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Press Release

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Investors Flock to US Lower-Middle-Market Private Debt

Sector is seen as less vulnerable to potential cycle change, while offering strong returns

A Preqin/NXT Capital survey* of private debt investors has found that 45% believe that the private debt market is at a peak, and that the coming months will see a correction. In response, investors are looking increasingly to US lower-middle-market direct lending** and counter-cyclical strategies. In fact, the survey reveals that many investors believe that US lower-middle-market direct lending will be less affected by a cycle change and other macroeconomic trends than private debt as a whole.

As a result, appetite for lower-middle-market direct lending in the US has been growing, and a majority of investors plan to increase their allocations to the sector in 2018. Returns expectations for the sector are also relatively high: the majority of investors expect returns of 8% or more from unlevered funds, and more than 10% from levered vehicles, which is higher than for the private debt asset class as a whole.

For more information and analysis, see the full *Preqin Special Report: Shifting Gears: Investors Head Toward the Lower Middle Market* here:

http://docs.preqin.com/reports/Preqin-NXT-US-Lower-Middle-Market-Direct-Lending-Report-June-2018.pdf

Key US Lower-Middle-Market Direct Lending Facts:

- Forty-five percent of private debt investors believe that assets are overvalued and that a correction is due.
- **Investors believe US lower-middle-market direct lending will be more insulated from the economic cycle and other macroeconomic trends** than private debt in general. Eighty-six percent believe this is a risk for private debt generally, but just 43% cite it as a risk for the US lower middle market.
- Eighty-six percent of investors have a dedicated allocation to US lower-middle-market direct lending, and **a majority (56%) are set to increase their exposure over the next 12-24 months**.
- Counter-cyclical strategies are also sought-after, with 46% and 37% of investors now viewing special situations and distressed debt funds respectively as presenting the best opportunities in the next 12-24 months. **Thirty-four percent of respondents identified straight senior debt as presenting the best opportunities** over the same timeframe.
- Beyond seeing US lower-middle-market direct lending as a potentially less volatile sector, the largest proportions of investors cited high relative returns (57%) and diversification (55%) as its key appeals.
- **Returns expectations are high**: 59% expect unlevered lower-middle-market direct lending funds in the US to return 8% or more, compared to 39% that expect the same for broader unlevered private debt funds.
- Similarly, 79% expect levered vehicles focusing on the sector to return at least 10%, compared to 60% that expect that standard for generic private debt vehicles.

Tom Carr, Head of Private Debt Products - Preqin:

"Given the widespread speculation about exactly where we are in the market cycle, it is not surprising to see that many investors are positioning themselves in anticipation of a correction. However, what is striking is the clear bifurcation of investor response – institutions are looking to the US lower middle market for safety while simultaneously moving up the risk/return curve in search of opportunity. In these circumstances, it is a mark of confidence in the sector that return expectations have remained so high, outstripping private debt as a whole. With such clear and widespread appetite, we can expect lower-middle-market direct lending in the US to be an increasingly active sector in the coming months."

Robert Radway, Chairman & CEO – NXT Capital:

"It may be tempting to view US lower-middle-market direct lending through the lens of an extended cycle, large capital inflows and a growing number of asset managers. But the Preqin/NXT Capital survey offers a more positive and compelling perspective. Investors recognise that US lower-middle-market direct lending offers them valuable benefits and market resilience, especially when they work with proven fund managers that have proprietary origination platforms and access to high quality deals. The next few years may present some challenges in terms of the rate of capital deployment among different managers and the inherent risks of lending at the peak of the economic cycle, but

NXT firmly believes that US lower-middle-market direct lending will continue to mature as an asset class. Over time, it will become a standard component of many investors' portfolios."

**Results are based on a survey of 78 institutional investors in private debt conducted by Preqin in April 2018.*

***The lower middle market is here defined as focusing on companies with less than $50mn in EBITDA, and/or making transactions with a typical size of $30-150mn.*

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NXT Capital is a leading provider of structured financing to the U.S. middle market. Since its formation in 2010, the company has originated approximately $20 billion in total financing volume spread over 600+ transactions. With $12 billion of committed capital at its disposal, NXT provides a full range of structured financing solutions on a direct basis through its Corporate Finance and Real Estate Finance groups. NXT manages capital for third parties through its asset management platform and offers investors proprietary access to primarily first lien senior secured loans that are not broadly traded or otherwise generally available without a loan origination platform. Investment offerings include levered and unlevered funds, separately managed accounts and CLOs. NXT's investor base includes public and private pension plans, insurance companies, endowments, foundations and other institutional investors. **NXT Capital Investment Advisers, LLC, a subsidiary of NXT Capital LLC, is registered with the SEC as an Investment Adviser**. For more information visit www.nxtcapital.com.

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