PERMANENT & PRIVATE CAPITAL
SUMMIT
2021

2021
Permanent & Private Capital Summit

KEY TAKEAWAYS

Dechert LLP

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SUMMIT OVERVIEW

The 7th Annual Permanent & Private Capital Summit, sponsored by Dechert, ING and KBW/Stifel, virtually convened fund sponsors and asset managers across the United States, Europe and Asia. During the two-day conference, panels of CEOs and other senior industry leaders from the world's top financial institutions discussed a broad range of trends and developments impacting the private credit and private capital space.

Dechert partner Jim Lebovitz opened the Summit recounting and reflecting on the extraordinary growth of the permanent and private capital sector since the first Summit. He anticipated hearing about the key factors impacting this market and driving its expansion, in particular, over the last year. Jim noted the disruption, dislocation and stress caused by COVID-19 and underscored how the pandemic tested the relationships between leveraged finance lenders and the funds they lend to, and direct lenders and the portfolio companies to which they lend. He ended his remarks looking forward to the panelists discussing lessons learned from the pandemic and the strategies they are implementing to create a competitive edge and capitalize on market opportunities.

The key takeaways from the ten panels are highlighted on the following pages.

During the two-day conference, panels of CEOs and other senior industry leaders from the world's top financial institutions discussed a broad range of trends and developments impacting the private credit and private capital space.

The Evolution of Private Credit: Strategies to Drive Growth and Scale

As the private credit market continues to mature, a panel of senior names in the industry identified the following key strategies and priorities for growth and scale in a sector that is ripe for further consolidation. These experts pointed to several vital priorities.

- **Consolidation** (as opposed to building a team from scratch) is the way to achieve the growth and scale, which, in turn, helps to cement and preserve relationships with customers. Scale enables efficiencies that address the high operating costs of running a private credit platform.

- Growth depends on **longer-term** strategies, not short-term results. Our panelists stressed the importance of focusing on high risk-adjusted returns for investors and maintaining superior asset quality.

- An emphasis on **differentiation** is pivotal to long-term results, recognizing that the middle market is more crowded and that larger teams are better able to deliver the deep industry experience, pattern recognition and an understanding of individual business models. Scale also provides the additional flexibility to support a business's entire credit needs, corresponding to its capital structure.

- **Flexibility** is key to accommodate the changing needs of portfolio companies, meaning there's less likelihood of having to re-underwrite for a new borrowing by a portfolio company every time there is an alteration in the business plan.

- Looking for a **balanced portfolio** means a mix of sponsor and non-sponsor business. According to one panelist, sponsors require a greater frequency of credit to support their pipeline of transactions, but that segment is increasingly competitive (and relationships with a sponsor tend to be more transactional). Non-sponsors are more difficult to originate as clients, and relationships can take much longer to cement, but they tend to be stickier and more long-term as borrowers.

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THE SPEAKERS

Moderator:
Omoz Osayimwese
Partner | *Dechert LLP*

Ted Goldthorpe
Partner and Head of Credit | *BC Partners*

Al Laufenberg
Managing Director | *KBW/Stifel*

Craig Packer
Co-Founder | *Owl Rock*

Sengal Selassie
Co-Chief Executive Officer and Co-Founder | *Brightwood Capital Advisors*

Commentary:
Ken Young
Partner | *Dechert LLP*

Venturing Through Alternative Asset Finance

This panel focused on the considerable opportunities for growth remaining in the private credit market, the structures to implement that growth and the capital providers to fund that growth. Here are the takeaways:

- **The private credit sector is not saturated.** Significant growth opportunity is driven by middle market private equity.
- **Successful private credit platforms range** from those creating niche specialty approaches to ones developing the size and scale to provide the skills, knowledge and flexibility to craft bespoke solutions for clients.
- Managing economic volatility such as the COVID-19 crisis **requires a reliance on diverse sources of capital and strong relationships with lenders.** Moving away from too much leverage and maintaining a buffer in the borrowing base is essential in times of crisis.
- **Private credit is becoming an increasingly attractive source of investment for insurers and reinsurers**, as they compete with traditional bank lenders.

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THE SPEAKERS

Moderator:
Jay Alicandri
Partner | *Dechert LLP*

Patrick Frisch
Managing Director | *ING*

Kristine Jurczyk
Managing Director |
Vista Credit Partners

Eric Lloyd
Global Head of Private Assets |
Barings

Dan Pietrzak
Partner | *KKR*

Commentary:
John Timperio
Partner | *Dechert LLP*

Pulse of the Market: An Overview of Today's Permanent & Private Capital Industry

The events of 2020 and 2021 did not interrupt the maturing of the permanent and private capital industry. Indeed, the development of new products and the further expansion of providers demonstrated the robustness of the industry. With strong demand from the middle market private equity industry in particular, and the enthusiasm for private credit amongst investors, our panelists concluded the industry looks to be in the best of health.

- **2020 turned out to be a milestone year for private credit** with directly-originated deals proving to be less volatile than broadly syndicated loans, and default rates on private debt never exceeding historical norms. The COVID-19 crisis also reinforced that balance sheet management is critical during turbulent times.

- The global COVID-19 pandemic **provided very strong investment opportunities for Business Development Companies (BDCs) and other private debt vehicles** that had available cash and a strong balance sheet.

- **Capital inflows into the private credit market remained strong during 2020 and into 2021,** both from retail and institutional investors.

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THE SPEAKERS

Moderator:
Tom Friedmann
Partner | *Dechert LLP*

Richard Byrne
President | *Benefit Street Partners*

Kipp deVeer
Director, Partner and Head of Credit Group | *Ares Management*

David Golub
President | *Golub Capital*

David Miller
Head of Private Credit & Equity | *Morgan Stanley Investment Management*

Commentary:
Richard Horowitz
Partner | *Dechert LLP*

CLOs and Their Role Within a Private Credit Platform

Despite the perception in some quarters that CLOs are risky, CLOs have proven time and again to be a resilient product through all economic cycles over the last 20 years, including during COVID-19. Effective CLO management is increasingly dependent on being part of a broader credit platform and the ability to analyze micro and macro trends. CLO managers are confident of further growth in a low interest rate economy, though there is wariness of the true impact of the COVID-19 crisis in the longer-term. Our panelists noted:

- **The CLO market has come through virtually unscathed** during COVID-19-related turbulence, proving once again its resilience as a product through all recent crises.
- **Effective CLO management stems from knowledge across the credit space**, being able to access colleagues with deep knowledge fundamentals, including special situations and structured credit, and taking a view at a micro and macro level. Another key advantage is being able to leverage IT infrastructures, other technologies and processes that come through a large platform.
- **More consolidation is expected** but will be concurrent with new entrants to the CLO management field, according to panelists. There are still opportunities for differentiation based on specialty and size, with investors now able to effectively select managers based on extensive and transparent data/deal information.
- **The growing enthusiasm for ESG stipulations marries well with assessing credit risk.** Analyzing ESG risk has become a core consideration in the market, including analyzing whether something is refinanceable. Investors are increasingly rewarding managers that are more forward-thinking on ESG.

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THE SPEAKERS

Moderator:
Chris Duerden
Partner | *Dechert LLP*

Christopher Condelles
Managing Director, Head of Capital Markets | *FS Investments*

Lauren Basmadjian
Managing Director, Co-Head of Liquid Credit and Head of US Loans & Structured Credit | *The Carlyle Group*

Adrienne Butler
High Yield Portfolio Manager and Head of US CLO Funds | *Barings*

Less Traditional Assets: Creative Solutions and Strategies in Portfolio Construction

New strategies to target less traditional credit assets are attracting considerable interest, notably with the development of platforms that offer a range of strategies and the potential for higher returns than traditional direct lending. Our panelists emphasized several key points.

- Investors are looking to diversify their credit portfolios to include less traditional credit investments, either as part of a broader credit investment, or through investments in credit assets that are tailored to particular solutions. As the appetite for private debt has increased as a recognized **separate asset class**, diversification across strategies is taking center stage. Financial innovation is leading to institutional disruption and greater disintermediation with private credit reinforcing disruption.

- Investors are keen for **opportunistic and more unique strategies**, particularly as traditional direct lending returns are narrowing.

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THE SPEAKERS

Moderator:
Bill Bielefeld
Partner | *Dechert LLP*

Michael Guarnieri
Managing Partner | *Evolution Credit Partners*

Dwayne Hyzak
Member of the Board and Chief Executive Officer | *Main Street Capital*

Stephen Nesbitt
Chief Executive Officer | *Cliffwater*

Putting the "Fun" in Fund Formation

Negotiations frequently become heated and complicated as part of the fund formation process. Listening to the counterparty and providing full explanations are pivotal to balancing key relationships with the need to achieve the best possible terms. Our panelists identified the following key strategies for longer-term results.

- **GPs depend on long-term relationships with investors** and are not solely concentrated on the current fund launch. Multi-strategy firms will also want to cross-sell other products. There needs to be goodwill throughout difficult negotiations.
- **Both sides need to be reasonable and compromise,** knowing that each can't get everything that they want. Each side must try to understand why the other is asking for something and explain why it is not possible to accommodate. It is important to understand where a request is coming from and the consequences to the investor of not having it. Pick up the phone and explore the issues to understand what is behind the requests.
- Wherever a party can, **it should offer an alternative solution that might work for both sides.** It shows a willingness to work with the other side.
- **Remain calm and not emotional when it comes down to the wire.** Even when a fund is near to closing, it can become easy to get frustrated. Parties should stay calm and not let emotions get out of control.
- **Provide real explanations for why something is essential or not possible.** The word 'market' is the most overused and ineffective argument in fund negotiations, according to the panelists.

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THE SPEAKERS

Moderator:
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Partner | *Dechert LLP*

Dean Collins
Partner | *Dechert LLP*

Anne Cook
Assistant General Counsel |
Principal Financial Group

Afsar Farman-Farmaian
Managing Director,
General Counsel and
Senior Compliance Officer |
Varagon Capital Partners

DE&I and ESG: As the World Turns

Diversity, Equity & Inclusion (DE&I) and Environmental, Social and Corporate Governance (ESG) have each become a primary strategic focus for asset managers. COVID-19 and recent heightened attention of global civil rights have turbo-charged the debate around these priorities, and regulators and the younger investors are demanding meaningful cultural change. Further, data indicates that these factors enhance financial performance rather than diminish it. Our panelists emphasized the following points.

- A **sustainable business is a better business**, with embedded ESG and DE&I having a direct impact on financial performance and expanding the investor base. It is no longer perceived as a choice between profitability and sustainability. An organization's credit rating may well become affected by its ESG and DE&I status.
- **EU regulations** have resulted in managers changing their policies in line with disclosure and reporting obligations. Institutional investors are now focusing more on green investments and alignment with the Paris Agreement on climate change.
- The DE&I debate has **gone beyond simple metrics**. There has been a significant shift towards inclusion and attention to how diversity impacts decision-making and the corporate culture. There is now a greater emphasis on whether diverse members are wielding sufficient power, whether leaders listen to the voices of others within the organization and whether people feel safe to speak up, even when their opinions differ from the leadership.
- **Generational shifts** are bringing a greater focus on ESG and DE&I, which presents additional challenges in relation to recruitment and retention. Talent will seek employers that hold values that are aligned with their own. Younger investors will want to invest in socially responsible companies.
- Ensuring diverse leadership at companies (and hiring diverse outside vendors) should be a focus for all firms – and it begins with the **tone at the top**, with leadership demonstrating its importance.

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THE SPEAKERS

Moderator:
Vincent Cohen, Jr.
Partner | *Dechert LLP*

Jennifer Ishiguro
Partner, Chief Legal Officer | *StepStone Group*

Greg Nixon
Head of Strategic Investments, Senior Managing Director and Senior Legal Counsel | *Cerberus Capital Management*

Ana Carolina Oliveira
Director, Head of Sustainable Finance Americas | *ING*

Mikhaelle Schiappacasse
Partner | *Dechert LLP*

Compliance and Enforcement Considerations for Private Fund Advisers

With a new United States administration comes a new SEC Chairman and enforcement agenda. Our panelists noted the following resulting in an agenda encompassing a more forceful approach to exams and rules, and requiring the private fund sector to be more attuned and prepared to deal with the new regime.

- Under new Chairman Gary Gensler, the SEC is expected to be a **more aggressive and assertive** regulator and rule maker.

- The SEC is likely to impose more rules around **market structure and transparency**, particularly with regard to bitcoin and cryptocurrencies.

- The SEC is expected to adopt a greater emphasis on **ESG** in line with the Biden administration's policy to combat climate change. The SEC's Division of Examinations' recent risk alert on ESG products, as well as the SEC's Division of Enforcement's creation of a Climate and ESG Task Force, sends a powerful signal to the market, including investment advisers and private funds.

- In the private funds world, panelists predicted a **renewed emphasis on exams and enforcement** with regard to fees and expenses, conflicts of interest, and adherence to compliance policies, including policies concerning MNPI.

- Given the close working relationship between the SEC exam and enforcement teams, panelists emphasized the importance of ensuring that exam responses are thorough and that any concerns identified by the exam staff are immediately addressed. Businesses should always remain respectful of the exam team and **ensure that senior management is fully informed**, that testing is substantive, and that the organization conveys the right tone at the top.

THE SPEAKERS

Moderator:
Cathy Botticelli
Partner | *Dechert LLP*

Bruce Karpati
Partner, Global Chief Compliance Officer | *KKR*

Guy F. Talarico
Chief Executive Officer and Founder |
Alaric Compliance Services

Scott Weisman
Managing Director,
Global Chief Compliance Officer |
Bain Capital

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View From the PE Firms: The Current Market for Financing Private Equity Transactions

The private equity sector has been transformed and empowered by private credit, particularly in the middle market. As the private credit offering continues to mature, the size of private equity deals that are now being financed has grown considerably with private debt now becoming established in large-cap transactions. Private equity houses are frequently choosing private credit thanks to its relative speed, flexibility and sector specialization, though traditional bank lenders are competing to maintain market share. Here are some thoughts from our panelists:

- **Speed and certainty** of execution and terms are the principal advantages of private debt versus traditional bank lending for private equity financing.
- Although better known for servicing the middle market, private equity panelists recognize that **private credit is starting to compete in larger cap deals**. This is especially true in the technology sector, where banks often face additional challenges in underwriting transactions.
- Private equity panelists acknowledge that **banks are competing hard** to maintain a strong position in middle market lending. Although they have traditionally struggled to offer the same flexibility around covenants and documentation, they are building their own middle market lending platforms and reinventing themselves in the private equity space.
- In the **distressed market**, private equity players are seeing the value in private credit through speedier decisions and less complexity than might be associated with dealing with a large syndicate of lenders. They also appreciate the deeper sponsor-lender relationship that they have with their preferred private debt providers.

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THE SPEAKERS

Moderator:
Chris Field
Partner | *Dechert LLP*

Christopher Bloise
Managing Partner |
Court Square Capital Partners

Scott Bronner
Managing Director |
Stone Point Capital

Milwood Hobbs
Managing Director and Head of North American Sourcing & Origination |
Oaktree Capital Management

Insights Into the World of Global Restructuring

With the unprecedented events of 2020 and 2021, the restructuring market has seen some notable changes in approaches to distressed situations, not least because of a new breed of stakeholders. While there is considerable dislocation between regions and industries, our panelists highlighted some key emerging trends.

- **Key risks to the credit markets lie in interest rates and inflation, but the dangers are non-linear**, and affect different industries differently with greater threats to automotive and real estate, among others. Inflation is a real concern in Europe as well as in the United States.
- **There is the potential for more short-term distress in emerging markets than in other economies.** Rising commodity prices are helping some markets, but financial support packages in developing economies are not at the same level as in the Western world.
- **The COVID-19 crisis has supercharged some longer-term trends**, such as additional distress in retail due to the faster pace of digitization and the shift away from bricks and mortar.
- **Restructurings are becoming less cumbersome** thanks to greater levels of capital looking for distressed opportunities, the increased savviness of incumbent investors and creditors, and the ease in which it is possible to buy into opportunities. Creditors are looking at Chapter 11 bankruptcies as being speedier.
- In the latest distressed cycle with credit funds and CLOs bringing higher levels of sophistication and more flexible documents, **they are looking for more efficiency and less friction in restructurings**. The development of restructuring statutes in many parts of the world has also given creditors more options and it is likely we will see much more forum shopping.

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THE SPEAKERS

Moderator:
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Alon Avner
Head of Credit (Europe) and Managing Director of Distressed and Special Situations | *Bain Capital*

Allan Brilliant
Partner | *Dechert LLP*

Jim Doak
Co-Head and Managing Director | *Miller Buckfire & Co.*

Erik Miller
Partner | *Canyon Partners*

Thank You

About the Permanent & Private Capital Summit

The Permanent & Private Capital Summit is one of the premier conferences covering the latest in private credit and alternative asset diversification. Since its debut in 2015, the Summit brought and continues to bring together leaders in the industry to address the rapidly developing financial and regulatory issues surrounding permanent capital.

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