# “$2 Billion is the New $1 Billion”: Unitranche Revisited (Second of a Series)

THE LEAD | August 12, 2021

According to Refinitiv LPC, US unitranche volume came to almost $22 billion last quarter – the highest level they’ve tracked historically. That activity was comprised of records for both the middle and the larger corporate markets.

At the same time, one-stop risk/return dynamics have moved in favor of issuers. The average debt/ebitda is now at a record high 5.9x, with all-in Libor spreads hovering around 600 bps.

And as we mentioned last week, more $1 billion-plus unis are coming to market than ever. So what are the drivers behind the frothy market for this innovative financing?

Here’s what we told *M&A* magazine in a recent interview:

“The disintermediation away from the loan syndication market to private credit, particularly for the upper end of the middle market, has been going on for a while now. This has been accelerated in the current M&A climate with sponsors requiring more flexibility, speed, and certainty of execution as they compete aggressively to win deals.

“The competitiveness of auctions for sponsors has included their credit providers on the financing side. Historically, $1 billion loans could only be done in the bank market. Yes, direct lenders can hold mega commitment chunks. But it’s also about reliability and being able to negotiate terms with one party. As one client told us, ‘You’re going to do my next deal, because you did the last one.’”

It’s also true that the overall environment is super constructive for credit. Interest rates remain low, the economy is humming along, and public equities and fixed income markets are increasingly bullish as inflation fears have moderated. Not to mention the enormous amounts of private equity dry powder available to snap up attractive businesses.

And unlike prior periods when unitranches came to the rescue if bank and bond markets were risk-off, these mega deals are on offer when loans and high-yield are equally frothy. Institutional investors in those markets are eager to put cash to work, so have latched on to higher leveraged transactions than typically seen in broad syndications.

Software borrowers, for example, can push debt-to-ebitda to seven times, thanks to staggering purchase price multiples that create healthy cash equity cushions. Single-B first-lien and second-lien spreads at (indicatively) L+450 and 700bps, respectively, are issuer and investor-friendly.

Predictably direct lenders are countering with increasingly attractive all-in unitranche spreads. Yet pricing isn’t everything. As our friend Kelly Thompson at Direct Lending Deals told us:

“The pricing gap between syndicated and private loans in the $1-3 billion range is under 100 bps. Not all, but many sponsors would prefer to pay a bit more and control who’s in their financing. Covid reminded them of the value of relationships. When in need, a smaller group of lenders is much easier to work with than a cacophony of faceless first- and second-lien investors.”