Lead Left Interview – Michael Ewald (Part 2)

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This week we continue our conversation with Michael Ewald. Michael is a Managing Director, the head of the Private Credit Group and Portfolio Manager for Bain Capital Credit's Middle Market Opportunities and Senior Direct Lending fund strategies. Bain Capital Credit, founded as Sankaty Advisors in 1998, is a leading global credit specialist with over $30 billion in assets under management and has more than 230 employees operating from a network of seven offices around the world. ***Second of two parts – View part one***

TLL: Michael, I noticed that Bain Capital Credit recently closed the firm's first BDC. Congratulations.

ME: This is our first BDC but it is surely not new asset class for my group. It's not really different from our current strategy. We obtained exempt relief, which allows us to invest alongside our managed accounts and commingled funds. The Credit business started in 1998 and middle market lending was one of our original strategies, augmenting our CDO business. This strategy evolved steadily into more senior debt post-crisis, when pricing gapped out. We saw real opportunities sourcing the same type of deals as we were already completing with junior capital. Senior investing is a bit different work than mezzanine; the terms and docs can vary but it's the same underlying business analysis. We raised a number of managed accounts to target senior direct lending and then smaller institutional funds asked us for a comingled fund; that led to Bain Capital Senior Direct Lending 2015. But we still had direct origination or leveraged income issues both for onshore tax-exempts and offshore funds. The BDC structure solves those concerns and we closed about $550 million in equity in October, and we expect that will grow. But there's really no difference in our strategy.

TLL: What do you think of the possibility of deregulation in the new administration?

ME: From the rhetoric so far, that seems likely, but the impact on middle market lending is unclear. The traditional banks have been getting out of leveraged lending since way before the GFC, so I think that's a bit of a red herring. With regard to Dodd-Frank and the Volker Rule, do I think someone like Goldman goes back into private equity? That could be good for us in that it provides for another sponsor in need of financing, though it would probably have very little impact in the middle market overall. Return of prop trading? That could be good for broadly syndicated loans, but again, not impactful for the middle market. Will the CFPB go away? That has nothing to do with the middle market. Leveraged lending guidelines? Well, there hasn't been much noise about these specifically as the banks are focused on investment grade or asset-backed lending now. It's tough to get back into leveraged lending overnight. Think about all the hiring you'd have to do, and most of those professionals have moved on.

TLL: What's been your biggest surprise this year so far?

ME: The Qlik transaction certainly got a ton of press. I suppose it shouldn't be too surprising that middle market clubs can challenge the typical syndicated market and I look forward to more such activity going forward

TLL: What about BDCs?

ME: I would be surprised if there weren't another public BDC or fully IPO'd BDC next year. Also, one or two large scale BDC managers may find candidates to merge with out there. However, the BDC structure can make it complicated.

TLL: What about 2:1 leverage being granted for BDCs?

ME: I don't think it happens; there's no proven need. It might invite some folks to get reckless, though it's unclear whether the lenders to the BDCs would even allow for additional borrowing even if it's approved from a statutory perspective. I think asset pricing (base rates aside) will probably be stable next year so returns with 1:1 leverage on senior risk should still be attractive for investors..

TLL: Anything else you'd like to end with?

ME: We focus about 30% of our investing outside the US in our senior direct lending strategy, including the BDC. In addition to our activities in Europe, we've had a fair degree of success in Australia and New Zealand. We've seen a number of mezzanine deals from our team on the ground there but there's a big difference between investing in the US and investing abroad—you really need to understand the local nuances and our teams on the ground are instrumental in doing so.

When I was consulting with Bain & Company many years ago, I visited a Stanley Works plant in Sheffield, UK, where they made screwdrivers. I also did some work on their paint brush manufacturing. The theory was, they could considerably reduce their SKUs and save a bunch of costs. However, consumers in different European countries really care about the kind and shape of screwdriver handle, what kind of hair is in the paint brush – natural vs. hog bristle vs. synthetic. These types of consumer preferences make it difficult to introduce wholesale changes, and without visiting the plants and gaining that understanding, we never would have known. It's just goes to show you that Europe is not a uniform market, by any stretch, and Australia is completely different again. Having local boots on the ground is critical to our success there.

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