Leverage levels diverged on middle market sponsored deals in 3Q17

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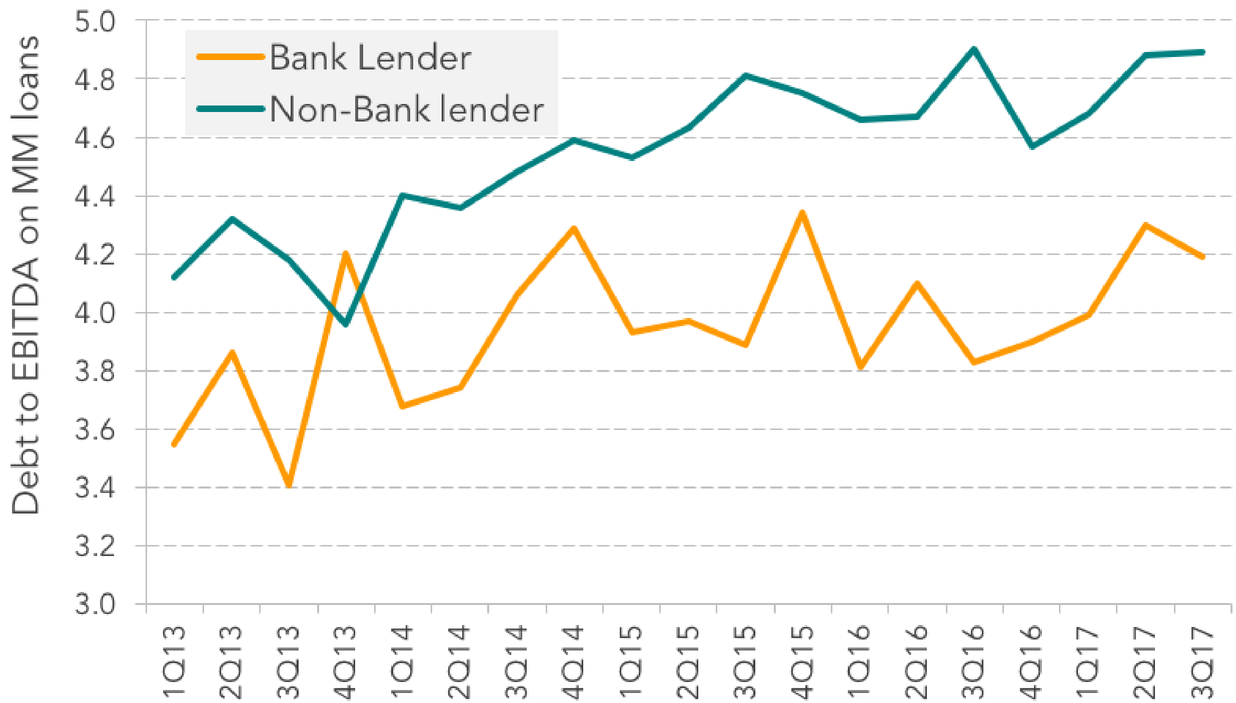

When it comes to lending to smaller issuers, bank and non-bank lenders have very different risk tolerances in today’s market. Back in 2013 banks and non-bank lenders both lent to middle market issuers at similar leverage levels. However over time that has diverged due to regulatory pressures on banks and strong fundraising efforts of direct lenders. In 3Q17, the average leverage on middle market sponsored backed deals led by non-bank direct lenders remained very elevated at 4.9 times. Very strong fundraising year to date of US$51bn for middle market lending has contributed to an extremely competitive environment and has continued to push leverage slowly higher quarter after quarter. Alternatively, banks who have been hampered by Leveraged Lending Guidance have continued to remain conservative on leverage multiples. The average debt to EBITDA for middle market issuers for bank-led deals was only 4.2 times in 3Q17, slightly down from 4.3 times in 2Q17 and up moderately from the 3.8 times average in 3Q16. However last week, the Government Accountability Office (GAO) confirmed that Leveraged Lending Guidance is in fact a rule and will be revisited which means that LLG could either be tweaked in banks’ favor or go away all together. Banks have seen their market share of PE-backed middle market lending fade over the years since Leveraged Lending Guidance was re-worked in 2013. In 3Q17, banks only submitted 20% of middle market sponsored-backed loan volume to LPC’s private sponsored database, down from 32% in 2Q17 and the lowest level tracked since LPC began collecting this data in 2013.

Contact: Fran Beyers
frances.beyers@thomsonreuters.com