TM Capital Debt Capital Markets Update Report

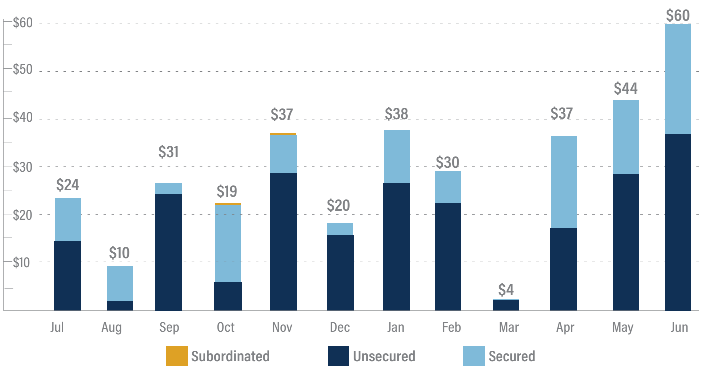
COVID-19 Financing Considerations

JULY 2020

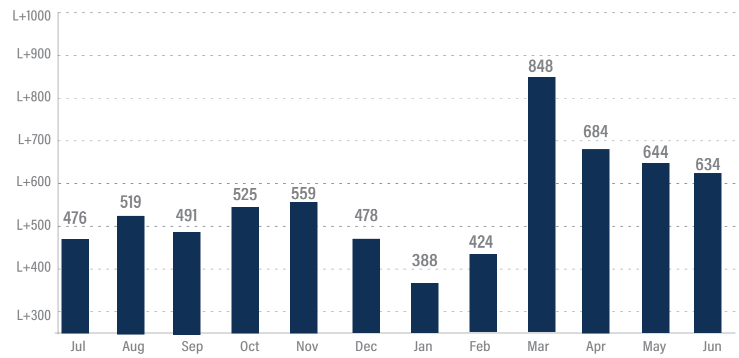
Q2 2020 RECAP

As the summer marches on and we enter month four of a COVID world, debt capital markets are slowly beginning to thaw. Some lending activity has resumed with activity accelerating in July, albeit under heightened scrutiny from capital sources and more stringent underwriting standards. Lenders continue to demonstrate reasonable flexibility with their existing credits, but new loans must meet more stringent underwriting standards due to the looming risk of a "second wave" that may lead to the return of operational restrictions as well as evolving business shifts which may become permanent. That being said, leveraged loan new issuance volume was at its highest level in months – $41 billion in June, up from a March low of only $13 billion and nearby double April and May levels – demonstrating how lenders are developing practices to price COVID risk and complete new financings, particularly for issuers that have successfully mitigated the impact of COVID. Going forward, we expect that new issuance volume will continue to be robust – as lenders become more comfortable with pricing COVID-related risks.

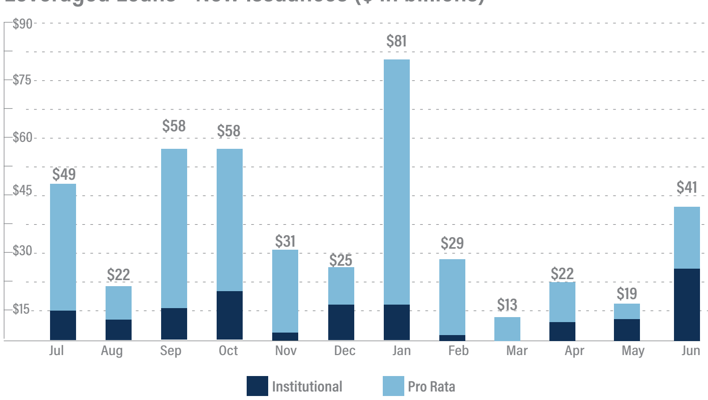
High Yield - New Issuances ($ in billions)



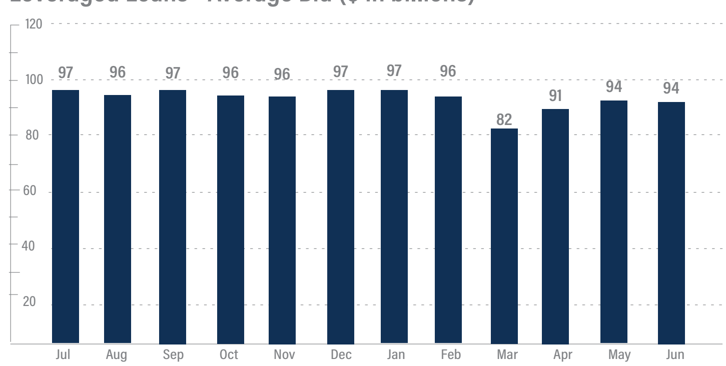
High Yield - Average Spread ($ in billions)



Leveraged Loans - New Issuances ($ in billions)



Leveraged Loans - Average Bid ($ in billions)



- High yield new issuances have recovered from March lows as spreads begin to stabilize
- Leveraged loan issuances have been slower to recover, evidencing the more onerous requirements on issuers to complete a transaction, however, bids have recovered close to pre-COVID levels after a rapid decline in March

Sources: S&P LCD

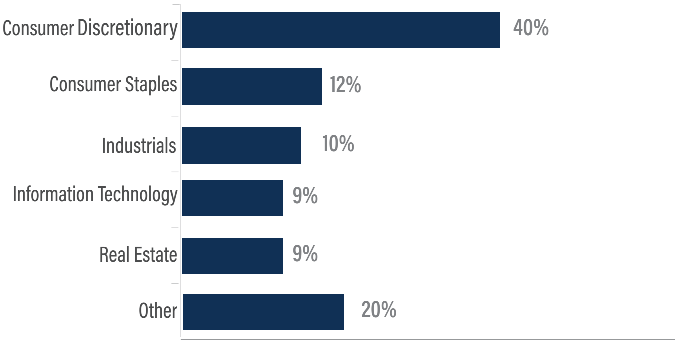
U.S. REVOLVING CREDIT DRAWDOWNS EXPANDED AND LOAN DEFAULT RATES REMAIN LOW

At the onset of the COVID-19 lockdowns, many companies accelerated their borrowing to maximize liquidity. From the beginning of March through the end of May, new revolver borrowings by U.S. companies totaled nearly $300 billion. Since then, revolver draws have stabilized, with an additional $17 billion added through mid-July.

Increased revolver draws and government-led liquidity programs including the Payroll Protection Program, the Main Street Lending Program and asset purchases have provided sufficient liquidity to dampen a significant increase in default rates, which have risen modestly but remain well below levels seen during and after the Great Recession.

CHANGE IN REVOLVER DRAWDOWNS SINCE MARCH 5, 2020

Total New Revolver Borrowings: $317 Billion



Sources: S&P LCD as of 7/10/2020

LOAN DEFAULTS BY PRINCIPAL AMOUNT: 2009 - Q2 2020

Sources: S&P LCD through 6/30/2020

COST OF CAPITAL REMAINS ELEVATED BUT STABLE

Relative to 2019, debt pricing remains meaningfully higher – reflecting the increased risks related to COVID-19. While leverage remained the same as May 2020, June saw a slight reduction in debt pricing as private credit markets begin to stabilize. Anecdotally, throughout July, competition for quality credits remains strong and could push spreads and leverage to pre-COVID levels in industries that have demonstrated resilient business models predicated on contractual or recurring cash flow

CHANGE IN MIDDLE MARKET PRIVATE CREDIT PRICING AND LEVERAGE

Unitranche Pricing			
	< $5m EBITDA	< $10m EBITDA	< $20m EBITDA
June 2020	L + 9.00% - 10.50%	L + 8.00% - 9.50%	L + 7.00% - 8.00%
May 2020	L + 9.00% - 11.00%	L + 8.00% - 10.00%	L + 6.00% - 8.50%
June 2019	L + 7.00% - 10.00%	L + 6.00% - 8.50%	L + 5.00% - 7.00%
Senior Cash Flow Pricing			
	Bank	Non-Bank < $7.5m EBITDA	Non-Bank > $15m EBITDA
June 2020	L + 3.75% - 4.50%	L + 7.00% - 8.50%	L + 6.50% - 8.00%
May 2020	L + 3.75% - 5.00%	L + 7.00% - 9.00%	L + 6.50% - 8.50%
June 2019	L + 2.50% - 4.50%	L + 5.00% - 6.50%	L + 4.00% - 6.00%
Total Debt / EBITDA			
	< $5m EBITDA	< $10m EBITDA	< $20m EBITDA
June 2020	2.50x - 3.25x	3.50x - 4.50x	4.00x - 5.00x
May 2020	2.50x - 3.25x	3.50x - 4.50x	4.00x - 5.00x
June 2019	3.00x - 4.00x	4.00x - 5.00x	4.50x - 5.50x

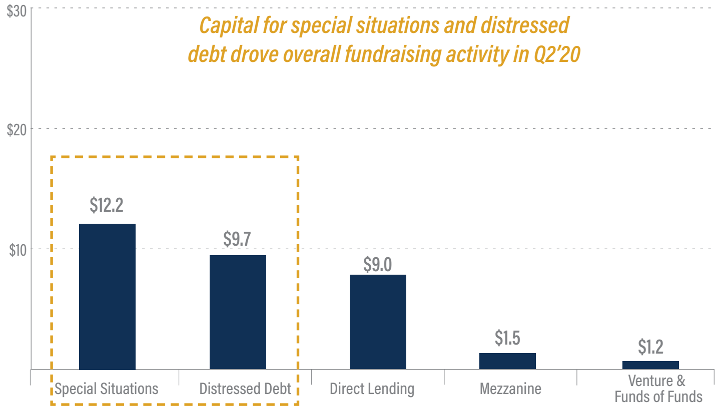
Sources: SPP

PRIVATE CREDIT LIQUIDITY AND GOVERNMENT PROGRAMS UNDERPIN NEAR-TERM STABILITY

Private credit funds focused on distressed debt and special situations drove fundraising activity in the second quarter. Overall capital raised for direct lending declined in Q2'20 over the prior year, but aggregate dry powder for direct lending remains significant. The new capital raised to execute on distressed / special situation investment strategies will help support restructurings and promote market stability. Overall, the amount of non-bank dry powder dedicated to credit strategies bodes well for issuers, as more lenders will seek opportunities to put capital to work.

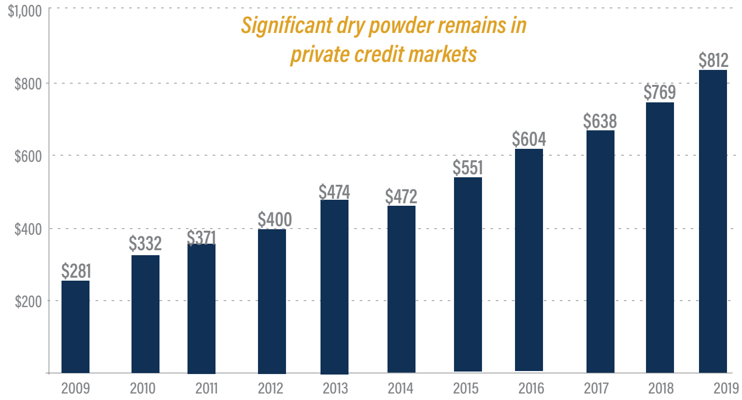
In addition to private capital liquidity, the Federal Government's "do whatever it takes" economic approach will continue to provide a stable economic foundation – the Fed recently extended its emergency lending facilities through the end of 2020. Both the Payroll Protection Plan and the Main Street Lending Program, which have allocated roughly $500 billion and $600 billion, respectively, to support lending to small and medium-sized businesses, are playing supportive and stabilizing roles as well. We expect that the next round of stimulus, which would inject another $1 trillion into the economy, will include additional PPP funds. Amid widespread action from the Fed to minimize the impact of COVID-related disruptions to the economy, rate hikes are not expected to occur until at least 2022.

Debt Fundraising Activity by Investing Strategy ($ in billions)



Source: Prequin

Private Credit - Assets Under Management ($ in billions)



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OVERVIEW OF MARKET DYNAMICS

	JUNE'20	MAY '20	APRIL '20	MARCH '20	JUNE '19
Indices					
10-Year Treasury	0.66%	0.65%	0.64%	0.70%	2.00%
10-Year vs. 2-Year Spread (basis points)	50.0	49.0	44.0	47.0	25.0
3-Month LIBOR	0.30%	0.34%	0.56%	1.45%	2.32%
DJIA	25,813	25,383	24,346	21,917	26,600
S&P 500	3,100	3,044	2,912	2,585	2,942
NASDAQ	10,059	9,490	8,890	7,700	8,006
iShares HY Corporate Bond Fund	81.33	81.84	78.99	76.83	86.93
iShares Barclays Aggregate	118.00	117.46	117.09	115.57	111.37
Commodities					
Crude Oil	$39.34	$36.20	$26.37	$20.48	$56.53
Natural Gas	$1.75	$1.85	$1.95	$1.64	$2.31
Gold	$1,801	$1,752	$1,694	$1,597	$1,420
Currencies					
GBP in USD	$1.24	$1.23	$1.26	$1.25	$1.27
EUR in USD	$1.13	$1.11	$1.09	$1.10	$1.14
USD in JYP	¥107.80	¥107.70	¥107.01	¥107.60	¥107.79
USD in CNY	¥7.06	¥7.14	¥7.06	¥7.08	¥6.87
Average New-Issue Loan Pricing - B+/B					
Total Spread (basis points)	599.0	627.0	N/A	452.0	424.0
YTM	5.89%	6.13%	N/A	6.24%	6.79%

Sources: S&P LCD

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