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Barings: Bigger is not always better in private credit

Barings' head of Europe and Apac private credit says the debate on which is the best market segment shouldn't focus on size but rather on who's leading and who's following.

BY **SELIN BUCAK**

The debate over which part of the private debt market offers a better risk-return profile raged on at the Super Return International conference this year in Berlin.

Some argue that larger companies offer more protection because they will be better able to handle any market wobbles, others believe smaller deals mean better terms for lenders.

Barings focuses on mid-market businesses with $10m to $50m of earnings before interest, tax, depreciation and amortisation (Ebitda). Stuart Mathieson, the firm's head of Europe and Apac private credit and capital solutions, said this is where you can find robust businesses.

'I can understand why some investors say big companies are more attractive than smaller companies,' he told Citywire at Super Return.

'People often focus on the larger vs smaller deal size debate, but really the focus should be around market leaders vs followers. They need to be market leaders in what they do. You don't want to be number five in a competitive sector because competition and pricing can be problematic.'

Mathieson argues that market leaders will have higher barriers to entry and defensibility, as well as stronger pricing power.

It is rare that Barings will lend to a company that has less than $20m in Ebitda but Mathieson is also happy not to go after the larger companies.

'If you're in that larger part of the market then you are not only competing against other managers but you're also competing with the syndicated world, which influences transaction structure, control and pricing,' he said.

Indeed, the broadly syndicated market, which had pulled back from the market as interest rates rose, has been coming back in, leading to rising competition among lenders.

According to PitchBook LCD data, in the first quarter of the year 21 companies issued a broadly syndicated loan to refinance $8.3bn of debt that was previously provided by direct lenders.

Rising competition boosts risk

Moody's Investor Services previously warned that the escalating competition in the private credit market will increase risk.

'There is an element of the market that's more aggressive. It tends to be in larger deals where the size is pushing towards the syndicated market, that's where the competition is most fierce on price and structure. In the mid-market space, you're more likely to get pricing pressure than pressure on the deal structure,' Mathieson added.

Pricing pressure is more acute in the US, in his view, as the deal market is more club focused, and features businesses that are slightly bigger than those in Europe.

'If you think about that environment where you have several lenders in a transaction and the ability to put pressure on pricing, you've got a dynamic there that's going to be more competitive. In Europe, you typically have a sole lender and in the traditional middle market we play in there is a bit more insulation,' he added.

'In the middle-market, you are more likely to be able to put in place a structure the borrower is comfortable with and they have the ability to tap you again to finance growth, such as for add-on acquisitions. However, that doesn't mean they won't ask for concessions on price.'

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