People

What are the biggest challenges and opportunities right now?

We asked three market professionals for their thoughts as coronavirus begins to make its impact felt in the private debt market.

By **Andy Thomson** - 1 hour ago

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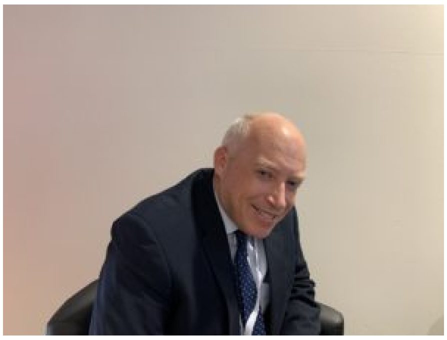
As the long benign environment for private debt investing appears to have come to an end, we ask industry players for their thoughts on the ups and downs of the current situation.



David Waxman

David Waxman, managing director, Azla Advisors, New York

Biggest challenge:

"Private debt's biggest current challenge is that potential slower portfolio company growth, due to a coronavirus-driven recession, will lead to defaults. Over the course of the last several years, as lenders have responded to the more competitive environment by being more aggressive, with lower loan-to-value ratios and more dependence on growth in a benign environment to fund interest and principal repayment, it may very well lead to stress and defaults. Relatively new lenders that have not been through the previous recession in 2008, will have their workout and distress skills tested, so LPs will have to keep a close eye on private debt managers that did not successfully manage a private debt portfolio in 2009 or 2000."

Biggest opportunity:

"Private debt's biggest current opportunity is the distressed opportunity that will likely be brought on by the coronavirus-driven recession. For many years, everyone has been talking about 'when will the cycle end'. Well now it looks like it will end this year and the capital that has been raised for distressed funds by the large asset managers and private debt managers can be put to work. The environment should also see the emergence of smaller niche private debt distressed managers or niche private debt managers that unveil a distressed fund specifically geared to their space, which should generate higher returns than the more generic, larger distressed managers."

Alex Schmid

Alex Schmid, founding partner, ESO Capital

Biggest challenge:

"We have been through multiple crises before. This is a rather unique situation, but the biggest challenge is always the same – cash. Do you have enough cash to buy time to figure out what is happening and to provide you with the capacity to work through the crisis in some form? Then comes our social responsibility. As investors in companies, we must assess what we need to do to support the common good, be that employees who need help or the families that rent houses from our real estate portfolio companies. We have a huge amount of experience through decades of investing that stand us in good stead to work through the situation and protect the downside as much as possible, but we must not forget we have a responsibility to protect everyone while protecting our investments."

Biggest opportunity:

"There will definitely be opportunities, there always are in a liquidity crisis. But it is too early to say where and when they will emerge. We are watching the market but deployment is not a focal point for us right now. I do have comfort in the fact that we are one the firms at the lower end of the market that has been around for a long time so have the scars borne of experience to work through these challenging times."

Christopher Parisi, managing director, Carl Marks Advisors, New York

Biggest challenge:

Chris Parisi

"The biggest challenge is simply to determine when we come out the other side and what it may look like. In the immediate term, we're likely to see a sharp reduction in consumer and business spending through the end of Q2 which will very likely produce a recession. Once a recession starts, it becomes a self-fulfilling prophecy for a period of time, so we can likely expect continued contraction in Q3. The final step is a sharp rise in corporate bankruptcies, putting tremendous strain on the banking and financial system. Near-term challenges: deals in process have been negotiated at historically high valuations, supported by earnings growth and strong leverage markets. Those two factors are instantly being vaporised, thus putting into jeopardy those current deals."

Biggest opportunity:

"Acting as trusted advisor to our clients and prospects. In times of great uncertainty, it's the unknown itself that causes paralysis of decision making. As an advisor servicing both the M&A and restructuring markets, we have tremendous insight into the full spectrum of economic and business activity. This collective knowledge can be passed on to our clients/prospects, enabling them to rely on us more, value our input and make the best possible decisions, with the greatest amount of information possible."