Invesco European Senior Loan Fund

A Sub-Fund of Invesco Zodiac Funds

Invesco Senior Secured Management, Inc.

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2024 Second quarter market review

The Credit Suisse Western European Leveraged Loan Index ("CS WELLI" or "Index") returned 2.04% during the quarter, consisting of interest income of 2.09% and principal return of -0.05%.[1] Year-to-date total returns at quarter end were 2.04%[1]

During the second quarter of the year, financial markets displayed a varied performance as investors concentrated on multiple risks. On the upside, equities continued to climb, with the S&P 500 Index reaching a new record high, driven by further gains from the Magnificent 7.[2] However, these equity gains were not widespread, and the equal-weighted S&P 500 Index actually fell during the quarter.

Fixed rate bonds faced some difficulties even though the ECB enacted their first rate cut for five years in June, decreasing their deposit rate by 25 basis points (bps) to 3.75%; investors are now expecting fewer rate cuts for the rest of the year, sending bonds lower. Forward rates today suggest that nominal interest rates will decrease further, to approximately 3.1-3.3% by year-end and to around 2.5%-2.8% by the end of 2025. Geopolitical risks were also a focal point and French assets declined during June after President Macron announced a snap legislative election.

At the same time, European macroeconomic data continued to improve. After recording Q1 GDP growth of 0.3%, the European Commission (EC) issued a full-year outlook of an accelerated 1.0% growth expectation for the European Union (EU) for the full year 2024 and 1.6% during 2025. Importantly, the EC expects all European countries to grow, with economic expansion in the southern rim of the EU (Spain, Portugal, Greece) still outpacing growth in northern and western Europe.

The leveraged loan market performed well in this macroeconomic climate witnessing growth picking up withing a "higher for longer" rate environment. As such, loan prices have increased to €97.10 during the year, up from €96.89 at the beginning of the year.[1] Year-to-date returns for the first half of the year stand at 4.13% (8.26% annualized)[1] and a feared spike in defaults is yet to materialize, with last-twelve-months default rate still low at 1.29%.[3]

The second quarter also saw a strong pick-up in primary transactions. During the quarter, €27 billion (bn) of new loan transactions priced, which was significantly higher compared to approximately €4bn during Q2 2023. Arrangers and issuers opportunistically took advantage of a strong market environment at the beginning of the month and launched a flurry of refinancing, repricing, and add-on transactions. New money leveraged buyout supply improved as well, with a handful of new sponsor buy-outs hitting the market.

Invesco Management S.A. (the Management Company) has appointed and delegated discretionary investment decisions with respect to the Fund to Invesco Senior Secured Management, Inc. ("The Investment Manager"). See prospectus for more information. All information as of June 30, 2024 unless otherwise noted. Fund launch date is May 31, 2012. Base currency is EUR.

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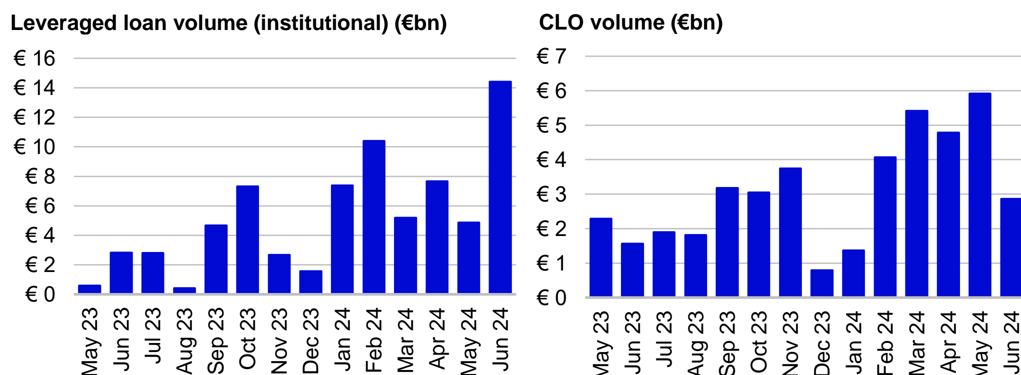
Figure 1: Supply/demand backdrop



Source: Pitchbook Data Inc. as of June 30, 2024.

New issue yields compressed slightly to 8.51%, with the typical B2/B rated loan priced around the EURIBOR + 425-450bps level with small original issue discount (OID) of approximately 0.5-1.0 points. While H2 2024 is expected to continue to feature more issuance compared to H2 2023, the current loan pipeline seems to suggest that volumes might cool somewhat from their Q2 highs.

European CLO activity remained very strong and year-to-date volumes stand at record high for the CLO 2.0 era at €24.4bn, which is more than double compared to the same period last year. Sell-side analysts now expect around €40-€45bn of CLO new issue for the year, which would exceed the previous record level of €38.6bn in 2021. This also compared to initial forecasts at the start of the year of just approximately €20bn.

AAA liabilities – whilst around the EURIBOR + 140-150bps area for most of the year – have now tightened further, with deals pricing around the EURIBOR + 130-135bps area. Even at such levels, CLO AAAs continued to offer strong relative value compared to other AAA asset classes. The asset arbitrage to the loan market is well functioning and a stream of repayments from CLOs outside reinvestment period returning cash to investors means that there continued to be investor capital available to support further solid new issue levels going forward.

Fundamentals

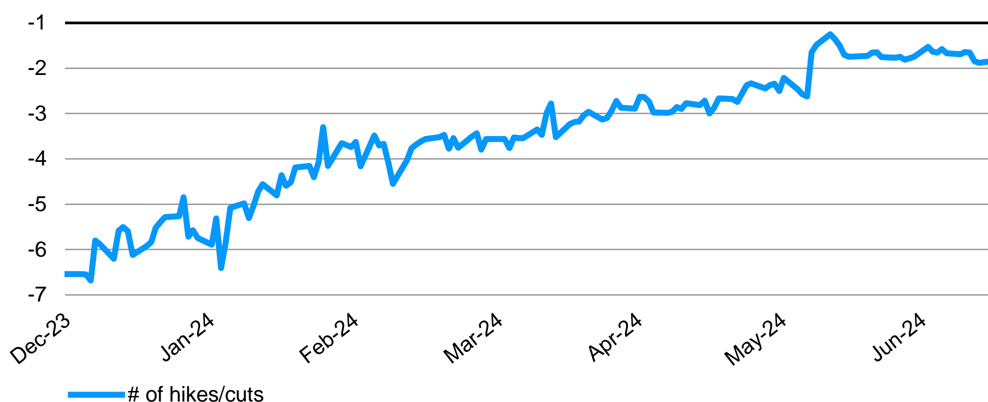
Euro area (EA) macroeconomic indicators moderated in the later parts of the second quarter. The region's composite output PMI (flash-estimate) declined by 1.3pts to 50.8 in June, which was below consensus of 52.5, and halted the upward trend seen between November and May when the PMI cumulatively increased by almost 6 points. The Manufacturing sector was the main detractor where the output index fell (by 3.4pts) to 46.0. Across countries, the decline in the area-wide index was broad-based. Furthermore, the EA economic sentiment survey declined 0.2pts to 95.9 in June. A rise in consumer confidence (via real wage gains) has been negated by a reduction in business confidence where sentiment is still stronger in services than in other sectors (e.g., Manufacturing, Retail, and Construction). Sentiment remains weakest in Germany. The election outcome in France, resulting in a hung parliament may cause some macro pressures in the upcoming quarter as the formation of a coalition is likely to take sometime to finalise.

Disinflation has broadly continued to occur, with June flash Eurozone inflation edging down by 0.1 percentage points (pp) to 2.5%, in line with consensus. The decline was driven by lower energy (-0.1pp to 0.2% year-over-year (yoy)) and food inflation (-0.1pp to 2.5% yoy). Core inflation was unchanged at 2.9% yoy, a small miss of consensus expectations of 2.8%. Within core, both goods and services inflation were unchanged at 0.6% yoy and 4.1% yoy, respectively.

As expected, the ECB began cutting deposit rates at their June meeting – the first cut since 2019. The rate was lowered to 3.75% from 4.0%. President Lagarde mentioned there was a "strong likelihood" that the dialing back of the restrictive monetary policy has started, although the language used by the ECB was thought to be more hawkish in tone. The ECB says it will continue to follow a "data dependent and meeting by meeting approach to determining the appropriate level and duration of restriction". It was also repeated that the ECB is "not pre-committing to a particular rate path."

The market is pricing around two more cuts in 2024, in September and December. Although a cut in September is not a done deal, with recent data suggesting that ECB staff need to revise the near-term inflation outlook, with growth at risk of underperforming and inflation still forecasted to be on target in 2025, a cut in September remains the most likely outcome. Overall, EA expectations for GDP growth remain positive for 2024 albeit below 1%. As the ECB cuts work through to the real economy, an increase in real disposable incomes should be expected.

Figure 2: Estimated number of hikes/cuts by December 2024



Source: Bloomberg as of July 16, 2024. Forward-looking statements are not guaranteed. They involve risks, uncertainty and assumptions.

The last twelve-month default rate for the Morningstar European Leveraged Loan Index (based on principal amount) is 1.29%.[3] The historical average annual default rate is 2.84%.[3]

Risk warnings

For important information on risks associated with this product, see the "Risk Factors" in Section 31 on pages 53-59 of the Prospectus.

Senior loans may be illiquid and more difficult to sell quickly at a fair price. Because of the risk of illiquidity of the instruments in which the product will invest, the processing of the redemption requests may be deferred in certain circumstances. Interest rates on senior loans depend on the level of an underlying rate; as such, they may change and cause fluctuations in the net asset value of the product. Senior loans are exposed to credit risk which is the ability of the borrower to repay the interest and capital on the scheduled dates. The product will hold debt instruments which are of lower credit quality and may result in larger fluctuations in the value of the product. The product may also use derivatives for investment purposes. The use of derivatives may result in the product being significantly leveraged and may result in large fluctuations in the value of the product. The product may invest in developing markets, this may cause large fluctuations in the net asset value of the product.

Invesco European Senior Loan Fund objective and strategy

The Fund seeks to provide a high level of current income, consistent with the preservation of capital, by investing primarily in adjustable-rate senior secured loans, collateralized loan obligations, second lien loans, mezzanine securities and credit derivatives relating to non-investment grade companies and denominated in Euro, Sterling, and other European currencies (including, but not limited to, Norwegian Krone, Swedish Krona, Swiss Franc and Danish Krone). The Fund invests primarily in senior, secured loans to non-investment grade corporations with interest rates that float at a spread above a base rate, resets about every 60 days. The Fund's team seeks loans to companies which, in the judgment of the analyst team, have excellent management teams, consistent and dependable sources of cash flow and reliable collateral packages providing a second source of repayment. To manage risk, the team keeps the portfolio broadly diversified and generally avoids industries they believe to be fundamentally flawed or speculative. The investment concerns the acquisition of units in an actively managed fund and not in a given underlying asset. While the portfolio manager may consider Environmental, Social and Governance (ESG) aspects, they are not bound by any specific ESG criteria and have the flexibility to invest across the ESG spectrum. Information used to evaluate ESG factors may not be readily available, complete or accurate. ESG factors may vary across types of investments and issuers, and not every ESG factor may be identified or evaluated. There is no guarantee that the evaluation of ESG considerations will be additive to a strategy's performance.

Past performance does not predict future returns. Please see the following returns for the Invesco European Senior Loan Fund's GX share class.

Performance

Time frame	Invesco European Senior Loan Fund GX share class gross (%)	Invesco European Senior Loan Fund GX share class net (%)	Credit Suisse Western European Leveraged Loan Index (CS WELLI) (%)
Q2 2024	1.59	1.41	2.04
Six months	2.87	2.50	4.13
1 year	9.17	8.39	9.78
3 years	3.75	2.97	4.82
5 years	4.35	3.57	4.33
10 years	4.19	3.41	3.82
Since inception (May 31, 2012)	5.12	4.31	4.47

Time frame	Invesco European Senior Loan Fund GX share class gross (%)	Invesco European Senior Loan Fund GX share class net (%)	CS WELLI (%)
6/30/19 – 6/30/20	-4.34	-5.04	-2.01
6/30/20 – 6/30/21	15.81	14.95	9.52
6/30/21 – 6/30/22	-7.26	-7.92	-5.21
6/30/22 – 6/30/23	10.30	9.40	10.68
6/30/23 – 6/30/24	9.17	8.39	9.78

Source: Invesco, as of June 30, 2024. Fund and benchmark returns are total returns in EUR. Returns may increase or decrease as a result of currency fluctuations. The benchmark index is shown for performance comparisons purposes only. The fund is actively managed and does not track the index.

Invesco European Senior Loan Fund performance and positioning

Q2 2024 / year-to-date performance commentary[4]

The GX shares of the Invesco European Senior Loan Fund (the Fund) amounted to 1.59% gross for the second quarter of 2024, which was 45 basis points (bps) behind of the Credit Suisse Western European Loan Index (CS WELLI) return of 2.04%.[1] The net return for the GX shares of the Fund over the quarter was 1.41%. The Fund's total return amounted to 2.87% for the year-to-date ("YTD") period ending June 30, 2024, which was 126bps behind the CS WELLI return of 4.13%. The net return for the GX shares of the Fund YTD was 2.50%.

During the quarter, the Fund's underperformance was primarily the result of the following factors as outlined below:

- **Asset Selection (Fixed Rate/Reorganization Equity):** The equity bucket was a detractor from performance due to withholding taxes applied when QuarterNorth Energy was sold to Talos Energy. This was a one-off event related to this reorganization equity position as the company is deemed a "real asset" under Foreign Investment in Real Property Tax Act (FIRPTA) because its operations were 100% oil & gas production in the US Gulf of Mexico. The Fund will recover any over-withheld taxes when it files its 2024 tax returns.
- **Risk Positioning (Loans and FRN Only):** The Fund is overweight the 'CCC' segment of the market, which underperformed during the quarter.

This underperformance was partially offset by the following factor detailed below:

- **Credit Selection (Loans and FRNs only):** The quarter saw very strong performance from the high conviction credits in the Fund, particularly Keter, Shop Direct, and MyAlarm. This was partially offset by weak performance of the Fund's holding in Hurtigruten, the Nordic River Cruise business.

Sector Positioning was neutral during the quarter.

The Fund's underperformance YTD was the result of the first factor outlined above. Offsetting Asset Selection, in part, were Credit Selection, Risk Positioning and Sector Selection which were all positive contributors YTD. Please refer to "Credit contributors to and detractors from performance" section below for details on the Fund's largest contributors.

The weighted average market price of the Fund was €85.86 at the end of the quarter, which is €11.24 less than the CS WELLI.[1] At the end of the quarter, the Fund had a weighted average spread of EURIBOR + 5.20%, which is above the CS WELLI's spread of EURIBOR + 3.99%.[1] At quarter end, the yield-to-maturity of the Fund was 13.20%.

We share a few brief thoughts on the loan market and strategy below:

- Euro area (EA) macroeconomic indicators have moderated in the latter parts of the second quarter. For example, the EA composite output PMI (flash/first-estimate) declined by 1.3pts to 50.8 in June, below consensus of 52.5 – breaking the upward trend seen between November and May when the PMI cumulatively increased by almost 6 points. The Manufacturing sector was the main detractor where the output index fell (by 3.4pts) to 46.0. Across countries, the decline in the area-wide index was broad-based. Furthermore, the EA economic sentiment survey declined 0.2pts to 95.9 in June. A rise in consumer confidence (via real wage gains) has been negated by a reduction in business confidence where sentiment is still stronger in services than in other sectors (e.g., Manufacturing, Retail, and Construction). Sentiment remains weakest in Germany.
- Disinflation has broadly continued to occur, with June flash Eurozone inflation edging down by 0.1 percentage points (pp) to 2.5%, in line with consensus. The decline was driven by lower energy (-0.1pp to 0.2% year-over-year (yoy)) and food inflation (-0.1pp to 2.5% yoy). Core inflation was unchanged at 2.9% yoy, a small miss of consensus expectations of 2.8%. Within core, both goods and services inflation were unchanged at 0.6% yoy and 4.1% yoy, respectively.
- As expected, the ECB cut deposit rates at their June meeting – the first cut since 2019. The rate was lowered to 3.75% from 4.0%. President Lagarde mentioned there was a "strong likelihood" that the dialing back of the restrictive monetary policy has started, although the language used by the ECB was thought to be more hawkish in tone. The ECB says it will continue to follow a "data dependent and meeting by meeting approach to determining the appropriate level and duration of restriction". While it was also repeated that the ECB is "not pre-committing to a particular rate path", the market expects a further cut in September (i.e., not at the July ECB meeting).
- EA expectations for GDP growth remain positive for 2024 albeit below 1%. As the ECB cuts work through to the real economy, an increase in real disposable incomes should be expected.
- On the demand side, CLO investors have been buoyed by an improved arbitrage environment, namely AAA liability spreads have compressed meaningfully. Thus, while refinancings have generally resulted in lower borrower all-in-coupons, the CLO-calculus continues to work given the reduced overall average cost of debt. This symbiotic relationship helps to maintain a floor in loan repricings margins.

- As funding costs become lower (base rates + credit/margin spreads) and as demand remains strong via CLOs and other market participants, we envision increased M&A activity as the year progresses – which, thus far, has been muted. Overall, the demand/supply technical remains favourable for loan assets.

Credit selection: *+11bps Q2 / +22bps YTD.* Credit selection was a positive contributor during the quarter and year-to-date. We outline the largest contributors and detractors in more detail below:

Credit contributors to and detractors from performance

- **Keter: *contributor Q2 / YTD***. Keter is a global manufacturer and distributor of resin-based household products and outdoor furniture. The Fund bought the first lien term loan at a significant discount to par in 2019. Thereafter, Keter saw strong commercial momentum coupled with cheaper resin prices, which led to a significant de-levering and rating upgrade. The business is a global consumer brand that resonates with its clients. The business is also well diversified in terms of product, geography, and client base with a proven track record of market shares gain and new product launches.

  Trading was good for the first three quarters of the year, with earnings growth driven by cheaper resin procurement price and the ability of the business to retain pricing power. In July 2023, the company announced an agreement with its lenders (ISSM was a driving force in the Steering Committee) to extend its maturity and to kick off a sale process. First round bids cleared the first lien debt and a handful of bidders moved into second round. On October 7, 2023, Hamas launched a terrorist attack in the South of Israel which started a conflict in the area. While Israel represents a fraction of the sales, the business manufactures some of these products in the North of the country (i.e., not near the Gaza band, Israel: 1/3 group production exported to Europe and US). Plants re-opened on October 10, 2023, and production continued without disruption since. However, this halted the M&A sale process. Given bids did not clear the first lien debt as stipulated in the transaction agreement from July 2023, there was an automatic transfer of ownership to the group of lenders who took over the business. The business successfully completed a smooth transition of the ownership with a de-levered capital structure and strong governance. The business continued to perform well.

- **Shop Direct (aka The Very Group): *contributor Q2.*** Shop Direct is the second largest pure-player online department store in the United Kingdom behind Amazon. Shop Direct has remained operational throughout the COVID-19 pandemic, delivering record revenues and strong profit growth now selling over 2,000 brands to nearly 5 million customers. Strong performance and cash-flow generation allowed Shop Direct to refinance its outstanding indebtedness in July 2021. Going forward, we believe that pure online retailers will continue to benefit from the channel shift seen in the Retail industry as shoppers spend more online.

  The business has continued to gain share vis-à-vis high street retail stores driving EBITDA growth from £164mm for FY14 to approximately £280mm for FY23. In our view, the strong resonance of the Very brand with its customers and the significant investments made in associated IT infrastructure helped Shop Direct outperform the UK retail market. The business is extremely cash generative, diversified in terms of retail categories, and gaining shares against the store-based channel. On May 22, 2024, the company reported its earnings for the calendar period January to March 2024 (Q3 earnings for the fiscal year ending 30 June 2024) with YTD group revenue flat yoy and pre-exceptionals EBITDA up +3.8%. Very UK's performance was consistently ahead of the UK online non-food retail market, implying market share gain during the period. The company recently announced an improvement in its governance, with new board representatives not affiliated to the controlling shareholders. According to press reports, the controlling shareholders have agreed to launch a sale process in 2025. We believe the debt is covered from a valuation perspective.

- **My Alarm: *contributor Q2 / YTD***. My Alarm, doing business as Alert360, is one of the top residential alarm monitoring businesses in the United States. The Fund opportunistically purchased the distressed bank debt of My Alarm and Alert360 before gaining majority equity ownership through Chapter 11 Bankruptcy proceedings in late 2021. Since the combination of the businesses concluded in mid-2023, the company has far outperformed our expectations both in terms of customer retention and free cash flow generation. Due to the illiquid nature of the asset, Invesco employs the use of third-party valuations to determine the fair market value of the asset, on a quarterly basis. During the most recent quarter, the company saw last-twelve-months EBITDA increased by 3% as well as refinanced their existing debt, adding leverage to fund a dividend to the ownership group.

- **Scenic: *contributor Q2 / YTD***. Scenic is a leading privately-owned luxury river cruise, land tour, and ocean cruise operator in Europe, Oceania, and North America. Founded in 1986, the company has evolved from a coach tour provider to a world-renowned luxury cruise industry leader. Following COVID-related lockdowns, the business has recovered, strongly benefitting from the global rebound of the cruise industry. Today – compared to 2019 – the company is operating four additional state-of-the-art vessels that were delivered in recent years. Most recently during 2023 and in early 2024, the company disclosed new recorded levels of bookings that are the highest received during its history. Booking levels point towards a highly successful 2024 based on the additional passenger capacity that the company is operating successfully.

- **Hurtigruten: *detractor Q2.*** Hurtigruten is a leading expedition travel company focusing on sustainable cruising. The business is the market leader in its home market, Norway, offering cruises along the Coast and Fjords of Norway as well as Expedition Cruises amongst others to exotic destinations such as the South Pole or the Galapagos islands. Pre-pandemic, the business was growing strong at around 7-8% per annum, driven by good demand for cruise ship travel and a competitive product offering.

  While Hurtigruten's brand-name and cruises remain globally leading, operations ramp-up post COVID have been slower than anticipated (marketing efforts directed at wrong booking windows, unfavorable routing decisions). In order to bridge to an expected operational recovery in 2024/2025, lenders and sponsor TDR have negotiated: (1) €185mm injection of new liquidity into the group; (2) deleveraging the operating group by reinstating some facilities into a new HoldCo facility (PIK pay); and (3) providing consent to implement the business separation on Hurtigruten Expedition and Hurtigruten Norway to position the group for future strategic alternatives with an expected sale of Hurtigruten Norway over the coming 12-18 months.

  Recent results have been more favorable. Q1 saw revenues increase to €187mm, up 16% with corresponding EBITDA of €9.9mm (compared to €3.3mm in Q1-2023). As of May 30, 2024, the company had €536mm in pre-booked ticket revenue for 2024 which stands at 3.5% higher compared to the same period last year. Booking trends for 2025 appear particularly encouraging at €130mm as of May 30, 2024, up 35% compared to the same period in prior year.

- **Talos Energy: *detractor Q2 / YTD*.** Related to the withholding tax due to Foreign Investment in Real Property Act (FIRPTA) which is a US tax law that requires all foreign persons to pay tax on dispositions of any interests in US real property assets. Real property includes oil & gas reserves. QuarterNorth operations were 100% oil & gas production in the US Gulf of Mexico, thus subject to FIRPTA. The Fund will recover any over-withheld taxes when it files its 2024 tax returns. This also had a negative impact on the March monthly distribution for the Fund as the Fund distributes all income earned during the month net of expenses and the withholding tax represented a one-time Fund expense.

- **Altice France: *detractor YTD*.** Altice France (SFR), formerly known as Numericable, is a French provider of telecommunication services offering a wide range of fixed, mobile, fiber, and asymmetric digital subscriber line telephony services. The company's services include digital and analog television, high-speed internet and a broadband digital telecommunications platform. The company is the third-largest player for fixed phone lines in France with 6.5mm subscribers and the second-largest player for mobile phones with 20mm subscribers holding a market share between 19-21% in both segments.

  We view the nature of Altice's business as defensive, with recurring revenue and cash flow derived from subscriptions. The company has executed an initial delevering strategy and has been successful in monetizing assets such as their minority stake in La Poste Telecom, data centers, media business, and xPfibre div recap for cumulative proceeds in excess of €3.9 billion (bn).

  On March 20, 2024, the company held its Q4'2023/ FY2023 earnings call. Altice France reported flat yoy revenue of €2.9bn and a modest yoy EBITDA decline of -1%, at €1bn. This was predicated on fixed/mobile subscriber losses and a decline in contracted build-to-suit Fiber To The Home (FTTH) construction revenues as France fiber roll-out reaches completion. While the proceeds of the disposal of the media group were above consensus, and the earnings were roughly in line with expectations, the price of Altice's debt fell since the earnings call. This was driven by (i) the revised earnings guidance for FY2024 (mid-to-high single digit decline in EBITDA) and (ii) other comments made by the management team during the Q&A. This led to a rating downgrade from B3 to Caa2 (CFR) with negative outlook on March 27, 2024.

  During the Q&A, management laid out a new plan to delever the company to 4.0x, which is greater than 2x of debt reduction, that would be achieved through a combination of asset disposals and "creditors' participation" in the form of par discounts captured via exchanges, tenders or debt repurchases. These comments came as a surprise to the market and contradicts the company's narrative shared with investors during the 3Q'2023 meeting which was centered around inorganic asset sales and deleveraging by approximately 1x. Despite the debt sell-off, we continue to believe Altice France is a valuable telco asset in France given the company's market shares and the quality of its underlying infrastructure.

  We also note recent transaction multiples in the space (Spain, UK, and Italy) have been higher than public market valuation. We believe the controlling shareholder is incentivized to protect its equity value by delevering the business by contributing the proceeds of the disposals and potentially raise additional proceeds from other silos (Xpfibre 50.01% stake or dividends from other telco businesses) and we continue to monitor the situation.

  ISSM is member of the Steering Committee and one of the key members organising the group of senior secured creditors. The real focus will be on asset sale proceeds application in line with asset sale covenant: paydown of senior secured creditors. Some considerations that offer downside protection to the senior secured creditors:

  - Consensus is senior secured creditors are covered from a valuation perspective.

- Traditional US-style liability management transactions are challenging (or not possible) given French jurisdiction.
- The controlling shareholder faces potential criminality if he strips out assets and upstreams to himself given the concept of “corporate interest” in France.
- The French safeguard process has been improved (EU Law harmonisation in 2021) and is more creditor friendly now.

- **Accell (Sprint BidCo): *detractor Q2 / YTD*.** Accell is a leading European e-bike manufacturer. Accell, like most e-bike companies was impacted by high inventory in 2023 as a result of over-ordering bike components in 2022. The higher orders were in response to peak e-bike demand during the pandemic. When the volumes declined to pre-pandemic levels, Accell’s inventory levels (and stocks at dealers) started rising. Subsequently, Accell had to introduce promotions to release the older (2020-2022) inventory, directly impacting earnings and leverage. Tight liquidity (with revolving credit facility (RCF) fully drawn) and higher leverage led to rating agencies downgrade in November/December 2023 to CCC. We believe the high inventory/working capital is an industry-wide issue and not specific to Accell.

  Positively, a 5-6% compound annual growth rate (CAGR) is expected for the e-bike industry in the next 4-5 years, driven by government infrastructure initiatives and a general trend towards more eco-friendly/healthier commute options. Accell’s brands in key regions (e.g., Netherlands, France, Germany) are well-positioned to address the upcoming long-term industry demand. However, we expect soft earnings in FY 2024, as management clears working capital on lower margins before positive earnings expectations in FY 2025. The business was also hit by a product recall for its cargo bike brand, Babboe (approximately 5% of sales).

  We believe the sponsor KKR has taken multiple supportive steps: (1) invested additional €300mm of capital to fund the liquidity gap given expectations of slow working capital unwind (this additional capital from the sponsor brings the total investment to more than €1.6bn, of which approximately €1.3bn (initial investment) is mostly from a new fund); and (2) revamped the management team and streamlined costs to be more in-line with 2024 bike sale expectations to protect margins. However, the path to recovery for Accell remains uncertain and we believe a restructuring of the debt to bridge over the current slump in profitability is likely.

Risk positioning (Loans and Floating Rate Notes (“FRNs”) only): *-10bps Q2 / +18bps YTD.* The Fund is overweight the “CCC” segment of the market, which underperformed during the quarter. However, on a YTD basis, the Fund’s overweight in the lower-rated credit quality buckets remained a positive contributor.

Sector positioning (Loans and FRNs only): *0bps Q2/ +6bps YTD.* We outline below some of the noteworthy themes in the largest sectors in the Fund.

- **Service:** The Fund is market weight the Service industry. In a climate of improving, but still low macroeconomic growth in Europe, the Service industry has broadly outperformed manufacturing and industrial businesses. In addition, market-leading Service businesses with pricing power are successfully managing to pass through inflationary cost to its end customers. The Fund continued to benefit from its exposure to businesses with recurring revenues with low customer churn, including credits in the education industry (e.g., Global University Systems, characterized by its defensive nature and stable underlying demand), security alarm systems operators (e.g., My Alarm), and market research providers and business solutions specialists (e.g., Kantar, delivers essential market insights to the food and consumer goods industry).
- **Travel/Leisure**: The bookings for the summer travel season have been good throughout March to June. The Fund is diversified in terms of sub-segments and saw solid earnings across leisure parks (Parques Reunidos), hotels (B&B hotels), concession catering operators (Areas). Scenic, a leading privately-owned luxury river cruise, land tour and ocean cruise operator, recorded levels of bookings that were the highest received during its history. Booking levels pointed towards a highly successful 2024 based on the additional passenger capacity that the company has operated successfully. The Fund bought the facility below par. Hurtigruten, a cruise operator, has seen a slower-than-anticipated recovery and was a detractor to performance.
- **Financials:** The Fund’s overweight position in the Financials sector largely stems from its allocation to the debt collectors space with investments in some of Europe’s leading collectors such as Lowell (Garfunkelux), Arrow Global, and Encore Capital. Over recent quarters, collections have performed broadly as expected. Resilient collections are aided by historically low unemployment rates in Europe and consumers’ ability to repay their debts. Furthermore, acquisition costs of NPLs (Non-Performing Loans) have fallen over the past year in a higher funding cost environment. This benefited operators who were able to deploy capital at attractive prices which should help de-lever balance sheets. At the same time, there has been some stress in the sector. Given capital-intensive business models, companies have felt the rising interest and funding costs on their debt. As a result, one of the industry leaders, Intrum (to which the Fund does not have any exposure) launched a recapitalization transaction with bondholders taking a small debt haircut (circa 10 cents) in exchange for equity in the business. We believe that across the industry, debt in the sector traded lower in sympathy with the highly levered Nordic debt collector. However, fundamentally we believe going forward that funding costs for the sector will improve as interest rates start coming down. We furthermore expect the low-growth, low-unemployment environment to remain supportive for collections. As such, the Fund

has built positions at what we believe are attractive entry prices in some of the leading players in the space.

Asset Selection (non-index exposure including Fixed Rate bonds and CLOs): *-46bps Q2/ -171bps YTD.* The Fund has a number of off-benchmark positions in the portfolio and, in particular to this quarter, senior secured fixed rate notes and reorganization equity. The drag on performance this quarter primarily stemmed from withholding taxes on the gain from the Fund's sale of energy exploration and production company QuarterNorth Energy to Talos Energy in March. As the Fund's interest in QuarterNorth is considered an interest in US real property by a foreign entity, FIRPTA ("Foreign Investment in Real Property Tax Act") withholding taxes apply. The Fund will recover any over-withheld taxes when it files its 2024 tax returns. This also had a negative impact on the monthly distribution for the Fund, as the Fund distributes all income earned during the month net of expenses and the withholding tax represented a one-time Fund expense. For the YTD period, along with the factors outlined above, the underperformance was primarily due to the Fund's exposure to the Altice complex (France and International).

1. Credit Suisse Western European Leveraged Loan Index (CS WELLI) in EUR as of June 30, 2024.
2. Moniker used to describe a group of high-performing tech stocks: Microsoft, Apple, Nvidia, Alphabet, Amazon, Meta and Tesla.
3. Morningstar European Leveraged Loan Index, average default rates covering June 1, 2007, through June 30, 2024.
4. Performance Attribution descriptions:
   - **Credit Selection:** contribution to performance from over/underweights in individual credits to the CS WELLI.
   - **Risk Positioning**: contribution to performance from ratings over/underweights relative to the CS WELLI.
   - **Sector Positioning**: contribution to performance from sector over/underweights relative to the CS WELLI.
   - **Asset Selection**: contribution to performance from non-benchmark (CS WELLI) assets (i.e., small non-index European loans, Floating Rate Notes, bonds, non-Euro loans, CLOs, etc.)
   - **Trade Execution**: contribution to performance from ability to execute inside the bid/ask spread of the European senior loan market.

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