

Perspectives

Debt capital markets update



FEBRUARY 2021

Crisis? What crisis?

Notwithstanding the economic impact of the pandemic, the debt markets have barely missed a beat. Clearly the pandemic is a very different crisis than the global financial crisis (GFC), but it's worth reflecting on how the evolution of the debt mid-market over the past dozen years has enabled it to shrug off the current challenges and continue apace. Ignoring that this crisis didn't start in the financial markets, there are several factors behind this resilience, most of which are founded in the evolution of the non-bank sector.

Depth of liquidity

Preqin calculate that the amount of dry powder among European direct lending funds increased throughout 2020 by 30% to €63bn. Given a model which pays fees on deployed funds, the incentive to lend contrasts sharply to that of the capital-strapped banks of 2009 where the priority was to protect existing loan books. After a short pause in Q2 2020, the competition for fewer deals has pushed market terms firmly back to pre-Covid levels, if not beyond.

Market diversity

Preqin tracks data from 244 Europe-focused private debt funds and our coverage of these names is extensive. This compares to just a handful of names pursuing senior direct lending strategies in 2009. Furthermore, as established funds reach into large-cap territory, more recent entrants have been at the lower-mid market end with players like Dunport and Kartesia creating private debt options for a broader range of lower-cap sponsors and owner-managed businesses.

Hold levels

A key selling point of debt funds is to deliver 100% of a deal. While this brings concentration risk, problem credits are more contained and impact less of the market. Most lenders have their share of COVID challenges but compared to a 2009 market where deals were often multi-banked, issues are more isolated.

Sector resilience

Whatever the liquidity, the market will struggle to deploy if all borrowers are trading badly, but while this crisis has left certain sectors deeply wounded, others are surviving relatively unscathed or indeed flourishing. It's well known that the technology, healthcare and financial services sectors have driven much of the deal volume since the second half of last year and it's no coincidence that it is in these sectors that Alantra has been most busy too. Recent examples include advising Inflexion on their investment in DWS, advising Baird Capital on their exit of Prescient Healthcare and advising Pollen Street Capital on the debt raise for their investment in Markerstudy.

Restructuring approach

In the GFC, banks' work-out teams ballooned to deal with the sheer scale of the task and large portfolios of credits were traded to help banks restructure their own balance sheets. Funds are heavily disincentivised to crystallise losses in this way and this drives generally more discrete restructuring. Funds are even turning this experience into a positive on fund raising, as a demonstration of a track record of managing problem credits.



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After a short pause in the second quarter of 2020, activity in the debt mid-market has bounced back strongly, underpinned by the ever-widening availability of private debt.

ANDREW SHELLARD,
MANAGING PARTNER, UK

ANDREW LYNN,
PARTNER, UK

The banks

This is not to rule out the banks altogether. As some continue to step back from the market, others seek to fill the gap, albeit with the bulk of the activity focused on providing super-senior revolvers. While not totally dead, the volume of FOLO structures has fallen and the longer-term role of banks as a source of term debt must be in question. Some banks such as HSBC and Investec have responded by raising third party funds to deploy alongside balance sheet commitments and others continue to rely on tied partnerships with institutions to provide higher hold levels. However, the deals where these options prove most competitive are diminishing.

The conclusion

Deal volumes were of course down last year, but Debtwire calculate that European direct lending loan volumes in the mid-market dropped only 13% to €15.8bn against €18.2bn in 2019. While this crisis has some way to run and its impact on borrowers will last longer still, this is further evidence of the market's ability to underpin deal activity and even to play a part in addressing the challenges from the fall-out. The breadth and diversity of the market is its strength, the challenge is the time and resource required to explore its full range of options. At Alantra, our integrated debt and M&A activities provide us with first-hand experience of how markets are

behaving across Europe, leaving us ideally placed to support our clients' needs. Whether the requirement is to raise debt for a new investment or to address challenges created by the current crisis, we would be delighted to discuss how we can support you.

Our recent UK debt capital markets experience

<p>JAN 2021 </p> <p>POLLEN STREET</p> <p>Debt financing</p> <p>MARHERSTUDY INSURANCE SERVICES LIMITED</p>	<p>JAN 2021 </p> <p>Prescient</p> <p>Sell-side advisory</p> <p>Endeavour</p>	<p>JAN 2021 </p> <p>HELIOS</p> <p>Sell-side advisory</p> <p>North Edge.</p>	<p>DEC 2020 </p> <p>Confidential</p> <p>Capital raise</p> <p>Integrated systems manufacturer</p>	<p>DEC 2020 </p> <p>Confidential</p> <p>Capital raise</p> <p>Industrial services</p>
<p>NOV 2020 </p> <p>GIACOM™</p> <p>Sell-side advisory</p> <p>digital wholesale solutions</p>	<p>SEP 2020 </p> <p>Confidential</p> <p>Capital raise</p> <p>Financial services</p>	<p>JUL 2020 </p> <p>Confidential</p> <p>Capital raise</p> <p>Travel services</p>	<p>APR 2020 </p> <p>Confidential</p> <p>Capital raise</p> <p>Food & Beverage retail</p>	<p>MAR 2020 </p> <p>BOWMARK CAPITAL</p> <p>Buy-side advisory</p> <p>focus</p>
<p>MAR 2020 </p> <p>LIVINGBRIDGE</p> <p>Buy-side advisory</p> <p>M247⁷</p>	<p>FEB 2020 </p> <p>TRISPAN sk:n</p> <p>Buy-side advisory and Debt financing</p> <p>adonia medical group ltd</p>	<p>JAN 2020 </p> <p>inflexion</p> <p>Buy-side advisory</p> <p>ASPEN PUMPS</p>	<p>JAN 2020 </p> <p>Richborough Estates</p> <p>Debt financing</p> <p>BEECHBROOK capital</p>	<p>JAN 2020 </p> <p>MML RETURN ON IDEAS</p> <p>Buy-side advisory</p> <p>arrow</p>

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