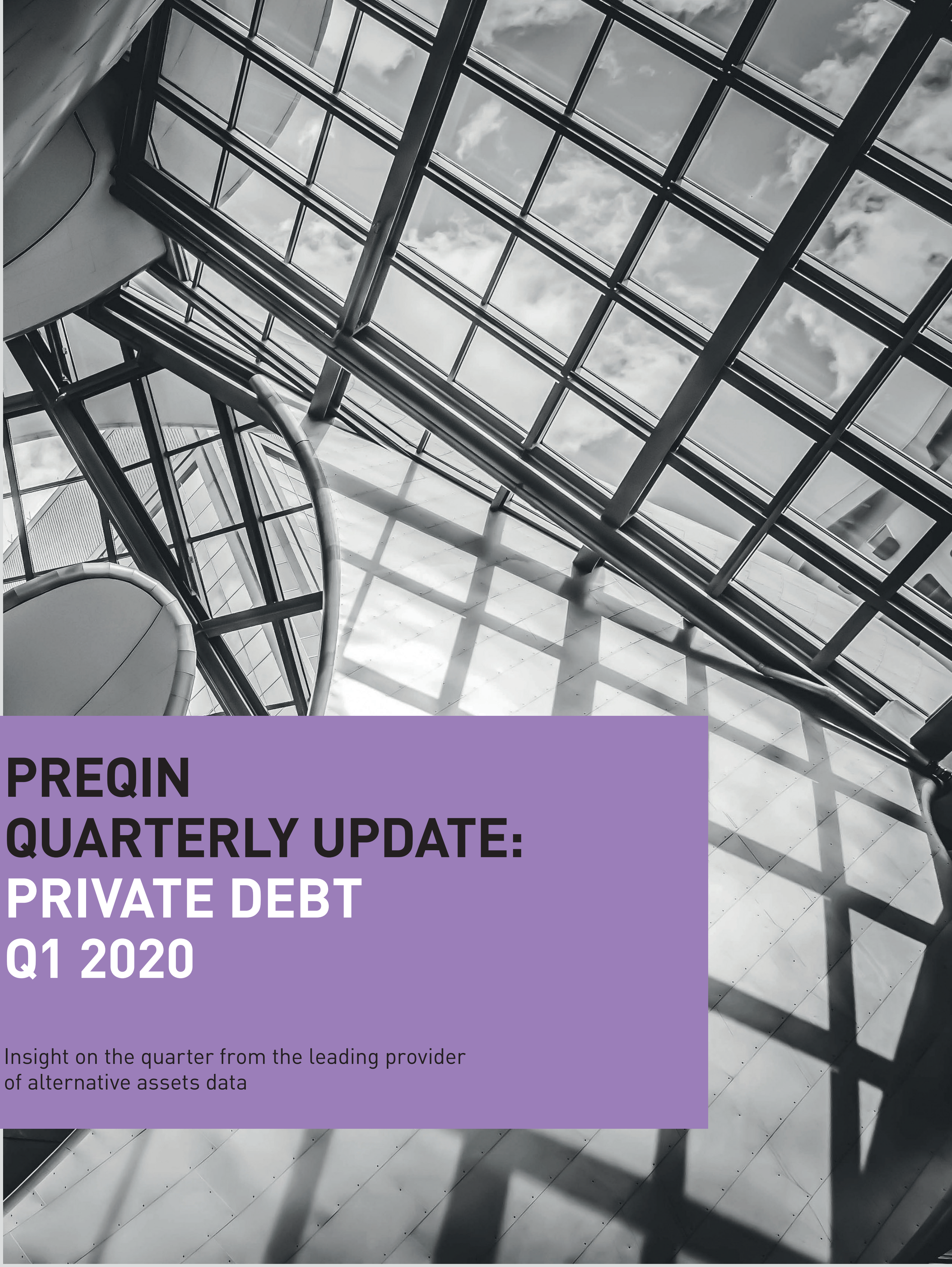

PREQIN QUARTERLY UPDATE: PRIVATE DEBT Q1 2020

Insight on the quarter from the leading provider of alternative assets data

Fundraising
Funds in Market
Investors
Performance
Dry Powder

preqin

Foreword

Fundraising in private debt slumped substantially over the first quarter of 2020, as fund managers evaluate the potential fallout from the economic volatility caused by the outbreak of COVID-19. Providers of high-yield debt and syndicated loans have pared back their offerings as the pandemic continues to test the robustness of a market that is yet to face a significant test globally.

A bleak picture emerged in the private debt fundraising market in the quarter, with total capital raised 41% lower compared with Q1 2019. In short, Q1 2020 represents the worst fundraising quarter for the asset class since Q3 2016. This comes as the pandemic halts global travel and changes working lives, postponing fundraising schedules and canceling investor meetings.

Adopting a more conservative approach to the asset class, private debt investors are rebalancing their portfolios in order to maintain allocation targets. While over a quarter of investors still intend to allocate more than $100mn in fresh capital in the coming year, the strategies they are targeting reflect the widespread uncertainty. We have observed a significant slump in the number of mandates issued for higher-risk distressed debt funds, for example.

Despite the economic turmoil, the number of private debt funds in market has continued to grow to a new record level. Where traditional lenders may be pulling back, many private debt firms may step in to fill the gap. However, this will heavily depend on the readiness of buyers and sellers to pursue deals in the current climate.

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Fundraising

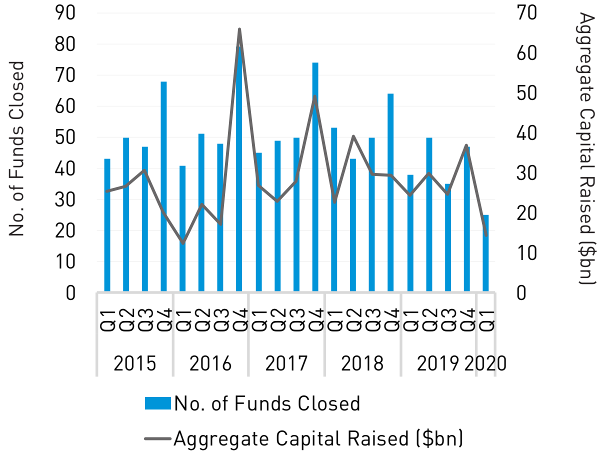
Q1 fundraising has slumped considerably as managers struggle to attract capital from investors

Private debt fundraising was lackluster during the first quarter of 2020. Only 25 funds closed, raising a combined $14bn in capital, which is 41% less than the amount raised in Q1 2019 (Fig. 1). This also marks the lowest fundraising quarter for the asset class since Q3 2016. Although private debt fundraising has followed a cyclical pattern over the past five years, whereby capital raised in Q1 is typically lower and fundraising picks up again during Q2, both totals are considerably below the average for Q1 in recent years.

Private debt funds focused on North America typically dominate the fundraising market, but in Q1 the balance shifted somewhat. Although the region accounted for just over half of total capital raised, Europe-focused funds represented 46%, and this was achieved from over half the number of funds closed (Fig. 2)

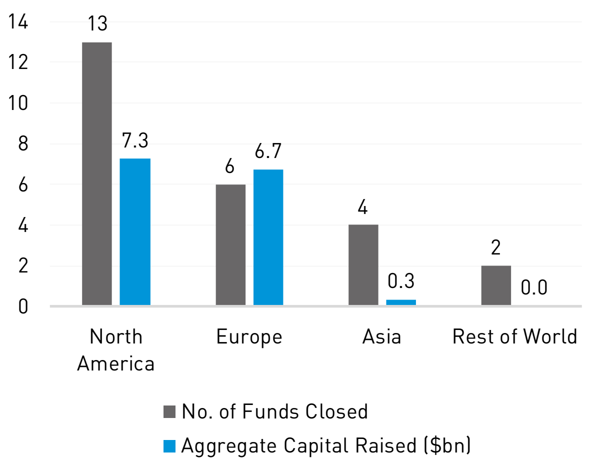
Although only three special situations funds closed in Q1 2020, the fund type accounted for over 20% of total private debt fundraising. One such fund is AG Credit Solutions Fund, which is managed by New York-based Angelo, Gordon & Co. and raised $1.8bn. A total of eight direct lending funds closed in Q1, raising the most capital ($9.4bn) of any fund type (Fig. 3).

Fig. 1: Global Quarterly Private Debt Fundraising, Q1 2015 - Q1 2020



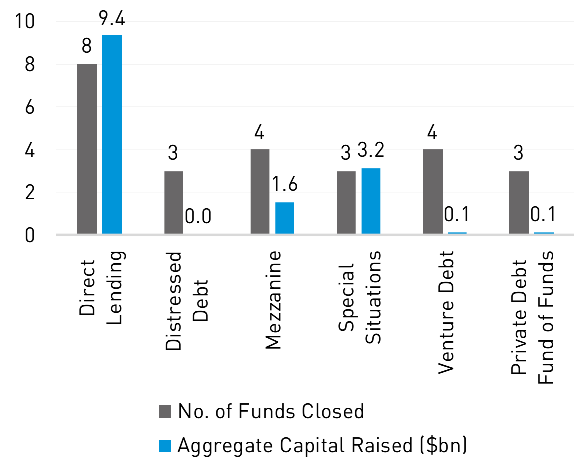
Source: Preqin Pro

Fig. 2: Private Debt Fundraising in Q1 2020 by Primary Geographic Focus



Source: Preqin Pro

Fig. 3: Private Debt Fundraising in Q1 2020 by Fund Type



Source: Preqin Pro

Funds in Market

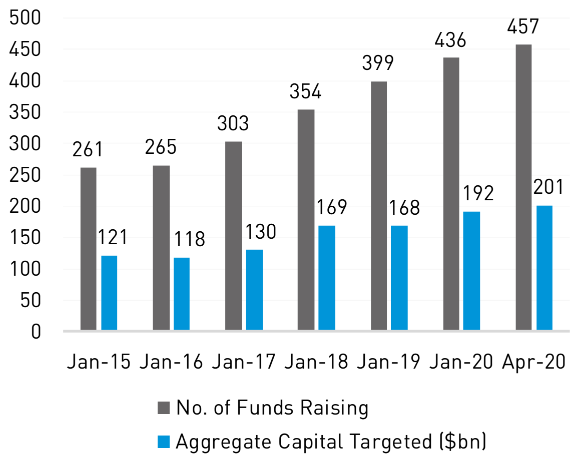
The pipeline of private debt funds raising capital is larger than ever before

While fundraising may be faltering, the number of private debt funds in market continues to grow. As of April 2020, there are 457 private debt funds in market, seeking a combined $201bn – these are the highest figures ever recorded (Fig. 4). The number of funds on the road has been rising consistently over the years, building to a fundraising market that is now more crowded than ever before.

The fundraising pipeline is little changed from previous quarters in terms of make-up. Direct lending funds account for the largest proportion of both the number of funds raising as well as aggregate capital targeted, with both at just under half of the total (Fig. 5). Meanwhile, special situations funds make up 12% of the number of funds in market and 14% of aggregate capital being sought, almost on a par with both distressed debt and mezzanine funds.

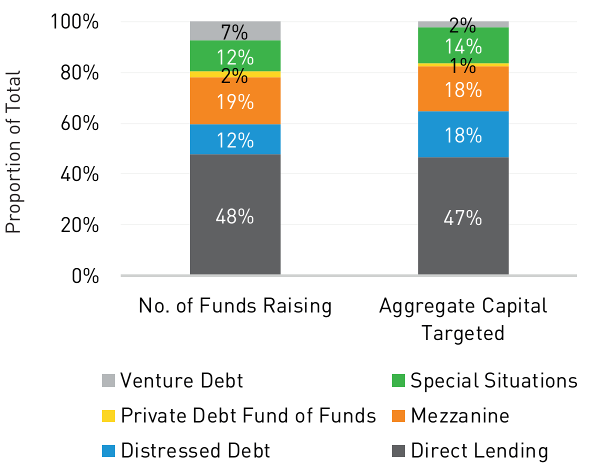
Funds in market are spread fairly evenly in terms of target size. Sixteen percent of private debt funds on the road are seeking less than $100mn, while 14% are targeting more than $1bn (Fig. 6).

Fig. 4: Private Debt Funds in Market over Time, 2015 - 2020



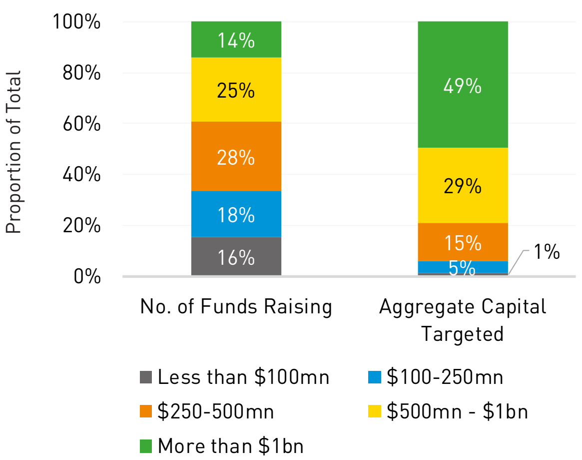
Source: Preqin Pro

Fig. 5: Private Debt Funds in Market by Fund Type



Source: Preqin Pro. Data as of April 2020

Fig. 6: Private Debt Funds in Market by Target Size



Source: Preqin Pro. Data as of April 2020

Investors

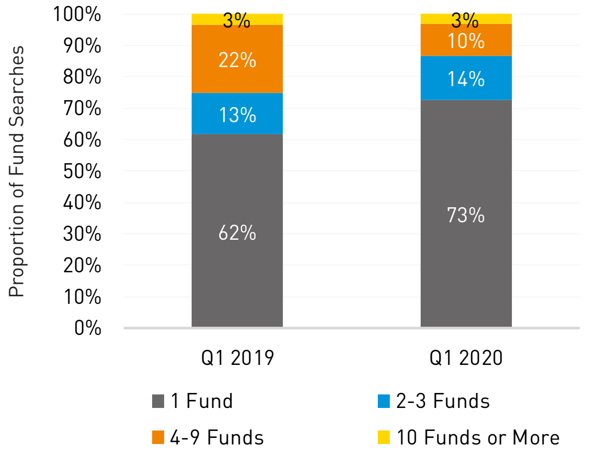
Private debt investors are making adjustments to reduce risk in the uncertain year ahead

Amid global economic uncertainty, investors in private debt are adopting a cautious approach to the next 12 months. Of the mandates issued for private debt funds in Q1 2020, the majority (73%) are for commitments to a single fund, which is up from 62% of mandates issued by investors in Q1 2019 (Fig. 7). Additionally, the proportion of investors looking to add four to nine funds to their portfolio in the coming year has more than halved from 22% in Q1 2019 to just 10% in Q1 2020.

Investors retain confidence in private debt, however. About a quarter (26%) are intending to commit more than $100mn to the asset class, which marks an increase of two percentage points from one year ago (Fig. 8). The proportion looking to commit $500mn or more has fallen from 10% in Q1 2019 to 7% in Q1 2020, though, and 55% are planning commitments of less than $50mn, up from 52% a year ago.

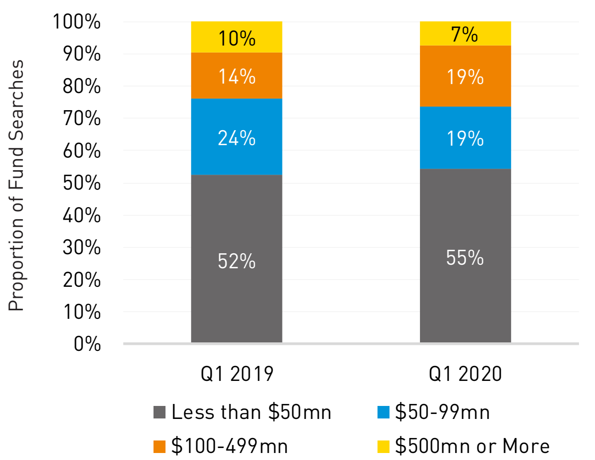
The strategies investors are targeting reflect the increasing economic uncertainty. Higher-risk distressed debt funds are less attractive to investors than this time last year, shown by the three-percentage-point drop in demand to 42% of mandates (Fig. 9). Appetite for direct lending has remained steady, with the same proportion of investors (49%) targeting the fund type as in Q1 2019.

Fig. 7: Number of Private Debt Funds Investors Plan to Commit to over the Next 12 Months, Q1 2019 vs. Q1 2020



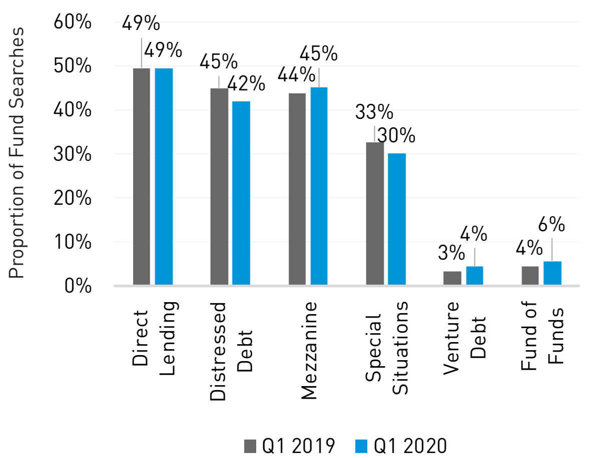
Source: Preqin Pro

Fig. 8: Amount of Fresh Capital Investors Plan to Commit to Private Debt Funds over the Next 12 Months, Q1 2019 vs. Q1 2020



Source: Preqin Pro

Fig. 9: Fund Types Targeted by Private Debt Investors over the Next 12 Months, Q1 2019 vs. Q1 2020



Source: Preqin Pro

Performance & Dry Powder

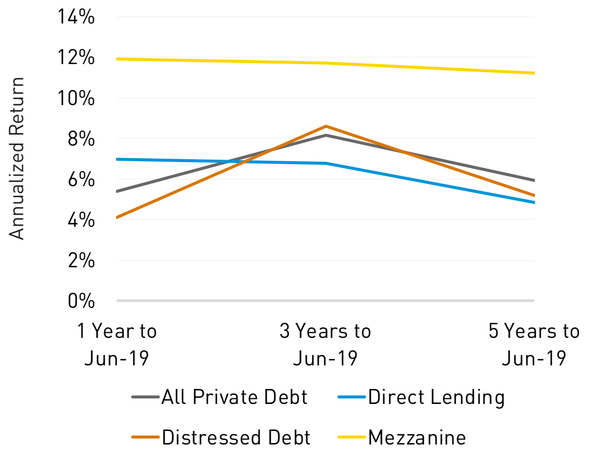
Private debt performance maintains a steady but unspectacular course

Annualized returns for private debt funds have slowed over the past year. In the year to June 2019, the asset class as a whole posted an annualized return of 5.4%, lower than any other private capital asset class during this period. Returns for direct lending, however, are stronger: over the one-year horizon, direct lending funds report an annualized return of 7.0% (Fig. 10). Mezzanine continues to outperform all other private debt fund types, and the asset class as a whole, by a significant margin over the one-, three-, and five-year horizons to June 2019.

As per the PrEQIn Quarterly Index, however, private debt has posted the third-highest returns of all private capital asset classes as of June 2019. The asset class is behind private equity and infrastructure, but has outperformed natural resources and real estate by a considerable margin (Fig. 11). Returns for the PrEQIn Private Debt Index have also been on an upward trajectory since December 2018.

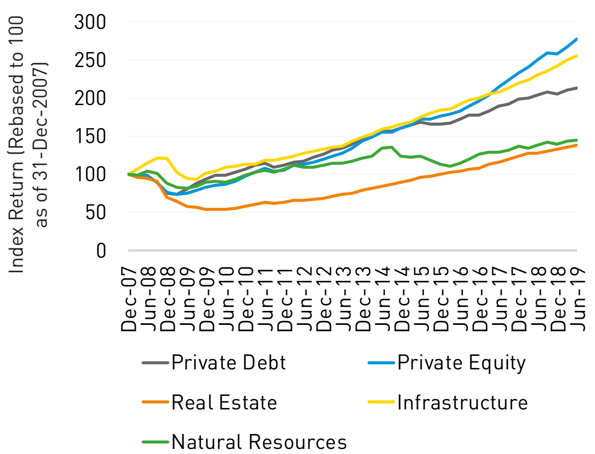
Direct lending funds continue to account for the largest share of assets under management (AUM) of all private debt fund types. As of June 2019, direct lending funds accounted for 36% of total private debt AUM, up by a single percentage point from December 2018 (Fig. 12).

Fig. 10: Private Debt: Horizon IRRs by Fund Type



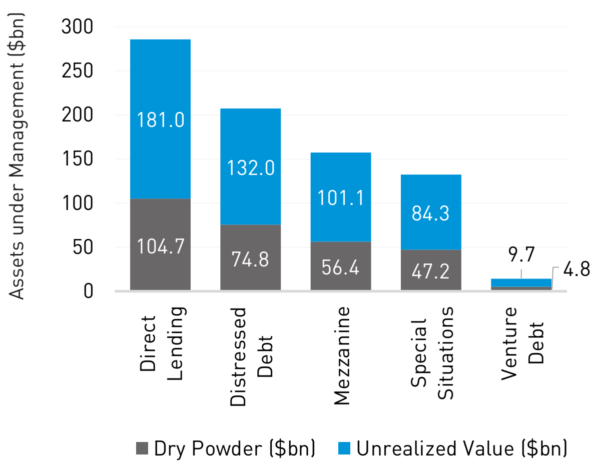
Source: Preqin Pro. Most Up-to-Date Data

Fig. 11: PrEQIn Quarterly Index: Private Debt vs. Other Private Capital



Source: Preqin Pro

Fig. 12: Private Debt: Assets under Management by Fund Type



Source: Preqin Pro. Data as of June 2019