



CLEAR PATH ANALYSIS

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# INVESTING IN PRIVATE MARKETS NORTH AMERICA 2021

Finding opportunities in the face of economic headwinds and inflationary pressures

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### 3.1 ROUNDTABLE DISCUSSION

## What role does corporate private placement debt have within an investment portfolio?

#### Moderator



**David Grana,**  
Head of North  
America Media,  
Clear Path Analysis

#### Panelists



**Jennifer Potenta,**  
Managing Director, Global  
Head of Corporate Private  
Placements, MetLife  
Investment Management



**Frank Monfalcone,**  
Client Portfolio Manager,  
Private Capital,  
MetLife Investment  
Management



**Thomas Metzler,**  
Managing Director,  
Institutional Client Group,  
MetLife Investment  
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### POINTS OF DISCUSSION

- *Investment-grade private credit provides favorable financial covenants and structures*
- *Since the onset of the pandemic, issuers have raised their liquidity levels, having accessed capital through the market*
- *Though this has been a market dominated by insurers, it is increasingly open to other investors, such as defined benefit pension plans*
- *A global rise in capital expenditure and M&A activity will likely open up new opportunities in the asset class*

#### **David Grana: How has private credit performed through previous economic crises and how do those numbers contrast with the current health crisis?**

**Jennifer Potenta:** It's important to level set where this team specializes in the private credit market, as it is a large and diverse market. Our expertise is the investment-grade segment, also known as the private placement market. Long-standing relationships with management teams, meaningful financial covenants and structures are the cornerstone of the corporate private placement market.

Looking back at the Global Financial Crisis of 2008-09, the asset class performed well, driven by the covenant protections that were in place, as well as management teams who protected cash flow and company balance sheets. The private placement market operates similarly to the banking market. Relationships, expertise, and a long history of lending to borrowers helps both markets work through challenging times together. The private placement market tends to be a longer-term lender, whereas the bank market tends to focus on shorter-duration loans.

Understanding and analyzing a vast array of industries, businesses and management teams helps private placement lenders make informed investment choices in private credit. In addition, covenant protections give lenders a seat at the table alongside other senior lenders during challenging times, allowing them to work closely with issuers to balance borrower needs with the needs of investors.

The pandemic has been different than previous crises, as every industry was affected by the disruptions. Transportation, leisure and travel were among the hardest hit. As a result, private placement lenders worked closely with borrowers alongside other senior lenders to ensure that companies had adequate liquidity to get through what was, at the time, an unknown period. Lenders that provided temporary relief through covenant waivers and adjusted reporting requirements were able to help borrowers maintain liquidity and cover any near-term liabilities.

“

THERE ARE CERTAIN INDUSTRIES THAT HAVE BEEN SLOWER TO RECOVER; HOWEVER, BECAUSE WE FEEL THOSE ASSETS HAVE GOOD LONG-TERM VALUE, THAT IS WHERE WE LOOK TOWARD EQUITY TO PROVIDE SOME SUPPORT

”

This allowed companies to work through these trying conditions and navigate successfully through the pandemic.

**Frank Monfalcone:** I would emphasize that having covenant protections built into the loan documents helps ensure that the private placement lender remains in the most senior part of the capital structure. This not only gives the lender a seat at the table during disruptions, but, we believe, the right seat at the table. Unlike in some circumstances, where bank lenders can jump ahead and become senior to other lenders, private placement lenders stay senior with bank lenders, which is critical in negotiating equitable solutions that work for both senior lenders and the issuers.

**David: What are some of the ways that you are protecting some of your positions and the positions of your investments through these short-to-medium-term difficulties that present themselves as we try to get back to some sense of normalcy?**

**Frank:** Steering affected issuers toward liquidity solutions has been our focus through this crisis. As Jennifer commented, certain industries were more dramatically affected and continue to be slower to recover. However, because those borrowers have business models and assets with good long-term value, we look toward equity to provide some liquidity support. In some cases, borrowers have gone into the public markets for equity infusions, while in other instances, owners have put cash directly into the business to provide liquidity. Lenders have also provided new capital into these businesses based on solid management teams and long-term business prospects.

**Jennifer:** In such cases, we have seen company management teams take the difficult but right steps to manage costs and optimize cashflows, and have been willing to add additional covenant protections and reporting for the near term.

**David: Why has the asset class been a favorite among insurers and how has it helped their portfolios achieve their return goals?**

**Jennifer:** The private placement market originated as an insurance company asset class, given the stable, intermediate-to-long duration, often-illiquid liability base.

In addition, the asset class is very customizable from both a tenor and currency standpoint. Within a diversified insurance company with short and long-duration liabilities, investors can invest anywhere along the curve. Due to a diversified client base, origination opportunities can be in any major currency, across the entire maturity spectrum, including short floaters to long, 30-to-40-year deals. This provides client portfolios with a robust, diversified opportunity set.

Moreover, there are the covenant protections which serve as key structural protections to dampen downside volatility. One of the key objectives for insurers is to minimize losses while generating incremental book yield. This asset class has a demonstrated track record of lower losses relative to other public asset classes, which makes it a nice fit for insurers.

The potential for incremental book yield private placements generate is through a combination of an illiquidity premium, as well as the opportunity for incremental income over time. This can be in the form of coupon enhancements in deals if a credit starts to deteriorate from its original credit profile, for example. This type of mechanism helps protect investors from a potentially higher capital charge. There are also prepayment protections built in to protect against a liability mismatch in a situation where private placement notes might be paid off early. All of these factors have made it an attractive asset class for insurers and one where we have seen increased allocation over time.







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