2021 PREQIN GLOBAL **PRIVATE DEBT** REPORT

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A Note on Our Theme

Plants have evolved to thrive in conditions that many would describe as incredibly harsh. Surviving in full sunlight, freezing temperatures, or rising seawater are just some examples of this adaptation and resilience in action. Similarly, we've seen alternative asset classes continue to grow and mature as the world faces a challenging pandemic, political instability, and change.

CEO's Foreword

Welcome to the *2021 Preqin Global Private Debt Report*.

COVID-19 impacted all markets and industries globally in 2020, with unprecedented falls in economic activity. Businesses dependent on physical interactions bore the brunt of the impact, so it is no surprise that private debt fundraising was down on 2019, with 200 funds raising a total of $118bn in 2020. The 10% fall in capital raised was the smallest of any alternative asset class.

Despite slower fundraising, private debt assets under management (AUM) rose to $887bn as of June 2020, from $842bn at the end of 2019 (see page 16). The 5.3% gain was smaller than in previous years, but the largest of any alternative asset class. LPs tell us they are sticking with their private debt programs; almost half (47%) of investors surveyed by Preqin expect to commit more capital over the next 12 months, with a further 40% intending to maintain investment levels (see page 86). In the longer term, 48% intend to increase allocation, with a further 40% maintaining them.

We expect private debt AUM to continue on an upward trajectory and reach $1.4tn by 2025. Our forecasted CAGR of 11.4% is the second highest of any alternative asset class, after private equity. In a low interest rate environment, private debt will be an attractive alternative to public markets.

While the medium-term outlook is positive, GPs face a horribly crowded and challenging fundraising market. Preqin tracks a record 547 funds in market at the start of 2021, seeking an aggregate $290bn, up 51% on one year ago (see page 29). The ratio of capital targeted to prior-year capital raised stands at 2.46x, a substantial increase from 1.45x in 2019.

The largest managers increased their influence on the market in 2020, as restrictions on travel and

Mark O'Hare
Chief Executive Officer

Preqin
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face-to-face meetings led LPs to prioritize existing relationships. The 10 largest private debt funds accounted for 39% of aggregate capital raised. Though larger than the 31% in 2019, it is on a par with much of the past decade (see page 26). Last year was particularly challenging for smaller and first-time managers, as investors favored established GPs and existing relationships. That said, there was a notable upturn in the number of small funds reaching a final close in Q4 2020. Clearly, investors still want exposure to managers in different parts of the market.

As the asset class has grown and competition increased, returns have trended downwards. Median IRRs have steadily declined from 10.4% for 2010 vintage funds to 8.2% for 2017 funds, and competition and asset valuations topped the list of fund manager concerns in our survey (see page 86). However, private debt occupies a different part of the capital structure to most other alternatives, and still offers its key tenets to investors: diversification, low correlation to other asset classes, and reliable income streams.

While the number and value of transactions declined in 2020, deals have got significantly larger in recent years. The average deal size in 2020, at $85mn, marked a 20% increase on 2019, and has more than doubled over the past five years. As COVID-19 shut down

swathes of the global economy, an expected flood of opportunities failed to materialize, largely because of the interventions and support programs initiated by governments and central banks. These actions may, however, have merely kicked the can down the road. Oaktree stepped in with a $1.3bn distressed loan for Brazilian carrier LATAM Airlines in May, while Apollo and Athene Asset Management invested $4bn in car rental company Hertz in November. In addition to increased investment in transportation (see page 48), deal values also climbed across the financial services, technology, and telecoms sectors.

Preqin expects private debt to increase its influence in alternative investing. Risk-averse mainstream lenders, low interest rates, and investor demand offer tailwinds for asset growth. The industry will continue to develop and evolve, and product innovations are targeting varied risk/return exposures to meet investors' needs.

In 2020, we took great strides in delivering you – our network of over 120k global alternative assets professionals – better data, tools, and insights to help you discover new opportunities, benchmark your performance, and find top-tier industry partners. This year alone, we:

- Opened new offices in Sydney and Dubai to enable us to deliver deeper local market knowledge
- Launched ESG Solutions to provide you with critical visibility of GP-LP environmental, social, and governance factors at a firm, portfolio, and asset level
- Kept you informed through more than 300 reports and content articles, published by our expanded team of research, journalism, and data science professionals
- Improved ease of access to our exclusive content, from all platforms and locations, through our refreshed mobile application and APIs
- Introduced timesaving and collaboration features across our products to help you find what you are looking for
- Achieved major data growth across our platform, with our investor profiles up 20% to almost 20k, our fund profiles up 12% to 117k, and our GP coverage up 10% to 43k profiles.

As you have come to expect from Preqin, The Home of Alternatives®, we will continue to heavily invest ensuring you have the most comprehensive view of the alternative assets industry.

Thank you for your ongoing support, and happy investing.

COVID-19 Creates Attractive Direct Lending Opportunities

We spoke with Ken Kencel, CEO and President of Churchill Asset Management, an affiliate of Nuveen, about the impact of the pandemic on direct lending

Ken Kencel
CEO and President

Churchill Asset Management
www.nuveen.com/churchill

How has COVID-19 impacted private credit investment activity?
After coming to an abrupt halt earlier in the year as a result of the global pandemic, the private credit market rebounded dramatically in the second half of 2020 and continued to get increasingly active through year end.

In fact, we saw record investment activity for our firm in the fourth quarter. For the first time in a long time, it's a lender's market. The long bull run in credit markets saw a rise in leverage levels, a steady narrowing in borrowing rates, and a general loosening in lender protections (e.g., covenants) as yield-starved investors competed to lend money to both public and private companies. In the middle-market lending space, this trend ended abruptly in March, when the rapid increase in COVID-19 cases – and ensuing lockdowns – drove many companies to draw down revolving credit lines and some to reach out to debt and equity providers for covenant relief.

Since then, new issue loan spreads in the private credit market have risen, covenants have tightened and equity cushions have become more substantial, reflecting a significantly more lender-friendly market dynamic. We see the current environment as very attractive for private credit managers like Churchill that have the scale and deep relationships in the private equity community. While we are very carefully evaluating new transactions and remaining highly selective, we believe the 2020/2021 vintage for private funds will be particularly strong for market-leading managers (similar to the GFC). There are many companies today that are looking to raise capital that have not been impacted by COVID-19, or maybe even benefited from it.

Nuveen, the investment manager of TIAA, is one of the largest investment managers in the world with more than $1tn in assets under management as of 30 September 2020. Managing a broad array of assets across diverse asset classes, geographies, and investment styles, we provide investors access to a comprehensive range of liquid and illiquid alternative strategies.

Churchill Asset Management, our private capital investment-specialist affiliate, provides customized financing solutions to middle-market private equity firms and their portfolio companies. With a long history of disciplined investing across multiple economic cycles and over $27bn of committed capital under management as of 1 January 2021, Churchill's solutions include first lien, unitranche, second lien, and mezzanine debt, in addition to equity co-investments and private equity fund commitments. *GAR-1433616PG-E1221X*

How has COVID-19 impacted private credit loan portfolio performance, and which sectors have outperformed?
Our focus on high-quality, recession-resistant businesses and emphasis on significant portfolio diversification proved to be extremely important. With minimal exposure to oil & gas, travel & leisure, restaurants, and retail, we have been well positioned to weather the pandemic. In fact, we did not experience a single COVID-19-related payment default or loss in

2020 in our investment funds. Interestingly, during the second half of 2020, we began to see a clear distinction emerge between the 'haves' and 'have-nots' in the private market. Sectors that have performed well – or in some cases, even better – during COVID include consumer staples, logistics/distribution, online learning, healthcare services, software, and B2B businesses. We remain focused on these sectors as we evaluate new opportunities.

Are investors looking at private credit differently today than they were before the pandemic?
The hunt for yield is still very much driving demand in private credit for institutional investors, particularly pensions, insurance companies, and endowments. We see this first-hand from our parent company, TIAA, who we invest on behalf of and which retains a robust appetite for senior lending and junior capital strategies.

Investors are actively allocating to private credit and are very excited about the current market opportunity, but of course want to focus on companies that are not adversely impacted by COVID-19 and are more cautious about where to put their money to work. Many realize this vintage could be the best in years with attractive pricing, reasonable leverage, and better structures. Investors are seeking strong, differentiated GPs with scale and a great track record through cycles; experienced managers with strong relationships appear to have a clear advantage given the due diligence challenges and need for certainty of execution in the pandemic environment.

There has been significant capital raised this year for distressed opportunities, but so far deal flow has been underwhelming. Why is that?
The early stage of the pandemic saw sectors like travel & leisure, hospitality, and retail hit dramatically. Public valuations initially took big discounts. But once the central bank intervened, prices bounced back. That gave investors a sense that Fed liquidity would carry the higher-quality businesses through the crisis. Of course, that didn't stop the big bankruptcies like Neiman Marcus, Brooks Brothers, and Hertz. There are always distressed opportunities in retail. The question is what's the outlook for middle-market companies that have been impacted by COVID?

Those owned by private equity firms can manage through the initial liquidity crunch if owners and lenders work together to provide transition capital and covenant flexibility. Of course, some businesses in more severely impacted sectors, like restaurants and retail, may disappear. Others may need outside rescue capital. But that's expensive, and not every borrower qualifies as having real recovery value.

It's also the case that for less impacted companies – the 'haves' in the economy – the recovery has been swifter than anticipated. Our experience with more defensive sectors, such as business services, technology, logistics/distribution, software, and some healthcare, shows that values were sustained through the crisis. Indeed, in some cases, valuations for the better-performing credits are higher than pre-COVID levels. Assuming vaccine distribution rolls out in the first half of this year, the window for distressed buyers could be narrower than in prior market disruptions.

We seem to be in a recovery, despite climbing infection rates. How quickly can private credit be deployed in this environment?
Once investors realized that the worst-case scenario for the economy and borrower defaults was short-lived, and limited to consumer-facing sectors, they began to focus on deploying capital – particularly given the attractive risk-adjusted returns provided by private credit.

As is almost always the case, superior investment opportunities come just as economic recoveries are underway. That was certainly the case this time. In the second half of 2020 we saw senior loans with generally lower leverage and higher yields than had been the case for some time. Our unique sourcing model, with deep LP/GP relationships, has successfully focused on directly originated private credit investments in the 'have' category previously mentioned. It was also the case that our stronger portfolio allowed us to lean into new deals when others were still struggling to manage their problem credits. We found the number of competitors had shrunk from pre-COVID levels and the commitment capacity of those that remained was significantly diminished.

Having successfully raised over $6.4bn in new capital last year, including closing a $2bn fund in March, we were able to deploy cash quickly. M&A activity also picked up markedly at the end of the summer; sellers of good businesses recognized the dynamic of improved purchase multiples. Private equity firms identified high-quality opportunities and began investing capital aggressively. As a result, we were able to deploy a record amount of capital in support of these investments – over $6bn in 2020 and more than $2.8bn in the fourth quarter alone – at better pricing, reasonable leverage, and for businesses that were generally not impacted by COVID-19. We see these positive trends continuing in 2021 as the impact of COVID-19 begins to fade.

How COVID-19 Has Shaped the Future of Distressed Debt Investing

We spoke with Andrew Amos, Director at M&G Investments, about how the rising levels of defaults are creating more opportunities in the space

Andrew Amos
Director

M&G Investments
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M&G Investments is a global asset manager with a long history of investing and innovating across both public and private markets. As an active manager we offer access to a broad range of capabilities that span both public and private assets including fixed income, equities, multi-asset, real estate, infrastructure, and private equity. Globally we manage over £271bn (at 30 June 2020) on behalf of individual and institutional investors including pension funds, endowments and foundations, insurers, sovereign wealth funds, banks, and family offices.

The events of 2020 drew a record number of distressed debt funds to the market, while other funds have pivoted toward opportunistic or special situations strategies. How will the sizable pipeline of distressed funds impact the market in 2021?
We are currently witnessing imbalance between the supply of distressed debt opportunities in more liquid leveraged loans and high-yield bonds and demand for each of those assets. Distressed debt funds raised a lot of capital in 2020 and mostly chased the same liquid opportunities, but the yields on these opportunities fell after markets rallied from April. Though opportunities will continue to arise while the pandemic prevents economies from returning to 'normal,' we expect this imbalance to continue through early 2021.

This being the case, we will continue to target less liquid distressed debt opportunities and special situations financings. Our ability to source such deals enables us to minimize the impact of the very cyclical nature of distressed debt investing, and deploy capital at a target return of 15% p.a. throughout the cycle.

Our experience as investors during and after the Global Financial Crisis (GFC) has taught us that 'good' distressed debt opportunities might take some time to materialize, but corporate stress continues long after the initial crisis and market sell-off. We were still finding opportunities yielding 15% p.a. from corporates six years after the GFC; we expect the same long tail of attractive investment opportunities following the pandemic.

Consistent with our approach of sourcing interesting illiquid opportunities, we tend to raise smaller funds (€300-700mn). This enables us to be highly selective and focus on smaller, less liquid, more time-consuming, and less competitive opportunities if public markets become over-competitive. If the opportunity set turns out larger than expected, we can rely on long-standing relationships with repeat investors to quickly raise additional funds.

What are the key factors for success as a distressed debt fund manager?
There are many ways to invest in distressed debt, all of which require different skillsets. Most funds prefer to target more liquid leveraged loans and high-yield bonds. In our view, this creates competition for opportunities,

which reduces returns or increases risk. We target smaller, less liquid deals and actively manage our investments, using a hands-on approach to bring companies back to financial and commercial health. To do so, we rely on several factors:

- **Broad and effective market tracking.** The best opportunities are often the ones that don't hit the radar screens of liquid distressed debt funds and the investment banks, advisors, and consultants that service them. M&G's extensive fixed income platform provides us with access to the entire universe of opportunities, including the smallest, least liquid, and least visible ones.
- **A specialist restructuring view from inside the deal.** M&G's restructuring team has been acting as an in-house restructuring advisory service since 2003. This allows us to develop a much sharper picture of how a restructuring might pan out, and tells us the real value of the underlying business. Given M&G's extensive fixed income book, we can develop this view on a large number of the restructurings in the market, enabling us to select only the most compelling opportunities in which to invest.
- **Full set of restructuring skills.** The 18-strong restructuring team has been built to have the deep expertise required for distressed debt and special situations investing: accounting, credit, legal, and the hands-on experience of helping stressed companies turn around.
- **Network of industry specialists and experienced board directors.** While we are a hands-on investor, we are cognizant of the fact that, in most cases, we are not specialists in the specific industry and in the day-to-day activities required for an operational restructuring. To address this point, over the years we have built a network of trusted senior industry specialists, who can help us achieve the positive change we target as members of a management team, board directors, or in an advisory capacity.

How can the risk/return profile of distressed debt be improved?

As a strategy that often targets a 15%+ IRR, distressed debt investing is considered a high-risk strategy. With that said, our experience over the past 20 years suggests there are a number of ways to reduce its risk profile.

We tend to choose investments where the main risks are in credit and execution of the restructuring and subsequent turnaround, i.e. aspects that we can control. In the vast majority of cases we only invest in opportunities where we can influence the restructuring process (in many cases by investing alongside existing M&G holdings) and exercise control during the turnaround phase (in many cases by obtaining enhanced governance rights as a condition of the restructuring). This allows us, to a large extent, to be in control of our own destiny.

Over the years, we've learned that even the most bullet-proof investment thesis can unexpectedly fail. For this reason, we only invest in situations offering a 'Plan B' option, enabling us to recover the invested capital and return it to our investors, usually by selling underlying assets or implementing an alternative recovery plan.

A lot of time and effort is spent fine-tuning the legal aspects of our investments, which provides us with the maximum number of 'levers' to recover our investment if things don't go as planned.

As specialists in distressed debt with direct deal experience in all jurisdictions across Europe, we are able to understand the idiosyncratic factors that impact risk/reward and deliver value from an investment.

What will be the medium- to long-term ramifications of the response to COVID-19 for distressed debt opportunities?

We have known for a while that the next distressed debt cycle will be driven by payment defaults, not technical defaults or covenant breaches, due to the steady increase of covenant-lite loans since 2012. In some cases, government interventions are delaying the inevitable for companies that entered the crisis in poor financial and commercial health. When government support eventually comes to an end, we expect the majority of these companies to urgently require an injection of capital, followed by financial and operational restructuring. We expect the response to COVID-19 to have an impact in the short term by delaying defaults, but a limited impact in the medium to long term.

As investors, we prepare for this scenario by monitoring many companies, with the help of 200+ professionals in M&G's fixed income business and through our in-house restructuring role. Additionally, we make sure we maintain access to dry powder, which will be needed to provide rescue financing. The ability to fund emergency liquidity is likely to be one of the more impactful ways of gaining control in a process.

We believe the coming months and years will offer attractive opportunities to invest our clients' capital while helping companies 'with a reason to exist' regain a stable financial and commercial footing.

1

Overview of the Industry

Executive Summary

The pandemic-led downturn helped drive private debt assets to new heights, but valuations and competition concern investors

Private debt emerged as a core alternative asset class after the Global Financial Crisis (GFC) and has again proved its worth in a volatile year, with the COVID-19-driven slowdown pushing total assets to new highs. AUM increased to $887bn as of June 2020, making private debt the third largest among the private capital asset classes, behind private equity and real estate.

For private markets, the fallout from COVID-19 has not been as severe as it was after the GFC, thanks to the swift and substantial action of central banks. Stimulus measures and bond-buying programs suppressed interest rates, in many cases below zero, driving debt portfolio valuations higher. The decline in economic activity drove demand for cash injections, but companies that were in need of bridge loans or cash injections were not short of options.

Private Debt Funds Raised $118bn in 2020

Funds continued to flow into the asset class, despite the logistical challenges. The $118bn raised across 200 private debt funds in 2020 was just over 10% down on both measures from 2019, though almost a quarter (24%) of funds raised 125% or more of their target.

Dry powder stood at $320bn as of December 2020, up 19% from a year earlier. A combination of reduced M&A and abundant liquidity in other debt pools slowed deployment rates. Increasing competition and the amount of capital chasing deals will put pressure on returns across the asset class, though opportunities for higher returns exist in more value-added strategies.

Capital Targeting Distressed Assets Increased

Distressed debt and special situations have been an area of growth for private credit managers. The proportion of capital for these strategies has climbed for most of the past decade, up from 16% in 2009 to 40% in 2020. Distressed debt AUM increased by $9bn over 2020 to June, driven by a 15% increase in undeployed capital. While the build-up of commitments was due in part to expectations of a surge in distressed and restructuring deals, emergency stimulus measures and loan facilities staved off distress for many companies.

Performance Met Investors' Expectations

Despite the difficult economy, private debt delivered for investors. More than two-thirds (68%) of those we surveyed at the end of the year said returns had met expectations in 2020, with 15% saying they had been exceeded. Only 14% will reduce their allocation to private debt in the next year. Investors told us they were most concerned by asset valuations and deal competition in the year ahead.

Private debt is no longer a niche product. As the asset class has grown and competition increased, aggregate returns have trended downwards but remain attractive relative to other fixed-income markets. Direct lending, which offers greater security, generated a median IRR of 8.3% for vintages 2008-2017, with a standard deviation of just 5.0%. Distressed debt returns have been more varied over the same period, with a standard deviation of 9.7%, but a higher return of 9.2%. Investors can choose the point on the risk/return spectrum that fits their needs.

Private Debt Megatrends

Key themes shaping the private debt industry

Growing Allocations to Alternatives

In an ongoing low interest rate environment, investors continue to turn to alternatives such as private debt to diversify and generate strong returns for their investment portfolios.

Capital Concentration

Larger fund managers continue to absorb more industry capital as investors seek out established managers.

Rise of the Mega Deal

Increased competition for deals has led to a larger proportion of mega deals (valued at $1bn+) in the private debt space.

Reversion to Wider Yield Spreads

The spread on US high-yield corporate bonds is likely to widen in the future, making private debt an attractive investment for investors seeking stable risk-adjusted returns.

ESG

ESG continues to grow in prominence within alternatives; we are seeing a fundamental shift in the attitudes of private debt investors toward ESG.

Private Debt in 2020: Key Facts

$887bn

Global private debt AUM as of June 2020.

$118bn

Total capital raised by the 200 private debt funds closed during 2020.

547

Number of private debt funds in market as of January 2021, collectively targeting $290bn.

780

Number of private debt deals completed during 2020.

3.3%

Net annualized return of private debt funds in the three years to June 2020.

90%

Proportion of surveyed investors that intend to maintain or increase allocations to private debt over the long term.

2

AUM & Dry Powder

Record-High AUM as Demand Surges

AUM has reached a new peak as investors search for yield in a near-negative interest rate environment

The global economic slowdown in 2020 has pushed AUM across private debt to new record levels. In order to counteract the economic setback caused by the pandemic, central banks and governments across the globe have injected trillions of dollars worth of stimulus, causing the prices of publicly traded debt and equity securities to surge. Private debt markets have not yet become saturated and have continued to benefit from the retrenchment of bank lending, receiving an influx of capital into the asset class.

As of June 2020, private debt AUM stands at $887bn, having increased consistently for the past 20 years (Fig. 2.1). The asset class is now the third largest in private capital, behind private equity ($4.74tn) and real estate ($1.09tn).

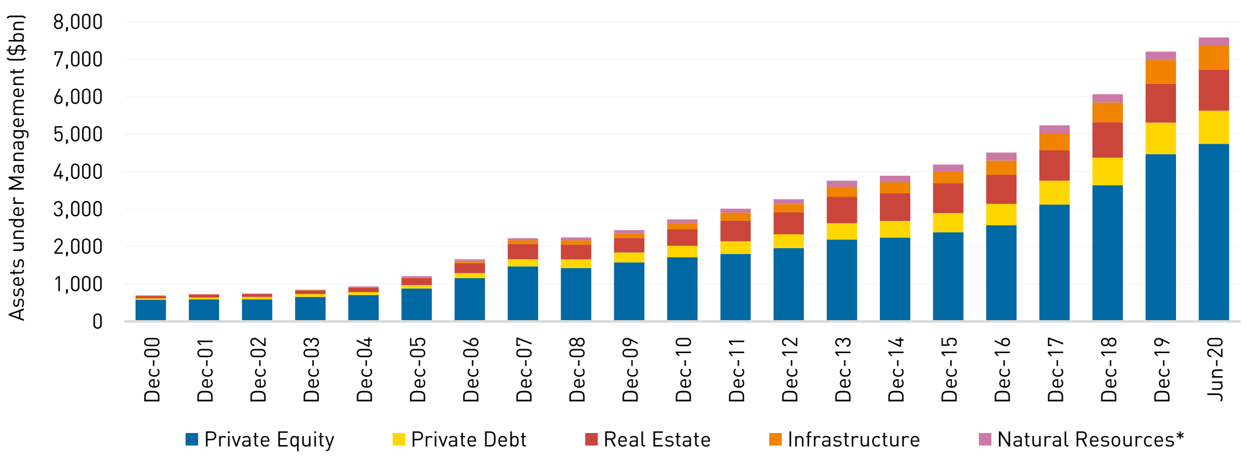
Historically, fund managers competing for assets in private debt largely consisted of North American private equity firms, such as Blackstone Group, KKR, and Oaktree Capital Management. But in recent times, more mainstream fund groups from across the globe have piled into the asset class.

In line with this trend, while funds focusing on North America constitute 61% of total AUM, other regions have gradually expanded their share (Fig. 2.3). This is particularly the case for Europe-focused AUM, which now makes up just under 30% of the total, up from just over a quarter five years ago.

The rise in demand for European private debt has been aided by an extremely low-yield environment. Economic growth in Europe is largely dependent upon small to medium-sized enterprises (SMEs), most of which make up the bulk of lending opportunities.

In fact, private debt's enhanced yields are proving to be particularly attractive across the globe, as the economic crisis upends corporate balance sheets. From a returns perspective, the asset class has displayed resilience over the past few years, and in a

Fig. 2.1: Private Capital Assets under Management by Asset Class, 2000 - 2020



*Excludes Private Equity and Infrastructure fund types with a focus on natural resources.

Source: Preqin Pro

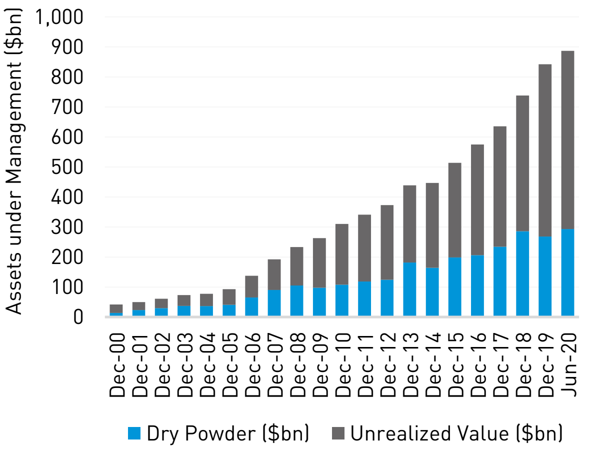
low-return environment investors are attracted by the potential for high yield, with the spread on US high-yield corporate bonds continuing to widen (see page 20).

Distressed debt AUM, in particular, has experienced a significant injection of cash. Many businesses previously viewed as financially sound or defensive in nature have endured increasing financial stress during global lockdowns. As of December 2020, distressed debt dry powder is up 18% on the previous year, standing at $79bn (Fig. 2.8). Distressed debt funds typically perform well during certain economic conditions, including periods when high-yield debt issuance is elevated.

At a time when global interest rates are near all-time lows, and as state-backed support measures ease off, debt restructurings and insolvencies are expected to increase globally. According to VoxEU[1], 90 countries have approached the IMF for short-term emergency assistance – around twice the number that requested assistance in the aftermath of the GFC. Repairing balance sheets and consolidating lockdown-related debts will be the main priorities, providing opportunity for fund managers to put the capital to work.

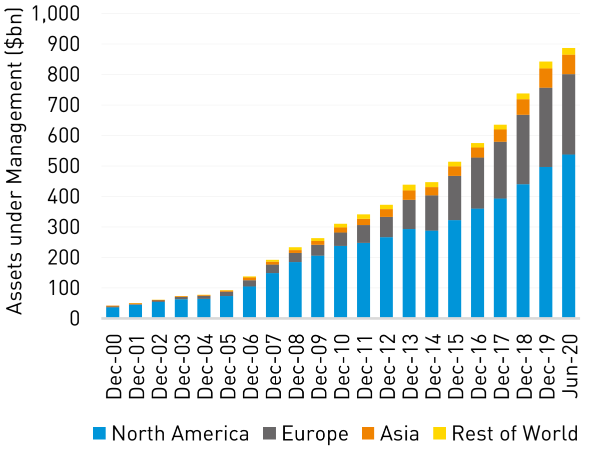
[1] https://voxeu.org/article/debt-restructuring-time-covid-19

Fig. 2.2: Private Debt Assets under Management, 2000 - 2020



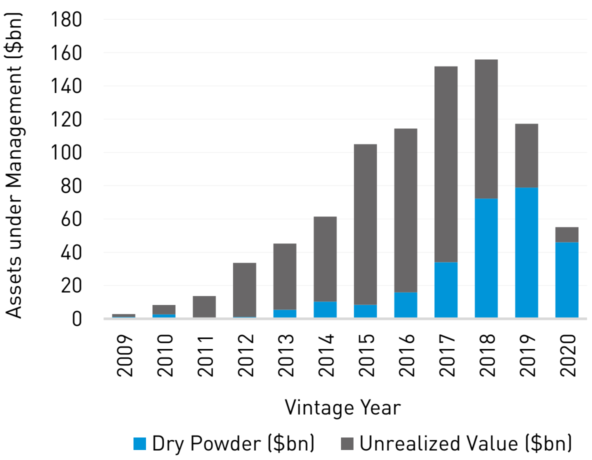
Source: Preqin Pro

Fig. 2.3: Private Debt Assets under Management by Geographic Focus, 2000 - 2020



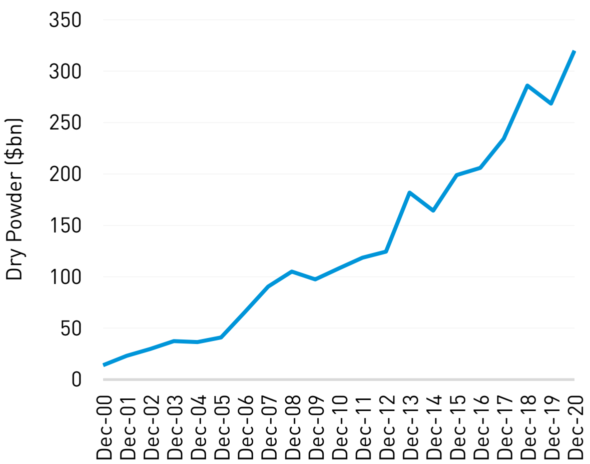
Source: Preqin Pro

Fig. 2.4: Private Debt Assets under Management by Vintage Year



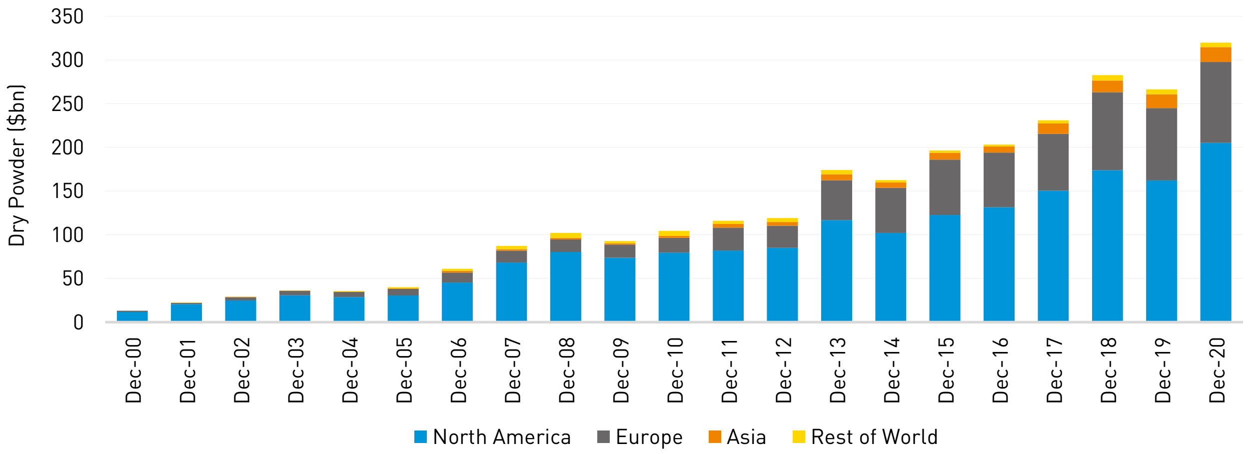
Source: Preqin Pro. Data as of June 2020

Fig. 2.5: Private Debt Dry Powder, 2000 - 2020



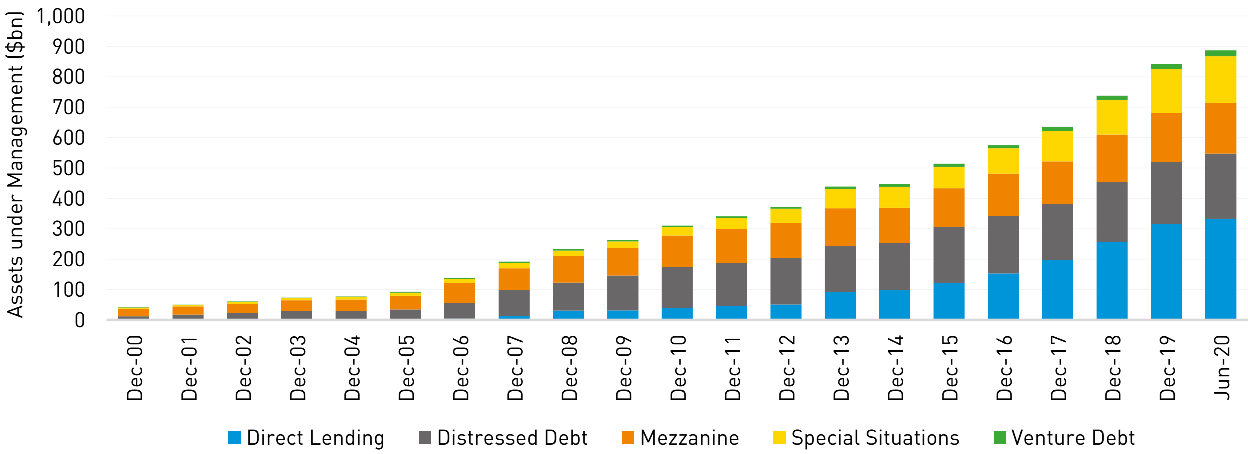
Source: Preqin Pro

Fig. 2.6: Private Debt Dry Powder by Geographic Focus, 2000 - 2020



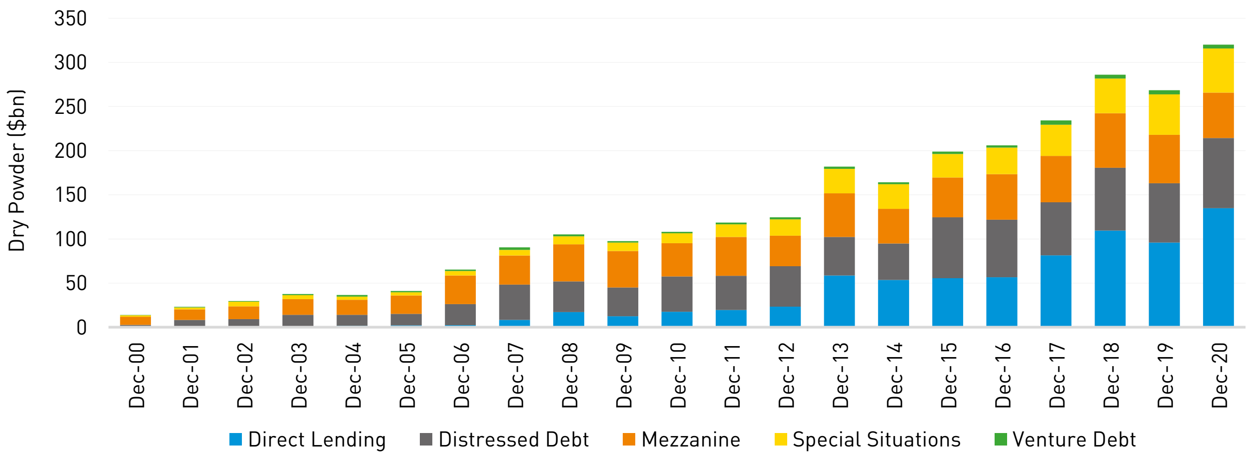
Source: Preqin Pro

Fig. 2.7: Private Debt Assets under Management by Fund Type, 2000 - 2020



Source: Preqin Pro

Fig. 2.8: Private Debt Dry Powder by Fund Type, 2000 - 2020

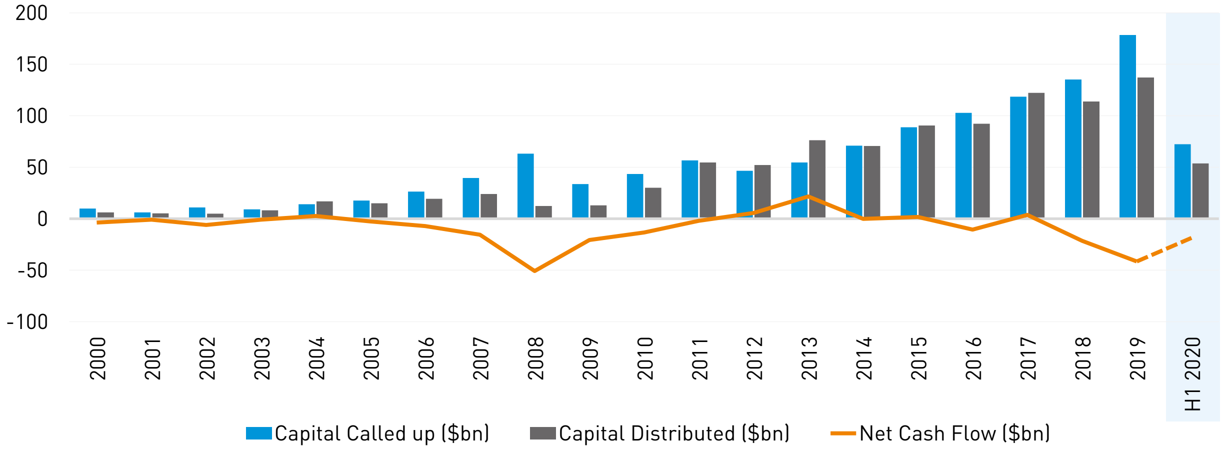


Source: Preqin Pro

Capital Calls and Distributions

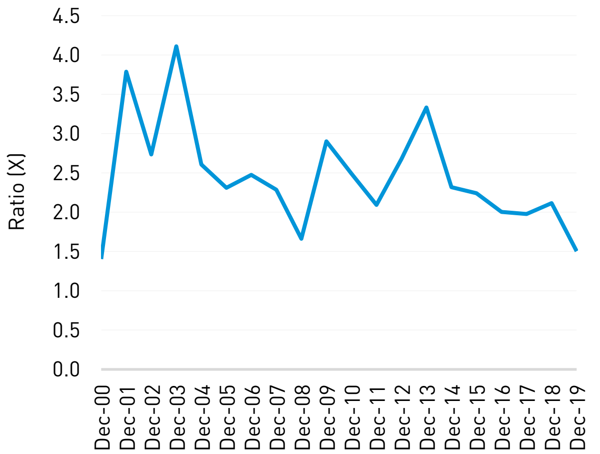
The ratio of year-end dry powder to annual capital called continues to fall, as managers seek out opportunities in private debt

Fig. 2.9: Private Debt: Annual Capital Called up, Distributed, and Net Cash Flow, 2000 - H1 2020



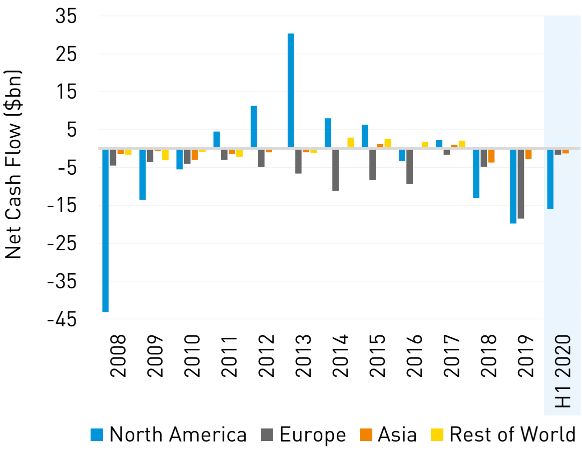
Source: Preqin Pro

Fig. 2.10: Private Debt: Ratio of Year-End Dry Powder to Annual Capital Called, 2000 - 2019



Source: Preqin Pro

Fig. 2.11: Private Debt: Net Cash Flow by Region, 2008 - H1 2020



Source: Preqin Pro

In Focus: Distressed Debt Looks Different Now

Spawned by the pandemic, distressed debt harks back to the GFC, but crowded markets and low yields mean it will not be the same this time

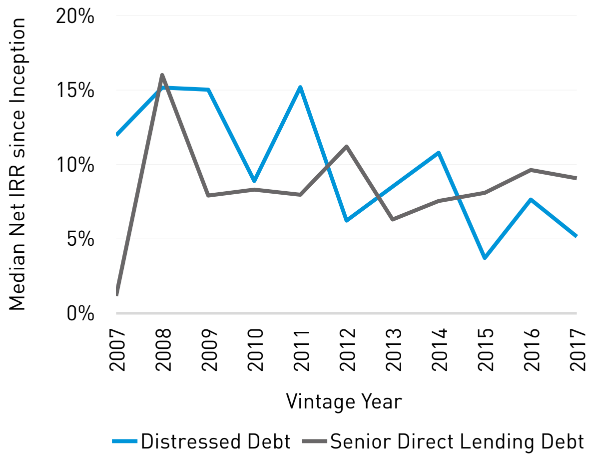
The pandemic put a freeze on much of the global economy in 2020, driving a large influx of capital and interest in distressed debt. As such, credit spreads (or corporate lending rates relative to the 10-year Treasury) rose to recessionary levels, particularly at the riskier end of the credit spectrum. Previously healthy borrowers found themselves in dire straits virtually overnight amid an already historic level of speculative, or high-risk, credit.

This apparent new stage of the credit cycle harks back to the GFC, which saw a spike in spreads, defaults, and downgrades. Last year, speculative-grade credit spreads were stretched their furthest since the darkest days of 2008. Average yields on debt rated BB and lower maxed out at 13.3% over 10-year US Treasuries (Fig. 2.13).[1] That is half of what we saw during the GFC – indicating how government and central bank interventions have played a significant role in stabilizing both markets and the broader economy.

Using the public market as proxy, distressed debt funds did indeed do well in the years following the GFC, outperforming their peer sub-strategies in most vintages. Distressed debt fund vintages 2008-2010 posted an average net IRR of 13.5% annualized over five- to seven-year fund lives – more than a full percentage point over the broader private debt asset class (Fig. 2.12).

The dispersion of those funds, however, was higher than for peer strategies; the standard deviation of distressed fund IRRs was more than double that of senior tranche direct lending and mezzanine funds.

Fig. 2.12: Median Net IRRs by Vintage Year: Distressed Debt vs. Senior Direct Lending Debt



Source: Preqin Pro. Most Up-to-Date Data

So, while the group as a whole performed well, the probability of picking a winner was smaller.

Given the riskier nature of distressed debt, this is not much of a surprise. High-risk profiles become more evident in a crisis, and opportunities may only be fleeting; windows close fast, if they open at all. Distressed funds may have performed well compared to their peers in the years immediately following the GFC, but they failed to keep up in the boom years characterized by low interest rates and ever-rising corporate debt. While the macro environment slowed the distressed market during this period, the overall quality of debt declined in that same period. Bonds rated BBB (a lower quality of investment-grade debt)

[1] *https://fred.stlouisfed.org/*

became a large piece of the debt puzzle, and below-investment-grade debt also swelled.

Will History Repeat, Rhyme, or Chart a New Path?

There are certainly parallels between 2008 and 2020. The years following the GFC saw an unprecedented rise in low-grade corporate debt, as relatively low interest rates, while still above that of Treasuries, provided easy money for borrowers and much-needed higher yields for investors. And data from S&P[2] shows more than 1,800 speculative-grade issuers were active at the end of 2019, of which more than one-quarter were rated B- or lower.

This debt boom in the wake of the GFC, accompanied by an overall degradation of debt quality, made fertile ground for private debt by proxy. Indeed, in 2020 more than $69bn in distressed debt funds were launched, the highest amount of any vintage, according to Preqin data. That surge of interest, no doubt spurred by the financial fallout of the pandemic, reflects the expanded opportunity available to those private credit managers willing to pick through the rubble.

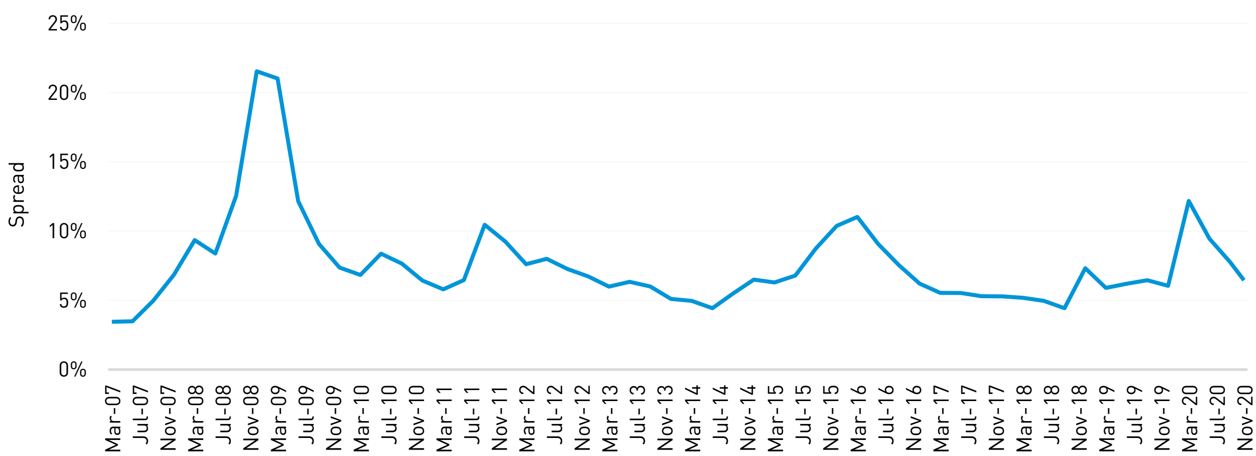
The good news is that the debris is far more diversified than in 2008. Back then, the bulk of the speculative-grade credit rated B- and below was in the telecoms, consumer, and energy sectors, with the rest lagging, according to S&P. This time around, that group, while much larger in dollars, is more evenly distributed and technology-heavy.
However, significant headwinds exist for those hoping to find diamonds in the rough. This crisis may have fundamentally changed the global way of life. Retail and energy experienced the highest number of defaults by late April, according to S&P. In the months following, oil prices held steady after turning negative for a short period, driven by a rare convergence of market dynamics, and have subsequently broken through the $50 per barrel mark, while brick-and-mortar retailers have faced an adapt-or-die scenario in the face of heightened competition and structural challenges. These industries are only the most obvious examples of the honeycombed nature of distressed credit's opportunity set.

Distressed debt is also facing the problem of a crowded house. With so much capital now in the market fighting for deals, expected returns should be more muted than they were following the GFC. Deal-sourcing for many managers, particularly those mega funds raised to target these opportunities, could also become an issue.

Distressed debt thrives in chaos. The high credit spreads induced by the pandemic were brief due to government intervention, but that intervention will ultimately be finite. It is possible that this impermanence will give distressed credit a second wind, at the expense of the companies at the heart of their deals. Given that the root cause of today's situation is a health issue, rather than a financial one, any road out of it will need to prioritize day-to-day life returning to something resembling normality.

[2] *https://www.spglobal.com/ratings/en/research/articles/191002-default-transition-and-recovery-a-double-digit-u-s-default-rate-could-be-on-the-horizon-11165582*

Fig. 2.13: Average Monthly Spread: Debt Rated BB, CCC, and Below



Source: Federal Reserve Bank of St. Louis


ACTIVE THINKING®

3

Fundraising

Why Private Credit Managers with a Dose of Paranoia Can Thrive

COVID-19 has sent many countries into a recession, with more defaults and financial restructurings the likely outcome. Against this background, attention has turned to the challenges facing private credit managers

Frédéric Nadal
Managing Partner, Chief Executive Officer

MV Credit
www.im.natixis.com/mv-credit

Private credit is in a different space compared to during the GFC. It has moved from being specialist and niche to a more established component of a diversified investment portfolio, with greater commitments to private corporate credit, greater AUM, and more opportunities for direct lenders and other non-bank institutional investors.

Which strategies within the private debt landscape will be the most robust as we come out of the current downturn, and how can private credit managers find opportunities to mitigate risks?

Credit Selection Is Critical for Downside Protection

We think managers should adopt an approach of 'healthy paranoia' at all times and ensure selectivity and caution when originating opportunities.

Some industries prove more resilient over credit cycles. For example, healthcare and subscription-based services generally prove more stable than highly cyclical industries, such as fashion retail, automotive, and leisure and travel. A key lesson we learned from investing during the GFC was to avoid industries such as household durables, which are correlated to economic cycles and are less able to sustain the leveraged structures deployed by private equity sponsors in a downturn.

We also learned to avoid businesses in the paper and forest products industry, where exposure to raw material price pressure can have a negative impact on company performance. In comparison, we have never experienced a loss on a company in the healthcare or information technology sectors which are less cyclical in nature.

Additionally, we target upper mid-cap companies which typically have lower credit risk. Smaller companies are usually more local or regional in nature and can have revenue streams more reliant on a single geography or product. Higher revenue diversification and larger scale make borrowers less sensitive to external shocks. This would suggest that strategies targeting smaller borrowers may be less resilient during a downtown. Private credit managers with strong monitoring processes can usually spot when a borrower company is underperforming by looking out for early warning signals. MV Credit, for instance, has a dedicated and impartial credit monitoring team that systematically reviews and monitors each investment alongside the deal team. This ensures that troubled credits can be proactively addressed early.

Founded in 2000, **MV Credit** is one of the first private credit firms to be established in Europe and has the longest-established management team in the private credit space. It invests in senior and subordinated debt across Europe, targeting noncyclical, defensive industries and regions where it has a deep understanding. It offers tailored financing solutions to high-quality businesses and adds value through active engagement. Over the years, MV Credit funds have invested more than €5bn in debt financing solutions and have delivered a consistent top-quartile track record. MV Credit funds invest in the debt tranches of companies undergoing leveraged buyouts or refinancing supported by reputable European private equity owners.

The Advantages of Private Equity Ownership

Private credit managers can seek to increase downside protection by investing in companies sponsored by private equity. Why? First, sponsors can be relied on to manage borrower companies and may be preferable to family-owned businesses, particularly in a stressed environment.

Second, private equity sponsors are typically able to reinforce or change a management team in difficult times. We believe this option is less likely in a family-owned business where the owners and management are sometimes the same person or related.

The support of private equity sponsors can be crucial in achieving a recovery on an underperforming business. We saw examples of this during the GFC, where some sponsors injected new equity and even undertook debt buybacks to reduce companies' leverage.

The Pitfalls of Distressed Credit

As investors seek attractive opportunities during this period of market turbulence, they may look to opportunistic strategies such as distressed credit. However, we believe that distressed lending has limitations.

Following the last downturn, for instance, private equity sponsors have tightened documentation on loan transfers, which has limited the opportunities available to distressed funds. Additionally, distressed buyers typically invest in more cyclical industries such as hospitality, retail, and automotive. We believe that the COVID-19 crisis may dramatically change the business models of such industries, potentially over the long term.

Distressed lending may create a conflict for ESG-conscious investors. For example, it creates additional pressure and instability on management teams and longer-term 'par' stakeholders during restructuring processes. Investors may be conflicted with the methods used when extracting value from failing companies.

Finally, subordinated credit funds outperformed distressed credit funds 60% of the time between 2003 and 2017, and their returns were less volatile. Distressed credit is a highly opportunistic asset class and tends to offer less favorable risk-adjusted returns compared to subordinated credit, apart from the odd vintage.

Sourcing Attractive Opportunities

During a downturn, volume and issuance of loans initially decreases, but an experienced private credit manager can leverage existing relationships to create opportunities.

Take the secondary market: the average bid price for leveraged loans in the S&P European Leveraged Loan Index (ELLI) took a sharp nosedive in Q1 2020, falling to 78.92 in March 2020 before rebounding somewhat. However, we were able to commit to a number of high-quality investments at attractive yields on the secondary market. Experienced managers with a focused database of credits are in a particularly strong position, as they have tracked some companies for years.

Then there are primary market opportunities. Private credit managers with a reputation for being reliable and constructive during the credit structuring process are still able to originate attractive investments. Also important are strong relationships with private equity sponsors.

Looking Ahead: A Reset Credit Cycle

Following a downturn, the credit cycle typically enters a period of repair and recovery. The post-GFC period was marked by better economics which drove attractive returns for private credit, with 2008 vintages notable for their high performance. We believe that 2020/2021 vintages will behave similarly.

Coming out of the downturn, we expect the strongest credits to come to market first, with portfolios that invest in cyclical industries struggling. Lenders may gain more information rights and other documentation rights (such as reducing cash leakage). ESG will likely remain an important consideration.

We believe this is a particularly attractive time to invest in private credit to secure attractive risk-adjusted returns. The best managers can draw on significant investment experience across multiple cycles and aim to build and proactively manage resilient portfolios.

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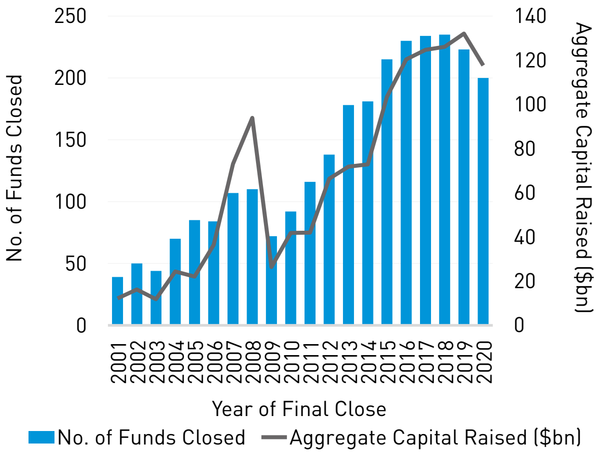
Fundraising Stable during Pandemic

While total figures have remained on trend, capital concentration is intensifying

Fundraising in private debt remained robust over 2020, in spite of coronavirus and its effects; 200 private debt funds reached a final close, raising an aggregate $118bn, down from the $132bn raised in 2019 (Fig. 3.1). In recent years, many companies have issued debt in order to take advantage of low borrowing costs[1], an additional leverage that left them vulnerable to disruptions caused by the pandemic. Resultant short-term dislocations have created more opportunities for private debt specialists to offer innovative financing solutions. And while expertise exists across the private debt space, large proportions of capital raised have been directed toward specific regions, strategies, and fund managers.

The majority of capital raised by private debt funds in 2020 is focused on North America. Funds targeting the region accounted for 63% of total capital raised (a 12 percentage-point increase on 2019, Fig. 3.6). This is, in part, driven by the yield spread over 10-year Treasury bonds. For many sectors in the region, and for investment-grade issues, yield premiums can be more than 150bps· making these investments attractive on a relative basis.[2]

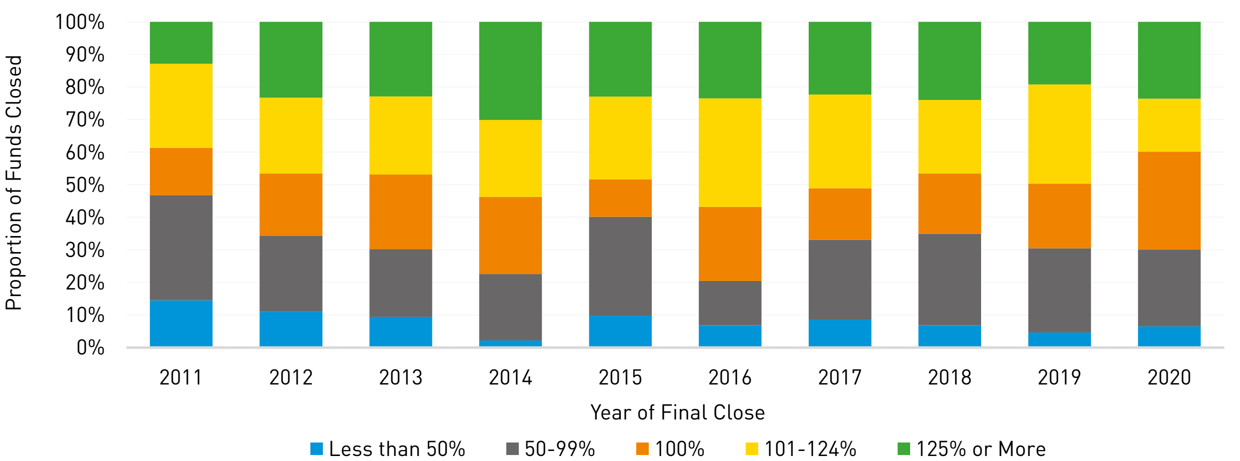
Fig. 3.1: Global Private Debt Fundraising, 2001 - 2020



Source: Preqin Pro

[1] *https://www.ft.com/content/29a4d5fc-64c9-4ad5-b91f-37c821af33fe*
[2] *Data from FactSet*

Fig. 3.2: Private Debt Funds Closed by Proportion of Target Size Achieved, 2011 - 2020



Source: Preqin Pro

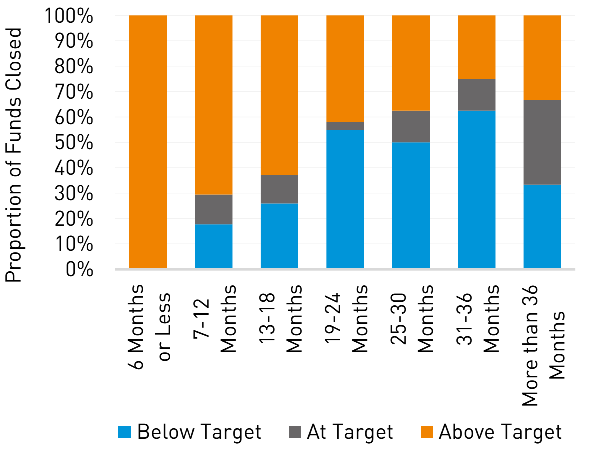
Mezzanine and special situations funds attracted an increased share of capital raised last year; mezzanine funds' share grew from only 7% in 2019 to 22% in 2020 (Fig. 3.9). The bulk of this capital came from HPS Mezzanine Partners 2019, managed by New York-based HPS Investment Partners, the third-largest mezzanine fund ever closed, at $9bn. With the pandemic triggering a wave of billion-dollar bankruptcies, the closure of mega funds such as this one is the latest indication that large-scale funds are still able to attract significant commitments.[3]

Special situations may have been boosted by the pandemic, which has caused dislocation for businesses, but direct lending funds still dominated private debt fundraising. The strategy accounted for 43% of aggregate capital raised in 2020, suggesting many investors are positioning themselves defensively.

Another result of the pandemic is compounded capital consolidation. Larger funds have become even more prevalent in the private debt space, and the 10 largest funds accounted for 39% of the capital raised in 2020, up from 31% in 2019 (Fig. 3.7). At the other end of the scale, funds outside of the top 50 constituted only 21% of aggregate capital raised, a fall of four percentage points on the previous year. A recent rush of inflows from large investors, such as Middle Eastern

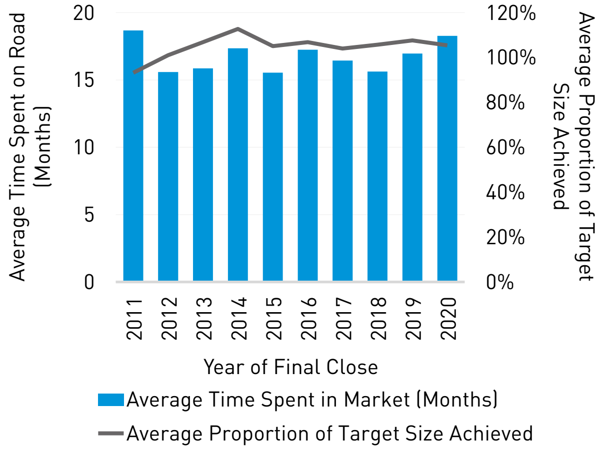
[3] *https://www.ft.com/content/277dc354-a870-4160-9117-b5b0dece5360*

Fig. 3.3: Private Debt Fundraising Success by Time Spent in Market, Funds Closed in 2019-2020



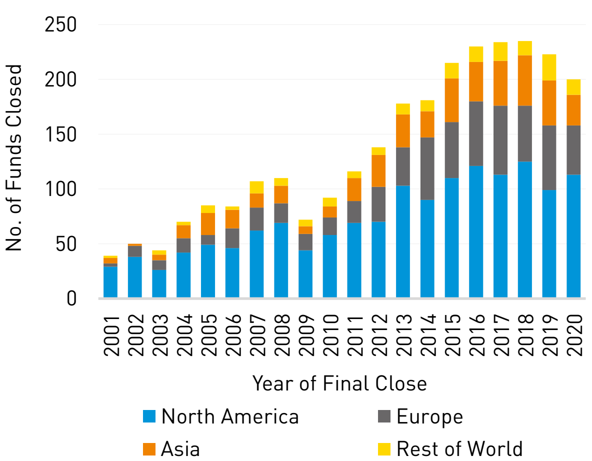
Source: Preqin Pro

Fig. 3.4: Private Debt Fundraising Success, 2011 - 2020



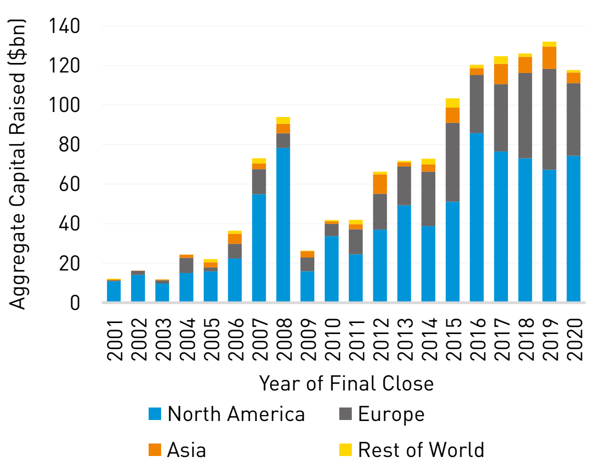
Source: Preqin Pro

Fig. 3.5: Number of Private Debt Funds Closed by Primary Geographic Focus, 2001 - 2020



Source: Preqin Pro

Fig. 3.6: Aggregate Capital Raised by Private Debt Funds Closed by Primary Geographic Focus, 2001 - 2020



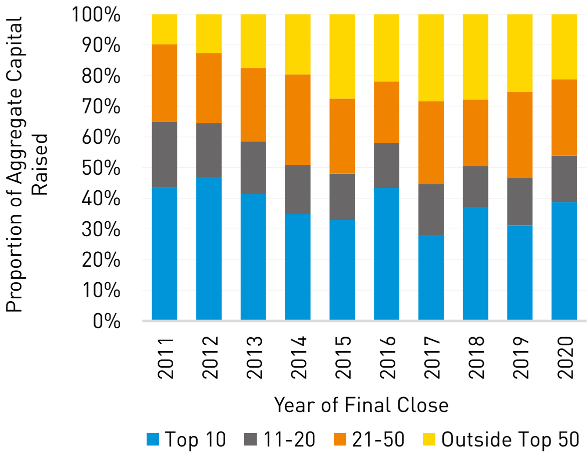
Source: Preqin Pro

sovereign wealth funds (SWFs), has led to larger, more experienced fund managers receiving a greater proportion of capital.[4]

Private debt is well positioned to ride out the effects of COVID-19. Fund managers hold unique expertise relative to banks, and those with the necessary skillset to identify targets and manage risk and liquidity constraints with the right type of capital (i.e., committed, longer-duration capital) could benefit further from pricing inefficiencies that may emerge. Many firms will require innovative and flexible financing solutions to guide them through the economic disruption. With banks unlikely to rise to the challenge, investors recognize that private debt funds will be a vital source of liquidity in the months and years ahead.

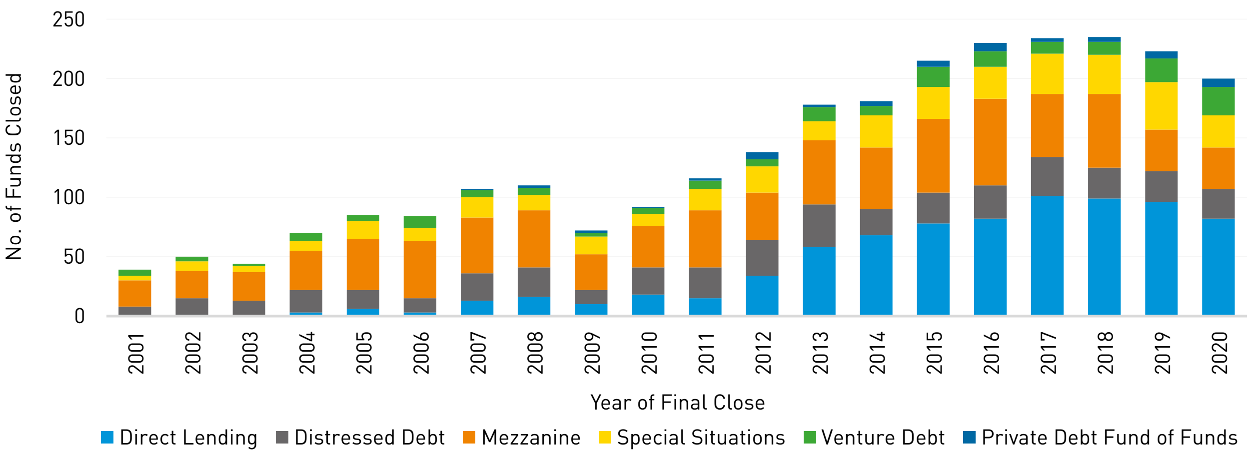
[4] *https://www.ft.com/content/6a05c195-1918-4a92-8b27-4ae24f8a70a8*

Fig. 3.7: Proportion of Aggregate Capital Raised by the Largest Private Debt Funds Closed, 2011 - 2020



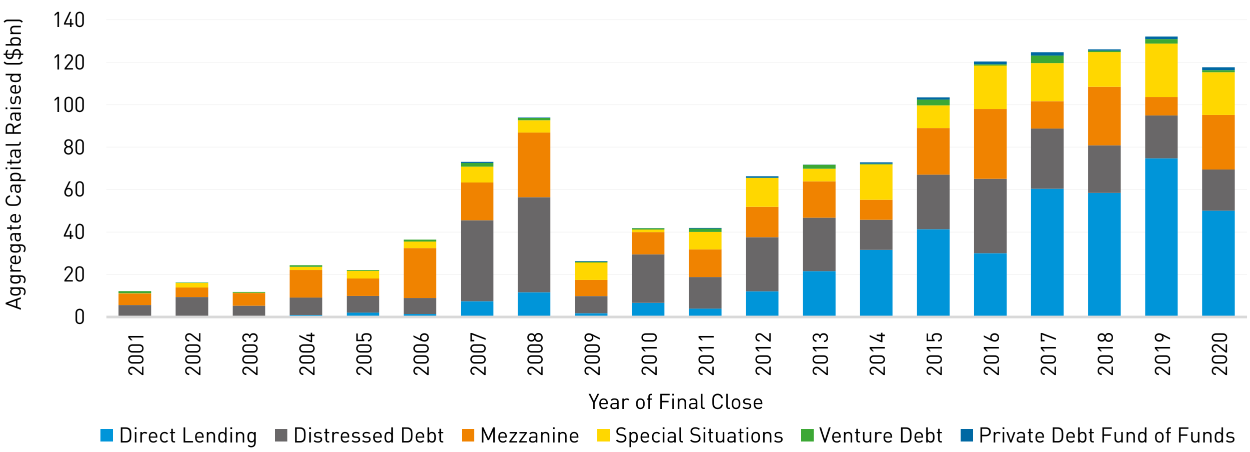
Source: Preqin Pro

Fig. 3.8: Number of Private Debt Funds Closed by Type, 2001 - 2020



Source: Preqin Pro

Fig. 3.9: Aggregate Capital Raised by Private Debt Funds Closed by Type, 2001 - 2020



Source: Preqin Pro

Funds Target Record Levels of Capital

Managers meet a surge in demand at the start of 2021

Private debt fund managers are seeking record amounts of capital in response to the uptick in demand for yield-driving allocations. As of January 2021, there are 547 private debt funds in market; these vehicles are seeking an aggregate $290bn in capital, a 51% increase on the previous year (Fig. 3.10). At the current stage of the credit cycle, managers believe private debt assets can deliver favorable returns. Given that the asset class is also taking over a large share of traditional bank funding, due to regulatory constraints and a need for banks to improve capital ratios, further growth appears inevitable.

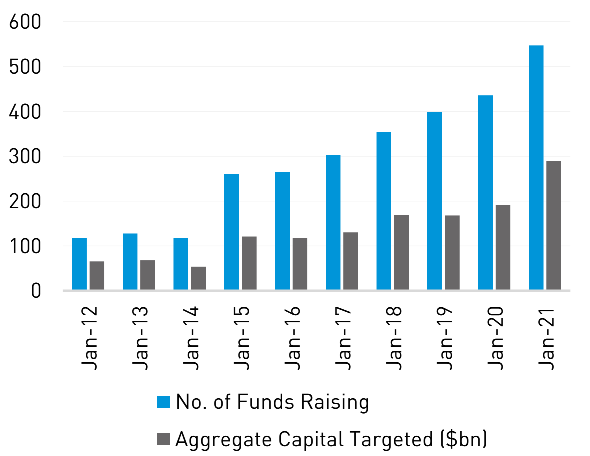
The number of special situations funds in market has risen sharply: at the start of this year there were 79 on the road, a 464% increase on January 2020 (Fig. 3.11). This strategy now accounts for 14% of private debt funds in market, although direct lending funds still dominate, accounting for almost half of all private debt funds.

As many private debt investors move up the risk curve in search of higher returns, demand for distressed strategies is increasing. Amid widespread pandemic-induced financial difficulties for SMEs, the pipeline of opportunities in the space is expected to reach a scale not seen since the GFC.[1] The largest fund operating in this market – Oaktree Opportunities Fund XI, managed by California-based Oaktree Capital Management – is targeting $15bn in capital; hitting this target will make it the largest distressed debt fund in history.

North America-focused funds such as this continue

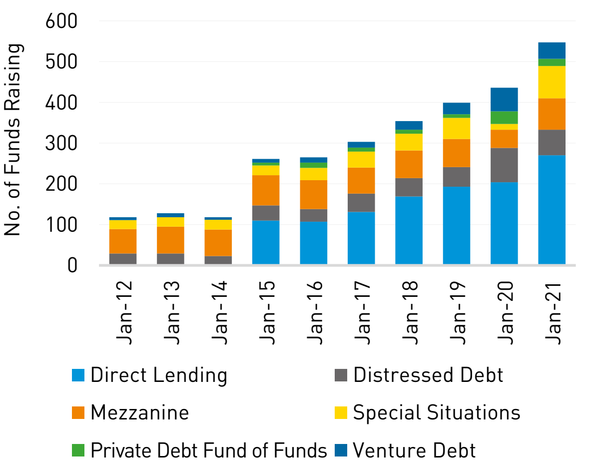
[1] https://www.ft.com/content/ca5fbc8a-61da-4585-9ca4-092255189497

Fig. 3.10: Private Debt Funds in Market, 2012 - 2021



Source: Preqin Pro

Fig. 3.11: Private Debt Funds in Market by Type, 2012 - 2021



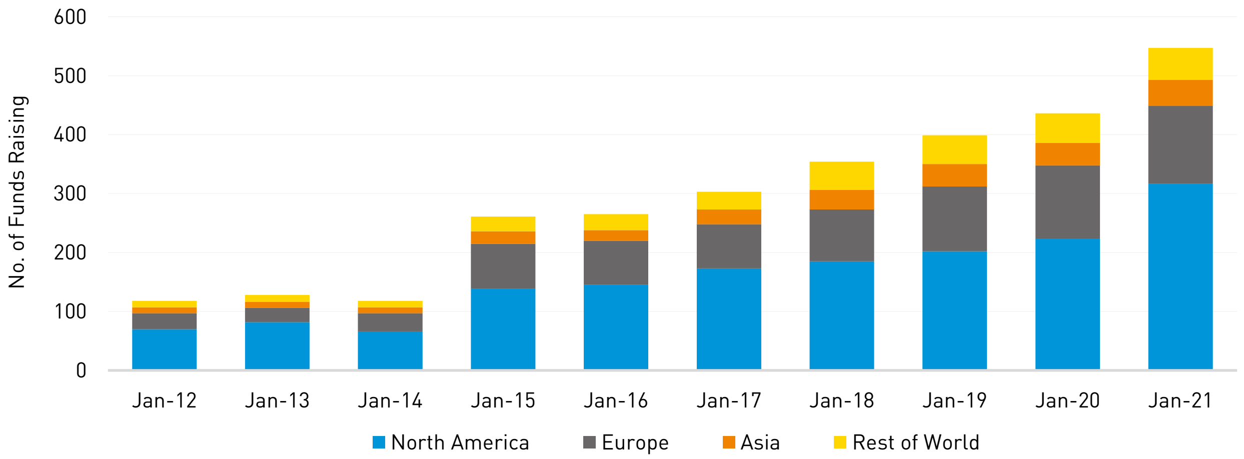
Source: Preqin Pro

to account for more than half of the private debt landscape, up from 51% in January 2020 to 58% in January 2021 (Fig. 3.12). US corporate bond issuance hit $1.92tn over 2020[2], smashing previous full-year records, and the Treasury bond yield spread continued to widen toward the back-end of the year[3], making the region an attractive prospect for yield-hungry investors.

Private debt's star had already been rising prior to the pandemic, but COVID-19 has sent it higher. Highlighting the sheer scale at which investors have flocked to the asset class in search of stability and strong returns, the ratio of capital targeted to prior-year capital raised increased from 1.45x in 2020 to 2.46x in 2021 (Fig. 3.13). We expect this ongoing shift to private markets to continue, as banks tighten credit risk management and investors maintain their search for yield.

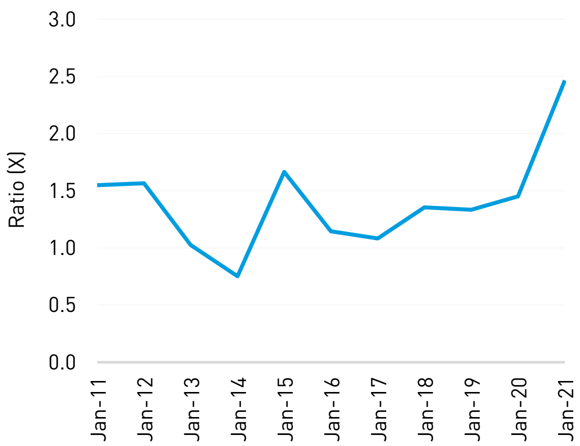
2 https://www.ft.com/content/a59c2a9d-5e0b-4cbc-b69e-a138de76a776
3 https://uk.reuters.com/article/usa-bonds/treasuries-yield-curve-steepest-since-june-as-u-s-stocks-sell-off-idUSL1N2HL2AL

Fig. 3.12: Number of Private Debt Funds in Market by Primary Geographic Focus, 2012 - 2021



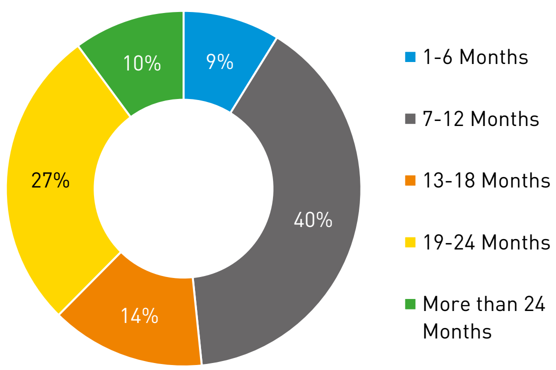
Source: Preqin Pro

Fig. 3.13: Private Debt: Ratio of Aggregate Capital Targeted to Prior-Year Capital Raised, 2011 - 2021



Source: Preqin Pro

Fig. 3.14: Private Debt Funds in Market by Time Spent on the Road



Source: Preqin Pro

4

Fund Managers

Fund Managers Flock to Private Debt

A record number of fund managers are active in the private debt space, with a notable uptick in distressed debt and special situations funds

The pandemic has left many companies facing financial difficulties, opening up intervention opportunities for fund managers active in distressed strategies. But with a record 1,947 private debt firms currently active, the market for both firms and funds is increasingly crowded.

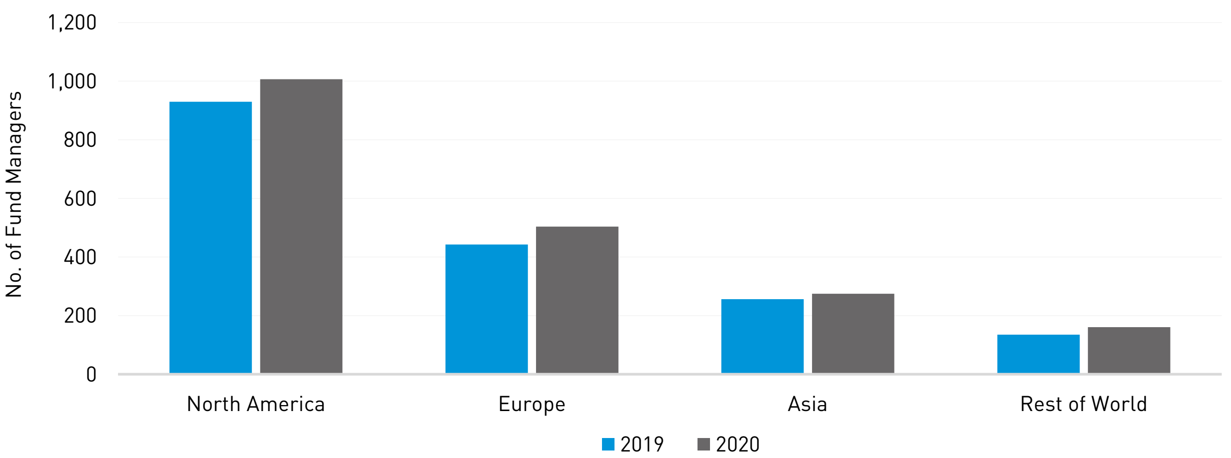
The proportion of private debt managers active in distressed debt and special situations markets grew considerably in 2020; distressed debt fund managers accounted for 17% of the market, up five percentage points on 2019, and the proportion of managers active in special situations rose by four percentage points, to 19%. These shifts suggest firms sense an opportunity to fund post-pandemic corporate restructuring. However, fund managers active in direct lending still dominated, with 30% of market share.

The number of fund managers active in Europe is creeping up – from 443 in 2019 to 504 in 2020 – although the largest share are still based in North America (Fig. 4.1). The region is attractive to global investors, whose evolving needs are not being met by public markets, according to M&G Investments.[1] This is largely down to the increasing levels of sophistication, depth, and flexibility in European private markets.

Record AUM and numbers of funds in market reflect an increase in the number of players in the private debt space, and there are concerns that the market is becoming frothy, with too much capital chasing too few deals. As more firms enter the space, managers could succumb to the pressure by agreeing to weaker loan terms, leading to a deterioration in credit quality and, ultimately, returns. In order to circumvent these

[1] *https://www.mandg.co.uk/institutions/articles/european-private-debt-shifting-dynamics/-/media/6FC6C90A27B04CF396F7D3A8387EB7F6.pdf*

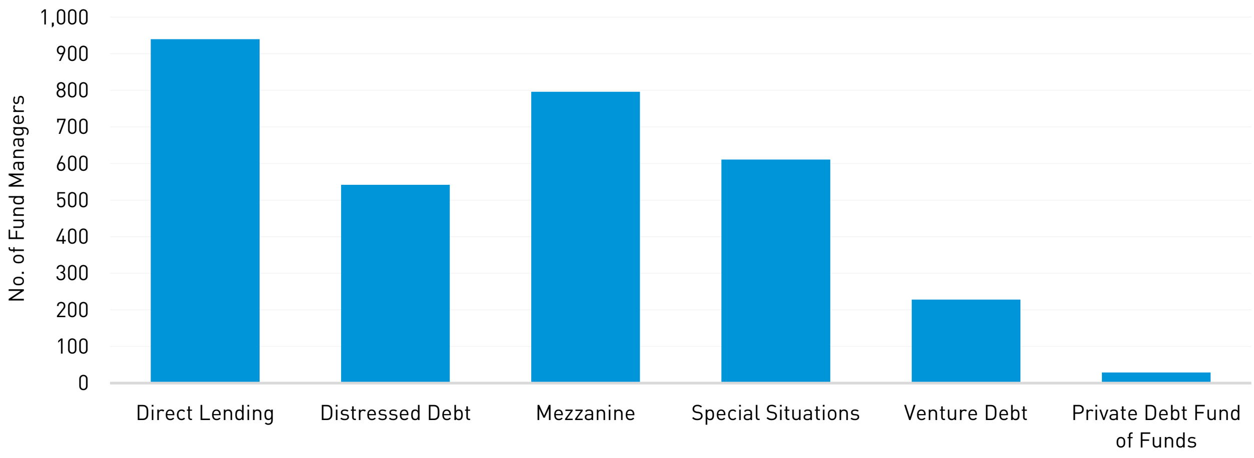
Fig. 4.1: Active Private Debt Fund Managers by Location, 2019 vs. 2020



Source: Preqin Pro

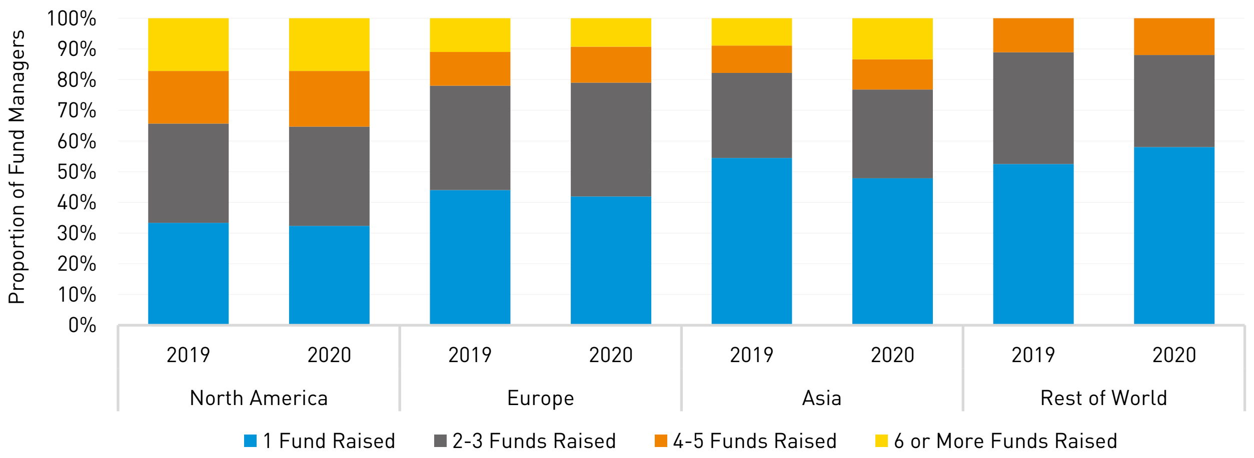
challenges, managers may seek opportunities in emerging markets, where competition is less of an issue. The downside to this would be a potential move into unfamiliar markets, where risks are higher.

Fig. 4.2: Active Private Debt Fund Managers by Fund Type



Source: Preqin Pro

Fig. 4.3: Active Private Debt Fund Managers by Manager Experience and Location, 2019 vs. 2020



Source: Preqin Pro

Manager Experience Key for Investors

First-time managers have struggled in a difficult fundraising environment as investors favor more established counterparts

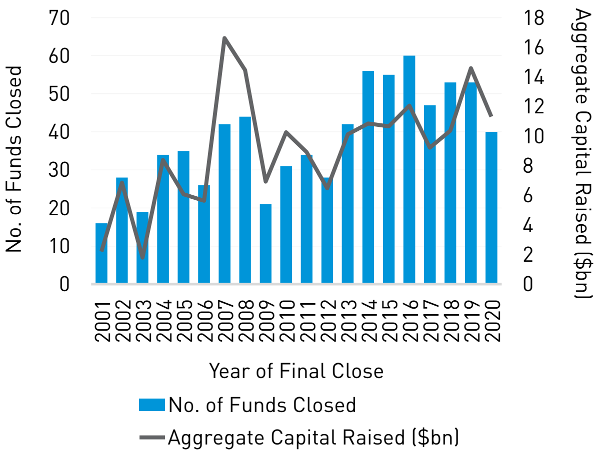
Although private debt as a whole fared relatively well during the economic instability of 2020, first-time fund managers had a harder ride. The proportion of capital raised by first-time funds as a share of total private debt fundraising declined, as investors turned to more experienced managers to guide them through the pandemic-induced turbulence. This, combined with the difficulty of cultivating new relationships, due to the near-impossibility of face-to-face meetings, led first-time fund managers to record a smaller share of fundraising, but average fund sizes have increased.

Aggregate capital raised by first-time managers as a proportion of total capital raised has declined slightly compared with 2019, to just 10% (Fig. 4.8). The percentage of funds closed that were first-time funds was also down, by four percentage points, to 20%.

Despite this, the average size of first-time private debt funds grew to its highest-ever level. First-time funds secured an average of $333mn, up from $298mn in 2019, suggesting that more capital is being shared among fewer first-time managers (Fig. 4.5).

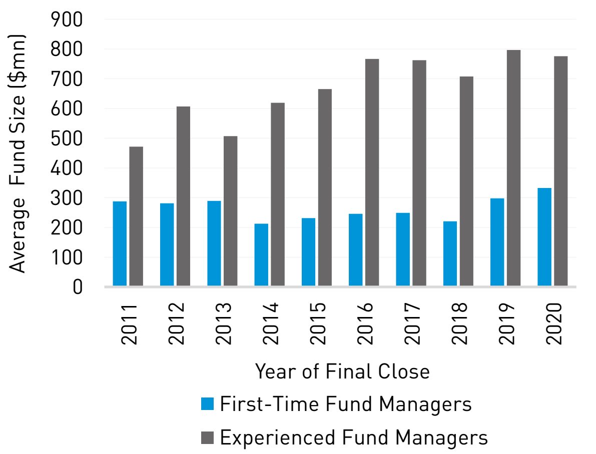
As competition continues to mount, it has become paramount for first-time fund managers to adequately differentiate themselves from their counterparts. But even if they can do that, success is far from guaranteed. Encouragingly, private debt activity in emerging markets is increasing. For instance, there are currently 44 funds in market focused on Asia, up from 38 at the beginning of 2020, and this trend is likely to continue accelerating. The private debt market is not as developed in Asia, and offers opportunities to managers – with or without a track record – particularly as this market is the most 'open' as we move into 2021.

Fig. 4.4: First-Time Private Debt Fundraising, 2001 - 2020



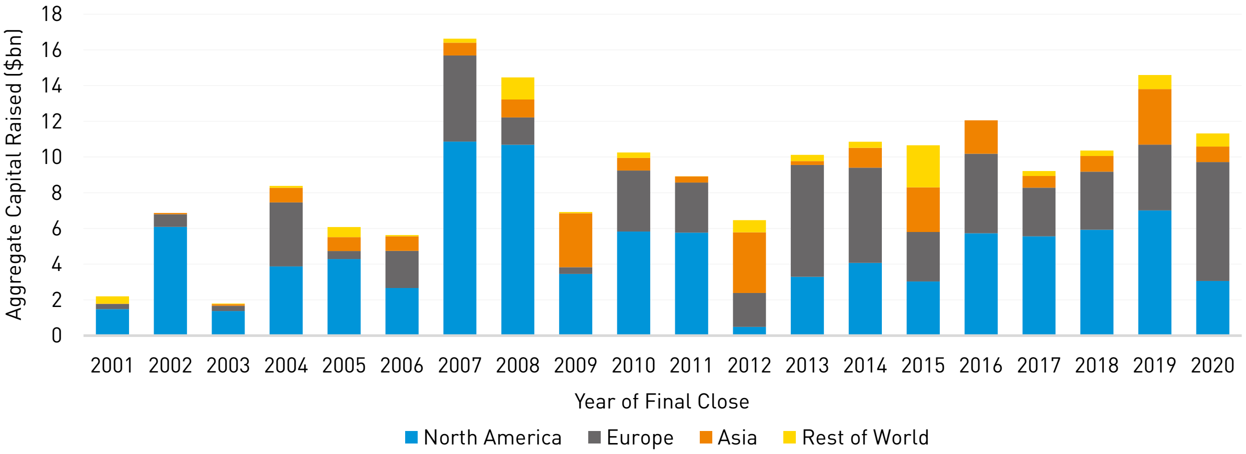
Source: Preqin Pro

Fig. 4.5: Average Private Debt Fund Size: First-Time vs. Experienced Fund Managers, 2011 - 2020



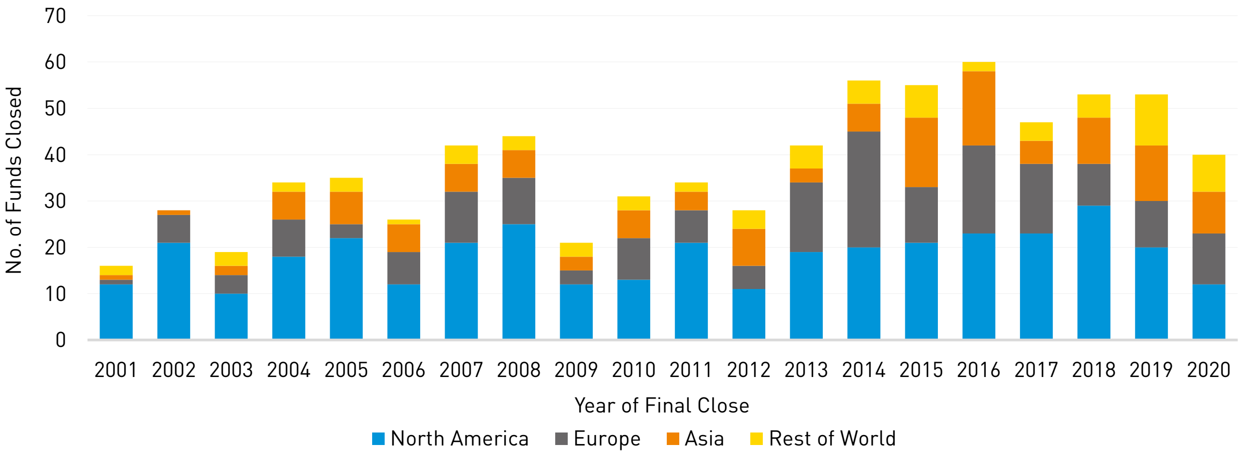
Source: Preqin Pro

Fig, 4.6: Aggregate Capital Raised by First-Time Private Debt Funds Closed by Geographic Focus, 2001 - 2020



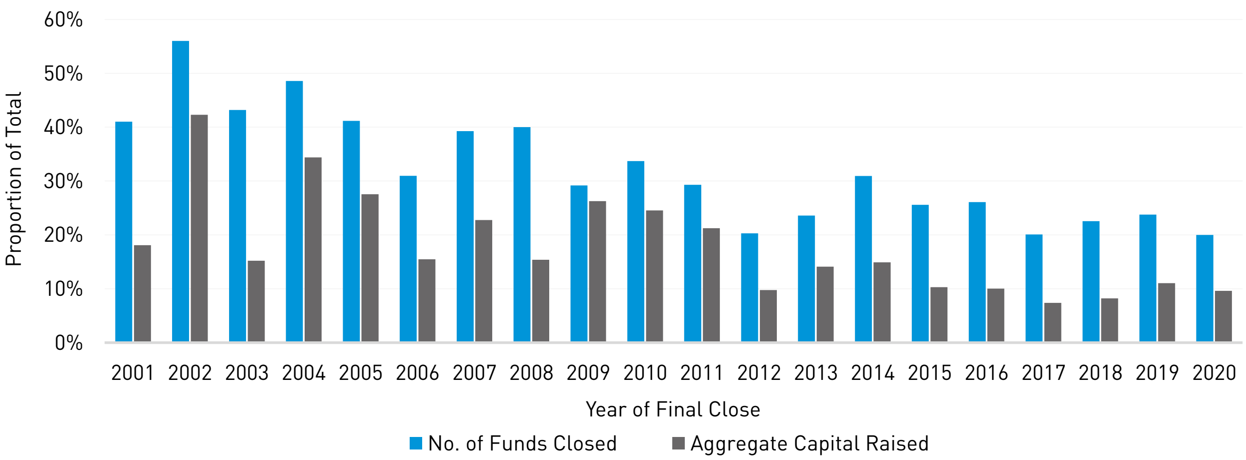
Source: Preqin Pro

Fig. 4.7: Number of First-Time Private Debt Funds Closed by Geographic Focus, 2001 - 2020



Source: Preqin Pro

Fig. 4.8: First-Time Private Debt Fundraising as a Proportion of Total Fundraising, 2001 - 2020

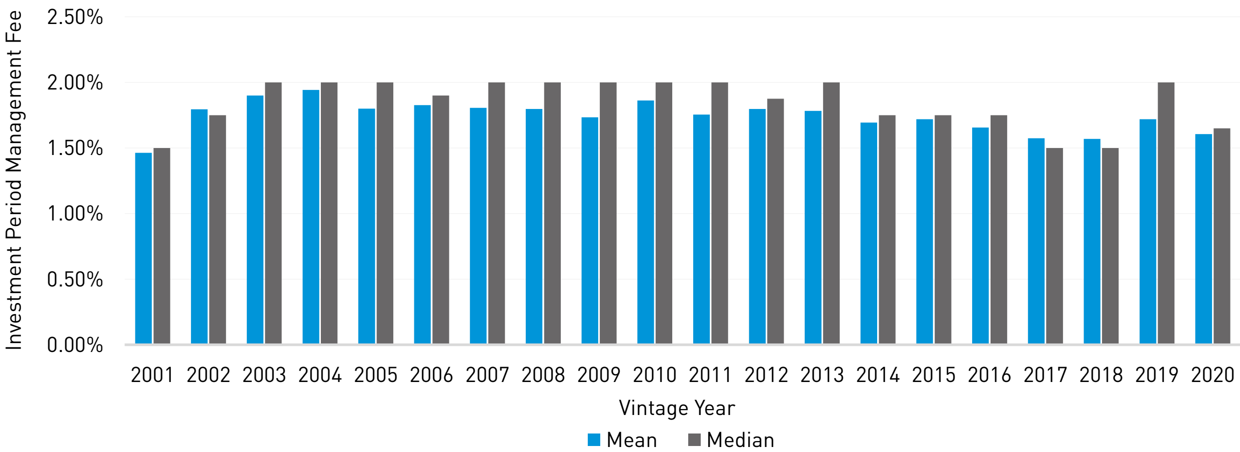


Source: Preqin Pro

Fund Terms & Conditions

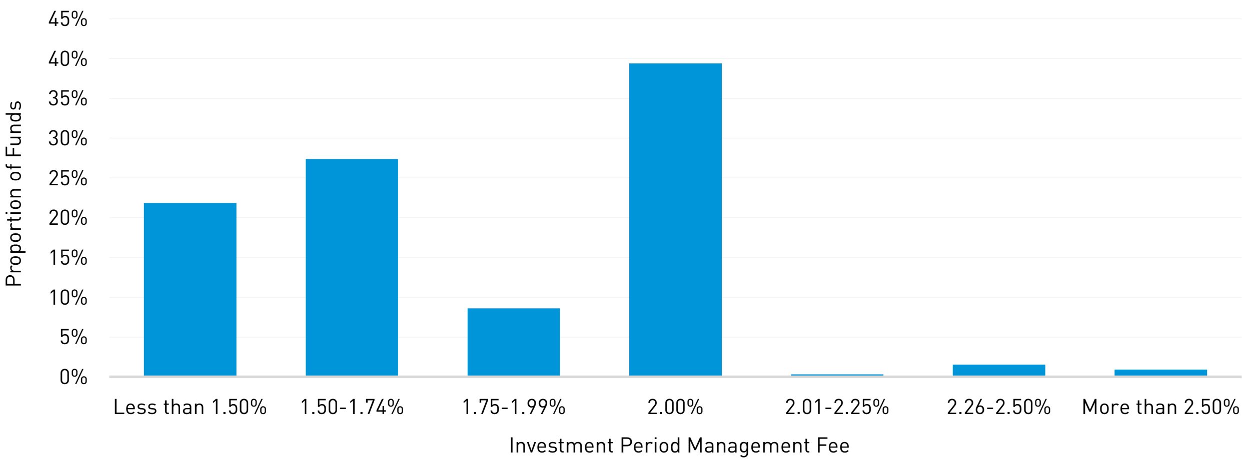
Mean management fees have fallen to their third-lowest level in the past 10 years as managers push to raise capital

Fig. 4.9: Average Management Fee Charged by Private Debt Funds by Vintage Year



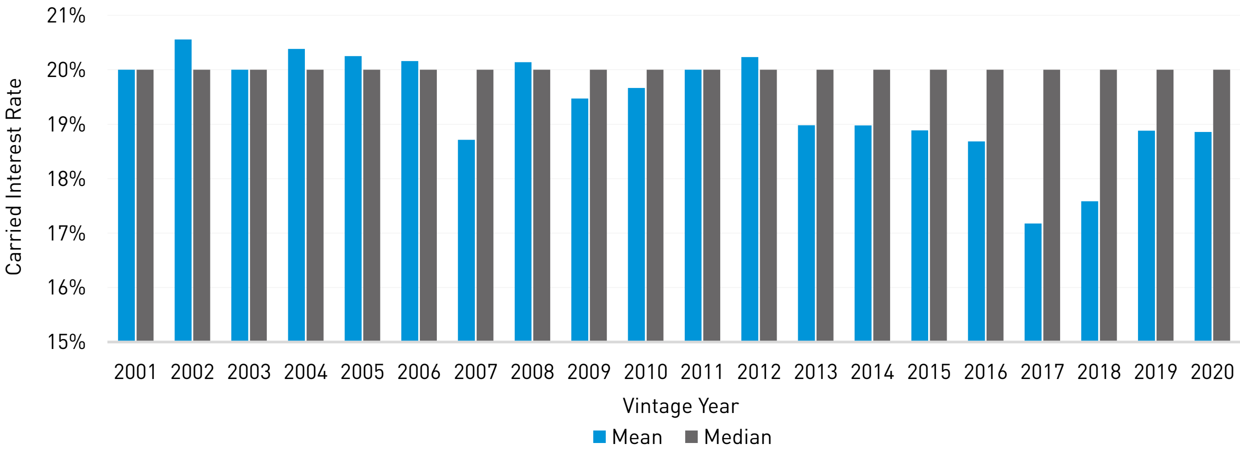
Source: Preqin Pro

Fig. 4.10: Management Fee Charged by Private Debt Funds (Vintages 2015-2020)



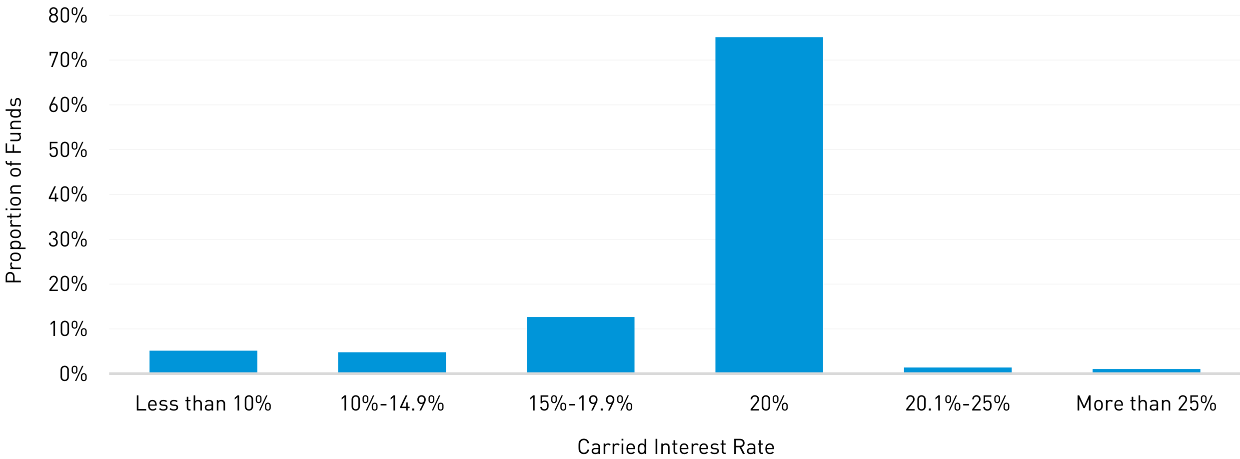
Source: Preqin Pro

Fig. 4.11: Average Carried Interest Rate Charged by Private Debt Funds by Vintage Year



Source: Preqin Pro

Fig. 4.12: Carried Interest Rates Charged by Private Debt Funds (Vintages 2015-2020)

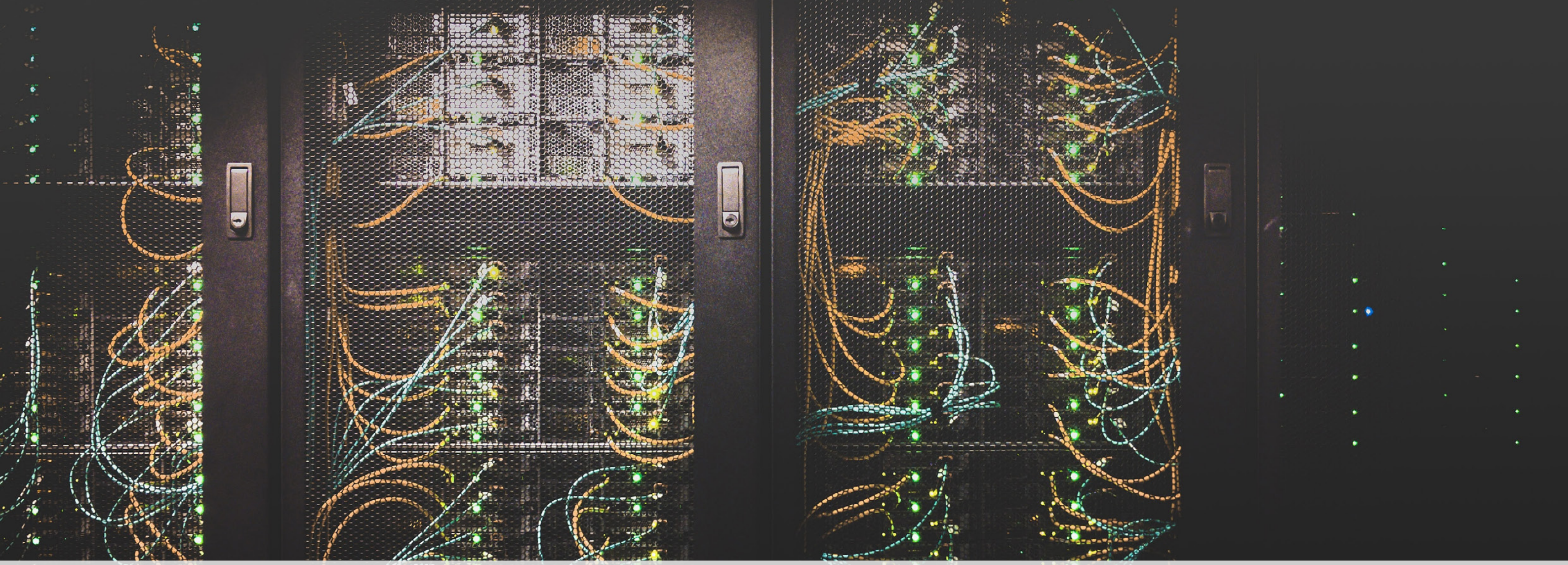


Source: Preqin Pro

Fig. 4.13: Median Management Fee and Carried Interest Rate Charged by Private Debt Funds by Type and Vintage Year

	Median Management Fee (%)				Median Carried Interest (%)			
Vintage	Direct Lending	Distressed Debt	Mezzanine	Special Situations	Direct Lending	Distressed Debt	Mezzanine	Special Situations
2015	1.75	1.75	1.88	2.00	20.0	20.0	20.0	20.0
2016	1.50	1.75	1.75	2.00	20.0	20.0	20.0	20.0
2017	1.50	1.88	2.00	1.50	16.3	20.0	20.0	20.0
2018	1.50	1.75	1.75	1.60	20.0	20.0	20.0	20.0
2019	1.88	1.75	2.00	2.00	20.0	20.0	20.0	20.0
2020	1.50	1.75	2.00	1.58	20.0	20.0	20.0	20.0

Source: Preqin Pro



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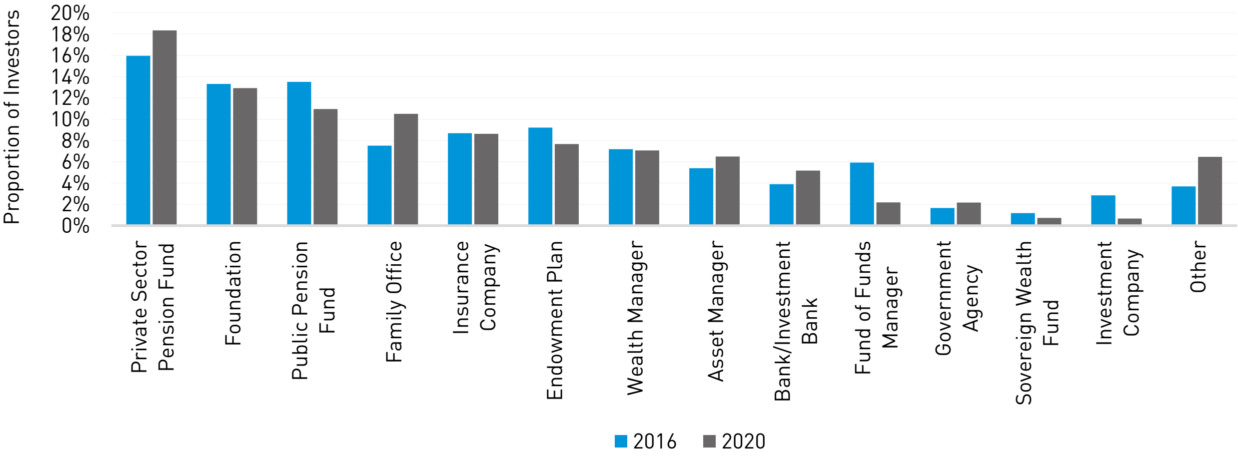
5

Investors

Investor Universe

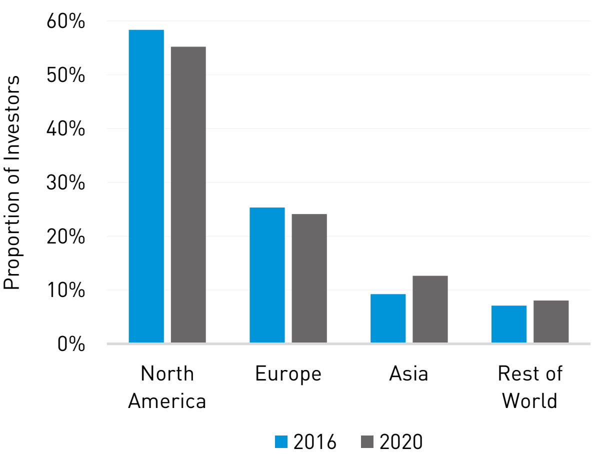
Private sector pension funds have increased their exposure to private debt over the past five years, and the investor pool is becoming more geographically diverse

Fig. 5.1: Investors in Private Debt by Type, 2016 vs. 2020



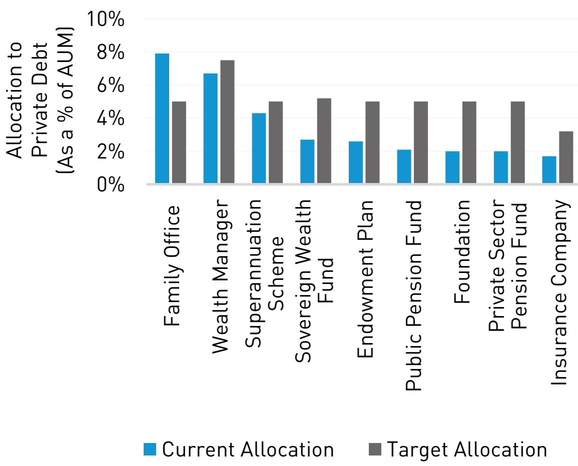
Source: Preqin Pro

Fig. 5.2: Investors in Private Debt by Location, 2016 vs. 2020



Source: Preqin Pro

Fig. 5.3: Investors' Median Current and Target Allocations to Private Debt by Investor Type



Source: Preqin Pro

Investor Mandates Are Increasingly Diversified

Though targeted commitments remain relatively small, investors located in Europe issued more mandates than those in North America – for the second year running

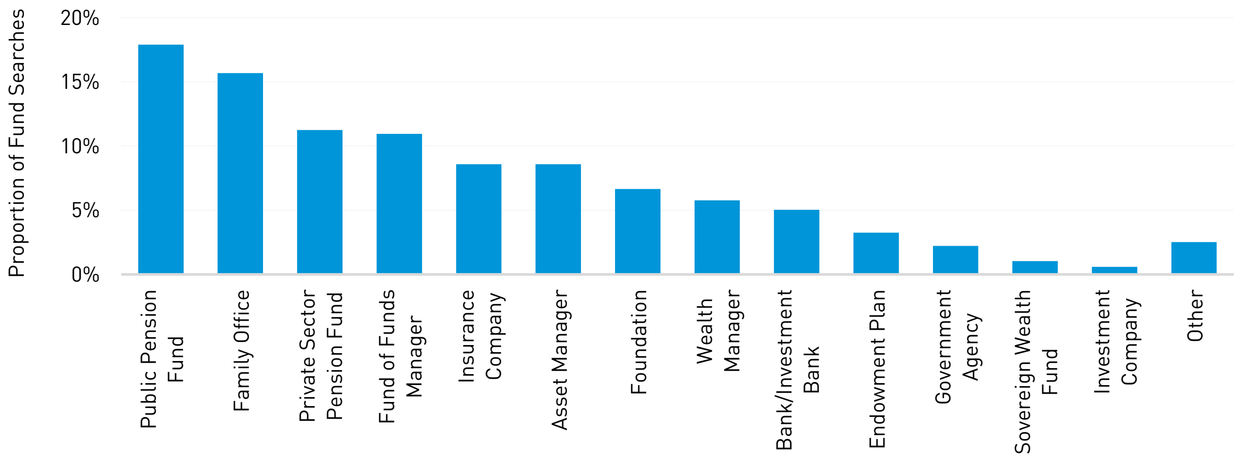
The regional composition of investors issuing private debt fund mandates has evolved over recent years. When the asset class emerged in the aftermath of the GFC, firms, investors, and opportunities were predominantly located in North America. Fast-forward to 2020, however, and the largest proportion (44%) of mandates were issued by Europe-based investors (Fig. 5.5). We identified this shift in 2019 and expect it to continue, as investors in emerging markets, such as Asia and the Middle East, increase their allocations to private debt in search of innovative yield opportunities.

A recent report by M&G Investments[1] found that Europe-based investors have assembled larger and more complicated private debt portfolios as their confidence in the long-term viability of the asset class has grown. And with the asset class posting stable, diversified returns over the past few years compared with public markets (see Chapter 7), the private debt market will appeal to more and more investors across the globe.

While the regional make-up of investors continues to expand, commitment sizes remain relatively small. Over half (54%) of mandates issued in 2020 were for commitments of less than $50mn (Fig. 5.6). Only 9% of mandates were sized at $500mn or more, although this marks an increase of four percentage points from 2019. These smaller mandates reflect the asset class's role as a diversifier in a wider investment portfolio. Investors new to the asset class will also typically dip their toe into the water with a small initial commitment.

[1] *https://www.mandg.co.uk/institutions/articles/european-private-debt-shifting-dynamics/-/media/6FC6C90A27B04CF396F7D3A8387EB7F6.pdf*

Fig. 5.4: Private Debt Mandates Issued in 2020 by Investor Type

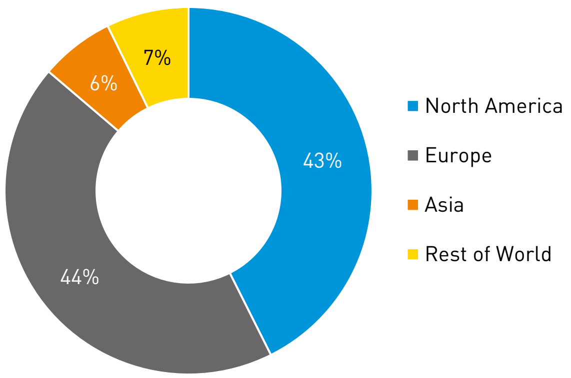


Source: Preqin Pro

Outside of North America, smaller private debt markets continue to grow in sophistication and depth, attracting more investors along the way. Large SWFs, in particular, are increasingly eyeing up the asset class, including Abu Dhabi-based Mubadala, which unveiled a new direct lending partnership[2] with New York-based Apollo Global Management in July 2020. As the economic effects of the pandemic continue to create global opportunities for private debt professionals, such initiatives might well become the norm.

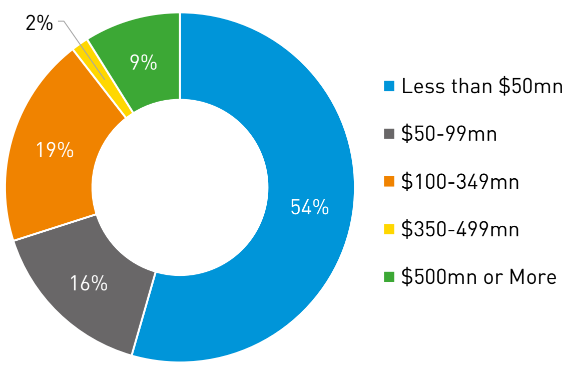
[2] *https://www.ft.com/content/6a05c195-1918-4a92-8b27-4ae24f8a70a8*

Fig. 5.5: Private Debt Mandates Issued in 2020 by Investor Location



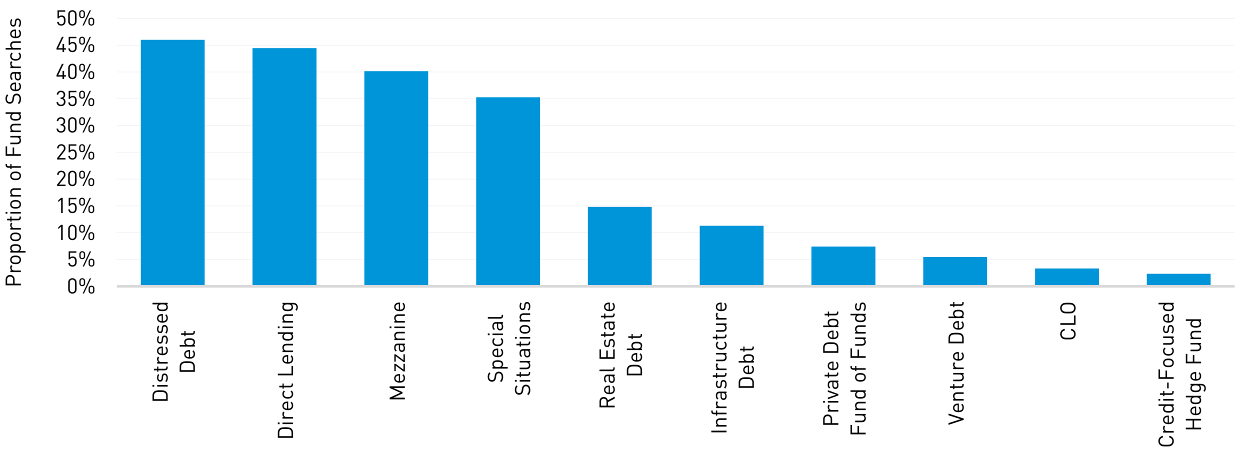
Source: Preqin Pro

Fig. 5.6: Private Debt Mandates Issued in 2020 by Commitment Size



Source: Preqin Pro

Fig. 5.7: Private Debt Mandates Issued in 2020 by Fund Type

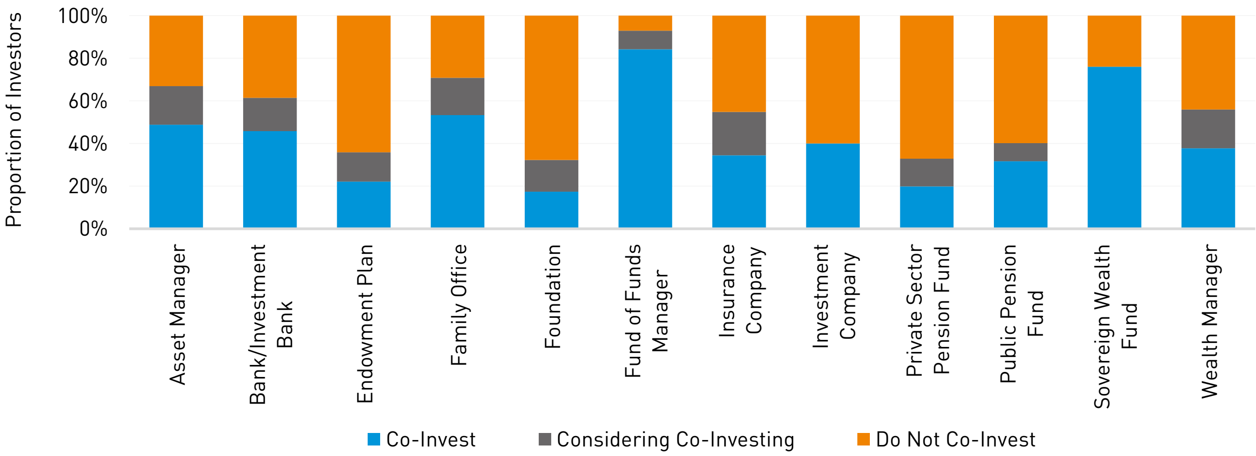


Source: Preqin Pro

Alternative Structures

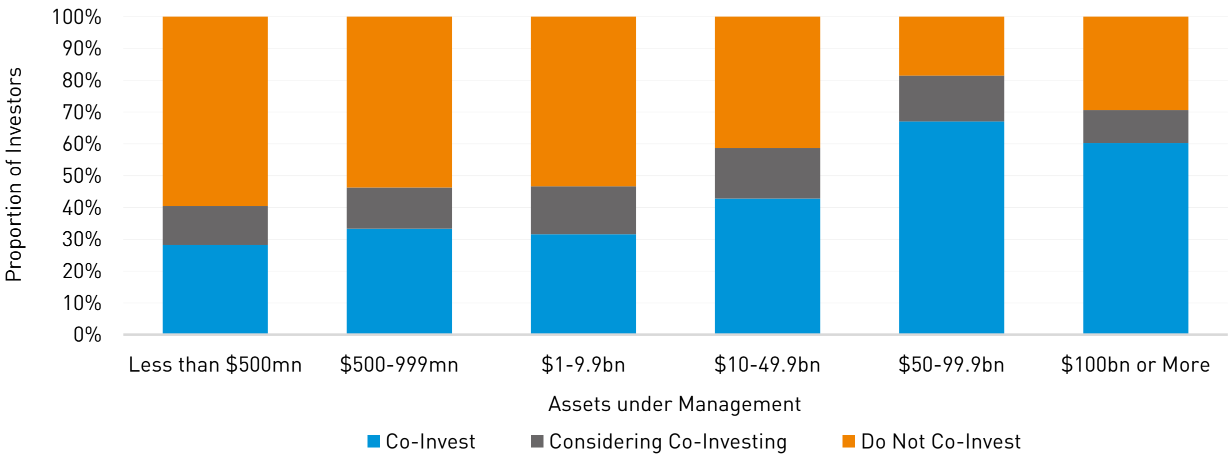
Co-investments and separate accounts are generally favored by larger, more sophisticated institutional investors

Fig. 5.8: Investor Appetite for Private Debt Co-Investments by Type



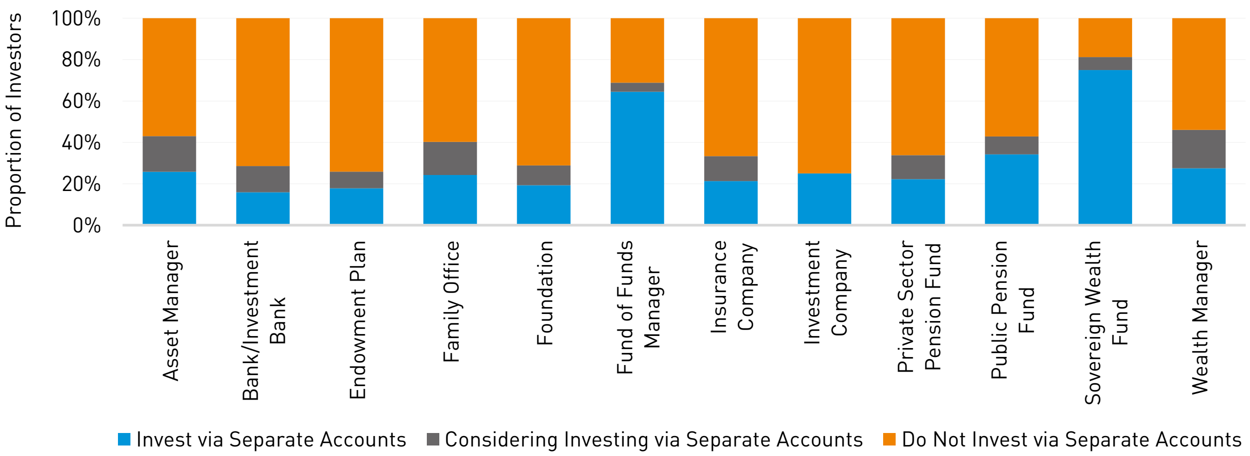
Source: Preqin Pro

Fig. 5.9: Investor Appetite for Private Debt Co-Investments by Assets under Management



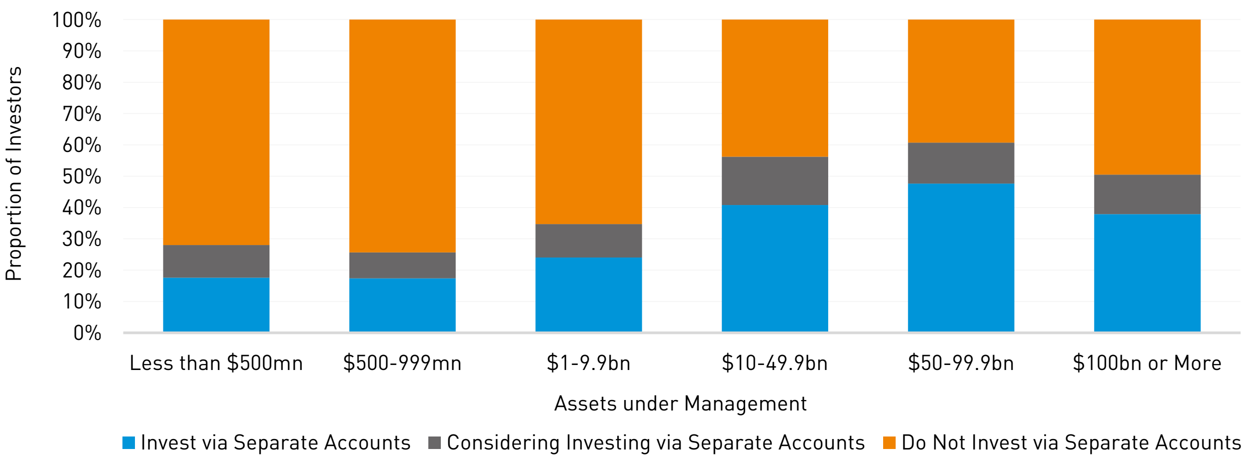
Source: Preqin Pro

Fig. 5.10: Investor Appetite for Private Debt Separate Accounts by Type



Source: Preqin Pro

Fig. 5.11: Investor Appetite for Private Debt Separate Accounts by Assets under Management



Source: Preqin Pro

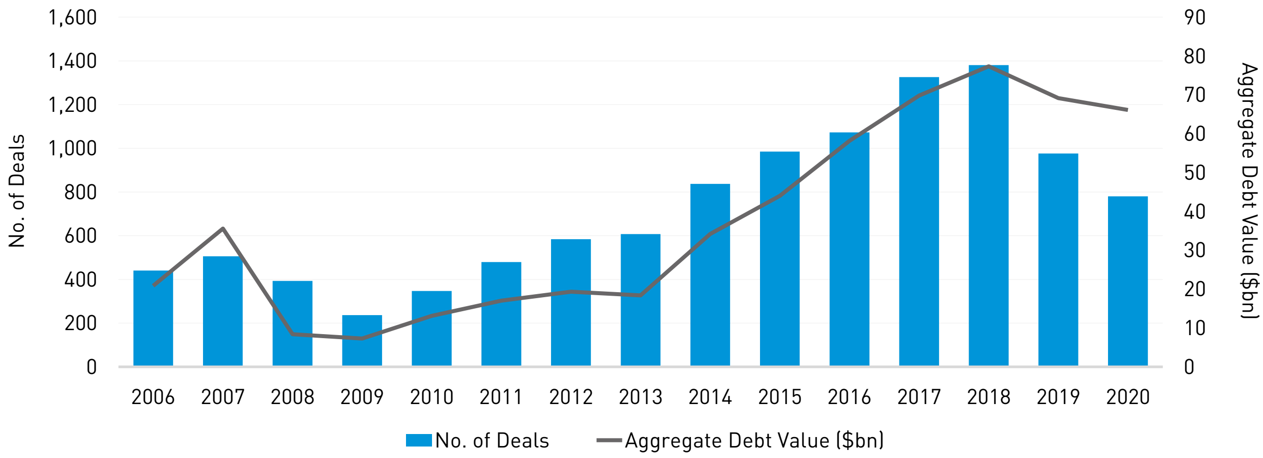
6

Deal Activity

Deal Activity

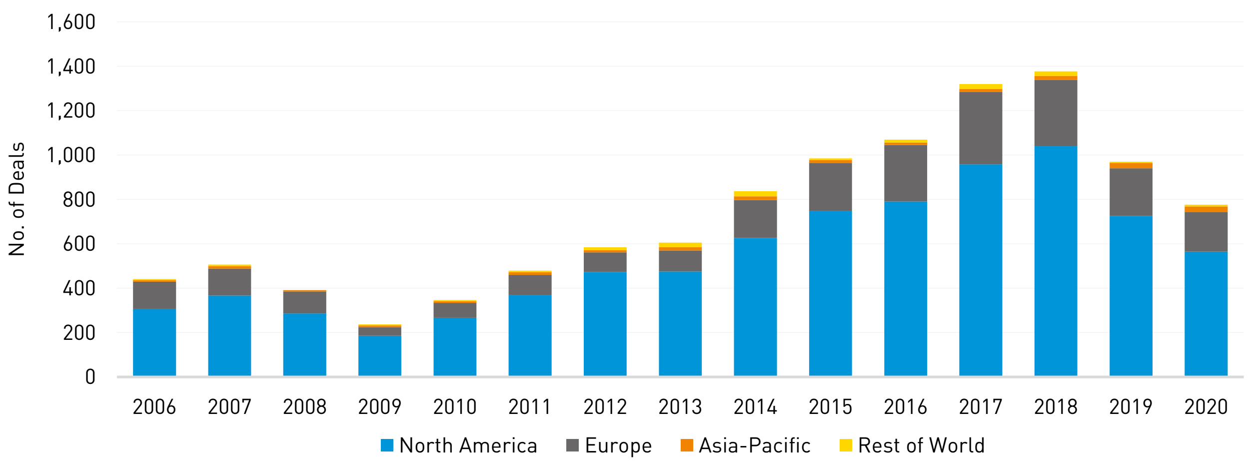
The amount of debt issuance continued to decline over 2020, but deal activity diversified across different sectors

Fig. 6.1: Global Private Debt-Backed Deals, 2006 - 2020



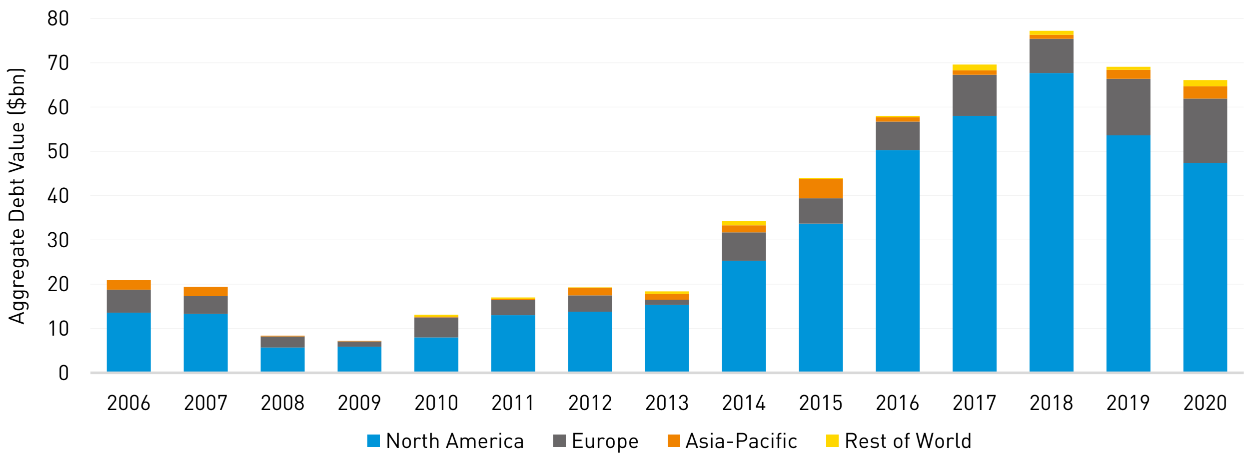
Source: Preqin Pro

Fig. 6.2: Number of Private Debt-Backed Deals by Region, 2006 - 2020



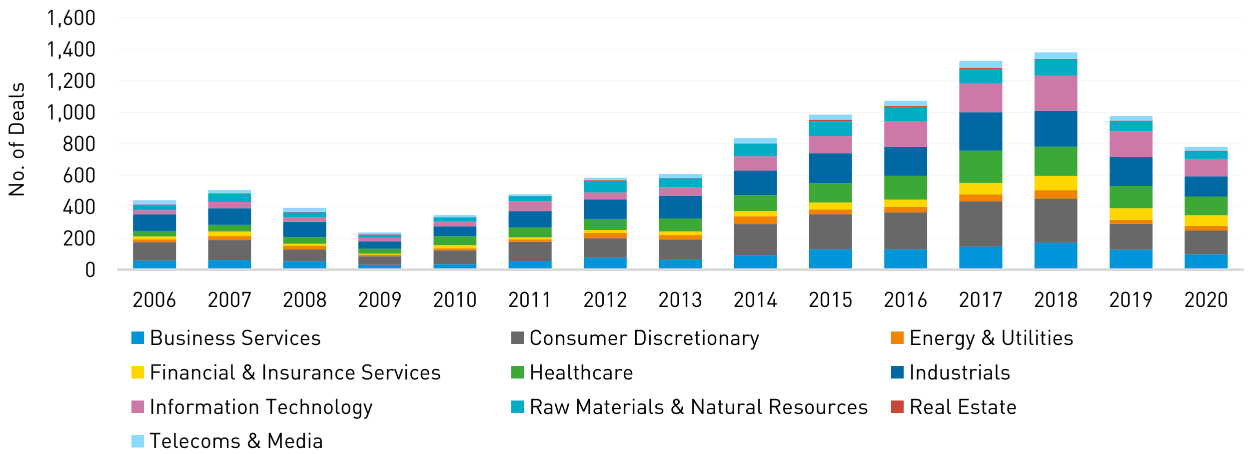
Source: Preqin Pro

Fig. 6.3: Aggregate Value of Private Debt-Backed Deals by Region, 2006 - 2020



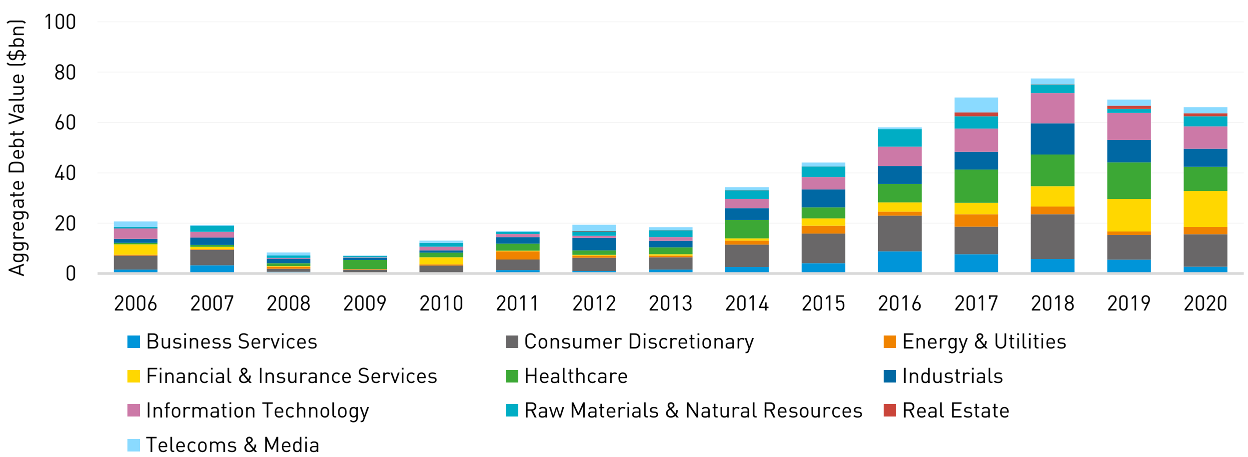
Source: Preqin Pro

Fig. 6.4: Number of Private Debt-Backed Deals by Industry, 2006 - 2020

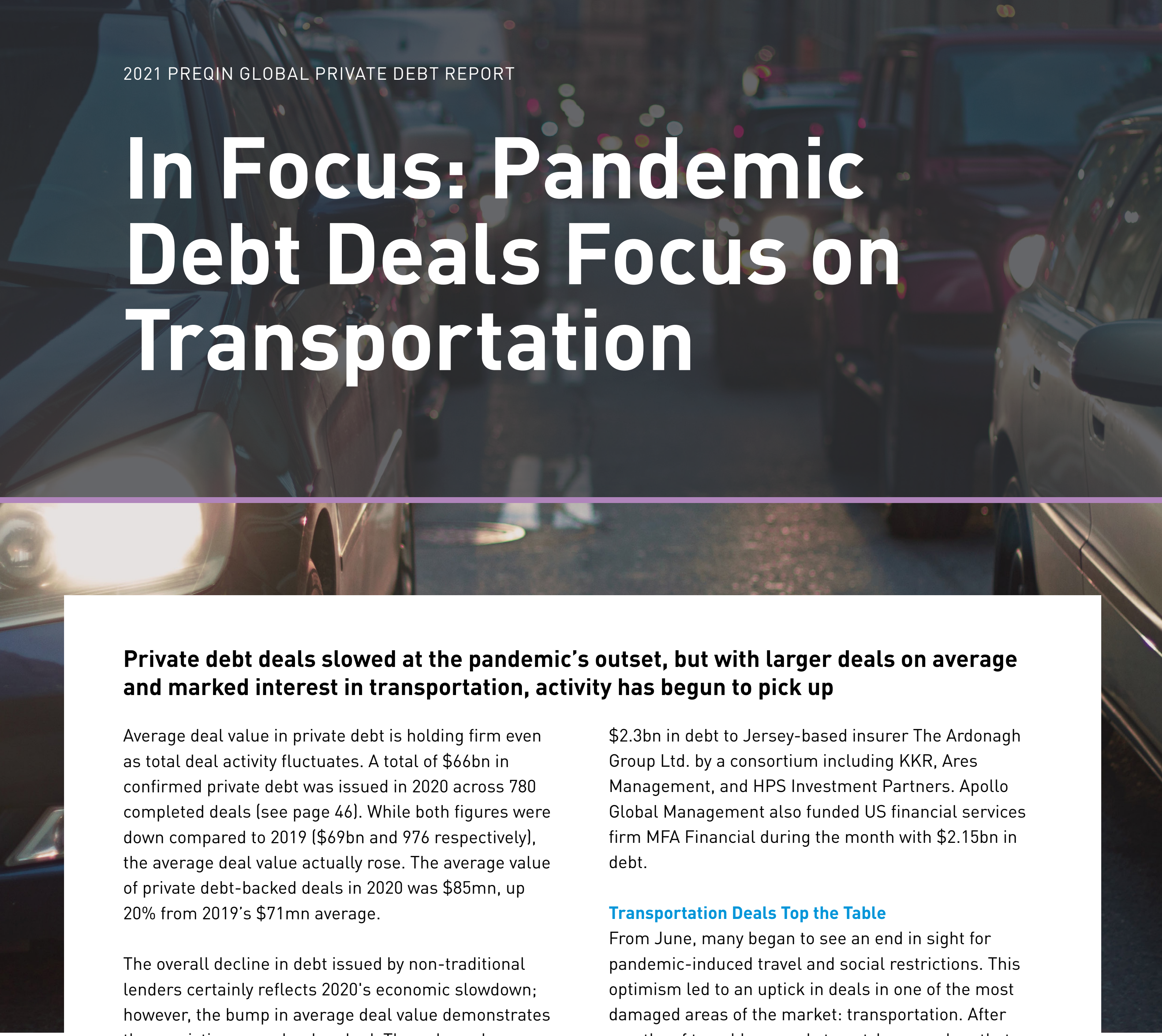


Source: Preqin Pro

Fig. 6.5: Aggregate Value of Private Debt-Backed Deals by Industry, 2006 - 2020



Source: Preqin Pro



In Focus: Pandemic Debt Deals Focus on Transportation

Private debt deals slowed at the pandemic's outset, but with larger deals on average and marked interest in transportation, activity has begun to pick up

Average deal value in private debt is holding firm even as total deal activity fluctuates. A total of $66bn in confirmed private debt was issued in 2020 across 780 completed deals (see page 46). While both figures were down compared to 2019 ($69bn and 976 respectively), the average deal value actually rose. The average value of private debt-backed deals in 2020 was $85mn, up 20% from 2019's $71mn average.

The overall decline in debt issued by non-traditional lenders certainly reflects 2020's economic slowdown; however, the bump in average deal value demonstrates the conviction some lenders had. The upheaval created by the pandemic, calmed at least temporarily by government intervention, created a large number of distressed assets or companies looking for bridge loans. From there it was up to debt fund managers to assess the depth and duration of the damage.

That assessment had to wait, however, until the dust cleared. Much like the rest of the world, private debt markets took a pause at the end of the first quarter and into the second. During 2019, 25% of the $69bn in total deal volume was closed during those two months, while only 9% of the $66bn in 2020 deals completed during this period.

Deal activity recovered in June, though, with about $13bn of the year-to-date total closing during the month. Among those deals were four of the year's 13 $1bn+ transactions. The largest deal in June was $2.3bn in debt to Jersey-based insurer The Ardonagh Group Ltd. by a consortium including KKR, Ares Management, and HPS Investment Partners. Apollo Global Management also funded US financial services firm MFA Financial during the month with $2.15bn in debt.

Transportation Deals Top the Table

From June, many began to see an end in sight for pandemic-induced travel and social restrictions. This optimism led to an uptick in deals in one of the most damaged areas of the market: transportation. After months of travel bans and stay-at-home orders that kept people local, the transport sector received an influx of debt capital.

In fact, the two largest deals of the year were in industries hurt most by the COVID-19 pandemic: car rentals and airlines. The transportation industry saw a notable jump in private debt financing to $5.4bn in total deal value, up more than $5bn compared with 2019. Financial services, technology, and telecoms also saw an uptick in total private debt-backed deal value (see page 47).

The $4bn deal between Apollo and its affiliate Athene Asset Management with rental car company Hertz headlined transportation deals in 2020. The debt, issued in November, came amid the company's bankruptcy; Hertz filed for Chapter 11 in May. The funds are slated for updating its rental fleet in 2021, a sign that the company, and Apollo, expect to see a rapid recovery for the travel industry. During the year, Hertz plans to purchase about 230,000 new vehicles through a wholly owned special purpose entity.

Oaktree's $1.3bn distressed loan to Brazilian carrier LATAM Airlines was also among the largest deals of last year. Similar to Hertz, LATAM's business was significantly impacted by the COVID-19 pandemic; the company eventually filed for Chapter 11 bankruptcy in late May. Oaktree's investment is part of a debtor-in-possession financing proposal.

Some of the largest private debt managers raised significant quantities of capital in 2020. Deal activity should build upon momentum in 2021 the new year. The speed and magnitude of added fiscal stimulus could hamper deal activity in the US, but, globally, the pandemic has created plenty of opportunity for both borrowers and lenders.

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7

Performance

Private Debt Funds Underperform but Mitigate Risk

Increased competition and central bank intervention put a strain on debt returns

Private debt underperformed most of its peer asset classes over the year ending June 2020. PrEQIn Index data shows the private debt benchmark grew by 5% during the period; comparatively, private equity was up 27% (Fig. 7.7). As the COVID-19 pandemic spread across the globe in Q1 2020, alternative assets recorded their worst quarter since the GFC, according to PrEQIn indices; private debt fund returns fell 17 percentage points, giving back more than 18 months of index returns.

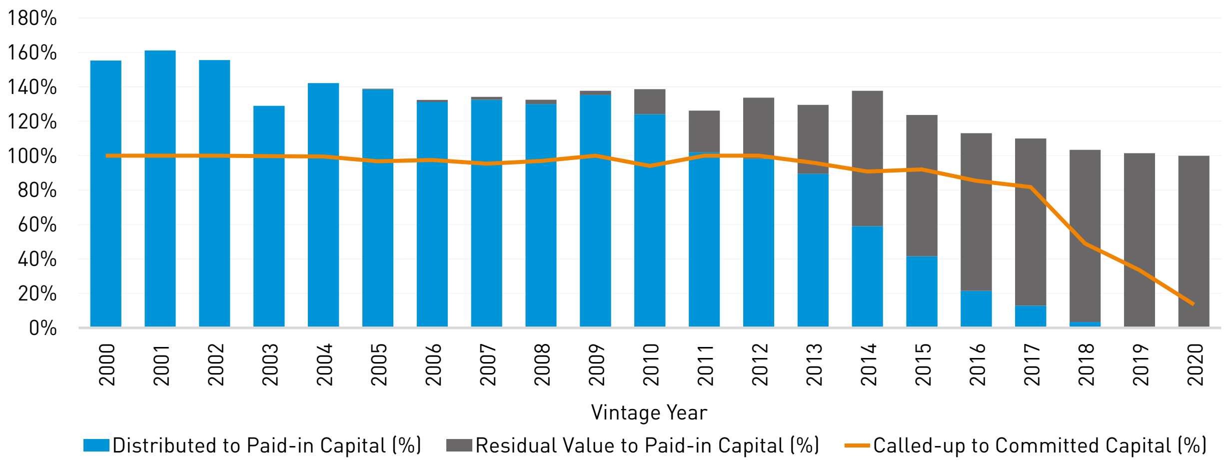
In fact, private debt began losing ground to private equity and infrastructure in mid-2015, as falling interest rates and increased competition dragged on returns. Deals priced on benchmarks such as LIBOR suffered as yields were dented by depressed corporate lending rates.

This trend has been accelerated by the COVID-19 pandemic. The rapid erosion of cash flows and revenues early in the year increased the need for liquidity from portfolio companies, as traditional banks became even more averse to risky business loans. Additionally, public high-yield and low-rated investment-grade yields collapsed in 2020 to historic lows, pressuring private debt yields even lower.

Although private debt has underperformed its peer asset classes, returns have been less dispersed. The median net IRR for funds of vintages 2008-2017 is below those of private equity (+14.4%) and real estate (+12.2%), at 8.8%, but investors can expect a tighter range of returns from private debt, with standard deviation of net IRRs at 7.7% the lowest among its peers (Fig. 7.5).

Private debt returns are generally guided by a spread relative to a base yield such as LIBOR, closely relating them to public debt performance. Although private debt has historically paid 150-200 bps over public debt,

Fig. 7.1: Private Debt: Median Called-up, Distributed, and Residual Value Ratios by Vintage Year

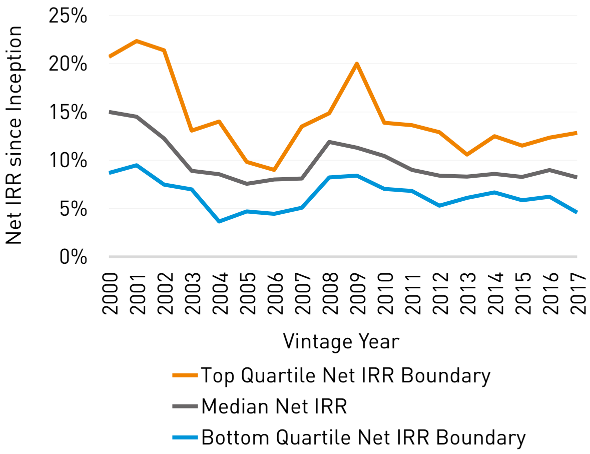


Source: Preqin Pro. Data as of December 2020 according to tenure and seniority, that support system has slid over time. Fortunately for investors, private debt, like private equity, is not a homogeneous asset class.

Across private debt strategies, returns and return dispersion data varies greatly, as seen in Fig. 7.6. Direct lending funds, characterized by more senior secured debt, have been a steady force, with a median net IRR of 8.3% for vintages 2008-2017 and a standard deviation of only 5.0%. Distressed and special situations funds fall in line with their profiles, offering investors more return in exchange for greater risk. Mezzanine funds show slightly more return and variance than direct lending.

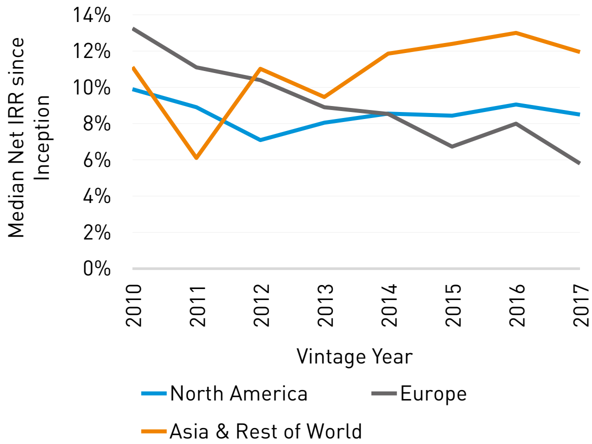
Despite these seemingly stiff headwinds, private debt offers investor portfolios a lower-risk allocation with steady, rather than stellar, returns.

Fig. 7.2: Private Debt: Median Net IRRs and Quartile Boundaries by Vintage Year



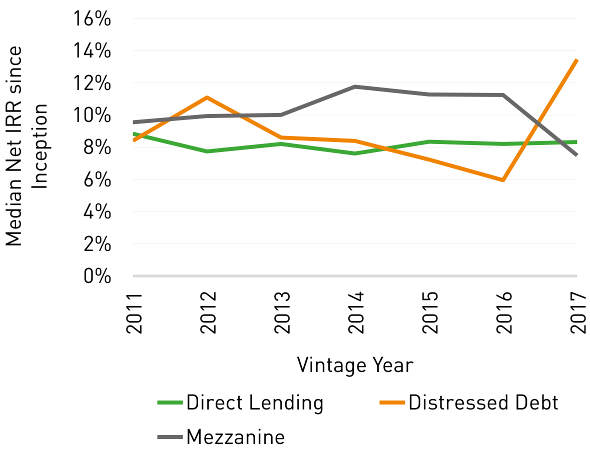
Source: Preqin Pro. Data as of December 2020

Fig. 7.3: Private Debt: Median Net IRRs by Primary Geographic Focus and Vintage Year



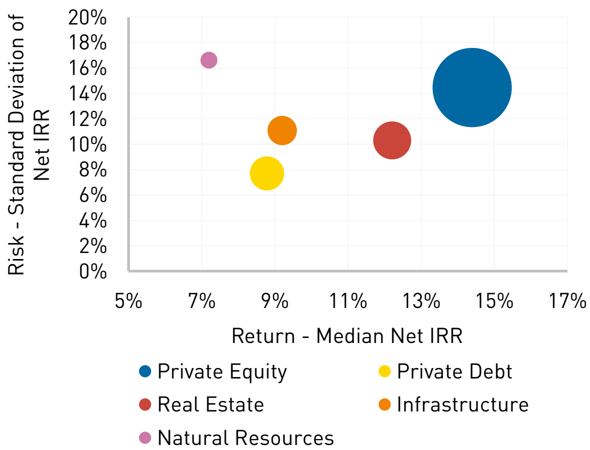
Source: Preqin Pro. Data as of December 2020

Fig. 7.4: Private Debt: Median Net IRRs by Fund Type and Vintage Year



Source: Preqin Pro. Data as of December 2020

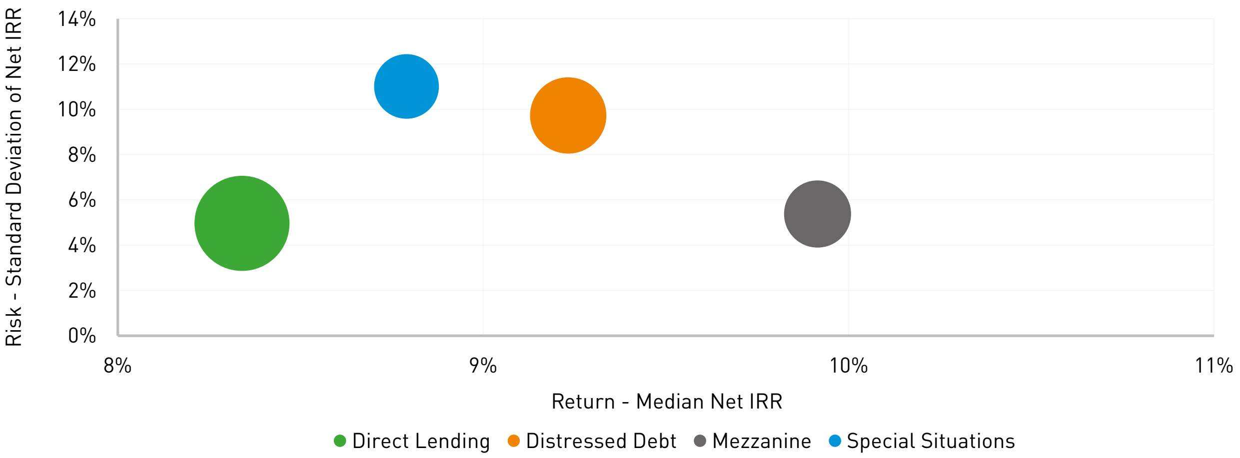
Fig. 7.5: Private Capital: Risk/Return by Asset Class (Vintages 2008-2017)*



Source: Preqin Pro. Data as of December 2020

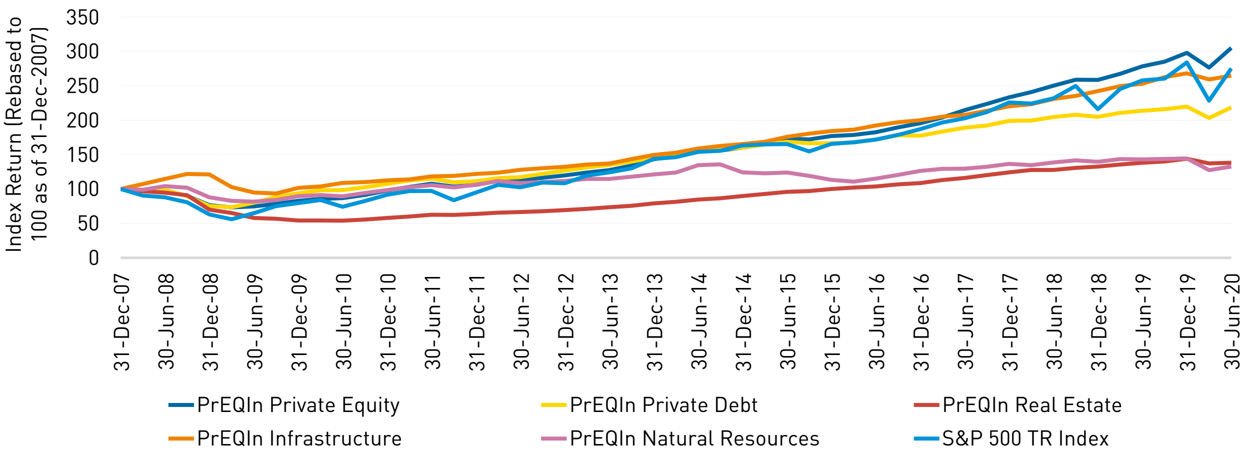
**The size of each circle represents the relative AUM size as of June 2020.*

Fig. 7.6: Private Debt: Risk/Return by Fund Type (Vintages 2008-2017)*



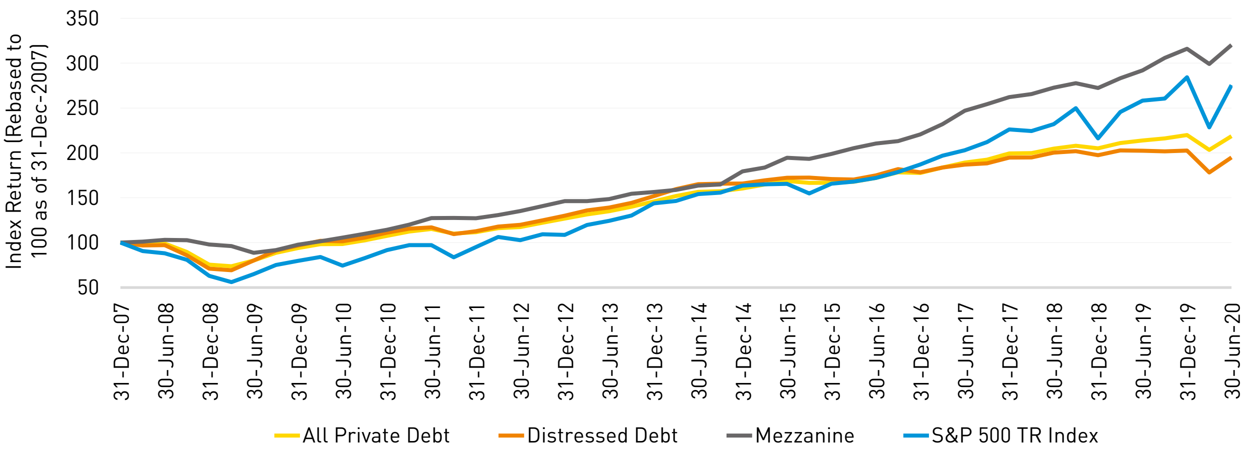
Source: Preqin Pro. Data as of December 2020

Fig. 7.7: PrEQIn Index: Private Capital Strategies vs. S&P 500 TR Index



Source: Preqin Pro

Fig. 7.8: PrEQIn Index: Private Debt Strategies vs. S&P 500 TR Index



Source: Preqin Pro

*The size of each circle represents the relative AUM size as of June 2020.

Horizon IRRs

Near-term IRRs decline due to low interest rates and pandemic-related write-offs

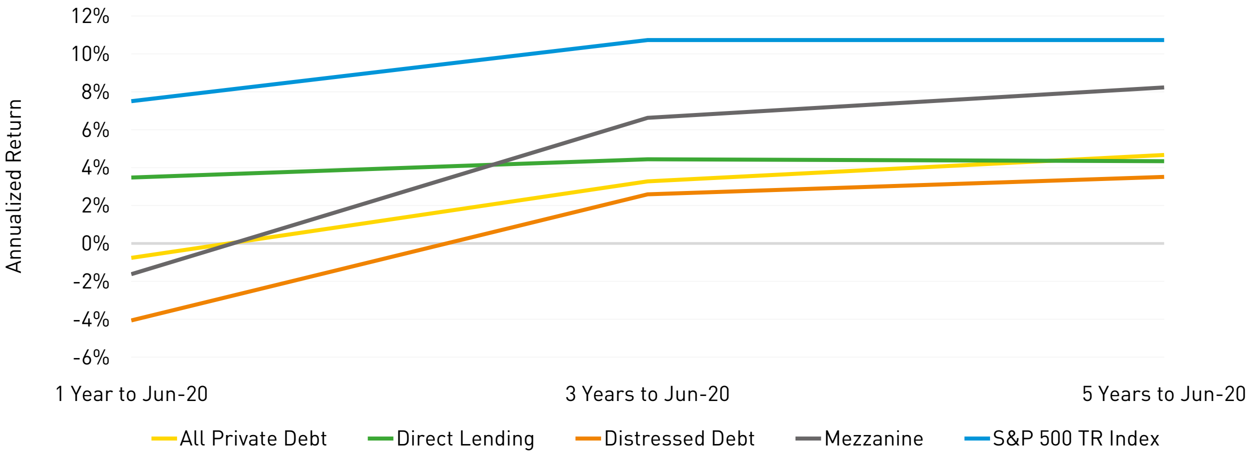
Private debt lags its peer asset classes over short- and mid-term investment horizons. A downturn in Q1 2020 dragged the broader private debt asset class down to a one-year IRR of -0.8% to the end of June (Fig. 7.9). However, three- and five-year IRRs are both still in the black. Near-term returns were dragged lower as write-downs, defaults, and expected defaults impacted portfolios, particularly at the riskier end of the private credit spectrum.

Low interest rates, particularly LIBOR, have suppressed longer-horizon returns in the industry, as central banks continued 'lower for longer' policies. But the maturation of the market following the GFC has also impacted long-term valuations, with more market participants competing for choice deals.

As Fig. 7.10 shows, real estate and energy-dependent natural resources were the only groups to underperform private debt over the most recent one-year horizon. Private equity and infrastructure, by comparison, held steady between their one- and three-year horizon IRRs. This short-term variance should not cause much concern for private capital investors, given that asset class IRRs have historically risen and converged.

Mezzanine debt underperformed private debt as a whole during a rocky first half of the year, with a one-year horizon IRR of -1.6% to 30 June, compared with -4.1% for distressed debt. Distressed debt funds faced a tidal wave of write-downs during Q1 2020, but expectations of future opportunities also rose significantly. Indeed, among the funds raised, Oaktree Capital Management's $15bn distressed debt-focused Opportunities Fund XI stands out as the largest ever of its kind.

Fig. 7.9: Horizon IRRs: Private Debt vs. S&P 500 TR Index

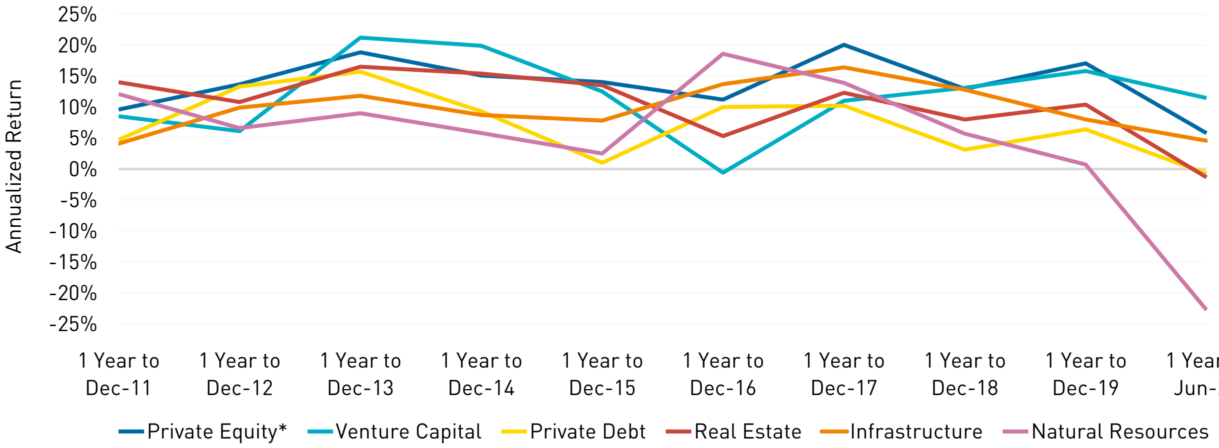


Source: Preqin Pro

Direct lending, the largest strategy by AUM, was up 3.5% over the same horizon. The subset has a historically lower risk/return profile but generally holds less volatile senior debt.

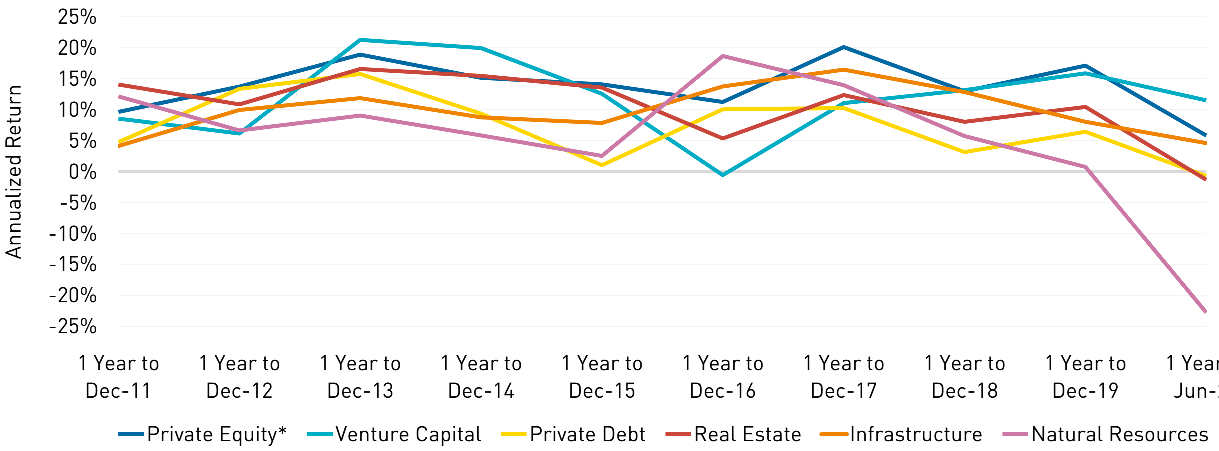
Private debt's position as an alternative to public credit and other high-yield portfolios will continue to influence the industry despite 2020's downturn. These strategies are a complement to traditional credit strategies, not an alternative. The liquidity the asset class offers will only grow as traditional banks avoid higher-risk loans, despite the potential higher rates of return.

Fig. 7.10: Private Capital: Rolling One-Year Horizon IRRs by Asset Class



Source: Preqin Pro

Fig. 7.11: Private Capital: Rolling Three-Year Horizon IRRs by Asset Class



Source: Preqin Pro

**Excluding Venture Capital.*

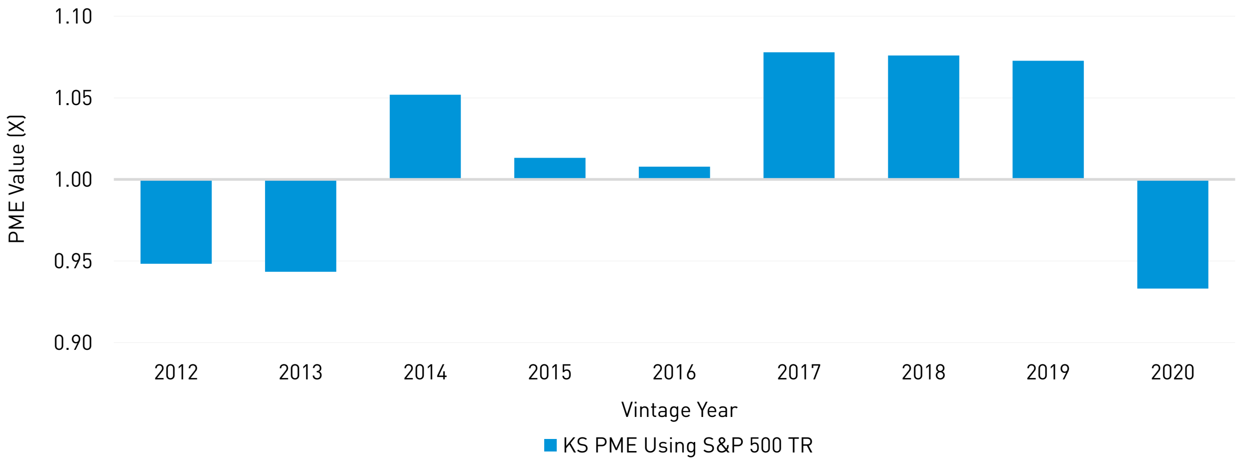
Performance Benchmarks and PMEs

Fig. 7.12: Global Private Debt Performance Benchmarks by Vintage Year

		Median Fund			Net IRR Quartiles (%)			Net Multiple Quartiles (X)		
Vintage	No. of Funds	Called (%)	Dist (%) DPI	Value (%) RVPI	Q1	Median	Q3	Q1	Median	Q3
2020	11	13.6%	0.0%	100.0%	n/a	n/m	n/a	1.06	1.02	0.90
2019	61	33.5%	0.0%	101.5%	n/m	n/m	n/m	1.08	1.02	0.99
2018	94	49.0%	3.4%	100.0%	n/m	n/m	n/m	1.12	1.06	1.01
2017	119	81.8%	12.9%	97.1%	12.8%	8.2%	4.6%	1.18	1.10	1.03
2016	93	85.4%	21.5%	91.5%	12.3%	9.0%	6.2%	1.26	1.15	1.09
2015	96	92.0%	41.6%	82.1%	11.5%	8.3%	5.9%	1.27	1.19	1.11
2014	73	90.8%	59.1%	78.6%	12.5%	8.6%	6.7%	1.43	1.24	1.16
2013	86	95.9%	89.4%	40.1%	10.6%	8.3%	6.1%	1.41	1.28	1.17
2012	46	100.0%	98.2%	35.4%	12.9%	8.4%	5.3%	1.48	1.29	1.14
2011	49	100.0%	101.9%	24.3%	13.6%	9.0%	6.8%	1.59	1.36	1.19
2010	50	94.1%	124.0%	14.7%	13.9%	10.4%	7.0%	1.67	1.48	1.28
2009	29	100.0%	135.3%	2.4%	20.0%	11.3%	8.4%	1.65	1.38	1.18
2008	50	96.9%	130.0%	2.5%	14.9%	11.9%	8.2%	1.82	1.47	1.26
2007	39	95.4%	132.5%	1.7%	13.5%	8.1%	5.1%	1.51	1.35	1.18
2006	38	97.5%	131.2%	1.2%	9.0%	8.0%	4.5%	1.56	1.36	1.20
2005	30	96.8%	138.6%	0.4%	9.8%	7.6%	4.7%	1.63	1.44	1.29
2004	22	99.6%	142.2%	0.0%	14.0%	8.6%	3.7%	1.58	1.48	1.30
2003	17	99.8%	129.0%	0.0%	13.1%	8.9%	7.0%	1.60	1.33	1.19
2002	22	100.0%	155.6%	0.0%	21.4%	12.3%	7.5%	2.24	1.57	1.37
2001	23	100.0%	161.2%	0.0%	22.4%	14.5%	9.5%	1.88	1.61	1.42
2000	26	100.0%	155.3%	0.0%	20.7%	15.0%	8.7%	1.99	1.55	1.28

Source: Preqin Pro. Data as of December 2020

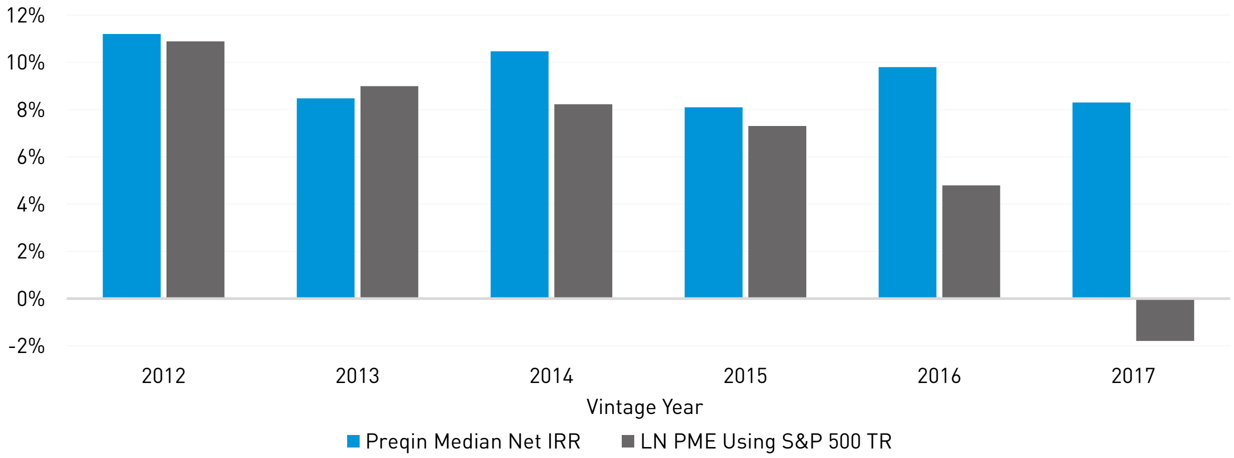
Fig. 7.13: KS PME: Private Debt – All Regions



NB: If PME index value (X) is > 1, private debt has outperformed the public market.

Source: Preqin Pro. Data as of June 2020

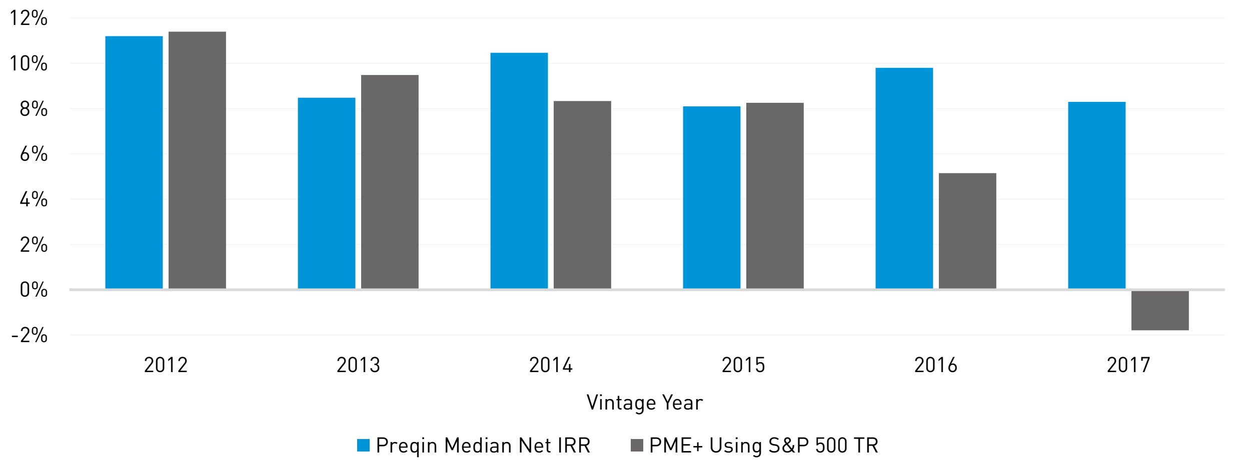
Fig. 7.14: LN PME: Private Debt – All Regions



NB: If median net IRR is > LN PME value, private debt has outperformed the public market.

Source: Preqin Pro. Data as of June 2020

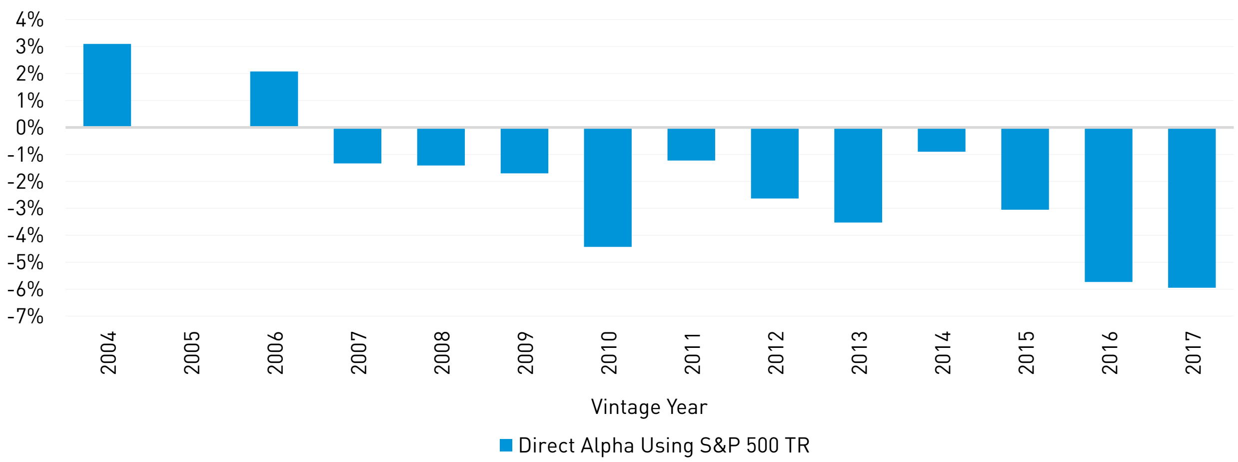
Fig. 7.15: PME+: Private Debt – All Regions



NB: If median net IRR is > PME+ value, private debt has outperformed the public market.

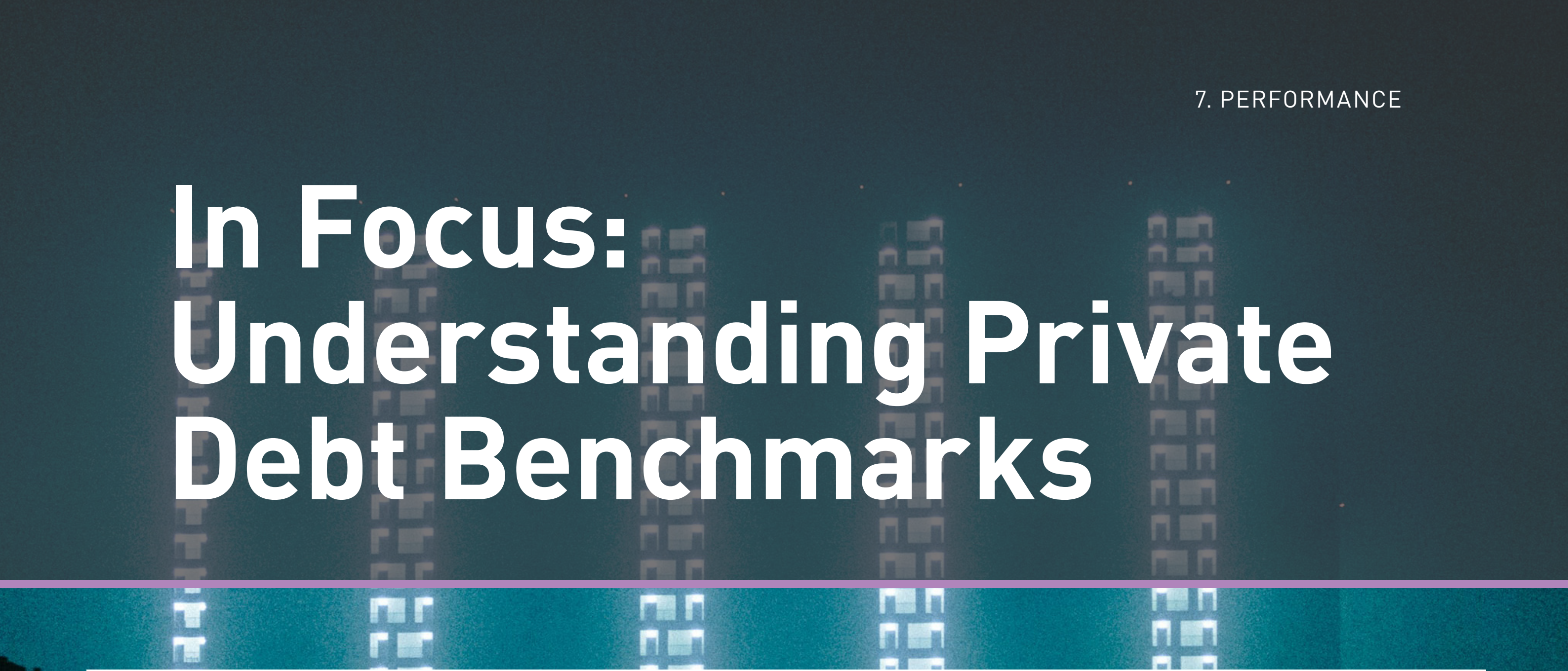
Source: Preqin Pro. Data as of June 2020

Fig. 7.16: Direct Alpha: All Private Debt – All Regions



NB: If Direct Alpha value is > 0, private debt has outperformed the public market.

Source: Preqin Pro. Data as of June 2020



In Focus: Understanding Private Debt Benchmarks

Interest in private debt has continued to grow, but LPs need to understand the risks and rewards to make better decisions

Due to the lack of yield in various parts of the market, interest in private debt has grown in the past year. Industry AUM has increased – from $233bn at the end of 2008 to $887bn as of June 2020 – but this uptick has not been uniform across all strategies; while dry powder held in mezzanine funds has declined by 6% over the past year, for example, distressed dry powder has increased by 18%.

Market participants have the option to invest in different parts of the private debt market, and each strategy has its own risks and rewards. Allocators and LPs need to constantly assess their portfolios against relative benchmarks to detect the gaps in their investments and reallocate capital. Although the S&P 500 TR Index is not the appropriate benchmark for many assets, especially private capital, it is frequently used to analyze the worthiness of various strategies. Generally speaking, private NAVs are lagged and appraisal/valuation based. This means price smoothing will likely be apparent in the data. As a result, it becomes extremely difficult to compare highly liquid equity indices such as the S&P 500 TR to highly illiquid assets.

The Unsmoothed Returns vs. the Most Liquid

For the purpose of this analysis, we used the unsmoothed returns of Preqin's private debt benchmarks vs. the S&P 500 TR. Although this is not an apples-with-apples comparison, and there are certainly better ways to benchmark private debt, many allocators rely on S&P as the baseline to judge various investment opportunities.

Standard deviation is a measure of the spread of returns; the higher the standard deviation value, the higher the risk associated with the investment. Fig. 7.17 shows that in each category, the unsmoothed standard deviation has increased compared to the base number, which is not surprising. The interesting observation here is that the all private debt category still shows a smaller standard deviation than the S&P 500 TR, and mezzanine's remains fairly stable.

Skewness is a measure of symmetry in returns, and a negative value indicates that we may observe frequent small gains and a few large losses. The data shows that skewness declines across the board, and even though the numbers are still negative, overall, this is considered good news. Distressed unsmoothed series show smaller skewness than the S&P 500 TR.

We observe a similar pattern in kurtosis numbers, and see a decline in all values, although the numbers remain large compared with the S&P 500 TR. Kurtosis is a measure that shows how heavy the tails of a distribution are – a high kurtosis value indicates a high probability of extremely large and extremely small returns. It is generally assumed that LPs do not like high standard deviation, value positive skewness, and want to avoid kurtosis.

Understanding Traditional Risk Measures

As the most accepted industry measure, the Sharpe ratio is generally used by market participants as a risk-adjusted measure to analyze investments. We understand that there are many assumptions behind Sharpe, one being normality. But as Fig. 7.17 shows, distributions are far from normal. Loosely speaking, a value above one is considered acceptable, as it indicates that the investment has generated a return above the risk the LP has taken on. We see a decline in all Sharpe values for the smoothed series, but that is not surprising, as the risk numbers have increased. It is important to note, however, that mezzanine is still producing a Sharpe value greater than one. This is particularly impressive since we are going back to 2008: the longer the series, the harder it becomes to maintain a good Sharpe ratio that is greater than one.

There are various ways to unsmooth data. It is important to keep in mind that model-based unsmoothing has its own issues – the biggest being that the unsmoothed returns may not represent the true value of the underlying assets. There are advantages, however, in unsmoothing returns. The good news is that long-term historical means are usually not substantially impacted by price smoothing. Risk measures such as standard deviation, on the other hand, are affected, causing favored investment assessment ratios, such as the Sharpe ratio, to produce the wrong conclusions.

Even after removing the lagged effect from our data and after considering the unsmoothed risk and distribution numbers, private debt remains desirable. The risk associated with the asset class is higher than observed on the surface, but it remains competitive from a risk-profile standpoint. Our analysis shows that each individual private debt strategy offers different risk/return parameters, and bundling them together can generate a distorted picture. A deeper knowledge of the layers within private debt is essential to help LPs make better investment decisions.

Fig. 7.17: Performance Metrics across Private Debt Strategies vs. S&P 500 TR Index

Results	All Private Debt	All Private Debt Unsmoothed	Distressed Debt	Distressed Debt Unsmoothed	Mezzanine	Mezzanine Unsmoothed	S&P 500 TR Index
Interval	Sep-08 - Jun-20	Sep-08 - Jun-20	Sep-08 - Jun-20	Sep-08 - Jun-20	Sep-08 - Jun-20	Sep-08 - Jun-20	Sep-08 - Jun-20
Return	6.8%	6.7%	6.0%	5.7%	9.9%	9.9%	10.0%
Standard Deviation	8.6%	13.0%	11.0%	15.8%	6.3%	7.2%	17.8%
Skewness	-1.77	-1.07	-0.91	-0.32	-1.03	-0.87	-0.84
Kurtosis	5.27	3.04	3.41	2.94	1.78	1.52	0.74
Sharpe Ratio	0.73	0.48	0.49	0.34	1.49	1.30	0.53

Source: Preqin Pro

8

League Tables

Largest Fund Managers

Fig. 8.1: All Private Debt - Largest Fund Managers by Aggregate Capital Raised for Private Debt Funds in the Past 10 Years*

Firm	Headquarters	Total Capital Raised in Past 10 Years ($bn)
Oaktree Capital Management	US	48.6
Ares Management	US	43.6
GSO Capital Partners	US	42.2
The Goldman Sachs Group	US	34.3
HPS Investment Partners	US	33.1
Intermediate Capital Group	UK	24.1
Cerberus Capital Management	US	19.5
Fortress Investment Group	US	17.7
KKR	US	17.3
TPG/Castlelake	US	16.7

Source: Preqin Pro

Fig. 8.2: All Private Debt - Largest Fund Managers by Estimated Dry Powder*

Firm	Headquarters	Estimated Dry Powder ($bn)
Oaktree Capital Management	US	19.8
Ares Management	US	15.5
GSO Capital Partners	US	14.7
The Goldman Sachs Group	US	13.7
HPS Investment Partners	US	8.4
Clearlake Capital Group	US	7.0
Intermediate Capital Group	UK	6.2
Alcentra	UK	5.9
KKR	US	5.2
Arcmont Asset Management	UK	4.4

Source: Preqin Pro

**Includes known separate accounts.*

Fig. 8.3: Direct Lending - Largest Fund Managers by Aggregate Capital Raised in the Past 10 Years*

Firm	Headquarters	Total Capital Raised in Past 10 Years ($bn)
Ares Management	US	37.1
Arcmont Asset Management	UK	13.8
The Goldman Sachs Group	US	11.8
Alcentra	UK	11.7
GSO Capital Partners	US	11.6
Golub Capital	US	11.1
HPS Investment Partners	US	10.4
Cerberus Capital Management	US	8.9
M&G Investments	UK	8.1
Angelo, Gordon & Co.	US	7.9

Source: Preqin Pro

Fig. 8.4: Direct Lending - Largest Fund Managers by Estimated Dry Powder*

Firm	Headquarters	Estimated Dry Powder ($bn)
Ares Management	US	12.7
Alcentra	UK	5.9
Arcmont Asset Management	UK	4.4
GSO Capital Partners	US	4.2
Churchill Asset Management	US	3.5
Golub Capital	US	2.8
Oaktree Capital Management	US	2.8
Permira Debt Managers	UK	2.8
Antares Capital	US	2.6
The Goldman Sachs Group	US	2.2

Source: Preqin Pro

Fig. 8.5: Distressed Debt - Largest Fund Managers by Aggregate Capital Raised in the Past 10 Years*

Firm	Headquarters	Total Capital Raised in Past 10 Years ($bn)
Oaktree Capital Management	US	32.1
GSO Capital Partners	US	19.8
Fortress Investment Group	US	15.2
CarVal Investors	US	12.0
Cerberus Capital Management	US	10.5
Värde Partners	US	10.2
Bain Capital Credit	US	9.3
Avenue Capital Group	US	9.1
KKR	US	8.2
Castlelake	US	7.1

Source: Preqin Pro

**Includes known separate accounts.*

Fig. 8.6: Distressed Debt - Largest Fund Managers by Estimated Dry Powder*

Firm	Headquarters	Estimated Dry Powder ($bn)
Oaktree Capital Management	US	14.6
GSO Capital Partners	US	9.3
The Goldman Sachs Group	US	5.5
Bain Capital Credit	US	2.9
Värde Partners	US	2.9
KKR	US	2.8
Monarch Alternative Capital	US	2.8
CarVal Investors	US	2.6
Oak Hill Advisors	US	2.2
Fortress Investment Group	US	2.1

Source: Preqin Pro

Fig. 8.7: Mezzanine - Largest Fund Managers by Aggregate Capital Raised in the Past 10 Years*

Firm	Headquarters	Total Capital Raised in Past 10 Years ($bn)
HPS Investment Partners	US	22.7
Intermediate Capital Group	UK	16.5
The Goldman Sachs Group	US	16.1
GSO Capital Partners	US	10.8
Crescent Capital Group	US	8.0
Prudential Private Capital	US	5.5
KKR	US	3.9
Park Square Capital	UK	3.6
Onex Falcon	US	3.5
CRG	US	3.2

Source: Preqin Pro

Fig. 8.8: Mezzanine - Largest Fund Managers by Estimated Dry Powder*

Firm	Headquarters	Estimated Dry Powder ($bn)
HPS Investment Partners	US	6.3
Intermediate Capital Group	UK	6.0
The Goldman Sachs Group	US	6.0
Prudential Private Capital	US	2.4
Onex Falcon	US	1.5
Crescent Capital Group	US	1.4
CRG	US	1.2
CAPZA	France	1.1
GSO Capital Partners	US	1.1
EMZ Partners	France	1.0

Source: Preqin Pro

**Includes known separate accounts.*

Fig. 8.9: North America - Largest Fund Managers by Total Capital Raised in the Past 10 Years*

Firm	Headquarters	Total Capital Raised in Past 10 Years ($bn)
Oaktree Capital Management	US	48.6
Ares Management	US	43.6
GSO Capital Partners	US	42.2
The Goldman Sachs Group	US	34.3
HPS Investment Partners	US	33.1
Cerberus Capital Management	US	19.5
Fortress Investment Group	US	17.7
KKR	US	17.3
TPG/Castlelake	US	16.7
3G Capital	US	15.0

Source: Preqin Pro

Fig. 8.10: North America - Largest Fund Managers by Estimated Dry Powder*

Firm	Headquarters	Estimated Dry Powder ($bn)
Oaktree Capital Management	US	19.8
Ares Management	US	15.5
GSO Capital Partners	US	14.7
The Goldman Sachs Group	US	13.7
HPS Investment Partners	US	8.4
Clearlake Capital Group	US	7.0
KKR	US	5.2
Bain Capital Credit	US	4.2
Apollo Global Management	US	3.8
TPG/Castlelake	US	3.7

Source: Preqin Pro

Fig. 8.11: Europe - Largest Fund Managers by Total Capital Raised in the Past 10 Years*

Firm	Headquarters	Total Capital Raised in Past 10 Years ($bn)
Intermediate Capital Group	UK	24.1
Arcmont Asset Management	UK	13.8
Alcentra	UK	12.5
M&G Investments	UK	10.7
Hayfin Capital Management	UK	10.2
Amundi Platform of Alternative and Real Assets	France	8.4
Park Square Capital	UK	8.4
Pemberton Capital Advisors	UK	7.9
Permira Debt Managers	UK	6.8
Tikehau Capital	France	6.4

Source: Preqin Pro

**Includes known separate accounts.*

Fig. 8.12: Europe - Largest Fund Managers by Estimated Dry Powder*

Firm	Headquarters	Estimated Dry Powder ($bn)
Intermediate Capital Group	UK	6.2
Alcentra	UK	5.9
Arcmont Asset Management	UK	4.4
Permira Debt Managers	UK	2.8
CVC	UK	2.5
CAPZA	France	2.2
Bridgepoint	UK	1.9
Ardian	France	1.7
Park Square Capital	UK	1.7
Pemberton Capital Advisors	UK	1.7

Source: Preqin Pro

Fig. 8.13: Asia & Rest of World - Largest Fund Managers by Total Capital Raised in the Past 10 Years*

Firm	Headquarters	Total Capital Raised in Past 10 Years ($bn)
PAG	Hong Kong SAR - China	8.7
Ares SSG	Hong Kong SAR - China	6.9
CPE Funds Management	China**	2.8
Edelweiss Alternative Asset Advisors	India	2.8
CDH Investment	China**	2.3
IMM Investment	South Korea	1.8
Heungkuk Asset Management	South Korea	1.7
Grupo Financiero Credit Suisse (Mexico), S.A. de C.V.	Mexico	1.6
Zhongchen Fund Management	China**	1.6
China Merchants Capital	China**	1.5

Source: Preqin Pro

Fig. 8.14: Asia & Rest of World - Largest Fund Managers by Estimated Dry Powder*

Firm	Headquarters	Estimated Dry Powder ($bn)
PAG	Hong Kong SAR - China	2.8
Ares SSG	Hong Kong SAR - China	2.4
Edelweiss Alternative Asset Advisors	India	1.1
Kotak Investment Advisors	India	0.8
OCP Asia	Hong Kong SAR - China	0.6
ADM Capital	Hong Kong SAR - China	0.5
Heungkuk Asset Management	South Korea	0.5
IMM Investment	South Korea	0.5
Dominus Investment	South Korea	0.4
Yuexiu Industrial Investment Funds Management	China**	0.4

Source: Preqin Pro

**Includes known separate accounts.*
***Excluding Hong Kong.*

Largest Funds

Fig. 8.15: Largest Private Debt Funds Closed in 2020

Fund	Firm	Fund Size (bn)	Fund Type	Geographic Focus	Final Close Date
HPS Mezzanine Partners 2019	HPS Investment Partners	11.0 USD	Mezzanine	North America	Oct-20
Clearlake Capital Partners VI	Clearlake Capital Group	7.0 USD	Special Situations	North America	Apr-20
GSO European Senior Debt Fund II	GSO Capital Partners	6.1 USD	Direct Lending	Europe	Feb-20
Permira Credit Solutions Fund IV	Permira Debt Managers	3.4 EUR	Direct Lending	Europe	Mar-20
Ares Special Opportunities Fund	Ares Management	3.5 USD	Special Situations	North America	Jun-20
Bain Capital Distressed & Special Situations 2019	Bain Capital Credit	3.2 USD	Distressed Debt	North America	Jun-20
Antares Senior Loan	Antares Capital	3.0 USD	Direct Lending	North America	Sep-20
Monarch Capital Partners V	Monarch Alternative Capital	3.0 USD	Distressed Debt	North America	Dec-20
KKR Dislocation Fund	KKR	2.8 USD	Distressed Debt	Europe	May-20
PGIM Capital Partners VI	Prudential Private Capital	2.2 USD	Mezzanine	North America	Dec-20

Source: Preqin Pro

Fig. 8.16: Largest Direct Lending Funds Closed in 2020

Fund	Firm	Fund Size (bn)	Fund Type	Geographic Focus	Final Close Date
GSO European Senior Debt Fund II	GSO Capital Partners	6.1 USD	Direct Lending	Europe	Feb-20
Permira Credit Solutions Fund IV	Permira Debt Managers	3.4 EUR	Direct Lending	Europe	Mar-20
Antares Senior Loan	Antares Capital	3.0 USD	Direct Lending	North America	Sep-20
Blue Ocean Fund	EnTrust Global	2.1 USD	Direct Lending	Europe	Dec-20
Churchill Middle Market Senior Loan Fund II	Churchill Asset Management	2.0 USD	Direct Lending	US	Mar-20

Source: Preqin Pro

Fig. 8.17: Largest Distressed Debt Funds Closed in 2020

Fund	Firm	Fund Size (bn)	Fund Type	Geographic Focus	Final Close Date
Bain Capital Distressed & Special Situations 2019	Bain Capital Credit	3.2 USD	Distressed Debt	North America	Jun-20
Monarch Capital Partners V	Monarch Alternative Capital	3.0 USD	Distressed Debt	North America	Dec-20
KKR Dislocation Fund	KKR	2.8 USD	Distressed Debt	Europe	May-20
Arrow Credit Opportunities	AGG Capital Management	1.7 EUR	Distressed Debt	Europe	Nov-20
Varde Dislocation Fund	Värde Partners	1.6 USD	Distressed Debt	North America	Nov-20

Source: Preqin Pro

Fig. 8.18: Largest Mezzanine Funds Closed in 2020

Fund	Firm	Fund Size (bn)	Fund Type	Geographic Focus	Final Close Date
HPS Mezzanine Partners 2019	HPS Investment Partners	11.0 USD	Mezzanine	North America	Oct-20
PGIM Capital Partners VI	Prudential Private Capital	2.2 USD	Mezzanine	North America	Dec-20
Falcon Private Credit Opportunities VI	Onex Falcon	1.3 USD	Mezzanine	North America	Dec-20
EMZ 9	EMZ Partners	1.0 EUR	Mezzanine	Europe	Mar-20
ICG Europe Mid-Market Fund	ICG	1.0 EUR	Mezzanine	Europe	Jan-20

Source: Preqin Pro

Top Performers

Fig. 8.19: Top Performing Private Debt Funds by Net IRR (Vintages 2007-2017)

Rank	Fund	Firm	Vintage	Fund Size (mn)	Fund Type	Geographic Focus	Net IRR (%)	Date Reported
1	Wazee Street Opportunities Fund	Wazee Street Capital Management	2012	15 USD	Distressed Debt	North America	156.4	Sep-20
2	HoldCo Distressed Fund III	HoldCo Asset Management	2011	6 USD	Special Situations	North America	70.7	Sep-20
3	Wazee Street/FFT Managed Account	Wazee Street Capital Management	2011	5 USD	Distressed Debt	North America	57.6	Sep-20
4	Courage Credit Opportunities Fund I	Courage Capital Management	2009	80 USD	Distressed Debt	North America	54.9	Sep-20
5	MNC Partners	Merced Capital	2009	76 USD	Special Situations	North America	43.5	Sep-20
6	Phillion II	Ion Pacific	2016	20 USD	Venture Debt	Middle East & Israel	43.0	Jun-20
7	Clearlake Capital Partners III	Clearlake Capital Group	2012	785 USD	Special Situations	North America	41.1	Dec-19
8	Clearlake Capital Partners IV	Clearlake Capital Group	2015	1,380 USD	Special Situations	North America	31.7	Mar-20
9	Northcreek Mezzanine Fund I	Northcreek Mezzanine	2010	65 USD	Mezzanine	North America	30.8	Mar-18
10	Accel-KKR Growth Capital Partners	Accel-KKR	2011	155 USD	Mezzanine	North America	29.3	Mar-20
11	CGC Royalty Investments II	Cypress Growth Capital	2014	40 USD	Venture Debt	North America	28.5	Mar-18
12	Apollo Credit Opportunities Fund I	Apollo Global Management	2008	1,500 USD	Direct Lending - Senior Debt	North America	27.4	Mar-20
13	SaaS Capital Fund I	SaaS Capital	2012	23 USD	Direct Lending - Senior Debt	North America	27.0	Sep-19
14	Permira Sigma 2	Permira Debt Managers	2012	30 EUR	Private Debt Fund of Funds	Europe	26.9	Sep-20
15	Energy Special Situations Fund II	Energy Special Situations Funds	2009	225 USD	Special Situations	North America	26.1	Sep-20
16	Stellex Capital Partners	Stellex Capital Management	2014	870 USD	Distressed Debt	North America	25.9	Mar-20
17	VSS Structured Capital II	Veronis Suhler Stevenson	2009	312 USD	Mezzanine	North America	25.5	Mar-20
18	Peak Rock Capital Fund	Peak Rock Capital	2013	700 USD	Special Situations	North America	25.1	Mar-20
19	CGC Royalty Investments I	Cypress Growth Capital	2011	27 USD	Venture Debt	North America	24.6	Mar-18
20	ICG Minority Partners Fund 2008	Intermediate Capital Group	2008	116 EUR	Mezzanine	Europe	24.4	Sep-20

Source: Preqin Pro. Data as of December 2020

Fig. 8.20: Most Consistent Top Performing Private Debt Fund Managers (All Vintages)

Rank	Firm	Headquarters	Overall No. of Funds with Quartile Ranking	No. of Funds in Top Quartile	No. of Funds in Second Quartile	Average Quartile Rank
1	Northern Arc Investments	India	5	5	0	1.00
2	GoldenTree Asset Management	US	3	3	0	1.00
=	Inveready Asset Management	Spain	3	3	0	1.00
=	Merion	US	3	3	0	1.00
=	Veronis Suhler Stevenson	US	3	3	0	1.00
6	Metropolitan Partners Group	US	5	4	1	1.20
7	Strategic Value Partners	US	4	3	1	1.25
8	ABRY Partners	US	6	4	2	1.33
9	AnaCap Financial Partners	UK	3	2	1	1.33
=	Bridgepoint	UK	3	2	1	1.33
=	Kartesia Advisors	Luxembourg	3	2	1	1.33
=	Patriot Capital	US	3	2	1	1.33
13	CAPZA	France	5	3	2	1.40
14	HoldCo Asset Management	US	7	5	1	1.43
15	Wazee Street Capital Management	US	4	3	0	1.50
16	Capitala Group	US	4	2	2	1.50
=	Harbert Management Corporation	US	4	2	2	1.50
=	Marlin Equity Partners	US	4	2	2	1.50
=	Partners for Growth	US	4	2	2	1.50
20	Cerberus Capital Management	US	12	8	2	1.58
21	Clearlake Capital Group	US	5	4	0	1.60
22	Fortress Investment Group	US	5	3	1	1.60
23	CarVal Investors	US	5	2	3	1.60
24	Golub Capital	US	9	6	1	1.67
25	Centerfield Capital Partners	US	3	2	0	1.67
=	Peak Rock Capital	US	3	2	0	1.67
27	Caltius Capital Management	US	3	1	2	1.67
=	Freedom 3 Capital	US	3	1	2	1.67
=	Oak Hill Advisors	US	3	1	2	1.67
=	Tikehau Capital	France	3	1	2	1.67
31	ICG	UK	15	7	6	1.73
32	Plexus Capital	US	4	3	0	1.75
33	Monarch Alternative Capital	US	4	2	1	1.75
34	Indigo Capital	France	4	1	3	1.75
=	MHR Fund Management	US	4	1	3	1.75
=	TA Associates	US	4	1	3	1.75
37	CDH Investment	China	5	2	2	1.80
38	Anchorage Capital Group	US	5	1	4	1.80
39	HPS Investment Partners	US	7	2	4	1.86
40	Monroe Capital	US	8	2	5	1.88

Source: Preqin Pro

Largest Investors

Fig. 8.21: Largest Investors in Private Debt by Location

Region	Investor	Allocation to Private Debt ($bn)	Investor Type	Location
Global	AXA Investment Managers	25.3	Asset Manager	France
	Bayerische Versorgungskammer	17.2	Public Pension Fund	Germany
	Virginia Retirement System	14.0	Public Pension Fund	US
	OMERS	11.3	Public Pension Fund	Canada
	Public Sector Pension Investment Board	10.5	Public Pension Fund	Canada
	Future Fund	9.4	Sovereign Wealth Fund	Australia
	Arizona State Retirement System	8.5	Public Pension Fund	US
	Texas County & District Retirement System	8.3	Public Pension Fund	US
	Teachers' Retirement System of the City of New York	7.7	Public Pension Fund	US
	New York City Employees' Retirement System	6.4	Public Pension Fund	US
North America	Virginia Retirement System	14.0	Public Pension Fund	US
	OMERS	11.3	Public Pension Fund	Canada
	Public Sector Pension Investment Board	10.5	Public Pension Fund	Canada
	Arizona State Retirement System	8.5	Public Pension Fund	US
	Texas County & District Retirement System	8.3	Public Pension Fund	US
Europe	AXA Investment Managers	25.3	Asset Manager	France
	Bayerische Versorgungskammer	17.2	Public Pension Fund	Germany
	BT Pension Scheme	6.1	Private Sector Pension Fund	UK
	BNP Paribas Cardif	5.0	Insurance Company	France
	Universities Superannuation Scheme	4.5	Private Sector Pension Fund	UK
Asia & Rest of World	Future Fund	9.4	Sovereign Wealth Fund	Australia
	Aware Super	5.5	Superannuation Scheme	Australia
	African Development Bank	5.3	Bank	Ivory Coast
	Muang Thai Life Assurance	4.9	Insurance Company	Thailand
	Industrial Development Corporation	4.0	Government Agency	South Africa

Source: Preqin Pro

Fig. 8.22: Largest Investors in Private Debt by Type

Type	Investor	Allocation to Private Debt ($bn)	Location
Fund of Funds Manager	Partners Group	22.0	Switzerland
	StepStone	11.3	US
	Amundi Platform of Alternative and Real Assets	9.9	France
	Ardian	6.8	France
	Golding Capital Partners	3.9	Germany
Insurance Company	BNP Paribas Cardif	5.0	France
	Muang Thai Life Assurance	4.9	Thailand
	Liberty Group	3.2	South Africa
	Eurovita Assicurazioni	2.2	Italy
	Ilmarinen Mutual Pension Insurance Company	1.8	Finland
Private Sector Pension Fund	BT Pension Scheme	6.1	UK
	Universities Superannuation Scheme	4.5	UK
	Pension Protection Fund	4.3	UK
	Lloyds Banking Group Pension Schemes	4.2	UK
	BVV	4.0	Germany
Public Pension Fund	Bayerische Versorgungskammer	17.2	Germany
	Virginia Retirement System	11.8	US
	OMERS	11.3	Canada
	Public Sector Pension Investment Board	10.5	Canada
	Arizona State Retirement System	8.5	US
Private Wealth	SCS Financial - Private Client Group	1.6	US
	BMO Family Office	1.2	US
	Medley Partners	0.8	US
	Cazenove Capital Management	0.7	UK
	Chang'An International Trust	0.7	China

Source: Preqin Pro

Notable Deals

Fig. 8.23: Notable Private Debt-Backed Deals in 2020

Portfolio Company	Investment Type	Deal Status	Investor(s)	Location	Industry	Debt Size (mn)	Deal Date
The Hertz Corporation	Senior Debt	Completed	Apollo Global Management	US	Transportation Services	4,000 USD	Nov-20
The Ardonagh Group Limited	Unitranche	Completed	HPS Investment Partners, Caisse de dépôt et placement du Québec, Ares Management, KKR	Jersey	Insurance	1,875 GBP	Jun-20
ProAmpac Holdings Inc.	Senior Debt	Completed	Antares Capital	US	Industrials	1,665 USD	Nov-20
Diligent Corporation	Unitranche	Completed	Churchill Asset Management	US	Information Technology	1,300 USD	Aug-20
LATAM Airlines Group S.A.	Junior/ Subordinated	Announced	Oaktree Capital Management	Chile	Transportation Services	1,300 USD	Jul-20
Pathway Vet Alliance LLC	Unitranche	Completed	Ares Management	US	Healthcare	1,280 USD	Mar-20
Bullhorn, Inc.	Unitranche	Announced	Golub Capital, Churchill Asset Management	US	Software	940 USD	Sep-20
Marston Holdings Limited	Unitranche	Completed	Alcentra, Arcmont Asset Management	UK	Financial Services	650 GBP	Jan-20
ForeScout Technologies, Inc.	Senior Debt	Completed	Owl Rock Capital Partners	US	Information Technology	440 USD	Feb-20
Schülke & Mayr GmbH	Unitranche	Completed	HPS Investment Partners	Germany	Chemicals	405 EUR	Apr-20

Source: Preqin Pro

Fig. 8.24: Notable Private Debt-Backed Deals in 2020 - North America

Portfolio Company	Investment Type	Deal Status	Investor(s)	Location	Industry	Debt Size (mn)	Deal Date
MFA Financial, Inc.	Senior Debt	Completed	Apollo Global Management, Barclays, Athene USA Corporation	US	Financial & Insurance Services	2,150 USD	Jun-20
MRI Software LLC	Unitranche	Completed	Golub Capital, Antares Capital	US	Information Technology	1,600 USD	Jan-20
Galway Insurance Holdings	Senior Debt	Announced	Antares Capital	US	Financial & Insurance Services	1,400 USD	Dec-20
Instructure, Inc.	Senior Debt	Completed	Golub Capital	US	Information Technology	825 USD	Feb-20
NuStar Energy L.P.	Junior/ Subordinated	Announced	Oaktree Capital Management	US	Energy & Utilities	750 USD	Apr-20

Source: Preqin Pro

Fig. 8.25: Notable Private Debt-Backed Deals in 2020 - Europe

Portfolio Company	Investment Type	Deal Status	Investor(s)	Location	Industry	Debt Size (mn)	Deal Date
LivaNova PLC	Senior Debt	Completed	Ares Management	UK	Healthcare	450 USD	Jun-20
TSG Group	Unitranche	Announced	ICG	France	Business Services	280 EUR	Jun-20
Consolis Rail	Unitranche	Completed	Hayfin Capital Management	France	Industrials	120 EUR	Dec-20
Sabio Ltd.	Unitranche	Completed	CVC	UK	Information Technology	117 GBP	Jan-20
FRA Group	Senior Debt	Completed	Barings	UK	Financial & Insurance Services	100 GBP	Mar-20

Source: Preqin Pro

Fig. 8.26: Notable Private Debt-Backed Deals in 2020 - Asia & Rest of World

Portfolio Company	Investment Type	Deal Status	Investor(s)	Location	Industry	Debt Size (mn)	Deal Date
SF Express	Mezzanine	Completed	CDH Investment	China	Consumer Services	300 USD	Mar-20
Summit Power International Limited	Senior Debt	Completed	Pierfront Capital Fund Management	Singapore	Energy & Utilities	140 USD	May-20
China Youran Diary Holding Ltd.	Mezzanine	Completed	Bain Capital	China	Consumer Discretionary	75 USD	Dec-20
Arzyz, SA de CV	Unknown	Completed	Inter-American Investment Corporation	Mexico	Raw Materials & Natural Resources	67 USD	Jun-20
Modern Transporte Aéreo de Carga S.A.	Mezzanine	Completed	H.I.G. Capital	Brazil	Logistics & Distribution	65 USD	Apr-20

Source: Preqin Pro

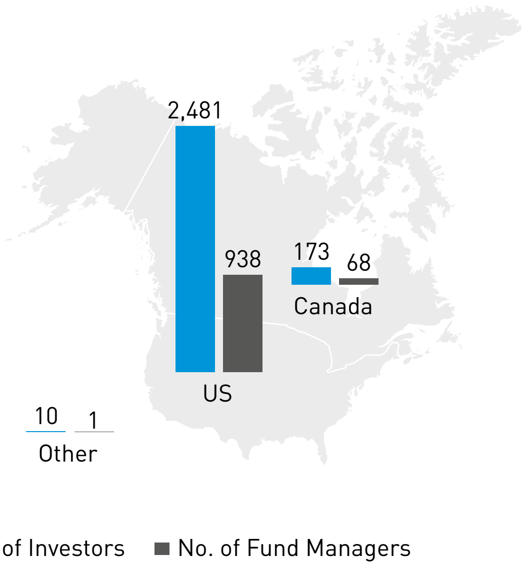
9

Regions

North America

2,664
No. of investors

1,007
No. of fund managers

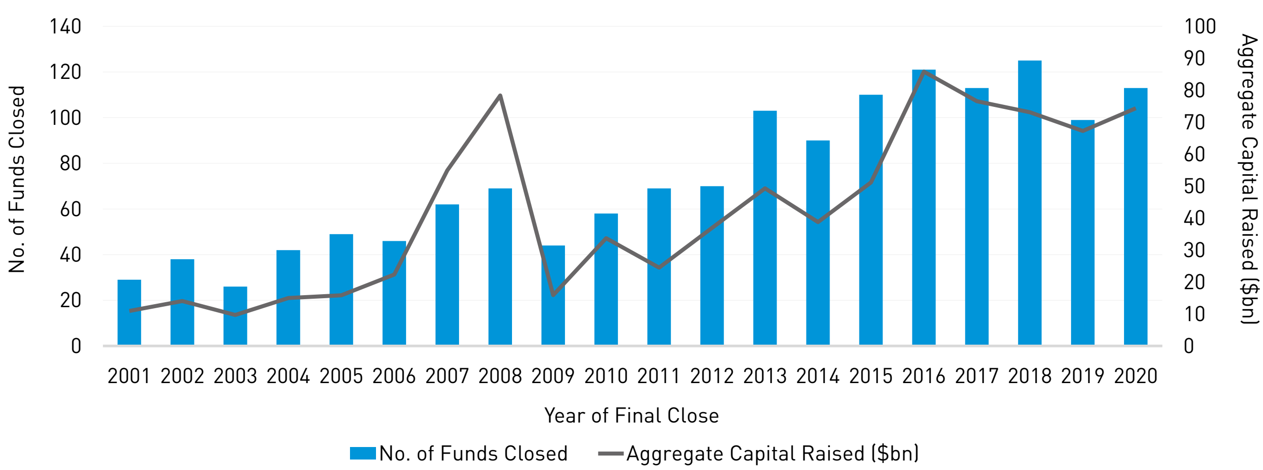


North America-Focused Private Debt Funds in Market (As of January 2021)

317
Funds in market

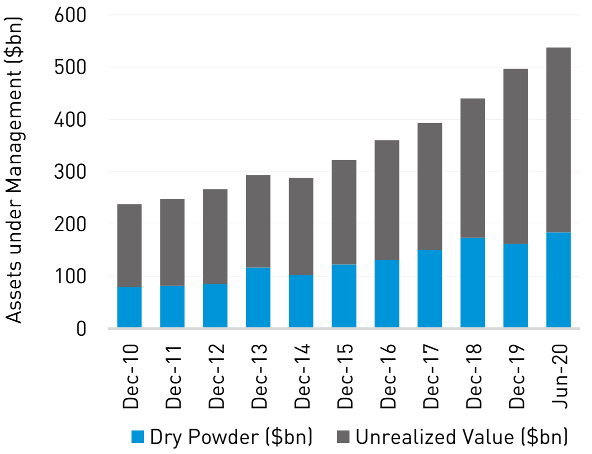
$168bn
Aggregate capital targeted

Fig. 9.1: North America-Focused Private Debt Fundraising, 2001 - 2020



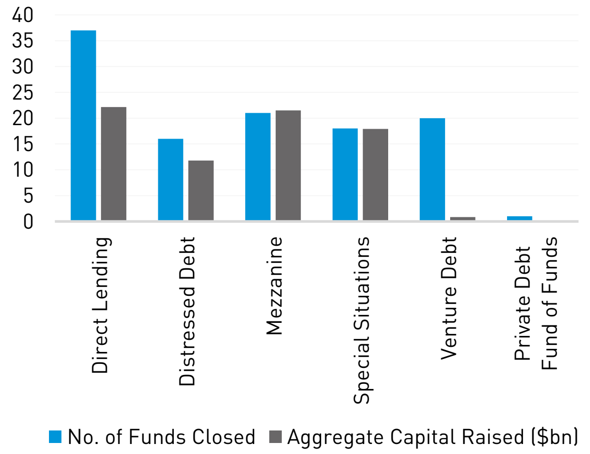
Source: Preqin Pro

Fig. 9.2: North America-Focused Private Debt Assets under Management, 2010 - 2020



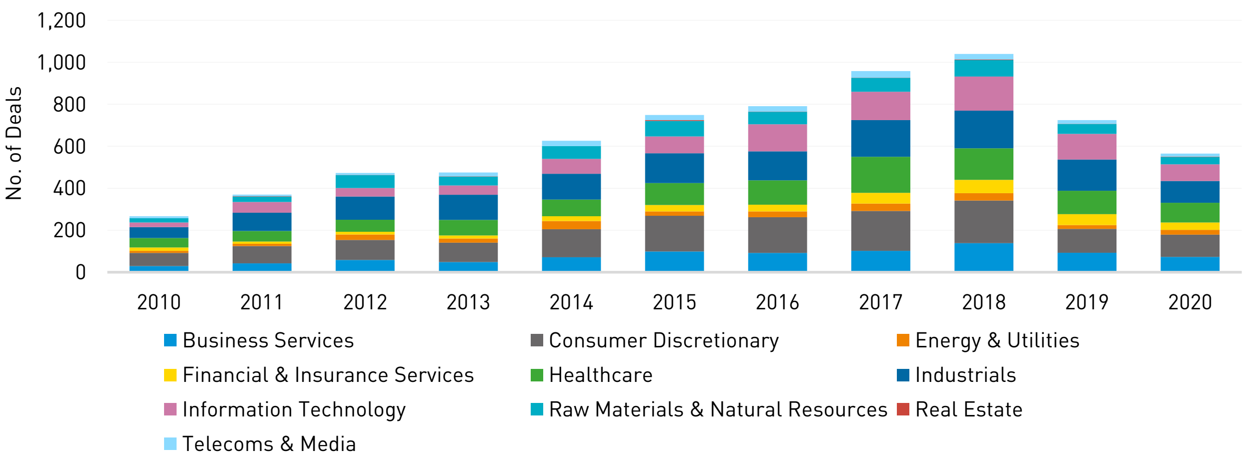
Source: Preqin Pro

Fig. 9.3: North America-Focused Private Debt Fundraising in 2020 by Fund Type



Source: Preqin Pro

Fig. 9.4: Number of Private Debt-Backed Deals in North America by Primary Industry, 2010 - 2020



Source: Preqin Pro

Fig. 9.5: Largest North America-Focused Private Debt Funds Closed in 2020

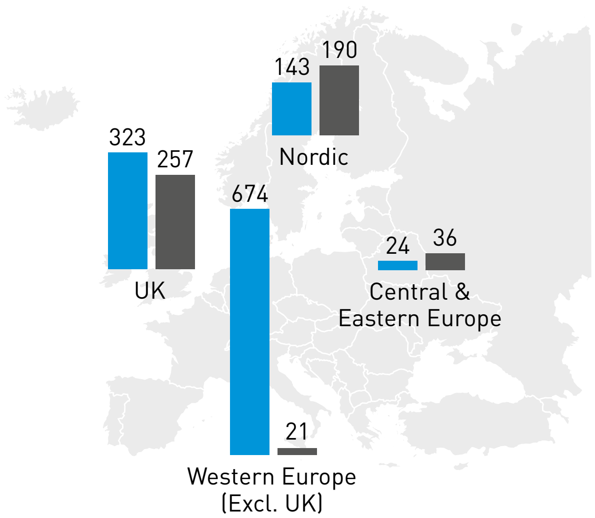
Fund	Firm	Headquarters	Fund Size (mn)	Fund Type	Final Close Date
HPS Mezzanine Partners 2019	HPS Investment Partners	New York, US	11,000 USD	Mezzanine	Oct-20
Clearlake Capital Partners VI	Clearlake Capital Group	Santa Monica, US	7,000 USD	Special Situations	Apr-20
Ares Special Opportunities Fund	Ares Management	Los Angeles, US	3,500 USD	Special Situations	Jun-20
Bain Capital Distressed & Special Situations 2019	Bain Capital Credit	Boston, US	3,200 USD	Distressed Debt	Jun-20
Antares Senior Loan	Antares Capital	Chicago, US	3,000 USD	Direct Lending	Sep-20

Source: Preqin Pro

Europe

1,164
No. of investors

504
No. of fund managers

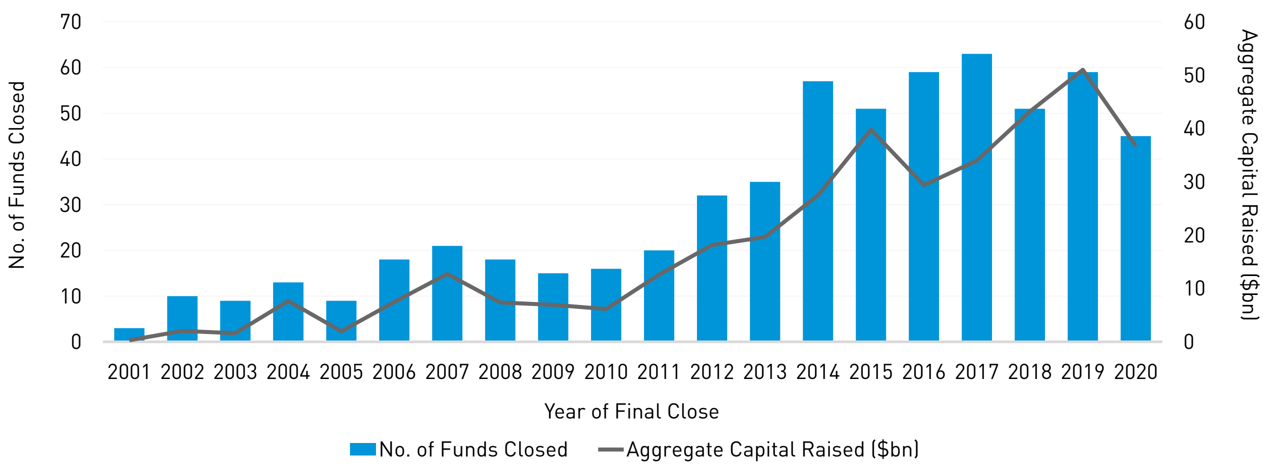


Europe-Focused Private Debt Funds in Market (As of January 2021)

132
Funds in market

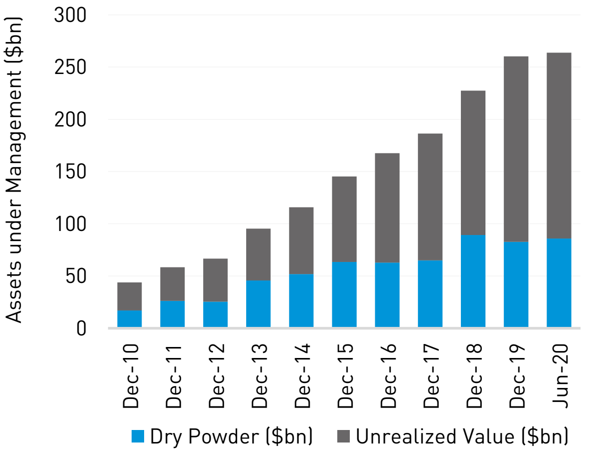
$98bn
Aggregate capital targeted

Fig. 9.6: Europe-Focused Private Debt Fundraising, 2001 - 2020



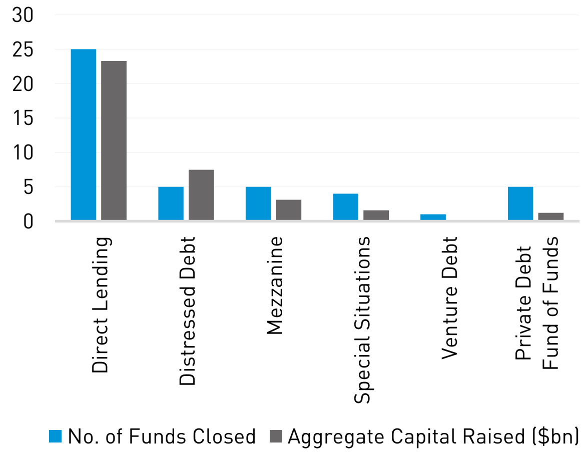
Source: Preqin Pro

Fig. 9.7: Europe-Focused Private Debt Assets under Management, 2010 - 2020



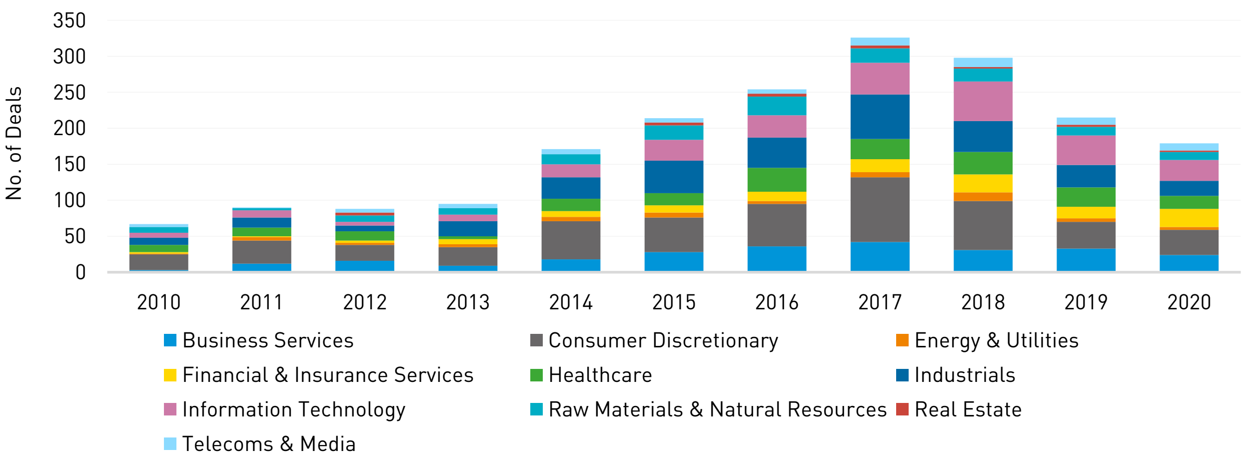
Source: Preqin Pro

Fig. 9.8: Europe-Focused Private Debt Fundraising in 2020 by Fund Type



Source: Preqin Pro

Fig. 9.9: Number of Private Debt-Backed Deals in Europe by Primary Industry, 2010 - 2020



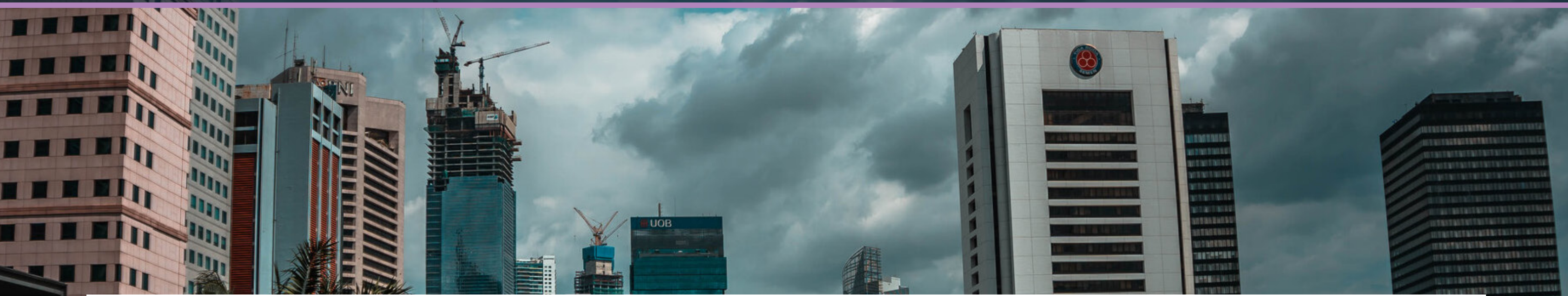
Source: Preqin Pro

Fig. 9.10: Largest Europe-Focused Private Debt Funds Closed in 2020

Fund	Firm	Headquarters	Fund Size (mn)	Fund Type	Final Close Date
GSO European Senior Debt Fund II	Blackstone Group	New York, US	6,102 USD	Direct Lending	Feb-20
Permira Credit Solutions Fund IV	Permira Debt Managers	London, UK	3,400 EUR	Direct Lending	Mar-20
KKR Dislocation Fund	KKR	New York, US	2,800 USD	Distressed Debt	May-20
Blue Ocean Fund	EnTrust Global	New York, US	2,100 USD	Direct Lending	Dec-20
Arrow Credit Opportunities	AGG Capital Management	Manchester, UK	1,700 EUR	Distressed Debt	Nov-20

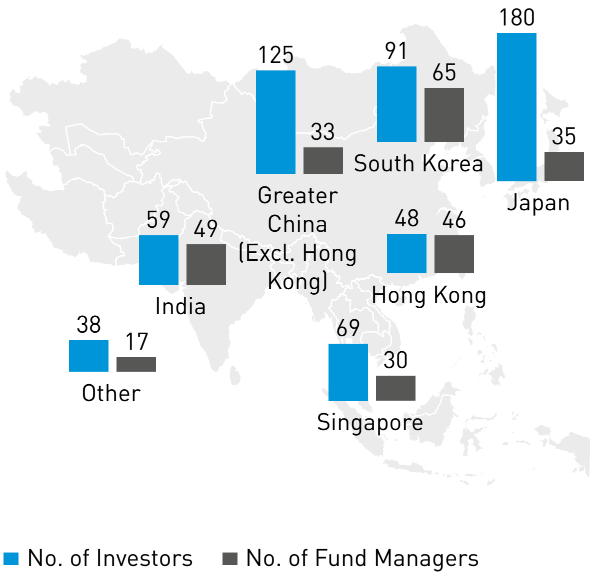
Source: Preqin Pro

Asia



610
No. of investors

275
No. of fund managers

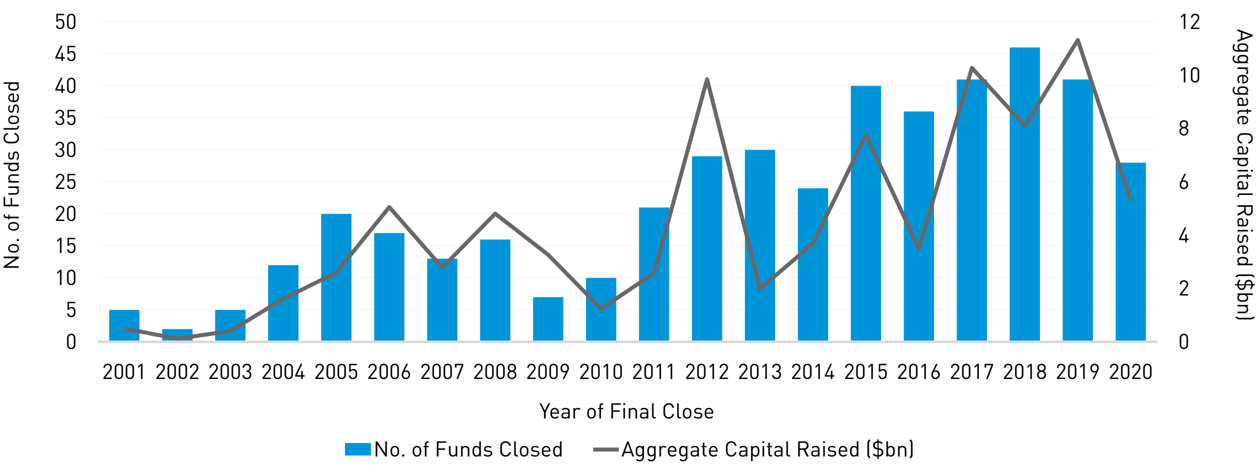


Asia-Focused Private Debt Funds in Market (As of January 2021)

44
Funds in market

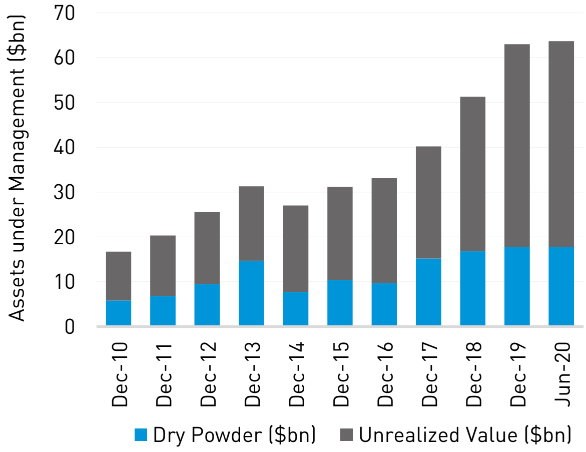
$11bn
Aggregate capital targeted

Fig. 9.11: Asia-Focused Private Debt Fundraising, 2001 - 2020



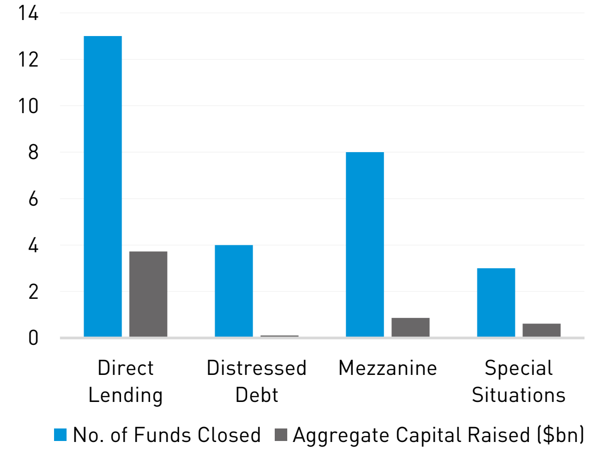
Source: Preqin Pro

Fig. 9.12: Asia-Focused Private Debt Assets under Management, 2010 - 2020



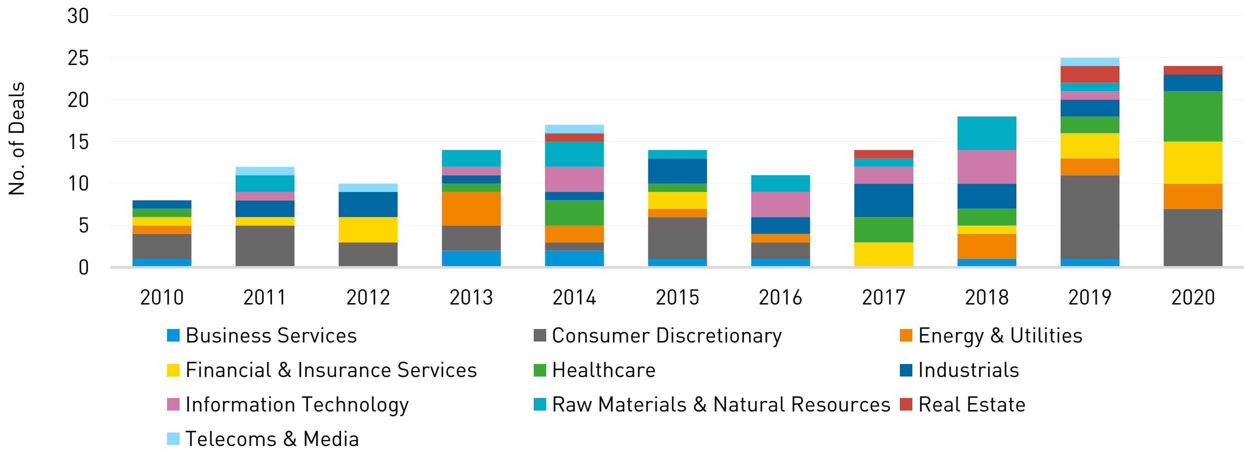
Source: Preqin Pro

Fig. 9.13: Asia-Focused Private Debt Fundraising in 2020 by Fund Type



Source: Preqin Pro

Fig. 9.14: Number of Private Debt-Backed Deals in Asia by Primary Industry, 2010 - 2020



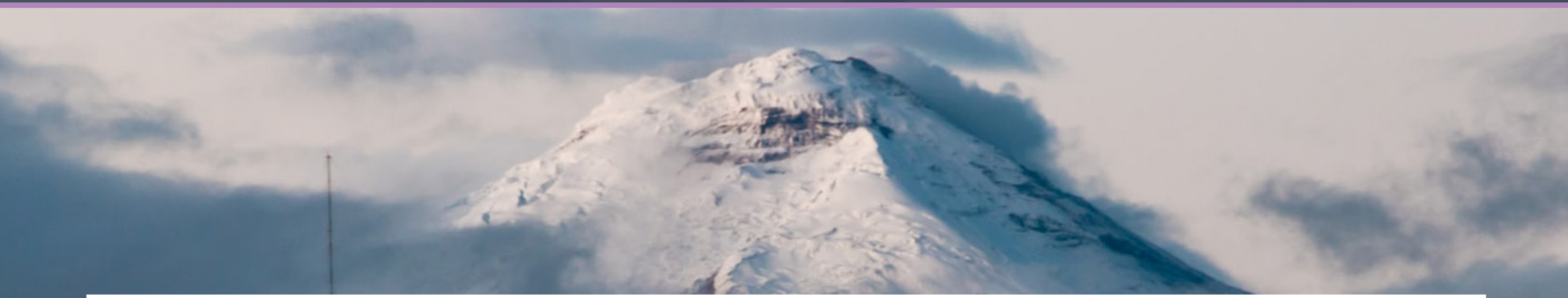
Source: Preqin Pro

Fig. 9.15: Largest Asia-Focused Private Debt Funds Closed in 2020

Fund	Firm	Headquarters	Fund Size (mn)	Fund Type	Final Close Date
PAG Loan Fund IV	PAG	Hong Kong, Hong Kong SAR - China	1,500 USD	Direct Lending	Jun-20
Edelweiss Special Opportunities Fund III	Edelweiss Alternative Asset Advisors	Mumbai, India	900 USD	Direct Lending	Oct-20
DCL Investments Special Situation RMB Fund III	DCL Investments	Beijing, China	3,000 RMB	Special Situations	Nov-20
PICC Yuexiu Greater Bay Area Industrial Fund I	Yuexiu Industrial Investment Funds Management	Guangzhou, China	3,000 RMB	Mezzanine	Mar-20
ADM Limosa Fund	ADM Capital	Hong Kong, Hong Kong SAR - China	420 USD	Direct Lending	Oct-20

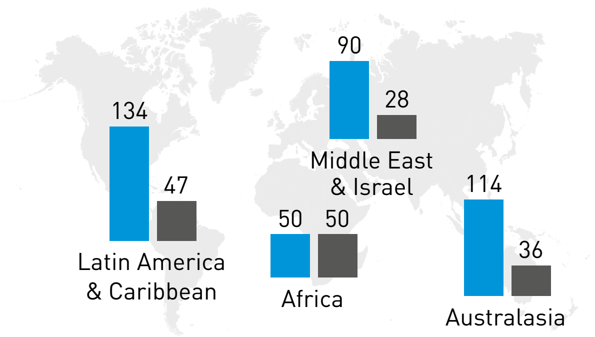
Source: Preqin Pro

Rest of World



388
No. of investors

161
No. of fund managers



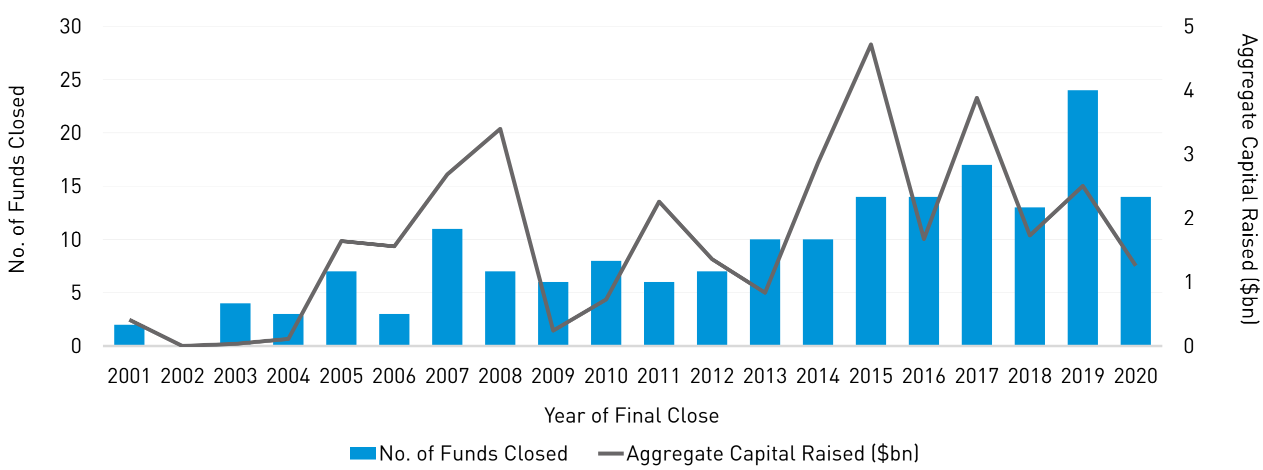
No. of Investors   No. of Fund Managers

Rest of World-Focused Private Debt Funds in Market (As of January 2021)

54
Funds in market

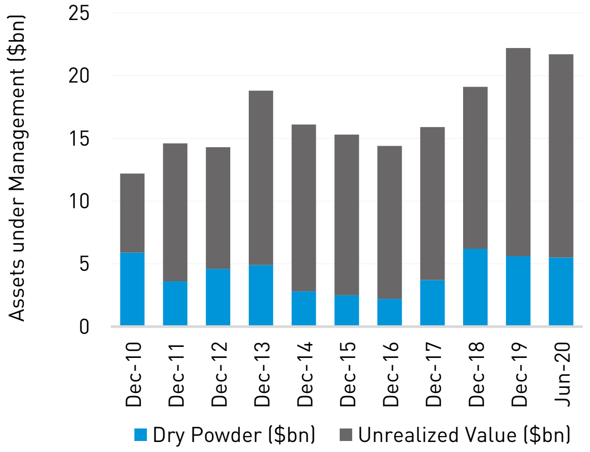
$11bn
Aggregate capital targeted

Fig. 9.16: Rest of World-Focused Private Debt Fundraising, 2001 - 2020



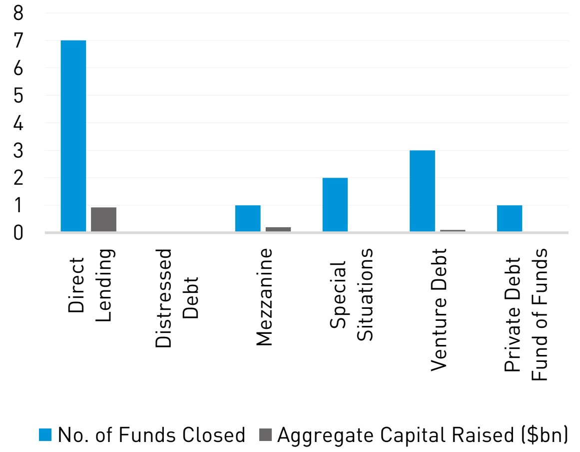
Source: Preqin Pro

Fig. 9.17: Rest of World-Focused Private Debt Assets under Management, 2010 - 2020



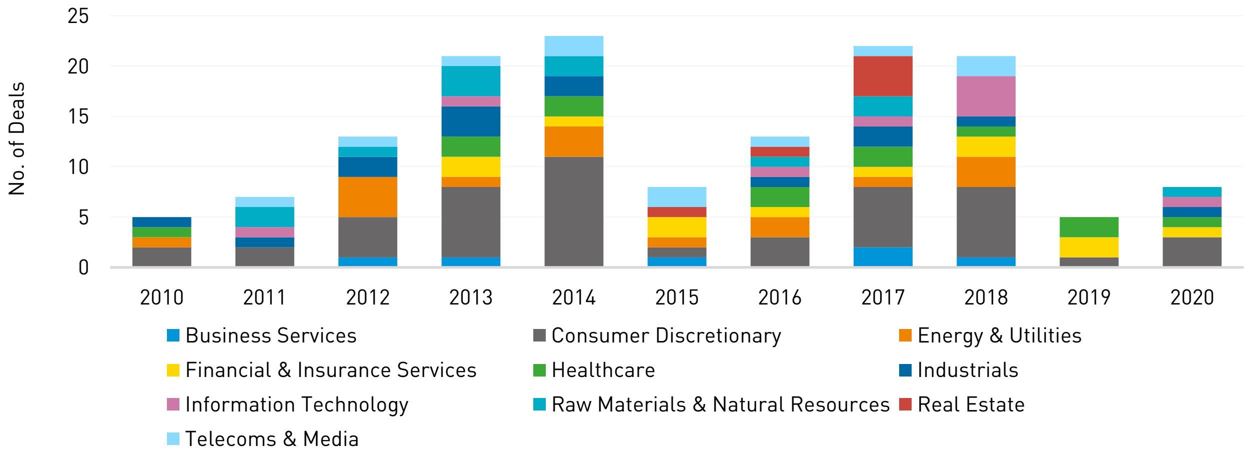
Source: Preqin Pro

Fig. 9.18: Rest of World-Focused Private Debt Fundraising in 2020 by Fund Type



Source: Preqin Pro

Fig. 9.19: Number of Private Debt-Backed Deals in Rest of World by Primary Industry, 2010 - 2020



Source: Preqin Pro

Fig. 9.20: Largest Rest of World-Focused Private Debt Funds Closed in 2020

Fund	Firm	Headquarters	Fund Size (mn)	Fund Type	Final Close Date
NN-FMO Emerging Markets Loan	NN Investment Partners	The Hague, Netherlands	397 USD	Direct Lending	Mar-20
Blue Like An Orange Sustainable Capital Latin America Fund I	Blue Like An Orange Sustainable Capital	Washington, US	203 USD	Mezzanine	Jun-20
New Mexico Recovery Fund	Sun Mountain Capital	Santa Fe, US	100 USD	Direct Lending	Apr-20
OneVentures Credit Fund	OneVentures	Sydney, Australia	AUD 78	Venture Debt	Jun-21
Latin America Growth Fund	SVB Capital	Menlo Park, US	USD 30	Venture Debt	Jul-21

Source: Preqin Pro

10

Outlook

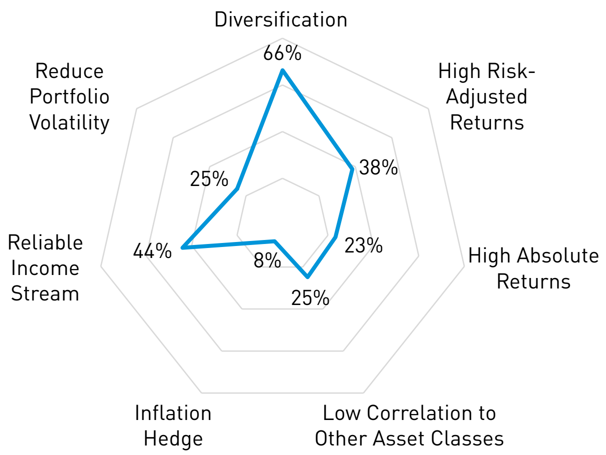
Outlook for Private Debt in 2021

Private debt activity appears stronger than ever and investors are satisfied with their portfolios, but competition is escalating and ESG adoption is lagging

Despite a rocky year, investors were largely pleased with the performance of their private debt portfolios over the past 12 months. Of investors surveyed by Preqin, 83% stated their private debt portfolio's performance had either exceeded or met expectations (Fig. 10.2). Investors expect this trend to continue, with 90% predicting that private debt will perform to the same level or better over 2021 (Fig. 10.3). That said, investors and fund managers do anticipate challenges in the year ahead. These include increased competition for assets, and a weaker emphasis on ESG implementation compared with other asset classes.

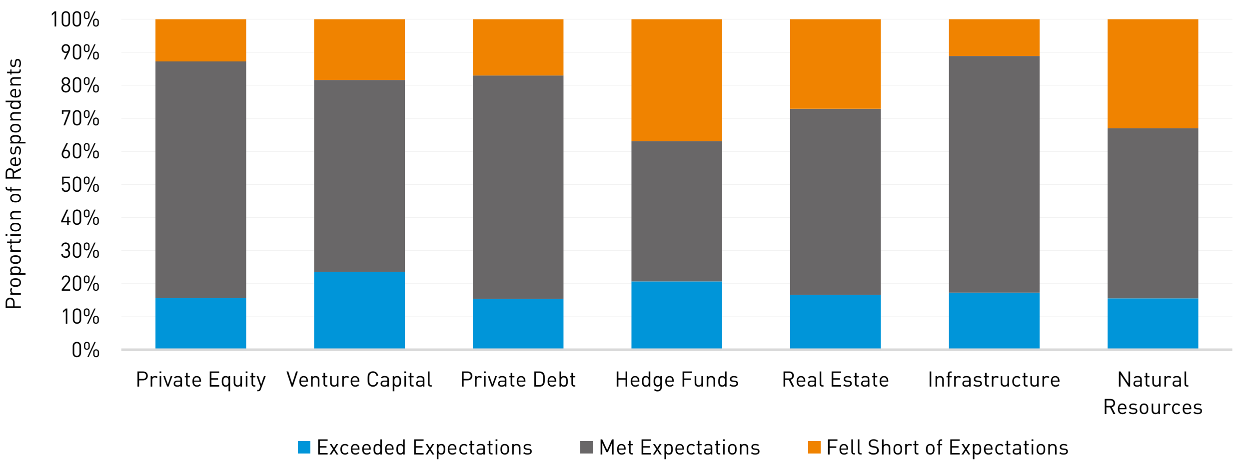
Heading into 2021, competition for assets is a concern for both investors and fund managers; a third of investors and 52% of fund managers believe that attractive opportunities will be more difficult to source due to heightened competition (Fig. 10.4). Of the investors we spoke to, two-thirds told us

Fig. 10.1: Investors' Reasons for Investing in Private Debt



Source: Preqin Investor Survey, November 2020

Fig. 10.2: Investor Views on Alternative Assets Performance over the Past 12 Months Relative to Expectations



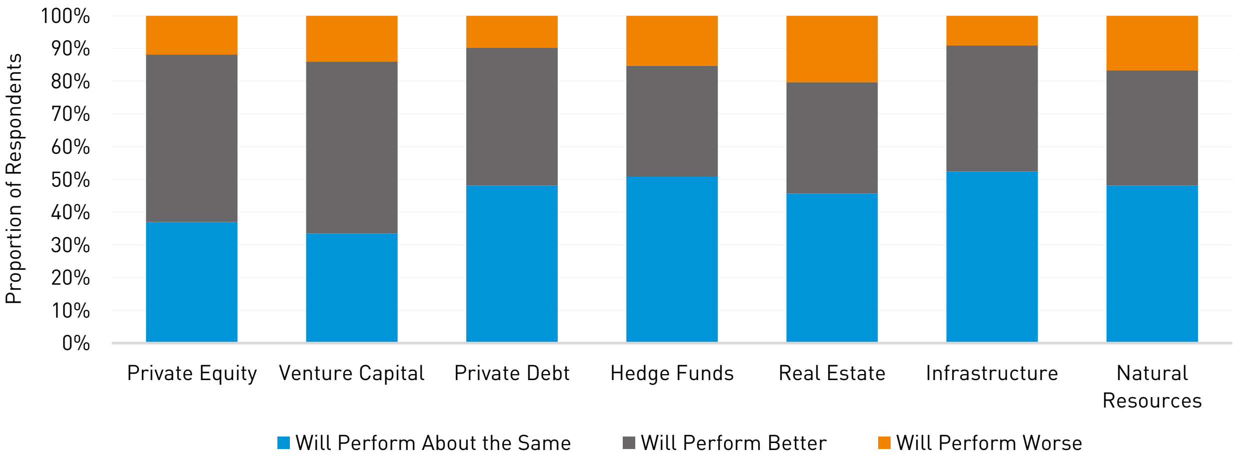
Source: Preqin Investor Survey, November 2020 that diversification was their primary motivation for investing in private debt (Fig. 10.1). Competition is therefore a threat, because a lack of opportunities down the line may hinder their ability to adequately diversify between strategies.

The survey results suggest that competition is largely focused on distressed debt and special situations strategies. Of fund managers surveyed, 65% have seen rising competition for distressed debt over the past 12 months, and 52% for special situations (Fig. 10.5). Market disruption caused by the pandemic has led to high levels of defaults being anticipated around the world, opening up opportunities for such managers. It is therefore of little surprise that distressed debt and special situations were cited by investors as the two fund types that will present the best opportunities over the next 12 months (Fig. 10.9).

Private debt's growth over the past 12 months has not been matched by ESG uptake within the strategy; 38% of investors have an ESG policy in place for private debt – the strategy comes fourth out of the six asset classes Preqin tracks. Moreover, only 11% of private debt fund managers are at the mature stage of the ESG-implementation lifecycle (Fig. 10.11), compared with, for example, 27% of private equity managers.

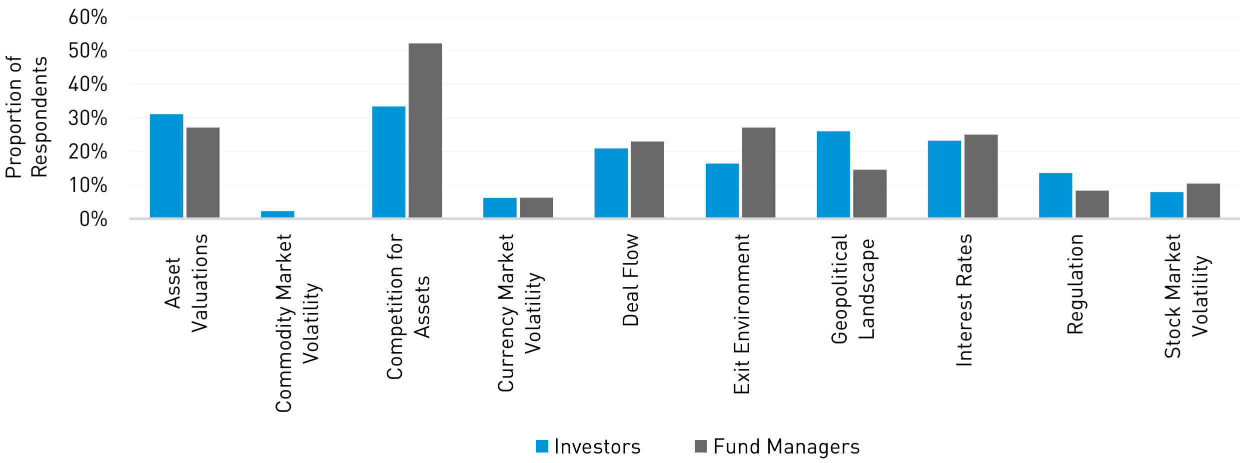
Furthermore, half of surveyed private debt managers do not require portfolio companies to report ESG metrics. A significant 68% cited a lack of quality/consistent ESG data as the main obstacle to successfully implementing an ESG policy. That said, 53% of fund managers have indicated that their ESG

Fig. 10.3: Investor Expectation for Alternative Assets Performance in the Next 12 Months Compared to the Previous 12 Months



Source: Preqin Investor Survey, November 2020

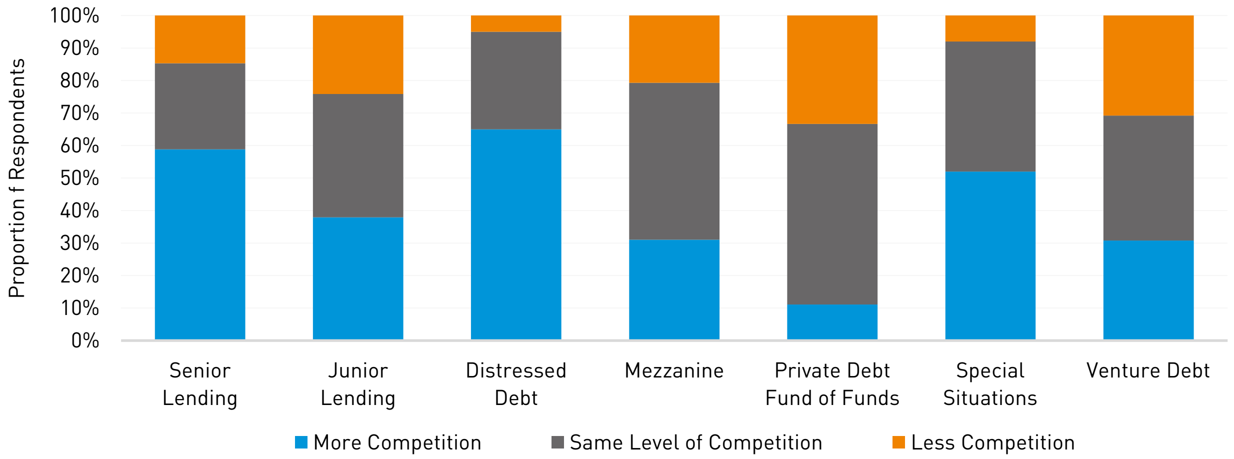
Fig. 10.4: Views on the Key Challenges for Private Debt Return Generation in the Next 12 Months: Investors vs. Fund Managers



Source: Preqin Investor and Fund Manager Surveys, November 2020 implementation is in progress, while just over a quarter of investors plan to have an ESG investment policy in place over the next 12 months.

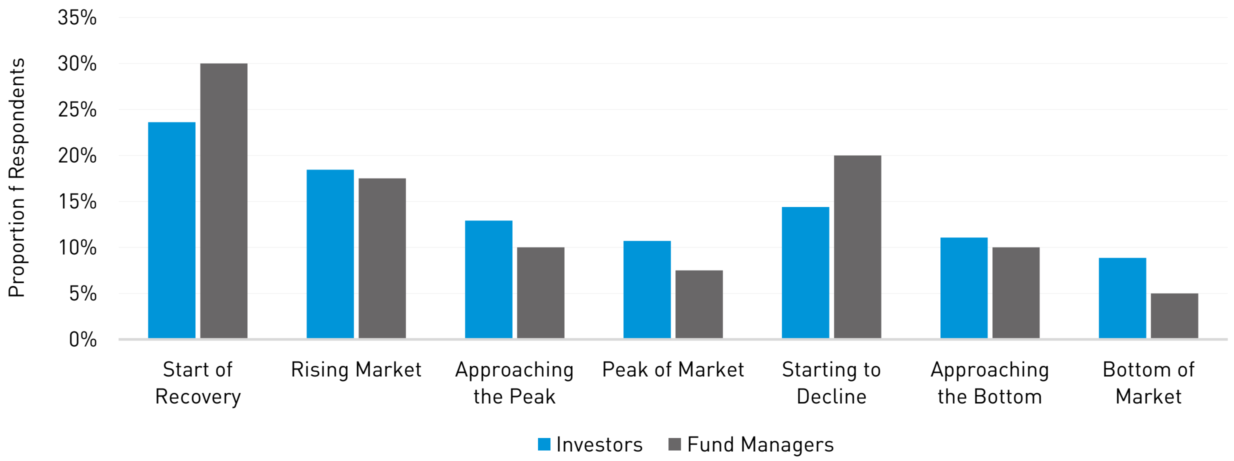
Favorable market conditions and robust investor appetite will likely foster significant industry growth in the near future. Back in November 2020, Preqin predicted that private debt would be one of the fastest-growing alternative asset classes over the next five years, forecasting AUM growth at a CAGR of 11.4% until 2025, to $1.46tn. Indeed, 87% of investors expect to invest more or the same amount of capital in the asset class over the next year, with an even greater 90% planning to increase or maintain their allocations over the longer term. And with 43% of fund managers expecting the spread between high-yield and investment-grade bonds in North America to widen over the next 12 months, opportunities will continue to present themselves.

Fig. 10.5: Fund Manager Views on the Level of Competition for Private Debt Assets Compared with 12 Months Ago by Fund Type



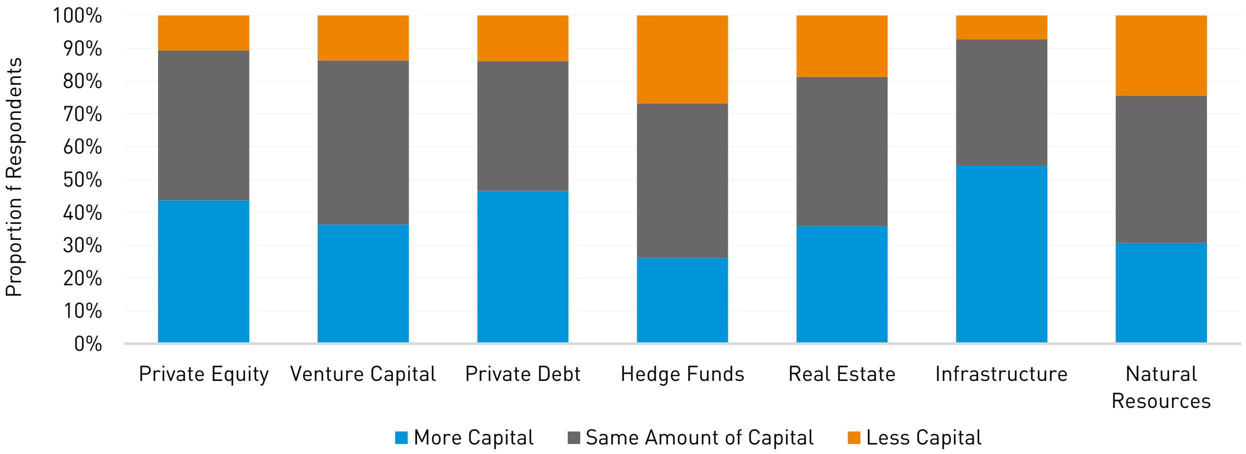
Source: Preqin Fund Manager Survey, November 2020

Fig. 10.6: Views on Where We Are in the Current Private Debt Market Cycle: Investors vs. Fund Managers



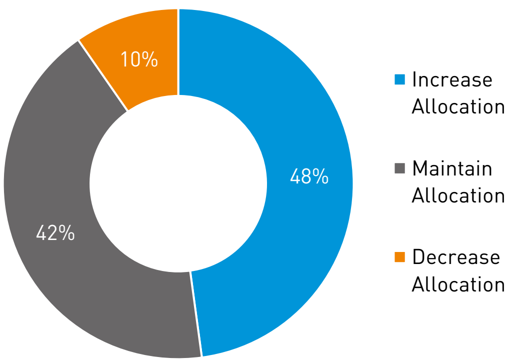
Source: Preqin Investor and Fund Manager Surveys, November 2020

Fig. 10.7: Investors' Expected Capital Commitments to Alternative Assets in the Next 12 Months Compared to the Previous 12 Months



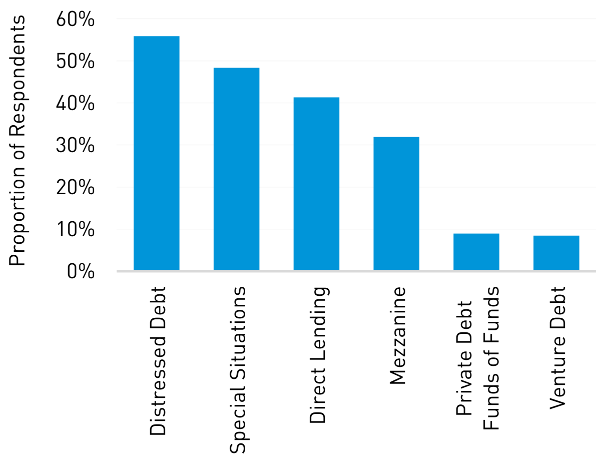
Source: Preqin Investor Survey, November 2020

Fig. 10.8: Investors' Intentions for Their Private Debt Allocations over the Longer Term



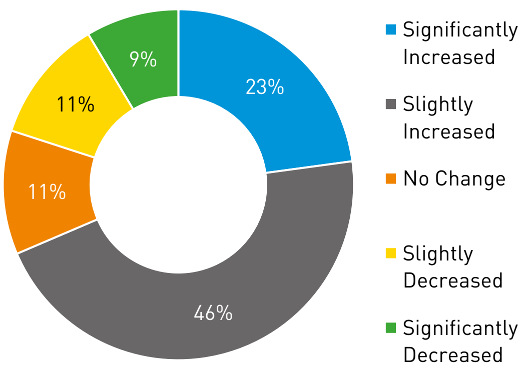
Source: Preqin Investor Survey, November 2020

Fig. 10.9: Private Debt Fund Types that Investors View as Presenting the Best Opportunities in the Next 12 Months



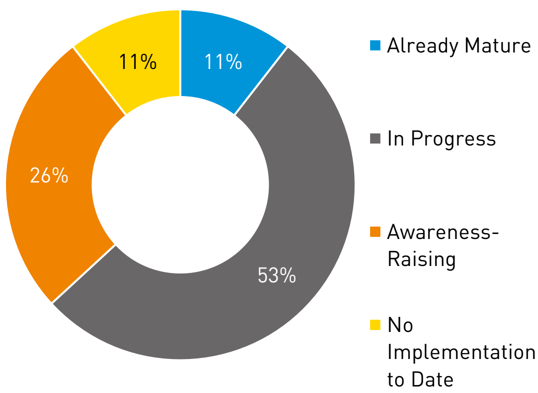
Source: Preqin Investor Survey, November 2020

Fig. 10.10: Fund Manager Views on How Investor Appetite for Private Debt Has Changed over the Past 12 Months



Source: Preqin Fund Manager Survey, November 2020

Fig. 10.11: Fund Manager Views on Where They Are in the ESG-Implementation Lifecycle



Source: Preqin Fund Manager Survey, November 2020

Preqin Predictions

We pick the top five trends that we think will shape the private debt industry in 2021 and beyond

Industry AUM will surpass $1.4tn by 2025

We expect private debt to continue on its upward trajectory over the next five years, as investors and fund managers flock to an increasingly attractive asset class. Our forecast sees private debt AUM surpassing $1.4tn by 2025, at a CAGR of 11.4% (2020-2025).

High-yield to investment-grade bond spreads will widen

Forty-three percent of fund managers surveyed by Preqin expect the spread between high-yield and investment-grade bonds to widen over the next 12 months in North America, increasing the value proposition of private debt investing in the region.

Competition for transactions will intensify

As more and more investors turn to private debt for yield in a low interest rate environment, sourcing attractive opportunities will become increasingly difficult. Diversification will be key for fund managers active in the space.

More capital will flow into special situations and distressed debt

In the ongoing aftermath of the pandemic, the level of defaults will continue to rise over the next 12 months. As a result, surveyed fund managers and investors alike expect special situations and distressed debt to present the best opportunities going forward.

Private debt markets in China and India will grow

The Asian private debt market has continued to grow significantly, and large proportions of investors and fund managers say China and Southeast Asia are the most promising targets for investment in emerging markets.

1 ANREV/INREV/NCREIF Fund Manager Survey 2020. Survey illustrated rankings of 140 fund managers globally by AUM as at 31 Dec 2019.