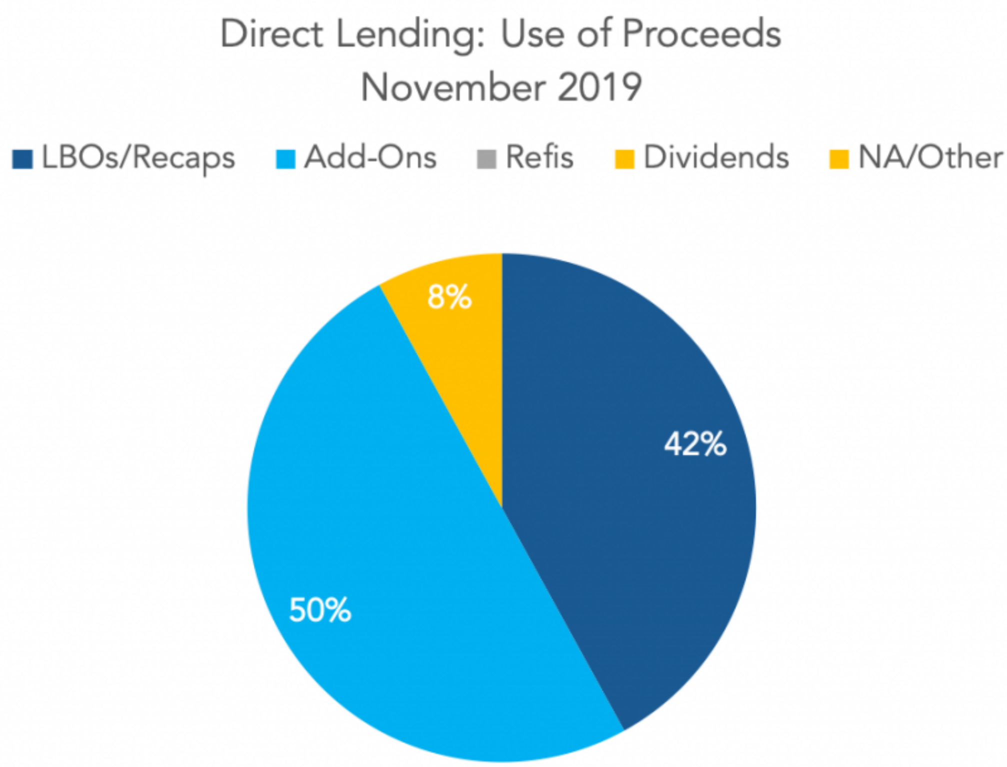
Direct Lending: Add-ons maintain share over buyouts in November

KBRA DLD | December 12, 2019



Add-on acquisitions continued to drive financings over buyouts in November, accounting for half the tally, compared to 42% for LBOs, according to *Direct Lending Deals.* Other proceeds, which include growth financing, accounted for 8% of volume, according to *DLD*.

Going forward, large-cap issuers are expected to propel M&A volume for direct lenders in 2020 as B-/B3 companies increasingly bypass pushback from CLO investors.

It's not that CLO managers have suddenly become averse to B-/B3 risk, it's that their baskets are full. If they are to book new paper at spreads over 100 bps higher than they were a year ago, they need heavy discounting to counter the hit they'll take unloading lower-priced loans in the secondary to make room for new credits. Two recent executions exemplify this: **Syncsort** (B-/B3) closed at a discount of 92 and a spread of L+600, while **Monotype Imaging** (B-/B3) closed at 94 at L+550.

This also leaves the door open for investor-friendly changes to documentation.

In the $10-40M EBITDA band, there is far less volatility because these technical issues simply don’t exist for two main reasons: 1) it’s an illiquid market, and 2) credit funds typically book to hold, and without the pressure of relative value plays and defined rating baskets.

Lenders expect add-on volume to continue apace, while buyouts will be harder to close. Uncertainty is the biggest enemy against buyers and sellers next year. Cyclicals face concerns about the credit cycle’s late stage, while industries affected by tariffs will see more scrutiny, as will healthcare, which will be impacted by who ends up in the White House.