THE INDEPENDENT VOICE OF EUROPEAN PRIVATE EQUITY

Real Deals

15.10.20/470/realdeals.eu.com

INSIDE

BVCA SUMMIT
ESG, value creation and the future of PE firms.

GP WORKSHOP
How to run a virtual exit process.

WEBINAR: DIGITAL PORTFOLIO MONITORING
Operating digital portfilio management tools.

INVESTING IN TECH PRODUCTS
Five things to consider.

SWEET ENOUGH?

Tempting offers and off market deals.

Q&A

CORPORATE FINANCE CORNER

JEFFREY SWEENEY

CEO, US Capital Global

Jeffrey Sweeney, CEO at US Capital Global, discusses how corporate finance advisers can optimise client outcomes in the current environment by leveraging partnerships with debt advisors.

By *Simon Thompson*

Debt finance has been on hand for some years. Why are we seeing an acceleration?

Because of everything that is happening just now, I would compare it to mid-2007. The mess has not fully hit the fan yet and it probably won't hit as badly. At the same time, you have a lot of sectors that are just ruined, such as city retail, hospitality and the airlines. These are sectors that are going to be tough for some time. Even outside of these areas, we're seeing a lot of restructuring, bankruptcies and debt financing to get these companies propped up—especially if they're overburdened with debt from when it was cheap and the economy was booming.

A key factor compounding all this is risk aversion in the market, with the banks continuing down the path of de-risking. It started in 2008, and they have increasingly moved away from anything that resembles risk. Their risk profiles are moving to consumer credit or mortgages, all the vanilla stuff. Banking institutions are considered to be quasi-government now. We call it the "post office-ication" of banking, with banks that are now more like post offices.

While this bank retrenchment has been an ongoing process, Covid-19 has just been accelerating it. A lot of banks' investment banking arms have been spun out and are now run as private entities. That's why private capital and private lending exploded after the financial crisis. It was fairly chaotic back then, but now it's a very mature sector, one in which we can expect to see a lot more growth.

To what extent is debt increasingly coming into transactions?

At US Capital Global, we have the full picture as we offer debt, equity, and investment products for lower-middle market companies and investors both in the UK and Europe and in the US. There are many corporate finance advisors who are used to making big

pitch decks and going out and raising equity, but that's tougher now. As a result, we're getting a lot of calls on restructuring, like we did in 2009-2010.

Compounding it further, there are many good companies that are about to become refugees from the banks. Banks are throwing them out, not because they're bad companies, but because the banks have to. These companies come to the debt guys, and if you're an investment bank with a focus on debt, it translates into a lot of deals.

What does the current situation mean for corporate finance advisors specialised in raising equity?

It means partnering with and bringing in debt advisers like us. If you're a general practitioner, you're not going to learn how to do heart surgery overnight; it's not going to happen. We are basically the debt surgeons. Debt people know how best to collateralize, structure, and syndicate debt financing. Those specialising in raising equity are doing big deals with equity, but when you move into debt, you have to bring in the "heart surgeon".

How can CF advisors' offerings be hybridised with debt?

If equity is cheap and is flooding in, you don't care. But if equity is a little tighter, you start needing to look at capital stacks and where you can leverage in order to free up capital and augment the lack of equity.

Early on, when the equity was flooding in, many companies would do a lot of things with equity that should have been done with debt. For example, they might buy equipment or finance working capital. All that sucks up their equity. You can only lever certain things for debt. So, you don't want to waste your equity on financing things that you can lever; you want to keep it for the things you can't borrow on. This becomes critical if there is a shortage of equity that can be raised, which is what many companies are facing right now.

How are partnerships between debt and corporate finance equity advisers configured?

We can raise capital through debt and equity and syndicate funding in both. When you bring in a global debt solutions firm like ours, it might be because you have reached the end of your expertise and the end of your rolodex. That is where we take the engagement with the client and give referral fees back to the introducer of the deal, or the introducer will have a separate agreement with the client whereby they receive fees for their arrangement. Usually we come to a V-split arrangement, or some other fair agreement on commissions and fees. It is something we do all the time; referrals are the lifeblood of our business. I value referral sources, especially when they have a relationship with the client. Ultimately, we look at the whole pool and come to an agreement that is fair for all parties. Any commissions come out of closing, when everybody gets paid.

How do you deal with introducers' concerns over losing their clients?

You have an agreement in place with the referral source. First, we execute an NDA, so we can't talk to the client. Next, we come to an agreement on the terms of engagement. The CF and client might want us to come in and structure a debt piece. But we won't enter into any agreement with the client that cuts the introducing CF out of their existing relationship with the client. Once the terms are agreed, we can move forward. We want to make sure all parties are protected.