



## **State of the Market—Proprietary Capital Markets Intelligence**

June 2020

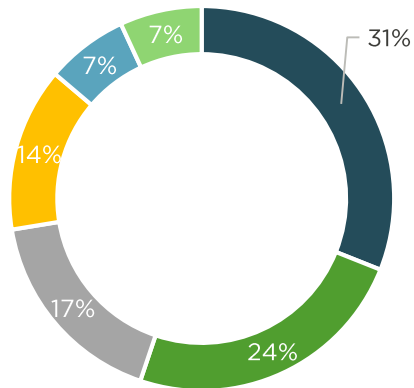
# The State of Capital Markets



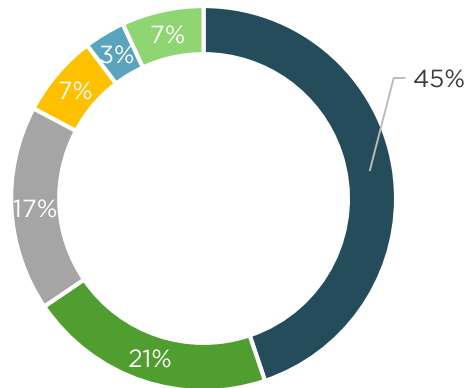
## In May came the thaw

- In late May and early June 2020, FocalPoint surveyed ~100 banks and non-bank cash-flow and ABL lenders and found that a majority are more optimistic now than 30 days ago
- Lenders are more optimistic in no small part due to a resurgence in deal flow, especially from financial sponsors
  - Lenders cite deal-flow drivers as primarily refinancing debt (45% of respondents) and private-equity sponsors making investments in new LBOs and add-on acquisitions (21% and 17%, respectively)
- Moreover, communication and cooperation between borrowers, lenders, and sponsors plus capital from PPP have boosted optimism
- This positivity, combined with strong primary-market deal-flow, suggests lenders have started to refinance debt and to support acquisition opportunities

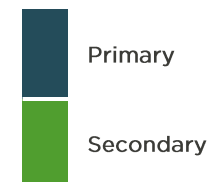
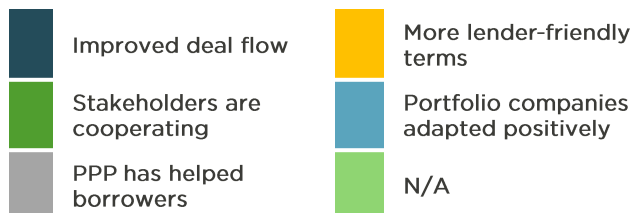
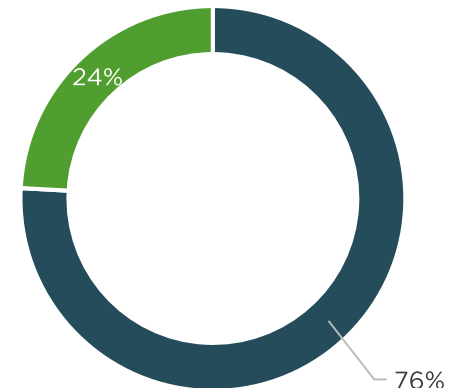
What is the most positive trend from the last 30 days?



What is most common purpose of deals you have seen recently?



Are most deals from primary or secondary markets?



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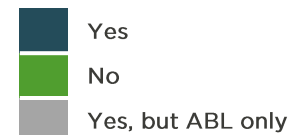
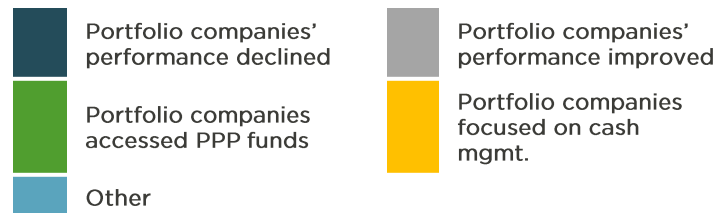
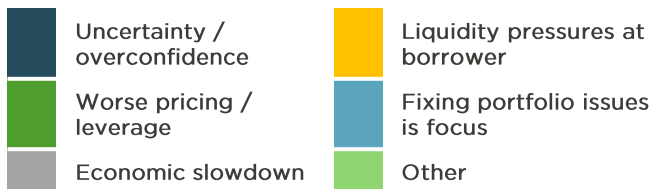
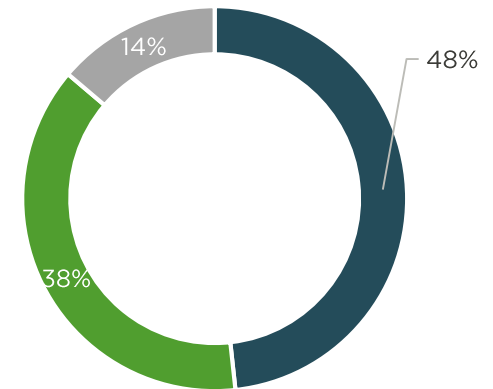
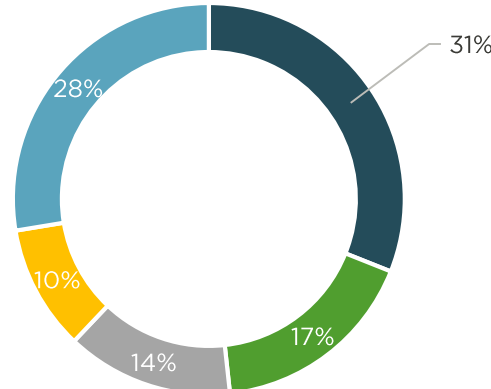
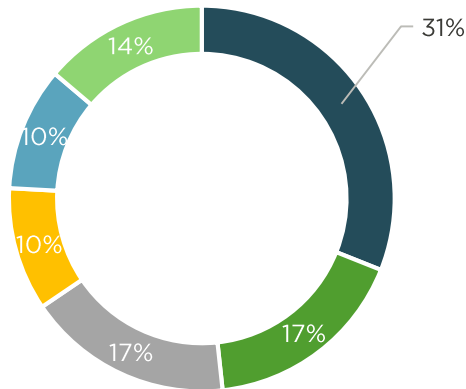
## Despite the thaw, some frost remains

- Lenders by nature focus on downside risks, and the current climate has focused their attention on macroeconomic challenges
  - 48% of lenders are concerned about the current economic slowdown or believe that any recovery is overhyped or still uncertain
  - 31% of lenders said the most significant recent trend in their portfolios was a decline in borrowers' financial performance
- As a result, 38% of lenders surveyed hadn't closed a deal with a new borrower in the last 30 days
  - FocalPoint also believes these challenges compounded bank-specific issues surrounding the level of risk capital
- **Critically, lenders were not concerned about accessing new capital**
  - A lack of survey responses on fundraising, and lots of dry powder, suggest lenders are focused deploying capital instead of accessing it
  - FocalPoint believes this, plus the passage of time, means that a plurality of lenders are ready to restart leveraged lending

What is the most worrying trend from the last 30 days?

What is the most significant trend you observe in your portfolio?

Have you put capital to work for a new borrower in the last 30 days?



# The State of Capital Markets—FocalPoint Perspective



## Recent market activity contrasts positivity with market sentiment

- Based on FocalPoint’s multiple in-market debt placements, we believe a credit markets recovery is underway
  - Lenders are increasingly comfortable with virtual due diligence; some have completed new-borrower transactions completely virtually
- “Real-time” market activity reflects less optimistic terms than before COVID-19, such as slightly lower leverage and higher pricing
  - Survey results indicate ABL lenders are concerned about the quality of borrowers’ and potential borrowers’ asset bases
  - Lenders have not regained an appetite for dividend recaps and other sponsor-friendly transactions, while equity cushions have increased
- **But, deal terms have approached pre-COVID-19 levels for certain industries faster than survey results would have suggested**
  - Sponsor-backed deals have led the resurgence and have drawn the most interest and best terms
  - Healthcare, technology, and other “recession-resistant” sectors remain attractive to lenders
- FocalPoint believes improving market sentiment reflects the significant dry powder held by private lenders
  - U.S. non-bank lenders, including multi-strategy and relative-value funds, held over \$260 billion in undeployed capital in Q3 2019<sup>(1)</sup>
  - Over half this figure was from funds raised in 2018 and 2019, suggesting lenders are still focused on new business development
- FocalPoint has observed that newer debt funds and “opportunistic” funds are the most aggressive in deploying new capital
  - Many of the market’s largest deployers of capital in recent years, including BDCs, are focused on their portfolios rather than aggressively looking to add new names to the portfolio in the coming months

### Disconnect Between Survey Results and Recent Capital Markets Activity

How Has Leverage Changed?		How Has Pricing Changed?		How Has Check Size Changed?	
Survey Results	Recent Market Activity	Survey Results	Recent Market Activity	Survey Results	Recent Market Activity
Senior leverage at least 1x lower than pre-COVID-19	Senior leverage approx. 0.5x lower than pre-COVID-19 levels	Pricing increased 150 to 200 basis points over pre-COVID-19 levels	Pricing increased 50 to 75 basis points over pre-COVID-19 levels	86% of lenders note check size remains unchanged or lower than pre-COVID-19	Lenders have noted they are focused on larger deals than before but prefer to syndicate the risk, suggesting overall risk appetite remains the same

(1) Pitchbook

# Key Takeaways



## Capital markets are open again for quality companies

- Despite what many are saying and reading in middle-market publications, FocalPoint has seen a significant improvement in current market conditions
- There is certainly a flight to quality in this market, as tougher credits are shunned until there is more clarity in market conditions
  - Nearly every lender expects a flood of distressed financings in the back half of the year once lenders have more visibility into borrowers' financial performance
- However, working with an investment bank may uncover new solutions for all industries

### Key Takeaways

Deal flow is improving, driven by a combination of sponsor activity (new LBO, add-on acquisitions) and sponsor-backed and non-sponsor-backed refinancings

Confidence has not fully returned to the market, but lenders remains supportive of and accommodating towards existing borrowers

Lenders are eager to put capital to work on new opportunities given significant dry powder

Lenders are looking to primary markets for deal flow rather than picking up opportunities on the secondary markets

Deal terms, such as pricing and leverage, have not returned to pre-COVID-19 levels, but they are not far off for quality companies

### How FocalPoint Can Help


FocalPoint has the one of the largest dedicated capital-markets team in the Middle Market

Our deep relationships with hundreds of middle-market lenders allow us to navigate any given capital-raise process with confidence and precision


# Capital Markets Specialists



Nationwide dedicated capital markets team led by a deep bench of senior professionals with nearly 120 years of cumulative experience




**Rajesh Sood**  
Managing Partner




**Gayane Kirakosyan**  
Director




**Clay Bryan**  
Managing Director,  
Sponsor Coverage




**Thomas Mills**  
Managing Director




**Clinton Miyazono**  
Senior Vice President



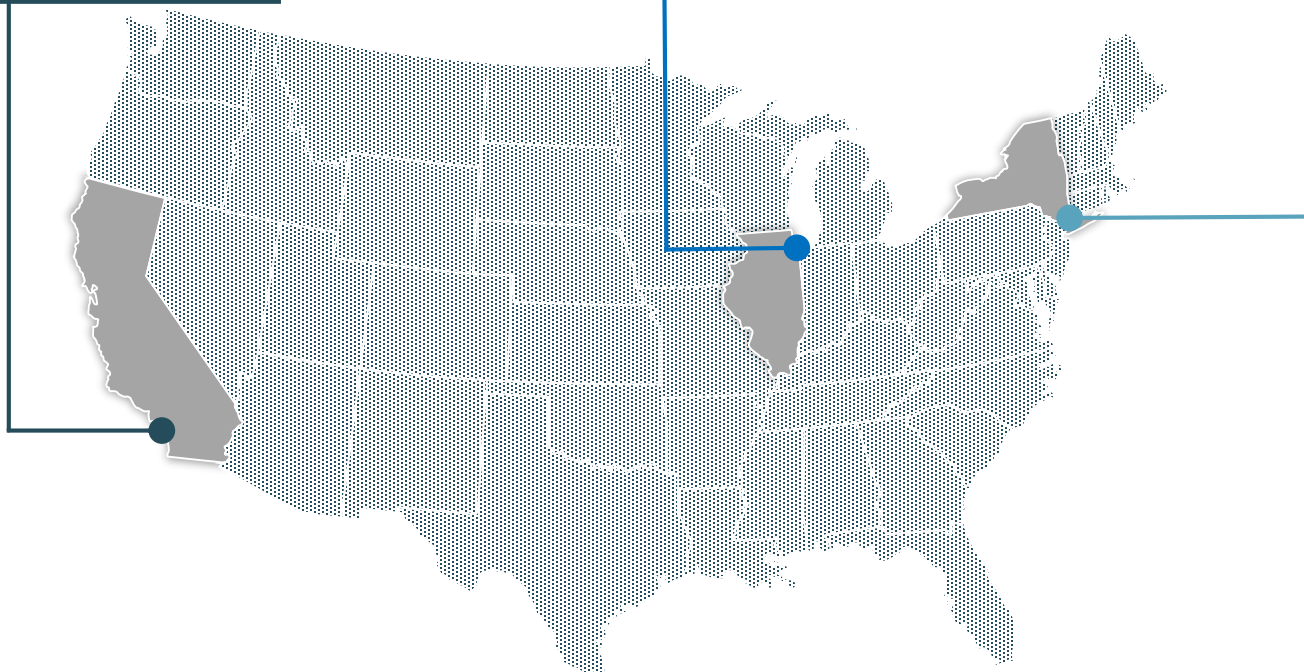
**Benjamin Tennenbaum**  
Associate



**Michael Brill**  
Managing Director



**Matthew Swing**  
Associate





## LOS ANGELES

11150 Santa Monica Boulevard · Suite 1550  
Los Angeles, CA 90025  
T 310-405-7000

## CHICAGO

150 N. Riverside Plaza · Suite 2820  
Chicago, IL 60606  
T 312-508-5788

## NEW YORK

599 Lexington Avenue · Suite 1203  
New York, NY 10022  
T 646-343-9848

## SHANGHAI

3706, Citic Plaza, 859 Sichuan North Road  
Shanghai, China  
T 86-156-1809-4182