Banking & Finance

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Current Forces of Debt Finance in Germany

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Introduction

There was widespread speculation about the influence of mergers and acquisitions on the German debt finance market for Q3 2024. Interestingly, new trends shaping the German debt finance market include an increase in infrastructure debt. In addition, corporate borrower refinancings have picked up, and we expect that this trend will continue into Q4 2024 and Q1-Q2 2025.

Infrastructure Debt

Infrastructure debt is becoming increasingly prominent, driven by private debt funds entering a market traditionally dominated by banks. In 2023, infrastructure debt fundraising more than doubled, with key players like Ares, Blackstone and Brookfield leading the way. These funds are diversifying into infrastructure, offering more flexible financing options for various project stages.

Infrastructure projects, supported by robust long-term growth fundamentals such as urbanization, decarbonization, and digitalization, require extensive investment. The Global Infrastructure Hub estimates a need for US$79 trillion in basic infrastructure investments between 2016 and 2040, excluding additional needs for digital infrastructure and decarbonization.

Private debt structures offer versatility, catering to different risk profiles and market conditions. This flexibility attracts investors seeking higher-risk opportunities during the development phase and stable cash flows from operational assets, making private debt an appealing alternative to traditional bank lending.

Macroeconomic Drivers

Several macroeconomic factors underpin the growth of infrastructure debt in Germany. Infrastructure investments provide essential services with inelastic demand, offering compelling performance even during economic downturns. Analysis indicates that infrastructure assets can adapt and potentially exceed market performance in inflationary and rising rate environments, making them particularly attractive during periods of economic uncertainty.

Sector diversification is also critical. Investments now include digital infrastructure and renewable energy alongside traditional utilities. For instance, data centers, which require substantial funding, are expected to see electricity consumption more than triple between 2022 and 2030. This expansion highlights the growing need for private debt in diverse infrastructure sectors.

Corporate Refinancings

Although interest rates are still substantially higher than in 2021, borrowing costs have fallen to a two-year low in March 2024. Further, the volatile macroeconomic conditions in 2022 and 2023 in other markets have resulted in a strong investor demand on the lender side for investment grade debt. On the borrower side, many corporates are facing a stream of debt maturities in the coming years. As a result, many corporates decided to return to the debt market in 2024 or are planning to return in early 2025. Although refinancing activity has been the main driver of issuance, there have also been new opportunities for issuers to raise capital for M&A growth activities and generate liquidity buffers.

Outlook

German debt finance had a strong first quarter in 2024. Q2 2024 was slower than expected, but we expect activity to pick up again starting in September 2024 and, in particular, after the US elections.

The German debt finance market is poised for continued growth, supported by a strong foundation in infrastructure investment and the return of corporate issuers. The shift towards private debt in infrastructure finance diversifies funding sources and provides stability and growth potential amid changing economic conditions. As these trends continue, infrastructure debt will play a pivotal role in shaping the future of German debt finance.

Practice Area News

Synthetic USD LIBOR ends September 24. Loan market participants who are still in the process of USD LIBOR transition should be aware of the impending deadline of the end of September 2024. All necessary steps should be taken now to be fully prepared ahead of cessation to mitigate any potential residual risks. While most have already transitioned, there are still a small number of transactions using synthetic USD LIBOR which need to be transitioned to a new base rate.

BaFin Publishes Final MaRisk 2024 Amendment. Germany's Federal Financial Supervisory Authority (BaFin) published the final version of the **8th amendment to the "Minimum Requirements for Risk Management" (MaRisk 2024)**. The update integrates the EBA guidelines on interest rate and credit spread risk management for investment portfolios. The changes are effective immediately, with institutions given until December 31, 2024, to comply with new credit spread risk requirements.

ESMA Issues New Guidelines to Prevent Greenwashing in ESG Funds. European Securities and Markets Authority (ESMA) has introduced new guidelines to prevent greenwashing in ESG funds. The rules require funds using ESG or sustainability-related terms to meet strict criteria, including specific investment thresholds and exclusion criteria. These guidelines, effective three months after publication, aim to ensure transparency and protect investors by holding funds accountable for their sustainability claims.

Significant Decline in Green Bond Issuance and ESG ratchets. The green bond market in Germany has seen a substantial decline in issuance volumes from 2022 onwards. While green bond issuance in Germany reached approximately €60 billion in 2022, the volume of green bonds issued in Germany had decreased to about €30 billion in 2023. This downward trend continued in the first two quarters of 2024, with issuances in Germany down to only €6 billion. Simultaneously, the ESG loan margin ratchet trend cooled down. Yet, on the other hand, we see that lenders focus increasingly on more comprehensive ESG reporting instead of just measuring one or two KPIs which are in any event linked to the existing business plan.

In the Firm

• **Our Global Reach.**

In 2023, we worked with clients from **128** countries on deals involving **201** countries

We are located on **6** continents, in **30** countries, in **44** offices

• **Highly Rated German Banking & Finance Team.**

• Seamlessly **embedded in a Top Tier global Banking Practice** (Band 1, Chambers Global 2024).

• **Across all major financial centers**, including New York, London, Frankfurt, Paris, Hong Kong, Tokyo and Singapore and many regional financial markets.

• **Combining** highly qualified **German, English and New York law finance** and respective language capabilities **in a single office**.

• **Known** as **market leaders for complex cross-border finance transactions** in Germany.

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