AlixPartners

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ALIXPARTNERS MID-MARKET DEBT REPORT: H1 2024 REVIEW AND H2 2024 OUTLOOK

After a prolonged period of elevated interest rates, recent cuts in both Europe and the UK should pave the way for increased deal activity and improved access to credit. Reignition of M&A and enhanced macro stability post-elections should continue to support this momentum. While the large-cap market has been busier in the first half of 2024, this has started to slow more recently. However, there are indications that this will convert into a greater number of smaller deals as H2 progresses, which bodes well for banks and private credit lenders in terms of deal counts through to the end of the year.

The 21st edition of the biannual AlixPartners' Mid-Market Debt Report covers more than 75 bank and non-bank lenders active in the UK and European mid-market (debt transactions valued up to €400m).

POSITIVE MACRO SIGNS

- While interest rates/bond yields have remained high through H1 in general, rate reduction expectations, followed by the UK cut in August, in combination with more stable forward-looking interest rate curves, have supported a slight pick-up in investor appetite to deploy capital with more expected in H2.

AN M&A RECOVERY?

- Q1 started slowly from an M&A perspective, however momentum started to build in Q2. M&A volume in EMEA increased by 33%[1] in H1 2024 compared to H1 2023.
- Businesses held off transactions during continued inflation increases and interest rate hikes, and M&A activity was expected to increase as soon as these pressures eased. Both corporates and sponsors have been eager to complete strategic transactions and realise investments.
- Stabilisation in the general macro environment is helping here, albeit political change and uncertainty continues to hang over markets to a degree. The conclusion of the UK and French elections, along with continued stability might unlock even greater activity in markets in H2 2024 and into 2025.

DEBT ACTIVITY REMAINS RESILIENT

- On average, participants in this survey completed 9.7 deals in H1 2024, up from 7.5 across each half of 2023.
- In addition to LBO and add-on activity recovering by 21%, refinancing activity increased by 10%. Sponsors have held onto assets longer than usual due to economic uncertainty and valuation divergence between buyers and sellers. This led to an increase in maturities with sponsors needing to refinance and defer exits.
- Pricing has been tightening and leverage has crept back up in Q2 in particular, indicating a general recovery in credit appetite that bodes well for H2.

BANKS FIGHTING BACK?

- Banks increased their share of leveraged transactions, participating in 46%, up from 32% over the last 3 years.
- Economic uncertainty has increased diligence requirements from credit committees; therefore, borrowers are experiencing slower processes and greater scrutiny from both banks and funds. Funds typically appeal to borrowers looking for flexibility and simplicity; however, lower pricing from banks is potentially of greater importance currently, particularly as borrower P&Ls are under pressure.

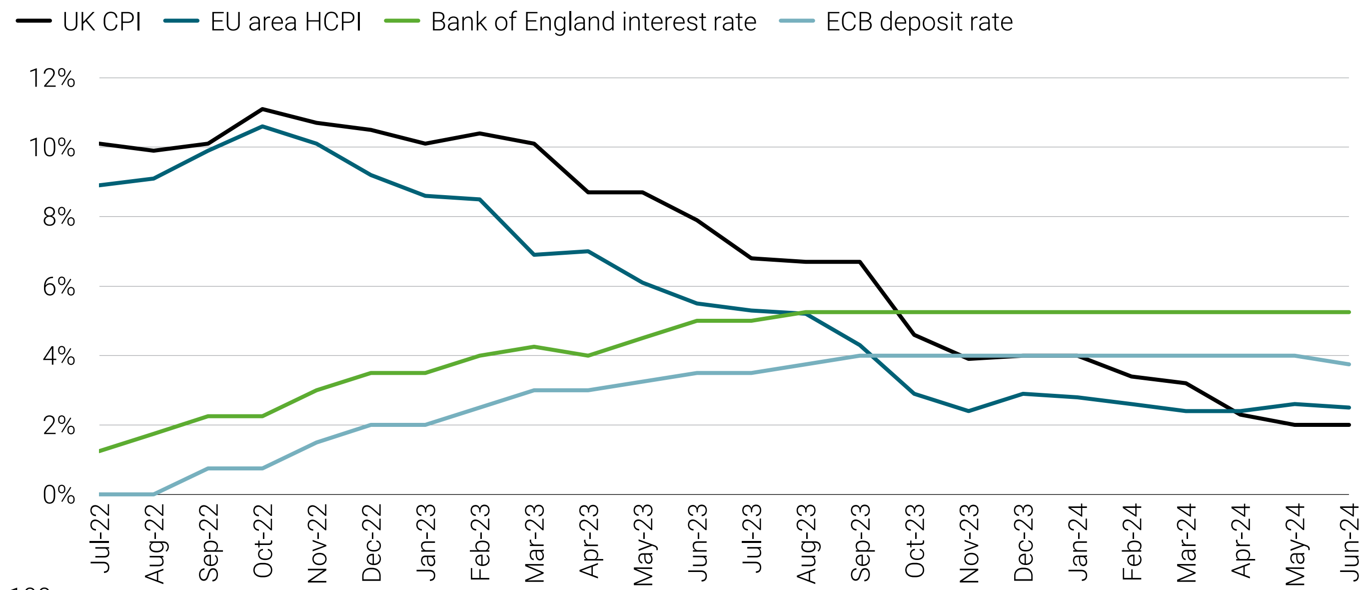
WILL EMERGING MACRO STABILITY CATALYSE TRANSACTION GROWTH?

- With credit market liquidity and lower deal flow, leveraged refinancings have been greater in volume than perhaps anticipated, as borrowers continue to find capital solutions. However, this may have deferred challenges that could still be prevalent across balance sheets and financial performance.
- Variables driving the cost of capital continue to stabilise on a global basis, creating a more amenable environment for capital decisions amongst borrowers, lenders, and investors. UK eyes now turn to the new Chancellor's Autumn Budget on 30 October to determine whether tax and policy announcements will drive an evolution in the cost of capital or free cash flow to service debt. We expect transaction volumes to continue growing in Q4 and through 2025.
- In private credit, there have been significant capital raisings ahead of the refinancing wave in the period to 2027. Total return on private capital continues to be attractive for lenders, and borrowers continue to adjust to the new normal, illustrated by relatively flat interest rate curves.
- The combination of sponsors extending hold periods and/or higher levels of leverage has catalysed growth in the market for Mezzanine, Second Lien, and PIK financing. This activity creates liquidity for borrowers or investors / owners, and also supports bolt-ons, which the M&A market continues to see much of.

1) Mergermarket M&A Highlights 1H24: In Recovery

A wave of elections shapes the geopolitical landscape for 2024 and beyond, while interest rates finally begin to fall

- **15-17 March 2024 –** Incumbent Vladimir Putin is re-elected for a fifth term of presidency in Russia.
- **6 June 2024** – The European Central Bank (ECB) cuts its main interest rate from 4% to 3.75% - the first cut since its steady rise from 0% in July 2022.
- **6-9 June 2024 –** Ursula von der Leyen re-elected as European Commission president.
- **4 July 2024 –** Sir Keir Starmer wins a landslide victory for Labour in the UK General Election.
- **7 July 2024 –** French parliamentary elections leave the country in political deadlock after no party achieves a majority.
- **1 August 2024 –** The Bank of England cuts interest rates to 5% from 5.25% - the first cut since the start of the pandemic in March 2020.
- **9 September 2024 –** The European Central Bank (ECB) cuts its main interest rate from 3.75% to 3.5%.



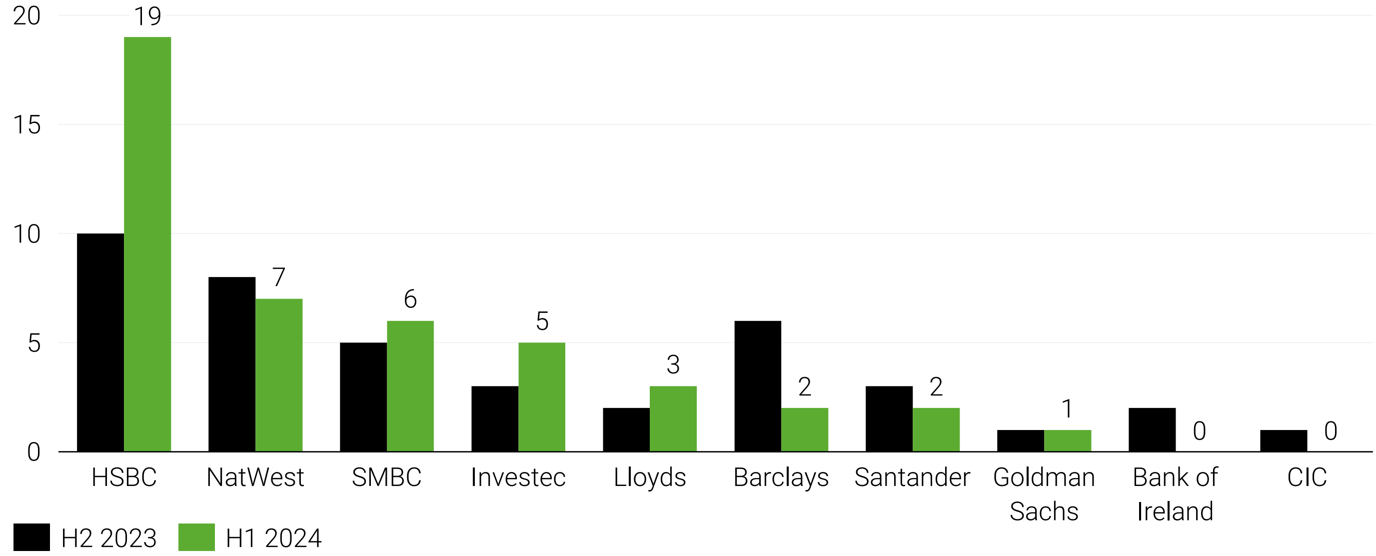
Q2 2024 SAW THE START OF THE RECOVERY IN DEAL ACTIVITY, WITH MACROECONOMIC FOUNDATIONS FOR A MORE DEBT- AND M&A-FRIENDLY ENVIRONMENT IN H2 AND BEYOND

Since Q4 2022, deal activity has been subdued, but activity has started to recover in Q2 2024. 258 transactions were reported in our survey in Q2 2024, an increase of 25% on Q1 2024, and only 10% lower than the peak in Q3 and Q4 2021. On average, participants in this survey completed 6.4 financings in Q2 2024, 50% higher than the average per quarter in 2023 and the highest level we have reported, except for Q3 2021. Expectations that interest rates would fall (which were realised in August in the UK) combined with stabilisation of forward indicators and a deceleration of inflation has increased investor appetite to deploy capital.

Sources: https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/june2023; https://www.bankofengland.co.uk/boeapps/database/Bank-Rate.asp; https://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html
Please refer to the disclaimer at the end of this report for further context on the data

Bank deal activity in the UK increased by 22%, driven by a surge in super senior financings; including European deals, activity increased by 36%

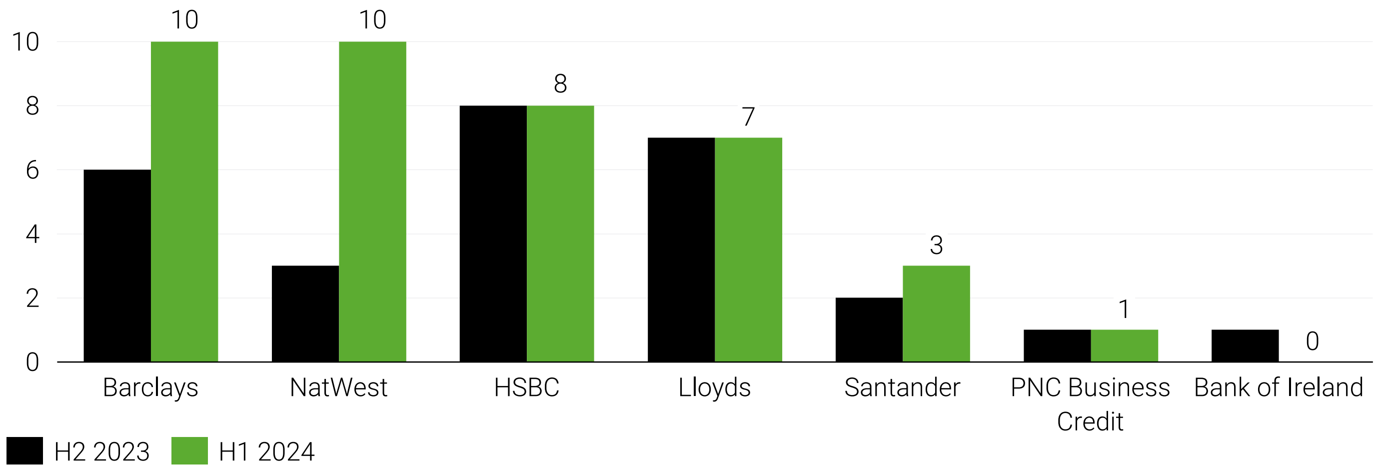
FIGURE 1: UK LEVERAGED BANK DEAL COUNT (EXCLUDING SUPER SENIOR)



INSIGHTS

- Excluding super senior deals, UK banking activity in H1 2024 increased by 10%, from 41 deals in H2 2023 to 45 deals. HSBC recorded the highest number of deals, up from 10 deals to 19. NatWest and SMBC remained active with seven and six deals respectively. Investec also increased activity to five deals, up from three deals in the previous half.
- Including deals outside of the UK, deal activity (excluding super senior facilities) increased by 28% from 104 deals to 133 deals. CIC completed 31 deals, an increase of eight from 23 in H2 2023. Bank of Ireland, Investec, Goldman Sachs, and SMBC all completed more deals in H1 2024 than in H2 2023 in Europe.

FIGURE 2: UK BANK SUPER SENIOR DEAL COUNT



INSIGHTS

- UK super senior RCF deal activity increased by 39% to 39 deals, up from 28 in H2 2023. In the face of higher financing costs, borrowers are focusing on lower cost products, such as super senior facilities. With the exception of Bank of Ireland, all lenders completed at least the same number of deals. Including European activity, PNC Business Credit and Bank of Ireland also increased activity in H1 2024.
- Barclays almost doubled the number of super senior financings in the UK from six to 10 deals. NatWest more than tripled their activity level from three to 10 deals. Both HSBC and Lloyds completed the same number of deals as the previous six months at eight and seven deals respectively.
- Including super senior deals, banking activity reached the highest level reported in this survey since 2018, up 36% to 183 deals, from 135. Across our survey, banks participated in 46% of transactions, the highest level since H1 2019. Super senior deals across Europe reached 50, only the second time that 50 deals have been reported in this survey (alongside H1 2021).

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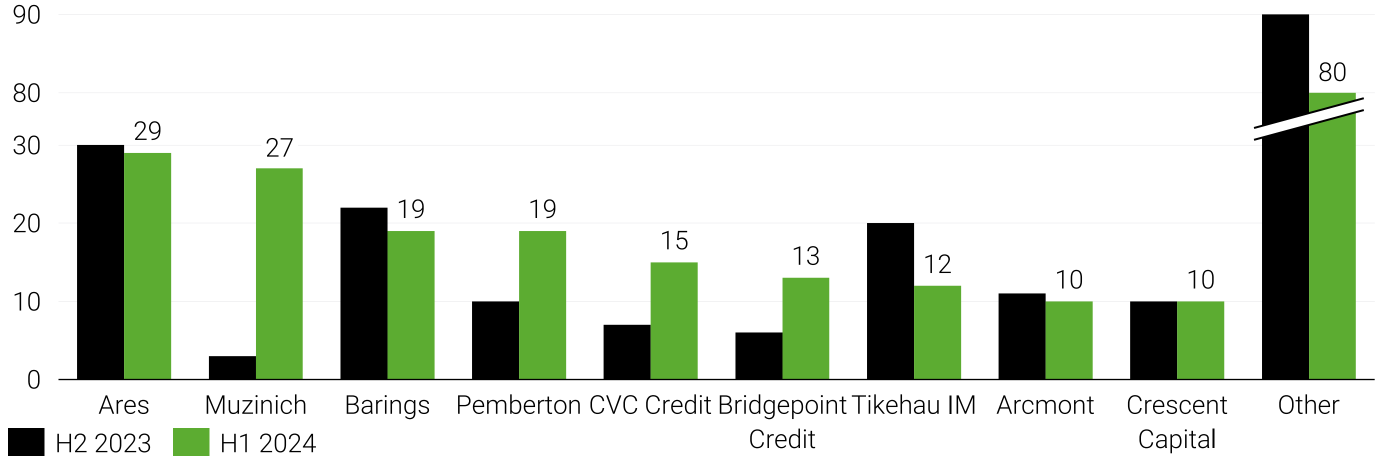
Non-bank activity increased by 12%, as credit conditions continued to improve and almost all sectors reported higher activity levels

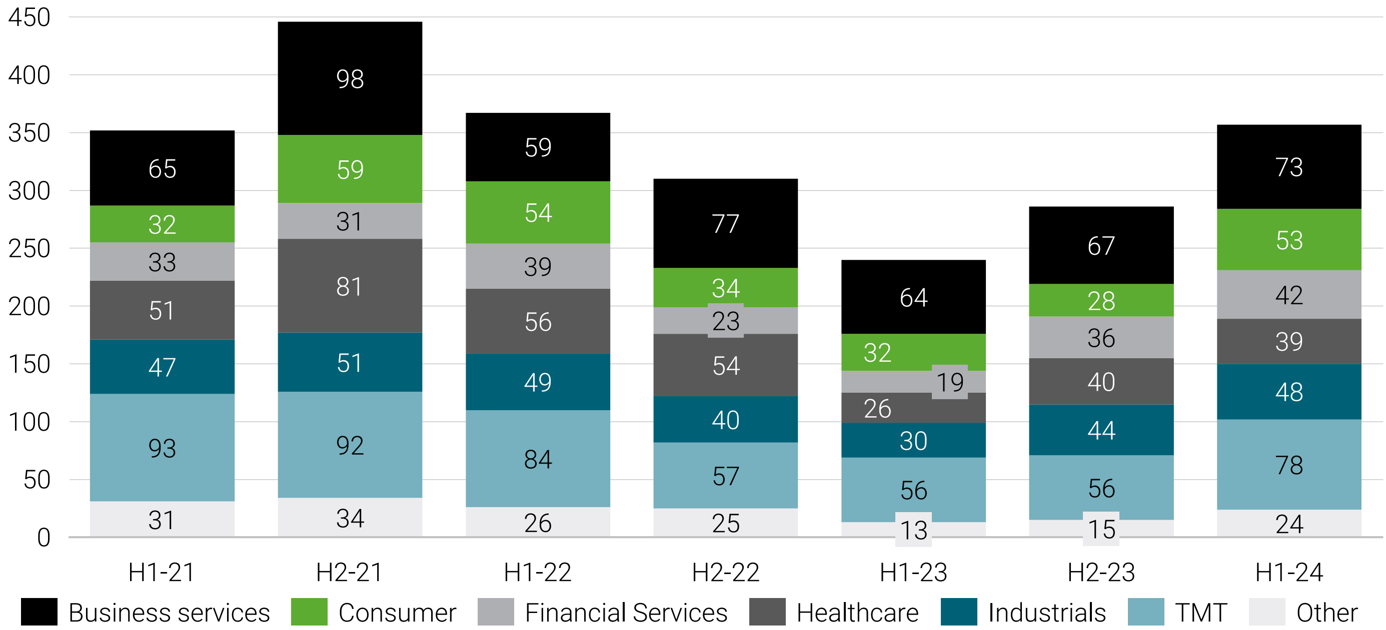
FIGURE 3: EUROPEAN LEVERAGED NON-BANK DEAL COUNT



INSIGHT

- 234 European non-bank deals were completed in the first half of 2024, an increase of 12% from 209 in H2 2023.
- Ares continues to be one of the most active lenders in this part of the market, completing 29 deals, down from 30 deals in H2 2023. Muzinich significantly increased deal activity, completing 24 more deals in H1 2024 than in H2 2023, with 27 deals. Both Barings and Pemberton completed 19 deals.
- Competition to raise funds and deploy capital to non-cyclical credits has been strong in the face of economic uncertainty and financial distress. This has led to polarisation in fund performance, with some excelling and others struggling to deploy capital and fundraise.

FIGURE 4: EUROPEAN LEVERAGED DEAL ACTIVITY BY SECTOR



INSIGHTS

- All sectors reported at least the same level of activity as the previous six months, except for healthcare that decreased by one deal. Despite consumer spending challenges, consumer-focused deals increased by 28 to 53, almost double the prior half. The increase was driven by a 167% increase in refinancings and a 90% increase in LBOs.
- TMT activity remained popular, accounting for 78 deals, up from 56. Most of the increase was driven by a recovery in add-on/acquisition activity, up from 13 to 27 deals, which is consistent with 2021 and 2022 levels. The recent boom in AI will have been a key factor and is likely to drive further activity in the space as more businesses deploy the technology.
- Healthcare activity remained steady at 39 deals, down one from 40 in the prior half. Healthcare deals boomed in 2021 and 2022 following the pandemic, and now appear to have cooled off, albeit at a level above the pre-pandemic average.

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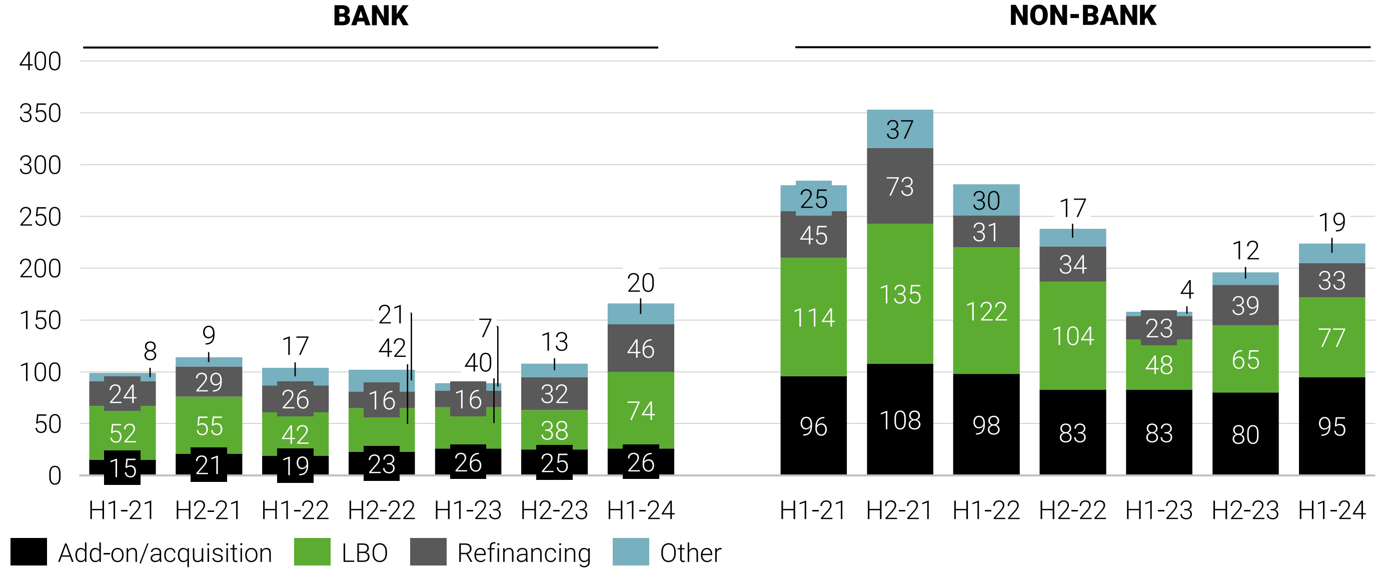
Banks increased their market share to levels last seen in 2018/2019, driven by an increase in both LBO and refinancing activity

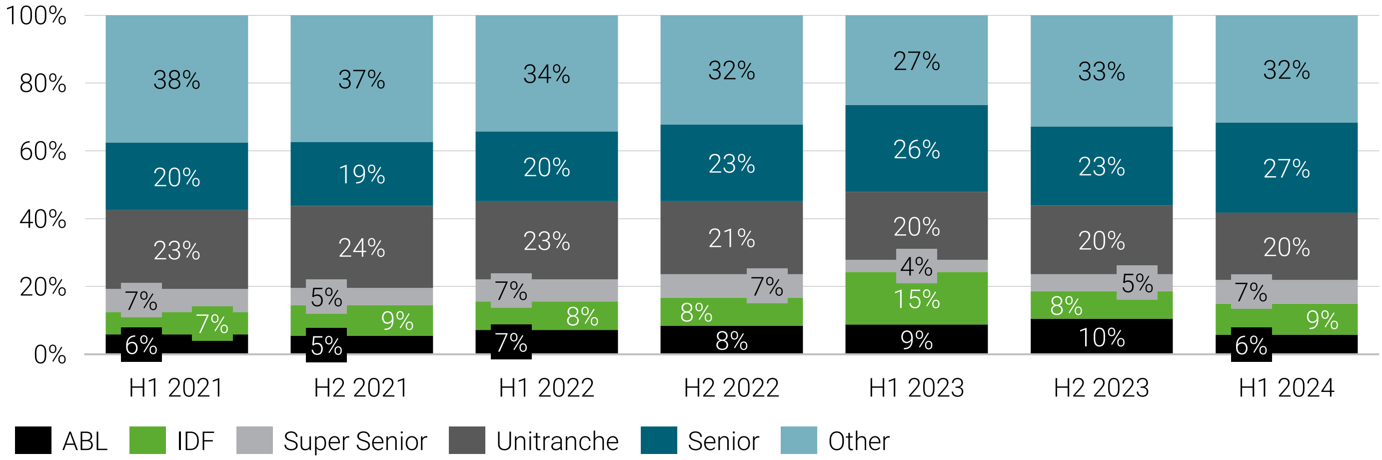
FIGURE 5: EUROPEAN LEVERAGED DEAL ACTIVITY BY PURPOSE, BANKS VS NON-BANKS[1]



INSIGHTS

- Banks were involved in 46% of transactions in H1 2024, equivalent to 166 transactions and an increase of 54% from 108 in H2 2023. Funds were involved in 224 transactions, an increase of 14% from 196. Because banks sharply increased activity, funds' involvement in deals dropped to 63%, the lowest level since 2018. Banks have faced significant competition from credit funds in recent years; however, in the face of higher interest rates and cost pressures across the P&L, borrowers are foregoing the simplicity/flexibility for lower cost, which favours banks.
- LBO activity increased by 40% to 130 transactions in H1 2024. This marks a significant recovery from the levels seen in 2023 and is higher than the average of 120 transactions reported from 2017 to 2019. Notably, LBO transactions involving banks almost doubled from 38 to 74, which is equivalent to banks being involved in 57% of transactions. Funds also participated in more LBO deals, up to 77 from 65 in H2 2023. This trend is consistent reported increases in LBO activity globally, Mergermarket reported EMEA buyouts increased by 113%[2] in H1 2024 compared to H1 2023.
- Add-on/acquisition deals increased slightly by 16% from 100 to 116, driven by credit funds. Refinancing activity slightly increased from 68 to 73 refinancings, which was led by increased bank activity, from 32 to 46 deals, but slightly offset by credit funds, who fell from 39 to 33.

FIGURE 6: EUROPEAN DEAL ACTIVITY BY STRUCTURE



INSIGHTS

- In recent periods, economic uncertainty has weakened investor appetite, and, in turn, borrowers/lenders have achieved financings by using more senior debt structures. 28% of deal activity in H1 2023 involved super senior, IDF, and ABL facilities. However, this reduced to 22% in H1 2024, which is more in line with the levels reported in 2021 and 2022. This indicates that lenders' concerns about cash flows may have started to ease, albeit potentially with reduced debt capacity.

1) Transactions involving both banks and non-banks are included in both charts
2) Mergermarket M&A Highlights 1H24: In Recovery
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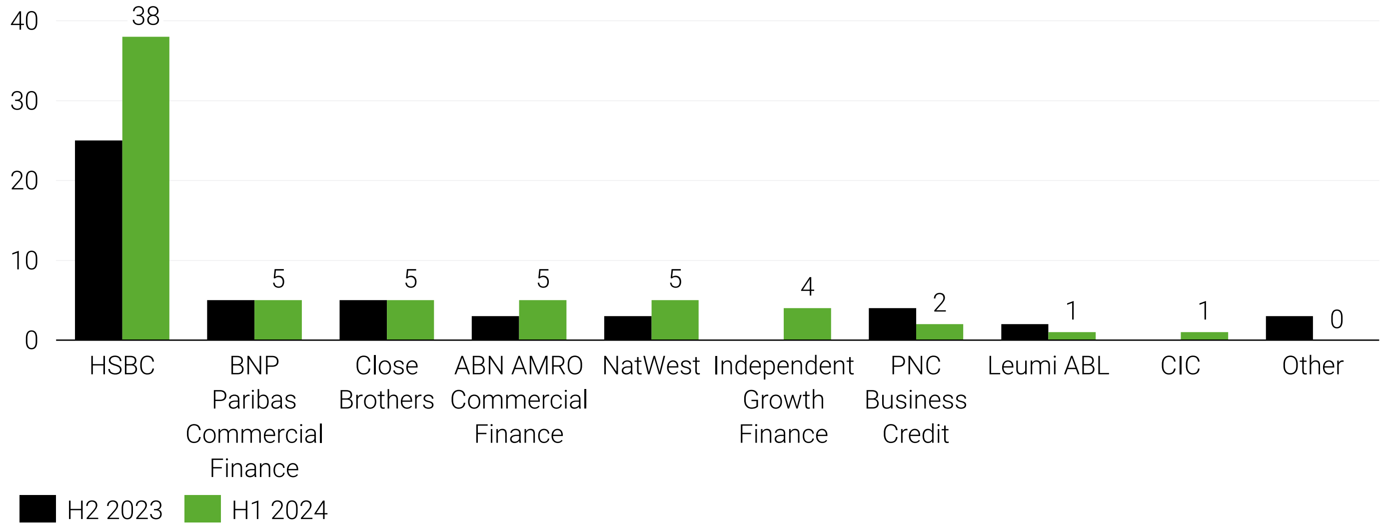
ABL and IDF activity declined by 6% in the first half of 2024, driven by a decrease in ABL financings

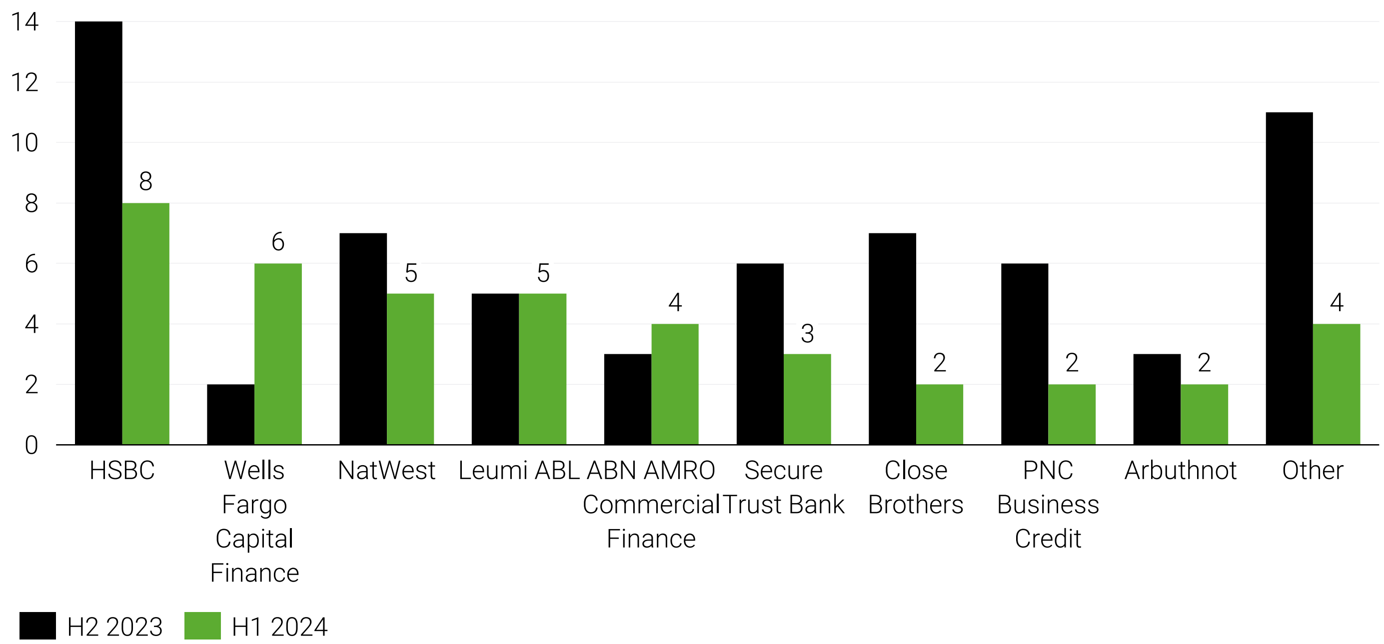
FIGURE 7: EUROPEAN RECEIVABLES/IDF-ONLY ABL DEAL COUNT



INSIGHTS

- IDF-only deals increased by 32% in H1 2024, up from 50 deals in H2 2023 to 66 in H1 2024.
- HSBC remained the most active lender in this space by a considerable distance, and saw its deal count increase by 52%, from 25 deals to 38. BNP Paribas, ABN AMRO, and NatWest all recorded five deals. Independent Growth Finance recorded four deals.
- The overall increase in IDF-only activity was driven by a surge in refinancing deals, up to 40 from 24 in H2 2023, equivalent to 48% of deals in H2 2023 and 61% in H1 2024.

FIGURE 8: EUROPEAN ABL DEAL COUNT (EXCLUDING RECEIVABLES/IDF ONLY DEALS)



INSIGHTS

- Multi-asset ABL deal counts fell significantly from 64 to 41, a 36% drop between six-month periods.
- HSBC's deals fell from 14 to eight, while Close Brothers and PNC Business Credit deals dropped from seven to two and six to two respectively. Only Wells Fargo and ABN AMRO recorded increases in activity, the former up from two deals to six.
- Across both IDF and multi-asset ABL activity, refinancings increased by 6%, up to 66 deals and equivalent to 62% of deals. The overall decrease was driven by a reduction in ABL deals supporting M&A transactions, which suggests banks increased their appetite for supporting LBO and add-ons with leveraged cash backed facilities.

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ABOUT US

For more than 40 years, AlixPartners has helped businesses around the world respond quickly and decisively to their most critical challenges – circumstances as diverse as urgent performance improvement, accelerated transformation, complex restructuring and risk mitigation.

These are the moments when everything is on the line – a sudden shift in the market, an unexpected performance decline, a time-sensitive deal, a fork-in-the-road decision. But it's not what we do that makes a difference, it's how we do it.

Tackling situations when time is of the essence is part of our DNA – so we adopt an action-oriented approach at all times. We work in small, highly qualified teams with specific industry and functional expertise, and we operate at pace, moving quickly from analysis to implementation. We stand shoulder to shoulder with our clients until the job is done, and only measure our success in terms of the results we deliver.

Our approach enables us to help our clients confront and overcome truly future-defining challenges. We partner with you to make the right decisions and take the right actions. And we are right by your side. When it really matters.