports informed decision-making in one of the most dynamic segments of the fixed-income market. For more information, visit <https://indexes.morningstar.com/leveraged-loan>.

About Morningstar Indexes

Morningstar Indexes was built to keep up with the evolving needs of investors—and to be a leading-edge advocate for them. Our rich heritage as a transparent, investor-focused leader in data and research uniquely equips us to support individuals, institutions, wealth managers and advisors in navigating investment opportunities across major asset classes, styles and strategies. From traditional benchmarks and unique IP-driven indexes, to index design, calculation and distribution services, our solutions span an investment landscape as diverse as investors themselves.

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