PILFOR
LENDING SOUNDNESS

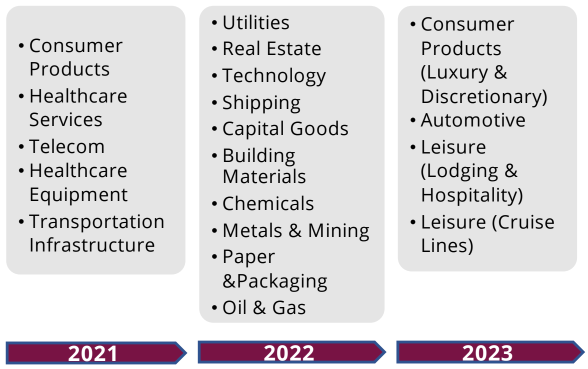
November 2020

Monthly Market Insights

Loan Market

Over the next couple of months we expect to see an increasing number of companies operating in «unloved» sector by banks due to (i) their high exposure to the pandemic, (ii) a high leverage and (iii) eventually mixed financial track record , or as a result of pandemic-driven leverage increases triggering effective or potential loan covenant breaches, struggling to secure (re-) financing. Indeed, when such enterprises fail to (re-) negotiate terms & conditions with the existing creditor and further do not succeed to secure a (re-) financing with a bank or non-bank lender that accepts higher leverage levels, the result is then typically a sale of assets or equity at a steep discount in order to bridge the liquidity or financing gap. The next months will show how the re-pricing of risk and potential retracement of banks from certain sectors and risk classes will result in a re-balancing of market shares between bank and non-bank lending activity.

Expected timeframe run-rate credit metrics recovery*

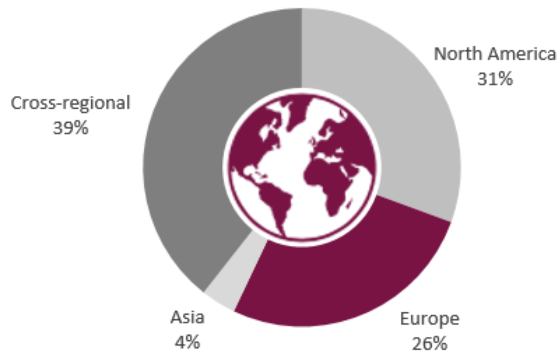


Sources: Fitch, Moody's, S&P *versus 2019 levels

Direct Lending

Direct lending has experienced a very impressive growth over the last couple of years, proving a stronghold within the private capital market. The COVID-19 crisis will show how direct lending funds can cope with potential multiple defaults within their portfolios, testing both the operational capabilities of managers as well as internal resources used rather for origination and performing loans so far. Its general outlook for the next months and years to come is set to remain sound: Massive capital inflows from yield hungry investors have fueled dry powder waiting to be put to work, banks turning more conservative again leaving gaps to be filled, and companies showing accelerating financing needs as we move further down the road. Lower leverage levels, a re-pricing of risk in favor of lenders and stronger documentation should further play in direct lenders' hands.

Geographical focus of debt funds raised 9M 2020

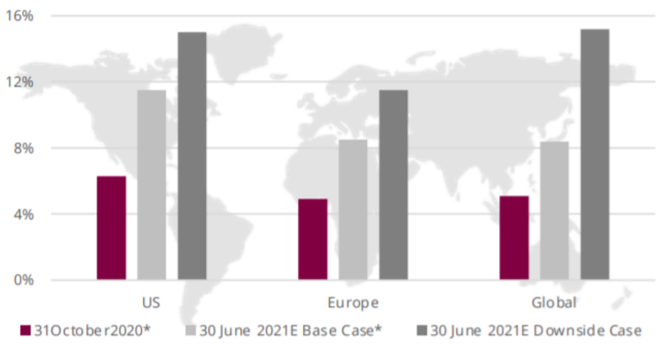


Source: PDI

Credit Ratings

When entering the unprecedented tidal wave of negative rating actions in March 2020, the global rated issuer landscape had already suffered from an ongoing quality deterioration with a marked concentration around the "BBB" and "B" category. As the virus spread, issuer ratings rapidly came under siege. The vast majority of rating actions occurred in the speculative area, with fallen angel debt being set to reach historic highs. Wide-spread monetary and fiscal stimulus measures helped to restore market liquidity, spurring corporate debt issuance and leverage. In addition to the needed recovery of cash flows, governments willingness and ability to provide a lifeline to excessively debt-loaded businesses will likely prove decisive for a number of issuers over the next 6 – 9 months in our view. As downside risks remain, default rates could well double by mid-2021, reflected by further deteriorating credit ratings collapsing under the weight of debt piles not made to weather storms.

Corporate default rate developments and projections



Sources: Fitch, Moody's, S&P *Note: 12 months trailing

PILFOR is an independent and specialized debt & capital advisor establishing and optimizing
funding access - financial flexibility - financing costs

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