

GLOBAL THOUGHT LEADER SPOTLIGHT

“With the slowdown in M&A placing downward pressure on pricing and eroding terms, diversity of deal sourcing becomes critical.”



MICHAEL JONES

Managing Director
PGIM Private Capital



I am responsible for overseeing [PGIM Private Capital's](#) Sydney office. Our team is responsible for sourcing, underwriting, and managing private credit investments across Australia and New Zealand. Our private credit offering spans the corporate, infrastructure and energy sectors.

Our investment capabilities are centred on longer-term (7+ years) investment grade or below investment grade debt, mid-market direct lending, and junior capital. We support publicly listed, private equity owned, as well as family or management owned businesses, with a total portfolio of over A\$11 billion (as of 31 December 2023) across Australia and New Zealand.

Key developments in private credit locally and internationally:

- There has been a proliferation of new private credit funds over the past couple of years, as ‘private credit’ has become more mainstream.
- Increased willingness and awareness for borrowers to take on non-bank funding, particularly in historically bank dominated markets such as Australia and New Zealand. The gradual disintermediation of the banking sector, changes in bank appetite, and challenges in the equity markets to IPO has made private credit more attractive for borrowers despite the higher pricing.
- The combination of interest rates remaining higher for longer than forecasted, coupled with a gradual slowdown in the economy, is likely to put pressure on mid-market businesses as operating costs continue to increase. As a result, firms need to ensure that they have adequate flexibility to manage their businesses through this uncertain environment.
- Slowdown in mergers and acquisition activity is putting downward pressure on pricing and eroding terms, as more lenders compete for deals to put ‘dry powder’ to work. This increases the importance of having diversity of deal sourcing.



How can institutional investors position themselves to capitalise on these developments?

Investors should consider the capabilities and track record of their managers in operating through business cycles. This encompasses whether the manager has in-house workout experience and capabilities.

Furthermore, they should also consider if their managers have unique sourcing angles as this helps when it comes to structuring and negotiating terms or covenants both up-front but then also when amendments might be required. This process ensures that adequate protections are built into the investment so that lenders can be back at the table early to protect their investment through a cycle, thereby improving their recovery rates if an investment does not go according to plan.

The Australian and New Zealand (ANZ) markets remain relatively underpenetrated compared to the US and European markets where private credit activity has been more prolific. This creates opportunities for an enhancement in the deployment of private credit to ANZ, as companies come to realise the benefits of having more patient capital, particularly during an uncertain economic period where they might need more time to execute organic or inorganic strategic initiatives. This is further catalysed by the presence of a capital provider that is willing to support them through time by creating a bespoke funding solution to fit their needs.

The current environment creates more stress on portfolio companies, as it limits their free cash flow generation. We are likely to see continued constraints on margins as costs rise (labour, rent, insurance, technology, energy) and firms are unable to push through price increases. This environment will test the amount of true equity value that is sitting behind the senior debt in the capital stack.

In hindsight, this highlights the importance of having a diverse asset manager, which can look across multiple markets and holds the expertise to do both private equity backed and management or family-owned (non-sponsored) businesses. They should also be able to deploy capital through cycles and obtain attractive pricing and well-structured transactions for their investors.

Mike will be presenting at Global Investment Institute's upcoming **Private Credit Investment Forum**, taking place on Thursday, 2 May 2024 at the Grand Hyatt Melbourne, Victoria.

Register your interest in attending [here](#) or for more information email zlatan@globalii.com.au.



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Mike is the Managing Director for PGIM Private Capital located in Sydney. He oversees the organisation's private credit investment activity spanning long-term investment grade and below investment grade lending (USPP), direct lending and junior capital/structured equity across Australia and New Zealand corporates, energy and infrastructure assets. Mike joined the organisation in 2008.

Mike is a CFA charterholder and has a Bachelor of Business Administration from the University of Michigan – Stephen M. Ross School of Business.



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