

CADWALDER

FFF Studios Launch – Live from Miami

February 17, 2023 | Issue No. 211

One of the best things about the FFA Global symposium is the opportunity to see and speak with so many members of the fund finance industry, including our wonderful clients. This year we rolled out a new concept, *Fund Finance Friday Studios*, which are recorded interviews with some of the most exciting and influential players in fund finance. Here are some of those conversations and we look forward to rolling out more of them soon. We thank everyone who participated and look forward to continuing this initiative and to speaking with more of you in the coming weeks and months ahead. Tune in [here](#).

Fund Finance Symposium Panel Recap: Secondaries and Continuations

February 17, 2023 | Issue No. 211



By **Bryan Barreras**
Counsel | Fund Finance

Cadwalader's own fund finance partner Brian Foster moderated one of the four panels focused on NAV financing at this year's Global Symposium, evidencing the growing relevance of NAV products in the fund finance market. The panel, titled "Secondaries and Continuations," brought together a group of industry experts to discuss developments in the Secondaries market and the opportunities and challenges facing that market. The panelists included: Darren Schluter, Managing Director in the Secondary Advisory Group at PJT Park Hill; Linda Rowland, Managing Director in the Ares Secondaries Group; Ray Meyer, Managing Director and the Head of Fund Finance Advisory & Origination at Natixis; Max Forton – Head of Trading for Fund Financing & Solutions in the Americas at Nomura; and Martins Marnauza – Partner at Collier Capital.

The panel noted that there have been a number of developments in the past year that have significantly impacted the Secondaries market generally, and the Secondaries financing market specifically. The fundraising market has become more competitive for private funds, especially so for sponsors without a long-established track record. Increased volatility in public markets has impacted traditional realization events for private funds' holdings (IPOs and M&A transactions) and affected such funds' ability to make distributions. Regulatory capital pressure has resulted in a pull-back on balance sheet deployment by bank lenders. And the rapid rise in interest rates throughout the year has increased the overall cost of NAV financing transactions, affecting a fund's decision whether to utilize financing.

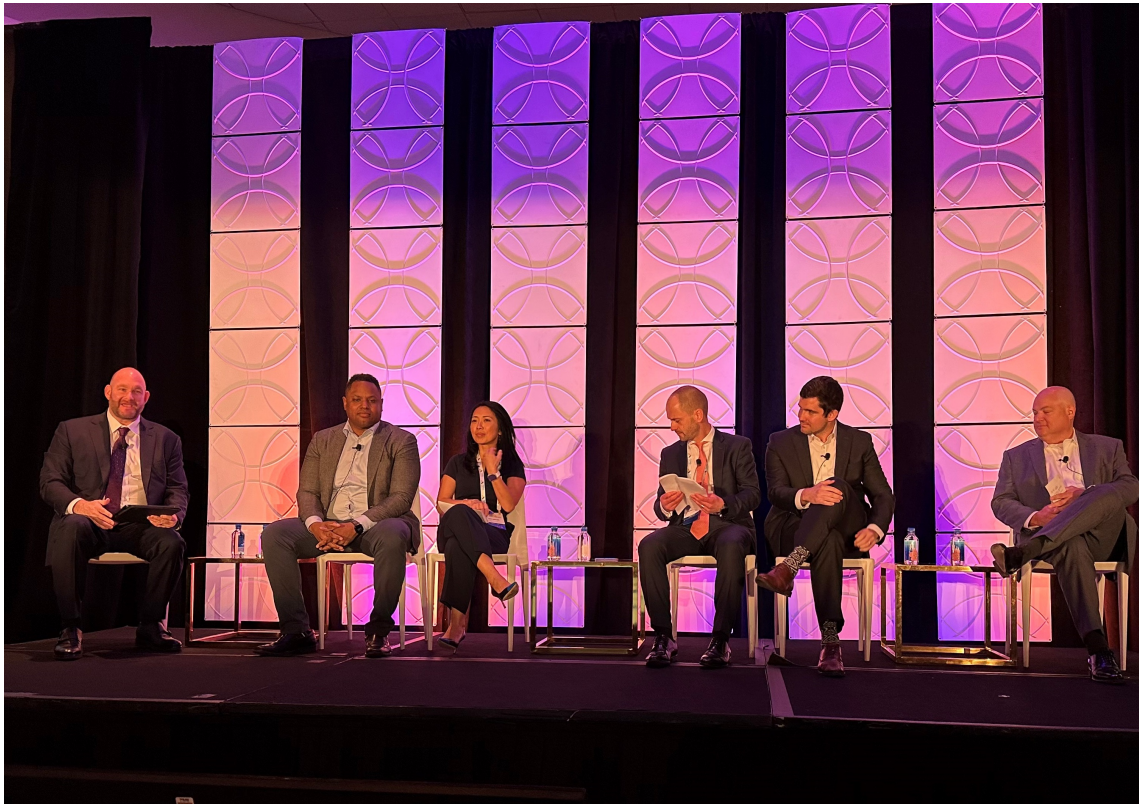
The discussion kicked off with a look at the Secondaries market over the past few years, with a particular focus on liquidity and fundraising. 2020 and COVID brought an accelerating demand for liquidity, but difficulties in valuations and underwriting diversified portfolios led to transactions involving more concentrated portfolios. More recently, there has been an increase in GP-led transactions, and transactions involving more diversified portfolios. Among the different strategies and regions, the panelists noted particular growth in infrastructure and credit during this time, with the bulk of assets in the U.S. The overall market was strong throughout this period, and 2022 continued that trend with over \$100 billion of transactions. Fundraising has also been consistently robust, especially among the larger sponsors with proven track records, and the Secondaries market had in excess of \$100 billion of dry powder entering 2023.

The panel then turned to trends in the financing market related to Secondaries. While financing activity overall has increased over the last few years, 2022 was really three separate markets, beginning with a strong first quarter (carrying over from a strong 2021) that saw an increase of activity and new borrower inquiries. This gave way to a slowing second and third quarter, as we started to see the impact of the developments mentioned above, especially the rise in interest rates. The fourth quarter saw a decrease in new activity, although the market has stabilized so far in 2023. The panelists noted that the lender market has changed considerably over the last two years. Historically, a handful of relationship lenders provided the majority of the Secondaries market financing needs, but as banks have pulled back on their use of balance sheet there have been both (i) new lenders entering the traditional financing market, most notably insurance companies, and (ii) an increased use of new products, such as second lien and mezzanine financing, as fund lenders look for higher returns. With respect to financial terms, LTV levels were noted to be generally stable, with well diversified portfolios seeing a range of 25-50%, whereas pricing has increased "enormously" – even though spreads have not moved dramatically, the increase in the benchmark rate has greatly increased the cost of financing.

As the discussion moved to the uses of financing, and the implications of the higher cost of financing, the sponsor panelists noted that their decision whether to use financing (and at what level to use it) is not predicated solely on the financial terms. They also look to their investors' need for liquidity, the quality of a portfolio (*i.e.*, whether it merits leverage), cash flow forecasts (including the impact of market volatility) and asset valuations/execution prices (which vary depending on strategy). The lender panelists noted that they take many of these same factors into consideration, looking for diversification across industries, stress-testing cash flows to determine whether they would support amortization of the facility, underwriting larger portions of the portfolio and analyzing the impact of continued interest rate increases. The lenders also noted that they take comfort from dealing with sponsors that have a record of achieving exit prices in line with their reported valuations.

The panel ended with a discussion of private credit secondaries, and uniformly described it as a hot topic. One panelist compared the current private credit secondaries market to where the private equity secondaries market was 10 years

ago, noting the level of growth and the increasing duration of vehicles in the space. They also noted that financing in this space has its own set of challenges, from pricing to underwriting, especially if a fund can invest across all types of products (which can range from senior secured unitranche transactions to preferred equity). While noting that there has not been much financing in this space yet, as both the lenders and borrowers work to figure out the product offerings here, the panelists said this has been the source of an oversized amount of interest, with one panelist calling it the “largest, smallest portion of the market.”



Fund Finance Symposium Panel Recap: Governance, Underwriting and Due Diligence

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The panel on governance, underwriting and due diligence featured seasoned bankers Gino De Bernardo (Comerica), Mike Henry (US Bank) and Guy Simpson (Bridge Bank), experienced lawyers Anthony Pirraglia (Loeb & Loeb) and Joe O'Donnell (Morrison Foerster), and accomplished fund professional Mary Jo Sanderson (Värde Partners). The clear takeaway of this session was that strong relationships with sponsors, advance preparation, thorough and extensive due diligence on investors, the limited partnership agreement and side letters, and clear and comprehensive term sheets have proven to be best practices in deal execution of a lending facility to a private equity fund.

All agreed that starting the due diligence process early provides advantages: understanding and rating all the investors and conducting proper due diligence of those investors is the best way to stave off surprises. While the current geopolitical environment created new challenges for funds because the sanctioned persons list had been relatively static for a long time, funds had the tools to quickly identify and remove from the borrowing bases the large increase in sanctioned persons bought on by the Ukrainian crisis. In most cases, the interests of the funds were aligned with lenders. More importantly, this underscored to lenders why it is important for the limited partnership agreement to be clear on issues such as sanctioned investors. In addition, strong agent banks that stayed on top of those emerging and critical issues were important to the syndicate lenders.

The panelists commented that funds are looking to put in lines of credit earlier than those lines were expected to be utilized, and that both the funds and experienced lenders have a good sense of the kind of diligence that will be required. Indeed, the lenders want to be part of the initial process and can often bring expertise to the fund when evaluating strategies and investors. One banker commented that their bank was developing its own database of investors and ratings for those investors. Others continue to use third-party services but noted that those services may contain flawed features. For example, investors who had been removed from the fund because of fraud or sanctions in some cases continued to be included in the database.

Experienced bankers review the limited partnership agreement up front to know what is involved and whether the document contains the protections that lenders require – lenders are looking for a bankable agreement and they review side letters and craft a borrowing base that will be available for review. If there is a material deviation from what the fund is expecting, the advance preparation work enables the parties to flush that out well in advance of the expected closing. Reviewing the fund's organizational documents and structure is key. Advance preparation was the dominant theme – no one wants to get a call deep into the negotiation process that there is an unexpected issue with the borrowing base. Side letters present increasing complicated issues that have driven up legal costs, citing complicated most-favored nation clauses, attorney general's views on enforceability, investment policy exceptions with politically sensitive industries and even the application of money derived from seized goods. If there is a bad side letter, that may affect all the other investors.

Banks want to understand what is important to the fund in its proposed financing: the focus of the fund, the utilization of the line of credit, and the expected interest rate. The business of providing financing to these funds is, first and foremost, relationship-driven. That means that the bank and the fund will be looking at all of these issues together with their respective fund counsel, and that the lenders have to be transparent about what is acceptable and what is not. Banks favor well-managed GPs where there is a broader institutional relationship across the institution. During times of tighter liquidity, banks will naturally gravitate to transacting with funds that have established their relationships with lenders through several cycles.



Fund Finance Symposium Panel Recap: New Suppliers of Capital in Fund Finance

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Against the backdrop of a changing landscape of fund finance providers and products, this session made for an insightful discussion of the challenges and opportunities our market faces. On the panel were Ana Arsov (Managing Director at Moody's Investor Services), Mike Durnin (Principal at Ares Management), Greg Fayvillevich (Head of Global, Funds Group at Fitch Ratings), Ron Franklin (Partner at Proskauer), Marc Silva (Global Head of Private Equity Subscription & Partner Finance at UBS) and Sherri Snelson (Partner at White & Case).

Changes in bank appetite

The panel discussed how the last few months have seen a number of banks pulling back due to a variety of factors, including increased regulatory costs and the shrinking of low cost deposits. Subscription finance in particular has been an easy target for the chopping block, given its relatively low interest rate returns. Among banks the focus is now more heavily on the growing NAV space, owing to the higher returns and sponsor demand as a result of the slow exit environment.

From a sponsor's perspective, the privacy of the market has made it difficult to ascertain the source of supply in a macro sense; however, the anecdotal evidence clearly points towards insurance companies, pension funds and asset managers picking up some of the slack.

Need for ratings

Ratings are becoming more and more important for capital efficiency and distributions, in both the subscription and NAV markets. The NAIC's crackdown on CFOs announced at the beginning of the year underlines the need for ratings in the insurance space, where they are required by regulation in the U.S. and Asia, while other geographies like Europe need them as a matter of insurers' own internal policies.

The rating experts on the panel described the increased demand they have seen in recent times, and provided insights into the methodologies they apply to subscription and NAV transactions. The robustness of the data now available, in part via the growth of the secondaries market, has been key to the development of these offerings.

Opportunities

The demand for subscription finance is outstripping supply, creating opportunities for those lenders with balance sheet available to deploy. The panel also considered how pricing pressure could be alleviated by creating tranches within facilities, which could be a way for banks to shore up their core relationships while making sure a deal still makes sense economically.

Meanwhile, the number of new entrants in the NAV space (such as insurers with more favorable capital treatment) is creating a more competitive environment for sponsors to exploit. Variety is also key from a sponsor's perspective, with the number of structures available offering a buffet of choice, albeit with a wide diversity of pricing.

Outlook for 2023

The panel were unanimous in the view that the market would remain challenging in the short term but shared optimism for the latter half of the year. Compared to the early days of the pandemic, the headwinds of rising rates and capital constraints appear more systemic now, such that the slow-down in activity and reduction in fund (and therefore facility) sizes is likely to be more prolonged than in 2020. But, all in all, a broader investor base in the fund finance market, and the variety of thought that goes with that, should be a cause for confidence in the longer term.

Fund Finance Symposium Panel Recap: The Evolving Lender Landscape & Impacts on Balance Sheet Management

February 17, 2023 | Issue No. 211



By **Katie McShane**
Special Counsel | Fund Finance

Laurie Lawler (Société Générale) did a wonderful job moderating last week's panel titled "The Evolving Lender Landscape & Impacts on Balance Sheet Management." The panelists comprised a group of industry experts, including Vicky Du (Standard Chartered), Missy Dolski (Varde Partners), Michael Orphanides (BMO Capital Markets), Steven Kahn (Assured Guaranty) and Steve Colombo (Goldman Sachs).

The Evolving Lender Landscape

During the first part of this panel, the panelists discussed how the lender landscape has changed and evolved over the years; it was interesting to hear each panelist's perspective on this point. The panelists discussed how five years ago (to put it simply), it was definitely a "good time to be a borrower," with lenders generally trying to grow their businesses and providing more favorable terms. Now, borrowers appear to have less leverage, and banks are being more strategic about how they are deploying capital and are seeking efficiencies across their platforms. Sponsors appear to be using sub-lines across all investment strategies, and with lots of demand, there isn't enough supply. One of the panelists noted a lean-in to syndication by the banks instead of large hold sizes and pointed out that, depending on the end goal, the current environment has forced lenders to narrow their focus on strategies and clients, which wouldn't have necessarily been the case in the early days. This panelist pointed out that it can be challenging for lenders to provide various types of fund finance products to multiple sponsors, so lenders need to specialize.

Current Challenges Facing Banks

The conversation pivoted to the challenges lenders are facing in managing their balance sheets. It was noted that we're in a tight liquidity market environment, with increased funding costs, and in the past six months, investment activity has slowed down. Some banks have been impacted by capital requirements; however, all banks are unique, and it's therefore important for borrowers to figure out and have direct conversations with lenders to find out what will push liquidity. Outside of capital challenges, banks are also facing single name concentration limits and portfolio limits.

Non-Bank Lenders and Fund Finance 3.0

The panelists discussed non-bank lenders entering the space. Assured Guaranty, which is relatively new to the fund finance market, is sourcing capital and credit capacity through the use of insurance products. Given that there isn't enough supply from the lender market, it was noted that we will most likely see a capital markets solution down the line (enter, "*Fund Finance 3.0*"). Reg cap trade was discussed, as was securitization. It was noted, however, that for securitization to work, it would take a lot of road mapping given the complexities associated therewith, such as risk retention, disclosure requirements and ratings. One of the panelists pointed out that lenders will have to play a leadership role given the current climate, and that the drive shouldn't just be coming from the borrowers. This panelist flagged that there's a very lucrative opportunity for banks right now and it's important for them to charge ahead! I'm hoping we'll see a panel dedicated to "*Fund Finance 3.0*" this time next year!

Fund Finance Symposium Panel Recap: Syndications Panel

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By **Chris Montgomery**
Partner | Fund Finance

The past year has seen a challenging environment for the balance sheet of many banks. The ability for a bank to sell and assign their commitments in fund finance facilities has therefore increased in importance. In the Syndication Update panel in Miami, panelists convened to discuss the latest trends in these efforts.

We heard from both sponsors and lenders on the panel, which gave a rich perspective we wouldn't otherwise see outside the Miami conference. Also of note: many of the lender panelists lead the syndication efforts at some of the largest agent banks in the fund finance market. It's not an exaggeration to say that the group of panelists are representative of who decides what sells and how in our market.

A More "Hands On" Approach

One theme we heard from the sponsor panelists is a more "hands on" approach to building out the syndicate. Previously, before markets tightened, sponsors would rely on the efforts of the agent bank. Today sponsors are helping to attract and land key participants in a broadly syndicated facility. Syndicate leaders on the lender side also agreed that selling commitments is now more "high touch" than previously.

Sponsors Can Be Smart in Leveraging Ancillary Business

The sponsor panelists also shared that a key tool for sponsors in attracting a broad syndicate is the ancillary business a sponsor can offer to the agent and syndicate lenders. Most banks are focused on the fund finance product as a way to cross-sell. Sponsors can be smart and understand how participant banks' business interface with the sponsor's borrowing needs outside of fund finance. Using the cross-sell isn't just for banks anymore. It's also a great way for a sponsor to fill out large commitment sizes.

Banks Are Under Pressure to Defend Commitment Sizes

In an environment of depleted deposits and an inverted yield curve, banks are now more focused on balance sheet management. The bank panelists confirmed what everyone in the market has felt, which is that the competition for capital means that each commitment needs to have a strong business case. That usually comes from the ability of a bank to cross-sell its non-fund finance services by leveraging its fund finance commitments. In addition, banks are prioritizing their key existing relationships when allocating capital rather than chasing new opportunities.

Keep It Simple and Provide Enough Time

Bank panelists also emphasized that things now take longer. There are more questions. Gone are the days where you can say, "Here is the document, take it or leave it." Therefore, it is wise for sponsors and agents to build greater lead time and longer runways for their facilities. Simplicity also helps – if you can keep sanctions, jurisdictions and currencies simple, then you will get more availability.

Conclusion

Sponsors can be smart and centralize their knowledge about their "wallet share to the street," according to a sponsor panelist. This will allow the sponsor to help the agent allocate effectively to syndicate lenders. Banks also need to see results from cross-selling: many lenders may not show up in the next round if the business case for the initial commitments (that is, the provision of ancillary or advisory services) never materialized. Finally, panelists noted that terminal rate clarity from the Fed will give the market more certainty with respect to capital deployment. And perhaps the most important observation: while fundraising has slowed, it's not getting smaller. The future looks to a capital markets solution to alleviate balance sheet pressure and provide greater lending capacity to a market that is now mature but still growing.

Fund Finance Symposium Panel Recap: Market Evolution & Industry Perspectives

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By **Eric Starr**
Special Counsel | Fund Finance

The 2023 edition of the Fund Finance Association's annual conference was again filled with interesting insights from a wide range of industry participants and leaders. The panel titled "Market Evolution & Industry Perspectives" was no exception, bringing together a panel which included bankers, attorneys and fund managers.

Each panelist shared their unique perspectives and thoughts on a variety of trends and changes in the fund finance space, including with respect to market dislocation, fund raising and evolving deal terms. The second half of 2022 saw a lot of changes in the subscription credit facility market; looking ahead to 2023, the panel was unified in the belief that the industry is likely to see many of those trends continue, and in some cases, intensify.

Dislocation in the Market

It's no secret that the market for subscription finance has changed in the last year. Panelists noted that some lenders are facing capacity issues and capital crunches. And in some cases, we have even witnessed lenders exits and reductions in exposure to the product. Many lenders are reevaluating their approach to deploying capital, in many cases leaning into existing relationships to the exclusion of potential new ones. On the fund side, managers are facing headwinds not previously experienced and are finding it necessary to work with new lenders and agents in order to put a facility in place. As one lawyer noted, this can lead to new headaches and growing pains as the parties learn to navigate new business partnerships.

Demand Remains Strong

Demand for subscription credit facilities remains strong. Despite an environment that is more challenging in terms of securing financing, the panel members unanimously agreed that a lack of interest in subscription finance facilities is not a constraint on the market. The strong demand, when viewed against the evolving landscape on the supply side, may well create opportunity for lenders who are active or even looking to expand their footprint. One panel member suggested there is a need for creativity and non-traditional solutions to solve some of the issues currently facing the market. The opportunity to solve these very real problems creates an interesting opportunity for enterprising bankers and creative, solution-seeking law firms.

Fundraising and Borrowing Base Issues

Panelists discussed the changing fund raising landscape and the impact on facilities. From a lender perspective it was noted that delays in fundraising or changes in anticipated investor bases – both of which have seen an uptick recently – can present challenges. Later-than-expected need for a facility can lead to pricing issues given the rapid rise in interest rates; and changing investor makeups can create issues with underwriting, particularly if the borrowing base looks meaningfully different than what was originally anticipated. Several panel members stressed the importance of constant communication and transparency when discussing potential changes to investor groups.

Changing Deal Terms

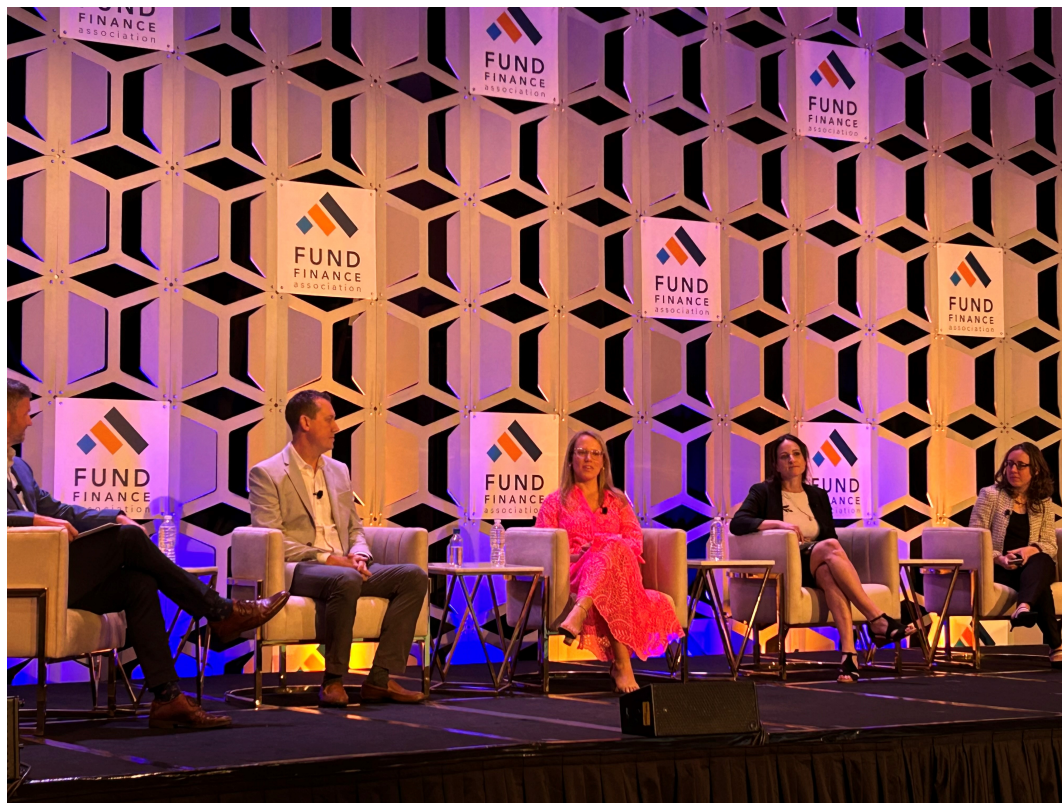
Funds still want long tenors, competitive pricing, facilities in place as soon as investor closings occur, same day funding options and committed facilities. But in an environment of higher interest rates and the previously-discussed dislocations in the market, many leaders are re-evaluating deal terms. In addition, one panelist noted that GPs often desire bigger commitments, but usage of facilities has not always supported such requests. Further, it was noted that this development threatens to cause further issues with supply and demand imbalances.

NAV and Environmental, Social and Governance (ESG) Facilities

Two hot topics in fund finance lending (NAV & ESG) were raised in the Q&A session that wrapped up in this panel.

NAV lending discussions are everywhere in the space. And some panelists expressed a belief that this may be the time such facilities finally explode in popularity. On the contrary, other panelists anticipate the opposite – that lenders will stick with the status quo and the products with which they are most familiar. Panelists expressed the concern that fluctuating and uncertain valuations present real hurdles to NAV lending in the current environment.

An audience member polled the panel on the question of whether ESG is dying, or at a minimum, not advancing as rapidly in the current environment? The responses were mixed. Funds continue to see value in ESG and are committed to pursuing it. From a lender perspective, it is also important to find impactful KPIs (key performance indicators), which is not without challenge. Finally, other panelists noted that banks gain no capital relief from ESG at this point, but are supportive to the extent it is important to their clients and investors.



Fund Finance Symposium Panel Recap: A Geopolitics Discussion with Pippa Malmgren

February 17, 2023 | Issue No. 211



By **Bryan Barreras**
Counsel | Fund Finance

One distinct and lasting memory that I have of law school is the feeling that I was being let in on a secret. Through the (hundreds of) cases that we read and our other coursework, we were learning about how the world really worked – not just the legal world, but also the government, politics, businesses (and the corporate world generally), property (and by extension property owners), the criminal system, and people generally. It was fascinating, and wholly unlike the rest of my education. It probably goes without saying that I very much enjoyed law school.

I got that same feeling of being let in on a secret about the way things really work at one of the final panels last Thursday at the FFA Global Symposium in Miami. The panel was “A Geopolitics Discussion with Pippa Malmgren.” Dr. Malmgren is an economist who advised the President of the United States during 9/11. She served on The National Economic Council and The President’s Working Groups on Corporate Governance and on Financial Markets. She has founded and supports several tech and other ventures and is also the author of a few books, including *The Leadership Lab*, which won the 2019 Business Book of the Year.

Dr. Malmgren discussed Chinese balloons, AI, the war in Ukraine, “wars” in various other places (including space), computing power, glocalization, yoga mats and other topics, and in each case explained why we should care about the topic (and managed to cover all of that in 50 minutes). We can’t discuss all of the topics she covered here, but below is a brief summary of a few of them.

A Hot War in Cold Places

Dr. Malmgren discussed a couple of areas here, and noted that there is not a lot of press about these because they are happening where there are no or few journalists. The first was the increasing tension and conflicts between superpowers (primarily the U.S. and China, but also Russia) at sea, with the South China Sea probably being the most prominent.

The bigger discussion was about the “war” for space, and among the same three countries. First she talked about satellites – the cutting of an underwater cable in the Arctic circle that carries virtually all satellite communications with Earth (there are redundancies, so this didn’t cut off the communications), Russia purposely blowing up a satellite and showering that orbit with debris (making it unusable by other satellites), NASA financing companies trying to clean up space debris, and China “dazzling” U.S. satellites when they pass over China. Next was the race to the moon (including Starship and the U.S.’s Artemis 1 rocket) – not just to reach the moon, but to stay there, build launch pads and manufacture on the moon. Dr. Malmgren stated that many of Earth’s problems can be solved with space-based solutions – unlimited cheap green energy, resources and connectivity. Mining asteroids for materials (noting that the value of the resources in a single asteroid, Psyche, would be enough to make every person on Earth a billionaire). Saudi Arabia is already working on space-based solar power. Some experts in this area see the race for space as a winner-takes-all scenario, with the potential to shift the geopolitical balance of power on Earth. All of this will have incredible spinoffs for the private sector (much bigger than in the 1960s and 1970s).

Invisible War and Spy Games

Why would China want to spy on Montana? Dr. Malmgren explained that most of the U.S.’s nuclear missile silos are in Montana (and Wyoming). And that data from a spy balloon could be fed into SenseTime’s facial recognition software, which can not only recognize faces but determine someone’s (like a silo operator) emotional state. She then showed a slide with a recent quote from the UN Secretary General – “This is the closest the clock has ever stood to humanity’s darkest hour, and closer than even during the height of the Cold War.” However, Dr. Malmgren managed to be positive, noting that all past issues re: nuclear alerts have been resolved. She also noted that preventing nuclear war is one of the few subjects that gets bipartisan support among the Republicans and Democrats, so that’s something.

Dr. Malmgren also discussed the war in the Ukraine and war, conflict and relations with Russia and China generally, noting their focus on resources in Africa and the Arctic and other areas of conflict (which includes access to computing power and technology) which are not receiving much attention, but that investors in these regions should be aware of. She also discussed how Russia and China will ultimately need to be included in resolving all of these conflicts and in rebuilding (both Ukraine and Russia, as well as getting China’s economy back on track) once they are over.

Computational Power and Digital Currency

In addition to the massive amounts of computational power necessary in connection with the space activities mentioned above, Dr. Malmgren discussed the Central Bank Digital Currency and the new monetary policy this could bring and the amount of personal data and financial information that will need to be processed, and the work that is already being done to develop the necessary hardware and software to accommodate this. Again, bringing it back to the audience, she noted that changing the whole system of money and accounting would affect all the deals that are being done. She had a slide showing that pre-1900 human knowledge doubled every century and in 2020 that had moved to every 12 hours – there is simply too much information to process without automation and computer algorithms.

Dr. Malmgren succeeded in giving us all too much information about a myriad set of topics to process, and discussing topics that could ultimately matter a great deal in our lives but that we knew little, if anything, about. From an investing and opportunity standpoint, the implications of the things she talked about are relevant to determine where the deals are, in what sectors they will be, and which sectors or deals may no longer make sense in the face of some of these technologies. She hoped she got us to lift our heads up from looking at the details of deals all day long and to draw our attention to whole new sectors that may be massive and full of deals and that will have implications for every other sector.

Fund Finance Symposium Panel Recap: CFOs – Collateralized Fund Obligations

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By **Joe Zeidner**
Partner | Fund Finance

As the private equity and fund finance markets continue to expand with new, innovative products, collateralized fund obligation transactions, or CFOs, are becoming increasingly popular. A panel of experts discussed the nuances of constructing CFOs, from the asset-based lending nature of the rated notes that underpin these deals to the complexity of cash flows, liquidity needs and legal considerations. With this deep dive into the world of these asset-backed securitized structures, it's no wonder the fund finance industry is abuzz with the emergence of CFOs. There is optimism that these structures will continue to develop as financing tools for both sponsors and investors and the market will continue to grow and mature over the coming years.

For more on CFOs, please check out the prior article and presentation from some of CWT's CFO experts [here](#).

[ICYMI] Fund Finance Symposium Panel Recap: 'Titans in Finance: The Rise of Private Debt'

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In Case You Missed It: A re-post from last week's FFF issue.

Coming off of the close of a badly bruised broadly syndicated loan market in 2022, it is no surprise that the global Fund Finance Association kicked off its 12th annual conference in Miami with a conversation with the "Titans in Finance" – Jonathan Bock, Senior Managing Director, Co-CEO of BCRED and BXML, Head of Market Research, Blackstone Credit; Ken Kencel, President and CEO of Churchill Asset Management; and Art Penn, Founder and Managing Partner of PennantPark Investment Advisers. The panel was moderated by Jocelyn Hirsch, Partner at Kirkland & Ellis, and Nick Mitra, Managing Director at Societe Générale.

The Titans were first asked about inflection points and the reasons for success in the growth of their respective businesses. Surprisingly, they responded not by citing market acumen, timing or even luck but as true leaders: emphasizing the ability and commitment to build a talented team and to invest in diligent training and growth of their people. They noted that, when looking back, many people want to get into the private credit space, but few understand the importance of and were willing to commit to invest in the human resources that are required to build and run a successful private credit shop. Fast forwarding to the way these businesses have developed with multiple investment vehicles and strategies, they commented that over 50 percent of their human resources are devoted to investor relations, operations, and finance, thereby reinforcing why talent development is so important. Their longevity in this space was a thread that permeated the discussion, which underscored to the audience why these leaders were selected from a crowded private credit space to address the Fund Finance Association in 2023.

The Titans discussed two major themes: market segmentation of the companies in the middle market (generally companies with under \$50MM in EBITDA) and the diversification of funding vehicles and strategies utilized to fund their respective investments in middle market companies. Private credit has historically targeted the middle market because these companies could not access capital in public markets or the broadly syndicated market. They discussed how the middle market should be segmented into upper middle market (\$50MM to \$100MM in EBITDA), lower middle market (under \$15MM), core middle market (\$15 MM to \$50MM), and then by specialties, such as healthcare, technology, aerospace, consumer, food and beverage, as well as sponsor and non-sponsored companies. Commenting that experience through economic cycles has shown that lower middle market companies are less able to weather cycles of increased interest burden from rising rates, it was noted that the sponsor-backed companies are favored because of the availability of sponsor equity support. It was also noted, however, that the most recent COVID years are not a good indicator of how these companies and their sponsors will behave in a downturn because, during COVID, the market understood and expected the economic situation to be temporary. More importantly, it was a period of low interest rates that allowed companies significant breathing room. Conversely, the current economic environment of high interest rates, high leverage, and very light or no covenants presents a more challenging lender environment. They acknowledged that sponsors may be less inclined to support the companies they do not believe will survive.

The disrupter of 2022 was the rise of large club deals. Approximately 15 private credit firms in the market, putting their multiple strategies to work, were able to write checks of up to \$500MM. This balance sheet strength is benefiting from the current volatile landscape. Public market volatility and uncertainty have also reinforced the popularity of private debt. All of the Titans reflected upon how their businesses diversified their funding vehicles and utilized structures such as BDCs, SMAs, CLOs, and institutional funds, and were additionally looking down the road to retail investors.

Comparing the syndicated lending market as "moving vs. storage," private credit won favor in the "storage" business because banks in the "moving" business – taking large fees to syndicate the loans to other lenders – which proved to be unsuccessful in 2022, now found themselves unable to sell their commitments. Able to negotiate better legal and financial terms with their large checks in hand and negotiating directly with the intention of holding these loans to maturity, private credit moved quietly from the sidelines to center stage to deliver to sponsors the credit they were looking to raise while the stalled syndicated loan market essentially shut down. The efficiency of this "storage" model appealed to sponsors. Larger companies, which traditionally only looked to the broadly syndicated market, were able to tap private credit. Despite negative press reporting the lack of deal flow in early 2023, deals are getting done and valuations are holding steady for higher quality companies. Pricing is up, overall leverage is moderated, and the best private credit firms and their portfolios remain in good shape. Being vigilant about designing and managing the portfolio is key. These market leaders have long histories with certain sponsors and believe they know how these sponsors will behave in a downturn.

“When is a strong M&A market returning”? asked one of the moderators. Possibly midyear, came the response from the panel. With the public markets essentially closed, private credit is well poised with approximately \$300BN in dry powder. This, coupled with the potential of a large retail market entering the space to provide additional funding, poses huge opportunities for private credit in 2023.

PFCFO Reports from Miami

February 17, 2023 | Issue No. 211

Private Funds CFO was on the ground in Miami to report on some key takeaways and insights from the FFA's Symposium. Read Day 1 [here](#) and Day 2 [here](#).

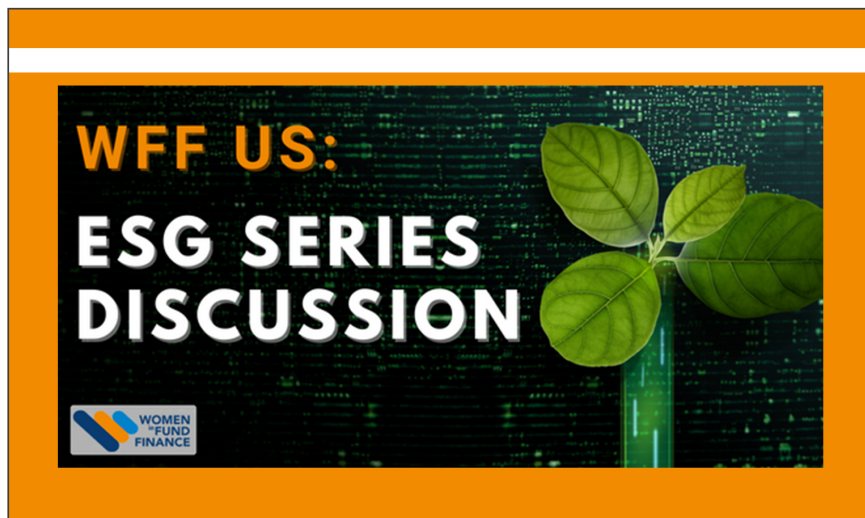
Fitch Releases Subscription Finance Report

February 17, 2023 | Issue No. 211

Fitch Ratings has released a report, *Subscription Finance: A Primer*, which covers common queries from market participants, including the effect of subscription facilities on fund cash flows and performance metrics, key features of subscription facilities, and market developments and historical performance. To access the report, click [here](#).

WFF U.S. ESG Series Discussion

February 17, 2023 | Issue No. 211



Women in Fund Finance (WFF) U.S. is hosting a virtual panel on “Navigating ESG Communications: Strategies for Challenging Times” on Tuesday, February 28 at 11 a.m. EST. The panel will focus on ESG data, disclosure, and ratings/scoring and will explore how different types of data may be used for risk analysis/mitigation, strategic planning/value creation and stakeholder engagement/communication. Click [here](#) to register and for the speakers list.

WFF London Event Celebrates International Women's Day

February 17, 2023 | Issue No. 211

Let's toast to the hardworking women of the Fund Finance industry! Raise your glass with the FFA and WFF at OXO Restaurant in London on March 8 at 6:00 p.m. for a networking reception in honor of International Women's Day. Visit [here](#) for more info.

‘The Funds Channel’ Podcast: New Episode

February 17, 2023 | Issue No. 211

Check out the new [episode](#) of Simpson Thacher’s podcast, *The Funds Channel*, for an insightful and in-depth discussion of NAV facilities and their increased presence in the Fund Finance market.

On the Move – Fund Finance Tidbits

February 17, 2023 | Issue No. 211

On the Move



Jose Liz-Moncion
Managing Director



Maddie Barnhart
Vice President



Caitlin Schwietering
Vice President

Bank of America's Subscription Finance Group has made some recent promotions, including: Jose Liz-Moncion was promoted to Managing Director, and Maddie Barnhart and Caitlin Schwietering were promoted to Vice President. Congrats to all!

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