Half-Time Report (Second of a Series)

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"July 4th is the worst holiday," one of our friends declared as our families sat watching the jaw-dropping fireworks display last Wednesday evening in Newport, RI. Huh?

"Think about it," he explained. "Now the summer will zoom by. Kids back in school last week of August. Then Labor Day. A month later, Halloween. Before you know it, bingo – Thanksgiving, Christmas, the whole winter thing." He sighed. "See what I mean?"

It *did* seem like just yesterday we were changing our snow tires. But we aren't ready to throw in the beach towel quite yet. At any rate not with the leveraged loan market demonstrating such uncharacteristically investor-friendly exuberance.

For the first six months of 2018, middle market sponsored loan volume weighed in at more than $40 billion, according to Thomson Reuters LPC. That's better than 2017's $37 billion and is on pace to beat last year's total of $78 billion. It also mirrors the trend occurring in the broader loan market, as we covered last week.

Unlike at the liquid end of things, however, the supply/demand dynamics are a bit different for direct lenders. Instead of CLOs and loan funds sopping up new deals, higher hold levels of those lenders are the culprit. And these players aren't generally underwriting to sell off paper and skim fees. They are buy-and-holders looking to spread out their exposure across a variety of vehicles managed on behalf of investors.

Yes, fundraising for private credit is following a similar pattern to new CLOs and fund cash-inflows in large cap land. This year we're on track for a third straight $100 billion year in new private credit money raised. Although, as we've outlined in the past, most of this capital will be directed to higher-yielding strategies like second-lien and mezz.

LevFin Insights reports that first-half capital raising for midcap dedicated funds was $27 billion, ahead of last year's $23 billion for the same period. New 1Q fund filings of $13.3 billion was at the highest level since LevFin started tracking data early last year. This fundraising includes middle market CLOs, new funds, and BDC equity raises.

As with the broader market, midcap deal flow continues to be robust. That flow, along with the buy-side friendly trends being seen in the broadly syndicated market, is having an impact on the syndicated tier of the upper middle market. That's the most liquid of an illiquid asset class since buyers tend to be similar to large caps – mostly CLOs, funds, and institutional investors.

Pricing flex, the canary in the capital markets' coal-mine, is pushing spreads and OID wider, particularly for transactions with some sort of story (see *Chart of the Week*). That includes more cyclical industries, toppy leverage, and ebitda addbacks.

Next week we look at issuer-friendly terms that have persisted in this market.