

TALKING POINTS

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William
Brady



Jennifer
Hildebrandt



Matthew
Murphy



Justin
Rawlins



Jennifer
Yount

Adapting to a brave new market

Private Debt Investor talks to US-based partners at Paul Hastings about the need to be creative in order to cope with these unprecedented times

Distressed debt and special situations fundraising was strong in the run-up to the pandemic

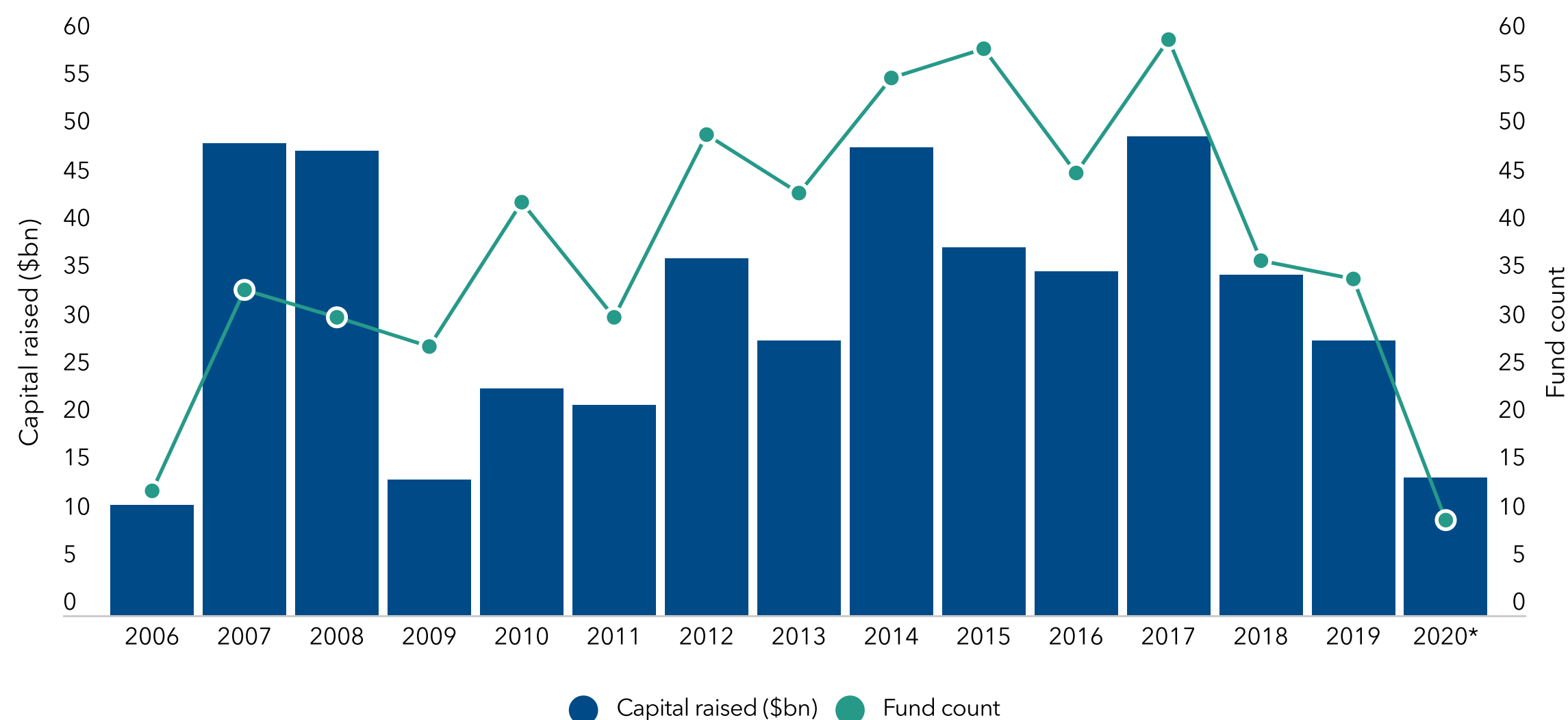
More than \$60bn was raised globally for distressed credit strategies in the two years before the crisis, and a further \$14bn was raised in the first six months of 2020



The fundraising we see in special situations is indicative of how nimble direct lenders are. Many have shifted from junior capital to special situations and we are starting to see the deployment of that cash in recent deals

William Brady

Global distressed debt and credit special situations fundraising by year



Source: PitchBook

Global direct lending fundraising was at record levels in 2019

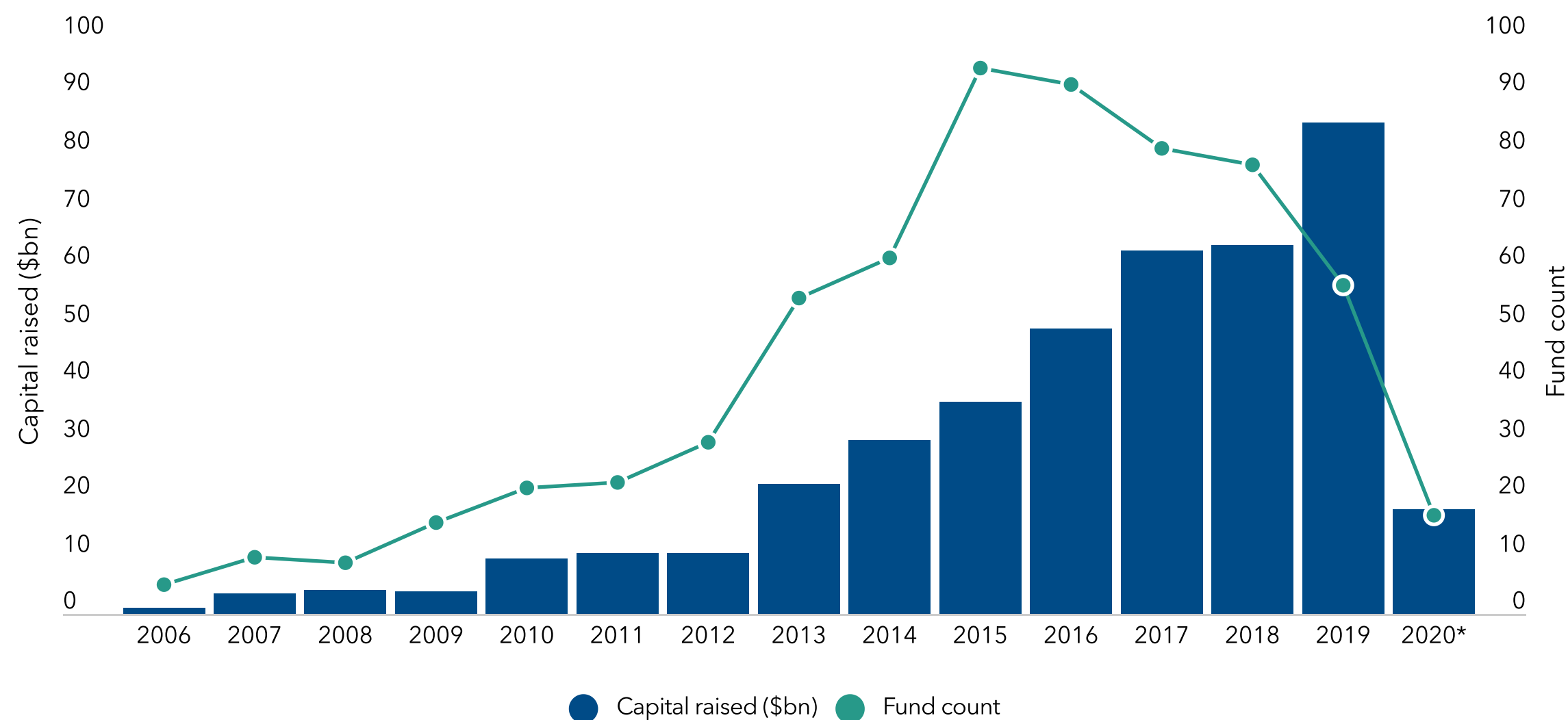
An unprecedented \$86bn was raised for global direct lending in 2019, up from \$64bn in the previous year

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As we began to navigate covid, many direct lenders had already achieved their fundraising goals and had capital to deploy. Many now need to invest that capital, in some cases by the end of this year

Jennifer Yount

Global direct lending fundraising by year



Source: PitchBook

North America accounted for half of global private debt fundraising in 2019

The dominance of North America in private debt over the past decade has fluctuated, with Europe accounting for a growing slice of global fundraising, making up 40% in 2019

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We have noticed that banks have pulled back from some of the international lending and deals with significant international components, so non-bank lenders will be able to step up

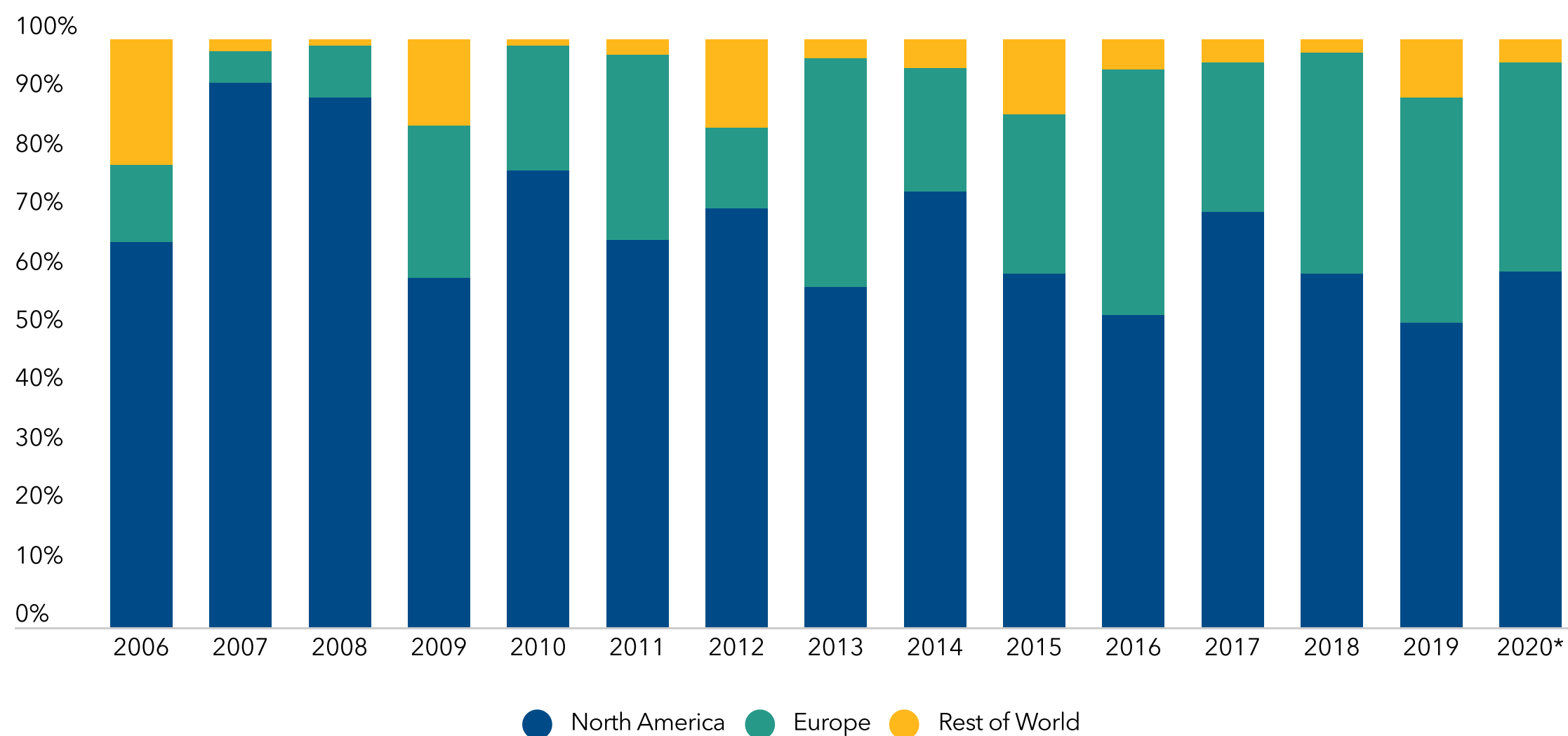
Jennifer Hildebrandt

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While cross-border deals have slowed, the fact that institutional banks appear to be pulling back in Europe may create an opportunity for non-bank lenders

Matthew Murphy

Private debt fundraising by region (\$bn)



Source: PitchBook

In 2019, private debt managers were sitting on dry powder worth more than \$260bn

The cumulative dry powder amassed over the last few years stood at near record levels by 2019, some dating back to pre-2017 vintages, putting managers under pressure to deploy

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There is a lot of dry powder out there and that is a fundamental difference from the global financial crisis of 11 years ago; that dry powder is a game-changer

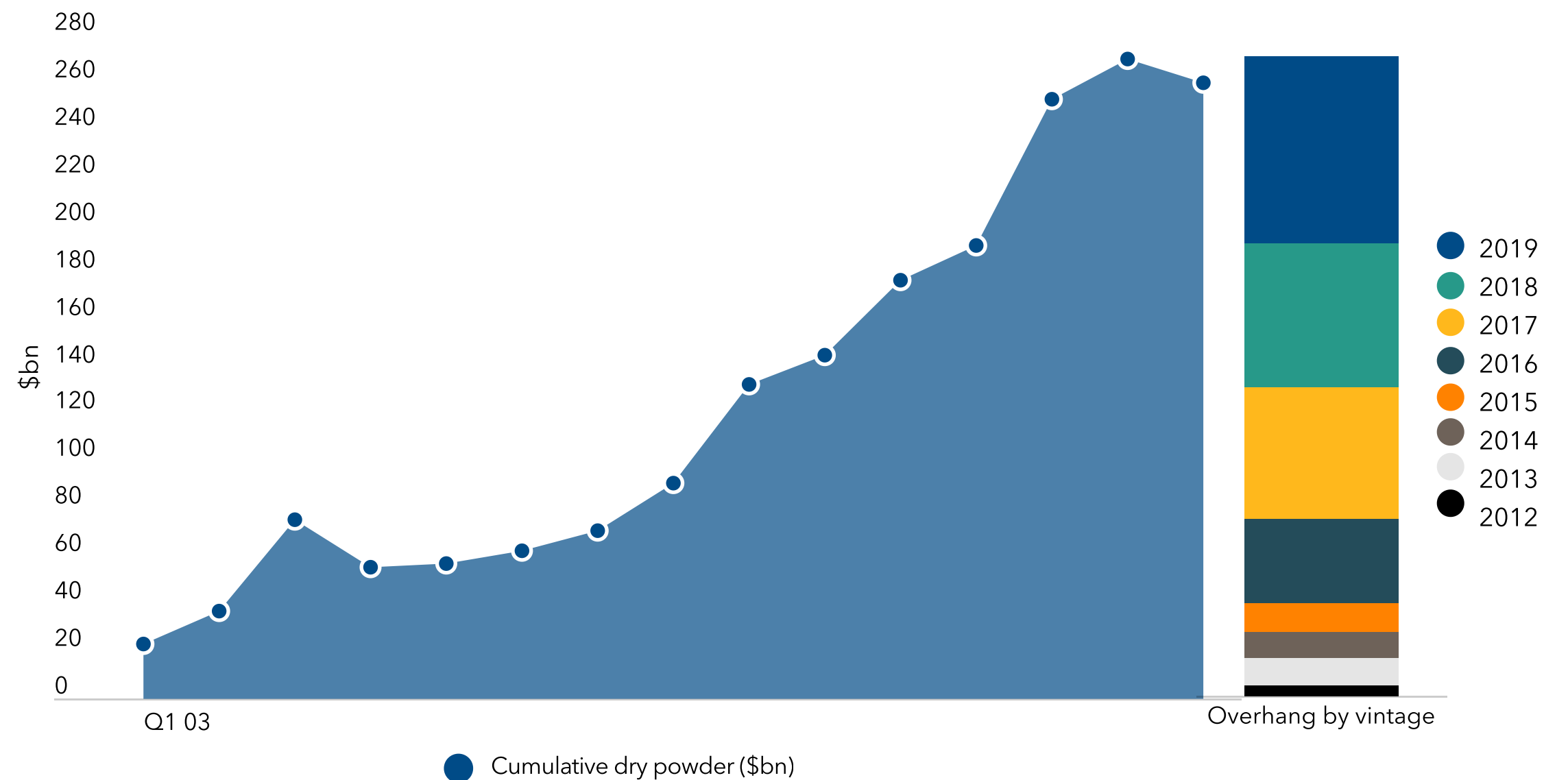
Jennifer Yount

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The uncertainty of the current situation, combined with pressure on managers to deploy capital and the underwriting pressure to invest wisely, really puts a premium on managers doing an even deeper dive in terms of due diligence

William Brady

Capital overhang (\$bn) by vintage year



Source: PitchBook

Direct lending and distressed debt accounted for nearly 70% of all private debt fundraising in 2019

Private debt fundraising by type has diversified considerably in 2020, with credit special situations fundraising much more significant in 2020 than in previous years



As an initial matter, it's imperative to understand all documents governing a distressed situation and the various leverage points of each of the stakeholders

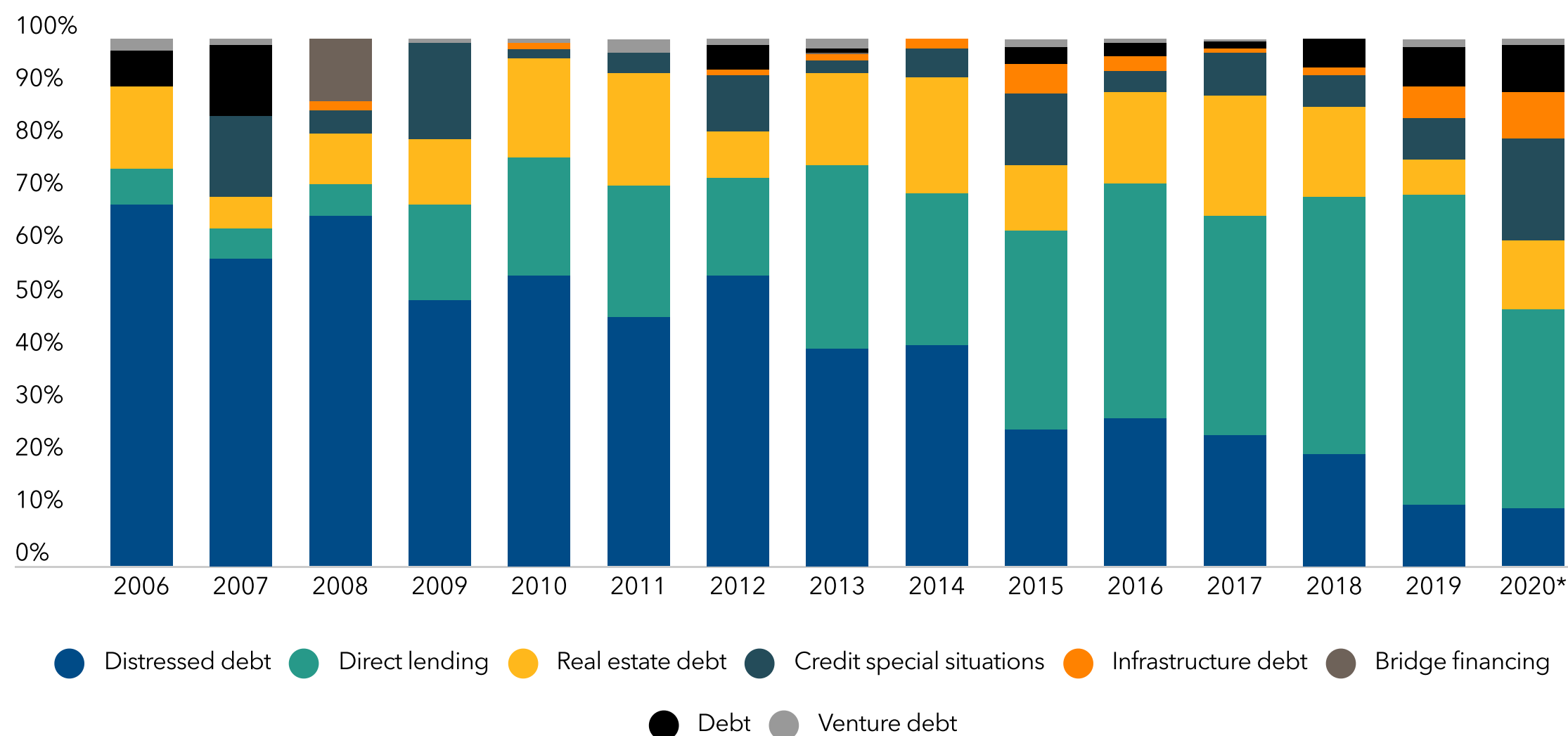
Matthew Murphy



Where companies have become troubled directly because of the pandemic, nonbank lenders have taken a measured approach, looking closely into the trajectory post-covid and modelling for recovery

Jennifer Hildebrandt

Private debt fundraising by type



Source: PitchBook

Credit markets are reacting to an unprecedented set of circumstances

That will require creative thinking and careful monitoring of a fast-changing environment in private debt markets



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The challenge is making sure you know what your client wants and figuring out how to accomplish that through the documentation you have. A key issue is what live opportunities exist, because the documents often leave many options

Justin Rawlins



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This is the most eclectic market I have seen in my career, and a creative approach is at the heart of it. If companies are going to adapt and evolve, they need innovative solutions from their lenders

Jennifer Yount

Click to read on

For more on our discussion with Paul Hastings' US partners, [check out the complete Q&A here](#)

Analysis

TALKING POINTS

The coronavirus crisis requires solutions to a series of problems never seen before in the credit markets, say Paul Hastings partners William Brady (New York), Jennifer Hildebrandt (Los Angeles), Matthew Murphy (Chicago), Justin Rawlins (Los Angeles and Houston) and Jennifer Yount (New York)

Covid-19 forces managers to be more creative

Q What is the state of the market on new issuances as compared to before the covid-19 crisis?

Jennifer Yount: Before covid-19, in the fourth quarter of 2019 and at the start of 2020, direct lenders were already shifting focus. Many felt that the over-confident market needed some correction, and were moving away from the highly-competitive acquisition financing market into areas with less competition, including lending to venture-backed business. 2019 was a particularly strong year for fundraising globally. As we began to navigate covid, many direct lenders had already achieved their fundraising goals and had capital to deploy.

Then, the pandemic hit and they regrouped. Many are now sitting on capital to deploy and they need to invest that capital, in some cases before the end of this year. It is clear there is a lot of dry powder out there and that is a fundamental difference from the global financial crisis of 11 years ago; that dry powder is a game-changer. We are seeing an uptick in new issuances, going from venture debt to special situations and up and down the capital structure in all combinations. The direct lenders are flexible and opportunistic, and August was one of the busiest months I have seen.

William Brady: In spring, people were trying to figure out what was happening, but since summer, it is a sale of two worlds. There are companies that went into covid-19 with good balance sheets and are not in the severely impacted sectors, where lenders are supporting refinancings, sale events or strategic acquisitions. However, there are the companies that were already unstable going into this, or in sectors that are in retail or hospitality, where as a result of the pandemic, the demand is for liquidity solutions and the issue is defence rather than offence.

Analysis

Q Which sectors have been hardest hit by the pandemic and which sectors have continued to perform?

Justin Rawlins: There are a number of sectors like retail, hospitality, and oil and gas where the hit has been really hard. Then there are other sectors that remain question marks, like hospitals, some of which have lost billions of dollars due to a lack of elective surgeries. Other sectors, including those related to travel and airlines, also remain highly stressed. In commercial real estate, however, there has not been as much distress "to date" as we had expected. We do expect a number of significant real estate restructurings in the future.

Jennifer Hildebrandt: The industries that have done well in recent months are the technology industries, including (though not limited to) virtual and online services, healthcare and pharmaceuticals (maybe apart from elective surgeries), nutritional supplement businesses, and video game companies. Technology and software companies have been the focus of intense competition among lenders – that was the case before covid-19 and has only intensified.

Q For new issuances, what type of investments are non-bank lenders making?

JY: This is the most eclectic market I have seen in my career, and a creative approach is at the heart of it. If companies are going to adapt and evolve, they need really innovative solutions from their lenders, so we have seen a wide range of structures covering senior, junior, first lien, second lien, unitranche, mezzanine, first out, last out, super-senior, preferred equity and hybrids of all of the above. Borrowers are calling direct lenders asking them for solutions to problems not seen in the past during similar economic pressures.

Q In what areas of special situations are you seeing the most activity?

Matthew Murphy: The specifics of a particular situation – the industry, geography of the borrower, financial situation of the borrower pre-pandemic, the lenders involved – determine whether you have a very active situation requiring immediate attention or a slowly moving collaborative process creating more runway for a borrower to address its issues. In some situations, clients enter into amendments, easing covenants, changing rates or deferring payments; other times, if the borrower was in distress prior to covid-19, the situation may need to be addressed more aggressively. Under either scenario, it is imperative to be proactive and be prepared to address a problem before it arises.

Source: PitchBook

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6 Private Debt Investor • October 2020

October 2020 • Future of Private Debt 7

Meet the Paul Hastings team



William Brady
Head of the alternative lender and private credit group, New York



Jennifer Hildebrandt
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Partner in finance and restructuring and chair of the Chicago office



Jennifer Yount
Partner and chair of global finance and restructuring practice, New York



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