



Portfolio Valuation and Fund Advisory Services

Direct Lending Update

FALL 2022



Introduction

Dear Clients and Friends,

Houlihan Lokey's Portfolio Valuation and Fund Advisory Services team is pleased to present the fall 2022 edition of the Direct Lending Update.

We have included key trends for more than 100 business development companies (BDCs) to help you stay ahead in this constantly evolving industry. We hope you find this update to be informative and that it serves as a valuable resource to you in staying abreast of the market. If there is additional content you would find useful for future updates, please do not hesitate to call or email us with your suggestions. We look forward to staying in touch with you.

Regards,

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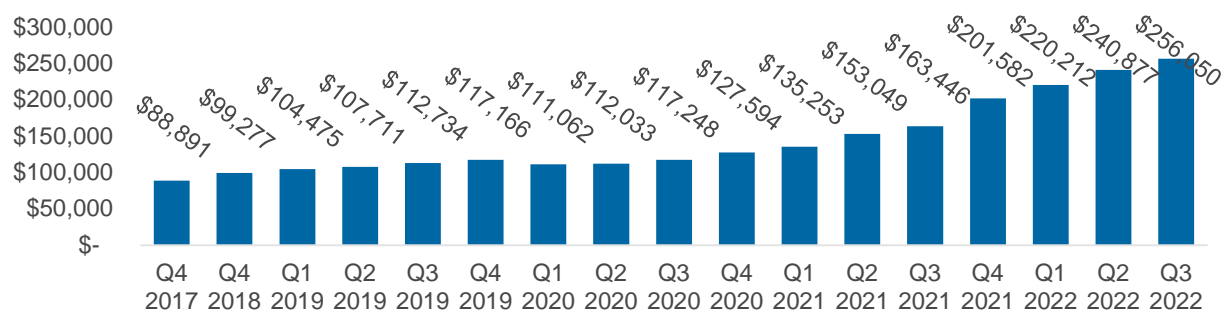


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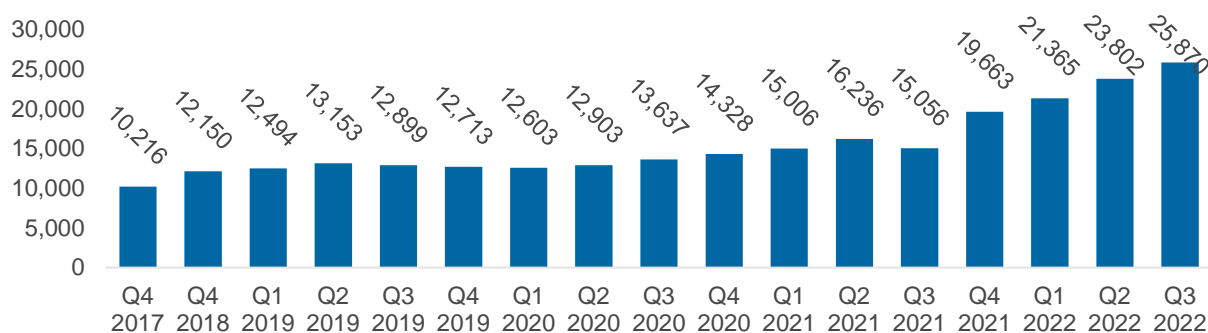
Key Trends

- Competition among direct lenders was robust going into Q3 2022, keeping pricing on new loans generally flat relative to the first half of 2022. As shown on the following pages, the median pricing for new first lien loans in Q3 2022 was S/L + 5.68%, which was only 7bps lower than new loans originated in Q2 2022. The pricing on new loans in part informs the valuation of existing loans in BDC portfolios, which was evident by looking at the Q3 2022 loan values. The weighted average price for performing first lien loans modestly declined from 98.0% of par to 97.8% of par, as shown on the following pages. The high levels of fundraising for direct lending funds over the past several years have left significant undeployed capital competing for new deals. Going into Q4 2022, we see a continuation of this trend and would anticipate pricing on new loans to remain relatively stable.
- One clear distinction we have observed is that the mega loans (loans above \$500 million) have experienced some spread widening because there is less capital to take down the deal flow and incremental spread is required to get deals done. There are simply fewer platforms that can write check sizes this large. As a result, major beneficiaries of the slowdown in the broadly syndicated market have been large asset managers with the scale and capital to take on deal sizes at the high end of the direct lending/private credit market.
- Leverage levels for new deals are coming down in response to rising base rates driving borrower interest costs up and thus reducing net cash flows. With LIBOR nearing 5%, sponsors are now financing leveraged buyouts at lower leverage levels relative to the past 12–18 months. According to our proprietary Private Performing Credit Index (PPCI), the average gross total leverage for portfolio companies stood at 5.1x as of Q3 2022. We generally expect new deals to be originated at leverage levels below this threshold to mitigate, among other things, the deterioration of interest coverage ratios in the current higher base rate environment. For more information regarding the PPCI, please visit the [Insights](#) section of HL.com.
- Interest coverage for loans has been declining due to rising base rates. The average EBITDA-to-interest-expense ratio on newly issued loans declined to 2.8x in Q3 2022 from 3.1x in Q2 2022—its lowest level since Q3 2019, according to Refinitiv LPC's Middle Market Sponsored Private Deals Analysis.
- In general, middle-market private companies have not shown significant financial underperformance. However, financial reporting for BDC portfolio companies typically lags by one to two quarters. For example, June financial statements are typically available in September. According to the Golub Capital Middle Market Q3 Report, middle-market private companies have experienced year-over-year revenue growth of 12% and an earnings decline of 2% during the first two months of Q3 2022. At the end of Q3 2022, the nonaccrual percentage for BDC loans, which is an indicator of distress, stood at 1.2%—its lowest level over the past several years.
- For new SOFR loans and existing loans transitioning from LIBOR to SOFR, credit spread adjustments (CSAs) are becoming less common. Over the past several quarters, CSAs typically ranged from 10bps to 26bps, with this amount meant to bridge the gap between LIBOR and SOFR rates. However, an increasing number of new loans and amendments are being structured with CSAs toward the lower end of the range or without CSAs altogether.

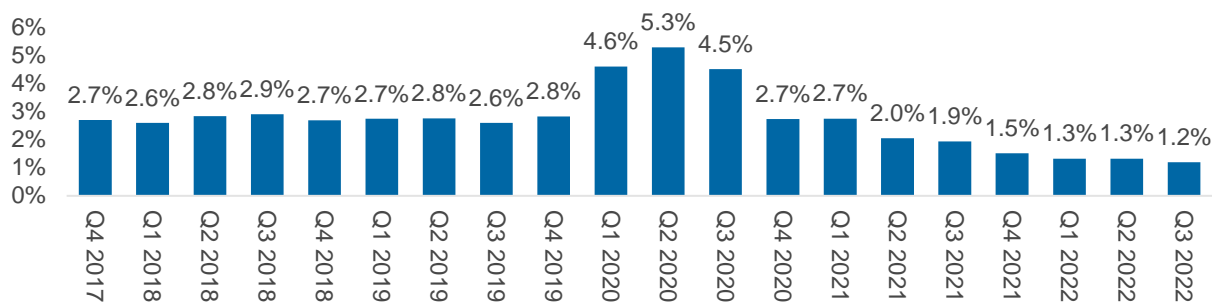
Fair Value of BDC Portfolios⁽¹⁾ (\$ in millions)



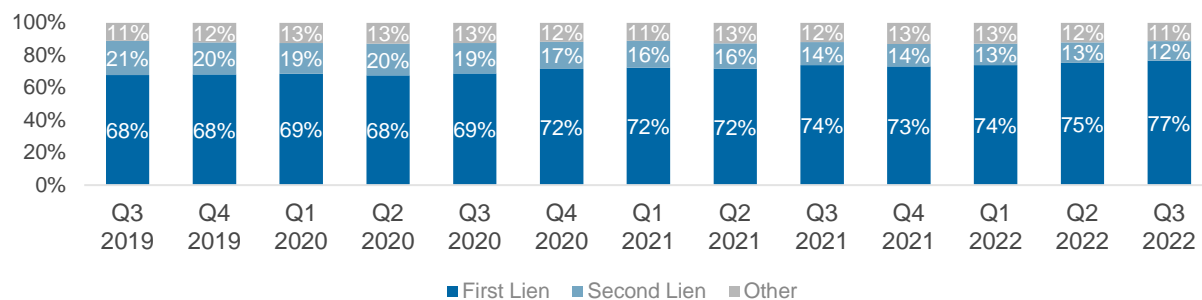
Total Number of Investments in BDC Portfolios⁽²⁾



Nonaccrual Investments as a Percentage of Total Portfolio⁽³⁾



BDC Portfolio Composition by Seniority Based on Fair Value⁽⁴⁾



Source: Advantage Data.

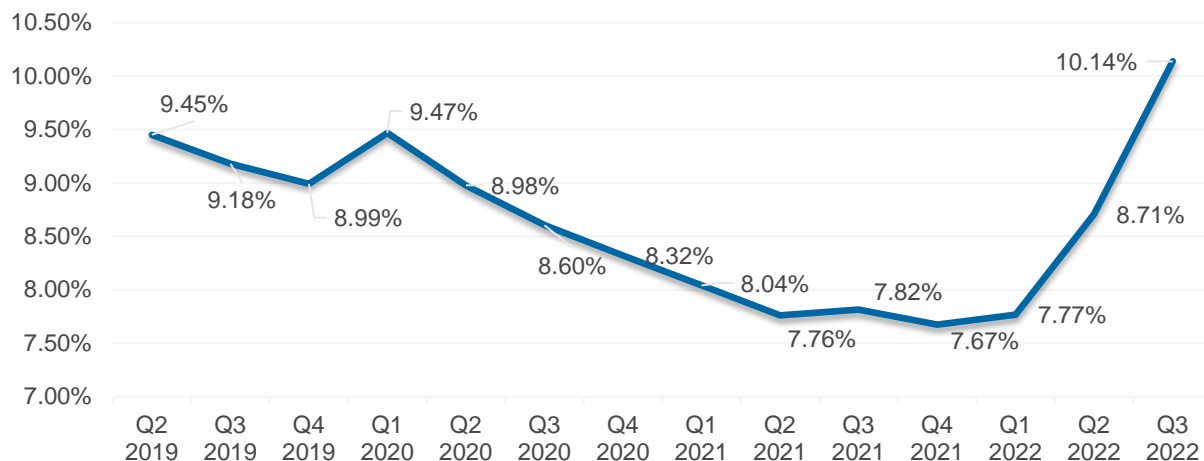
(1) Reflects the fair value for BDC portfolios tracked by Advantage Data.

(2) Reflects the total number of investments for all BDCs tracked by Advantage Data.

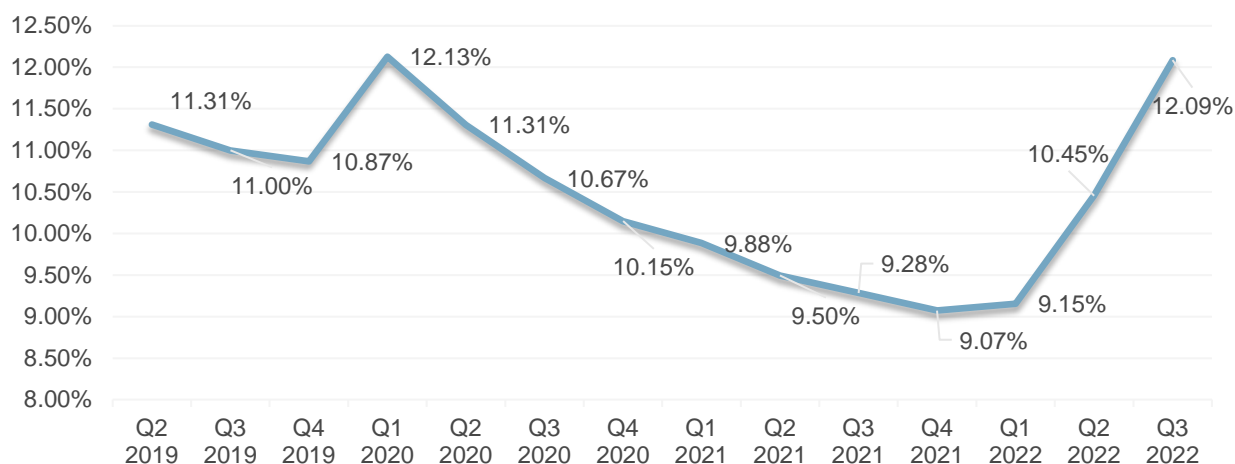
(3) Reflects cost of nonaccrual investments as a percentage of total portfolio cost for BDCs tracked by Advantage Data.

(4) Represents the aggregate composition of all BDC portfolios tracked by Advantage Data.

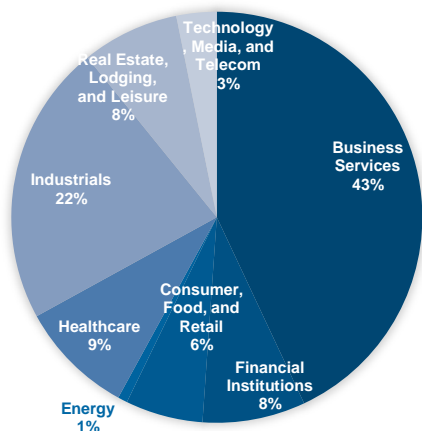
Average First Lien Yield—BDC Investment Portfolios⁽¹⁾



Average Second Lien Yield—BDC Investment Portfolios⁽¹⁾



Industry Breakdown by BDC Portfolio Company—Q3 2022⁽²⁾



Industry Breakdown by BDC Investment Yields—Q3 2022

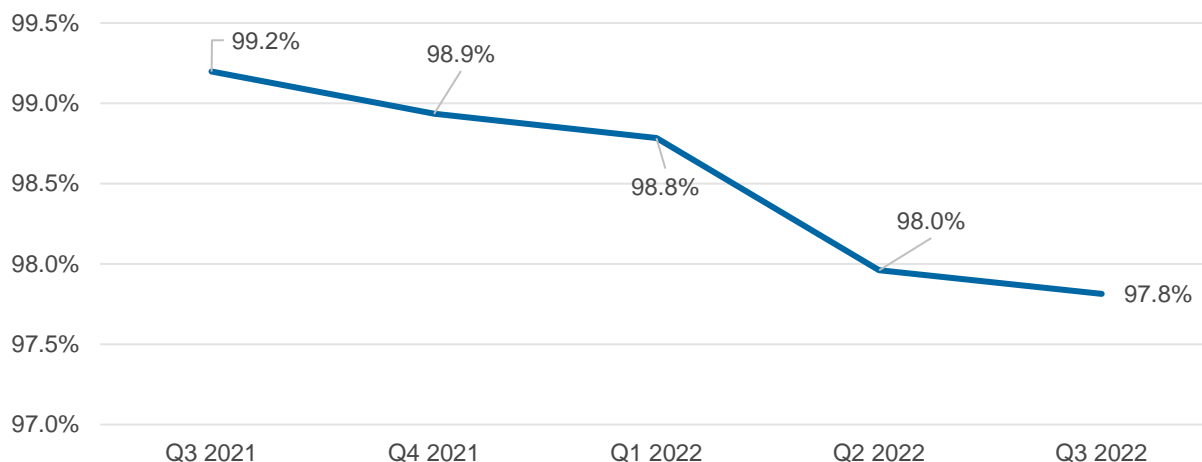
Industry	First Lien	Second Lien
Business Services	10.12%	11.82%
Financial Institutions	10.03%	12.26%
Consumer, Food, and Retail	10.07%	11.91%
Energy	10.37%	11.60%
Healthcare	10.23%	11.67%
Industrials	10.23%	12.38%
Real Estate, Lodging, and Leisure	9.99%	11.77%
Technology, Media, and Telecom	10.12%	13.35%

Source: Advantage Data.

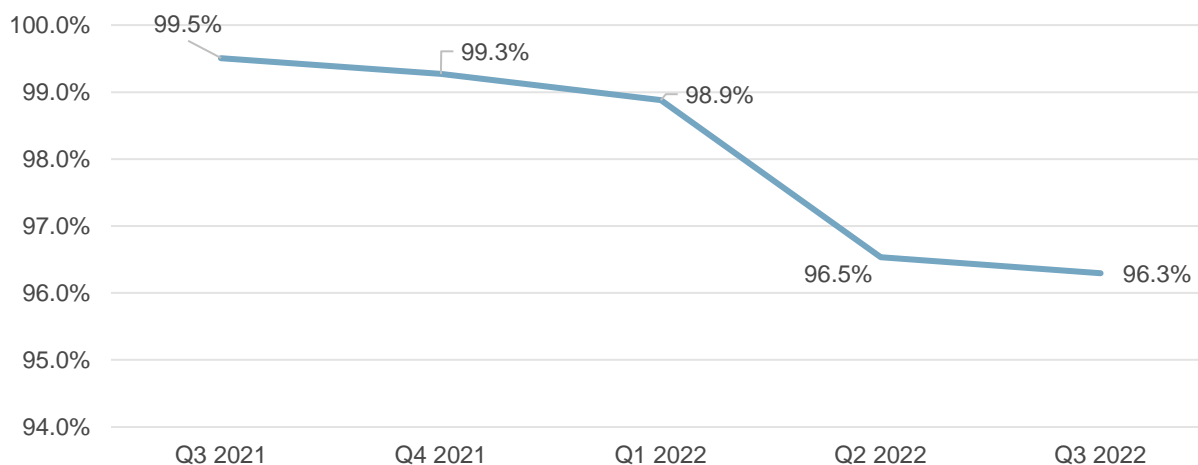
(1) Yield is based off of reported fair value, stated maturity, and stated interest rate. Represents data for all BDCs tracked by Advantage Data. Excludes outliers.

(2) Industry is based upon the industry of each BDC portfolio company and is broken down by aggregate principal for each BDC investment.

Weighted Average First Lien % of Par—BDC Investment Portfolios⁽¹⁾



Weighted Average Second Lien % of Par—BDC Investment Portfolios⁽¹⁾



New Loan Pricing⁽²⁾

	Base Rate	First Lien ⁽³⁾	Second Lien ⁽³⁾
Q3 2022	SOFR/LIBOR +	475 – 568 – 635	694 – 775 – 850
Q2 2022	SOFR/LIBOR +	450 – 575 – 675	725 – 775 – 850
Change	SOFR/LIBOR +	25 – (7) – (40)	(31) – 0 – 0

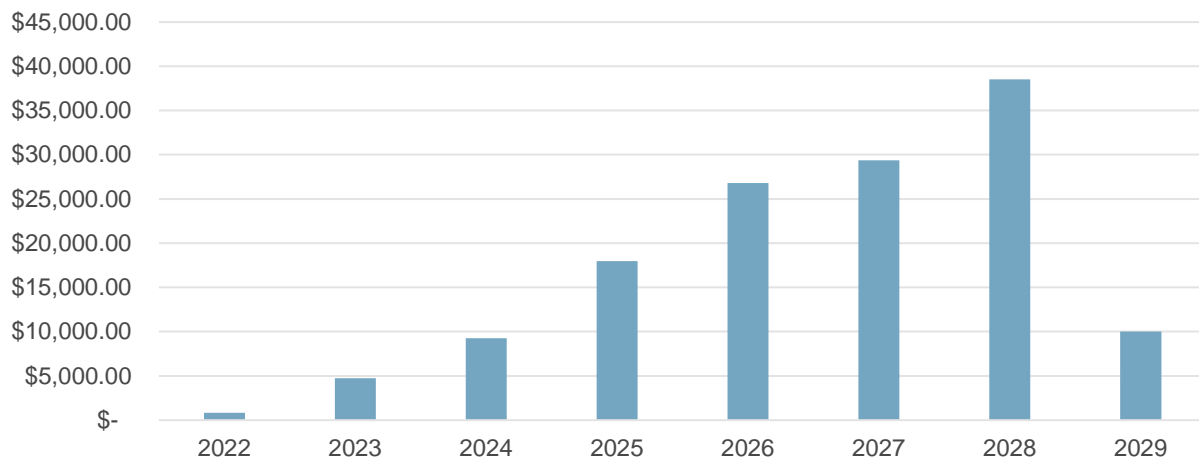
Source: Advantage Data.

(1) Expressed as a percentage of par. Represents data for all BDCs tracked by Advantage Data that filed as of the date of this report. Excludes outliers. The data is meant to reflect performing loans only.

(2) Represents new loans in each respective quarter from the universe of BDCs tracked by Advantage Data.

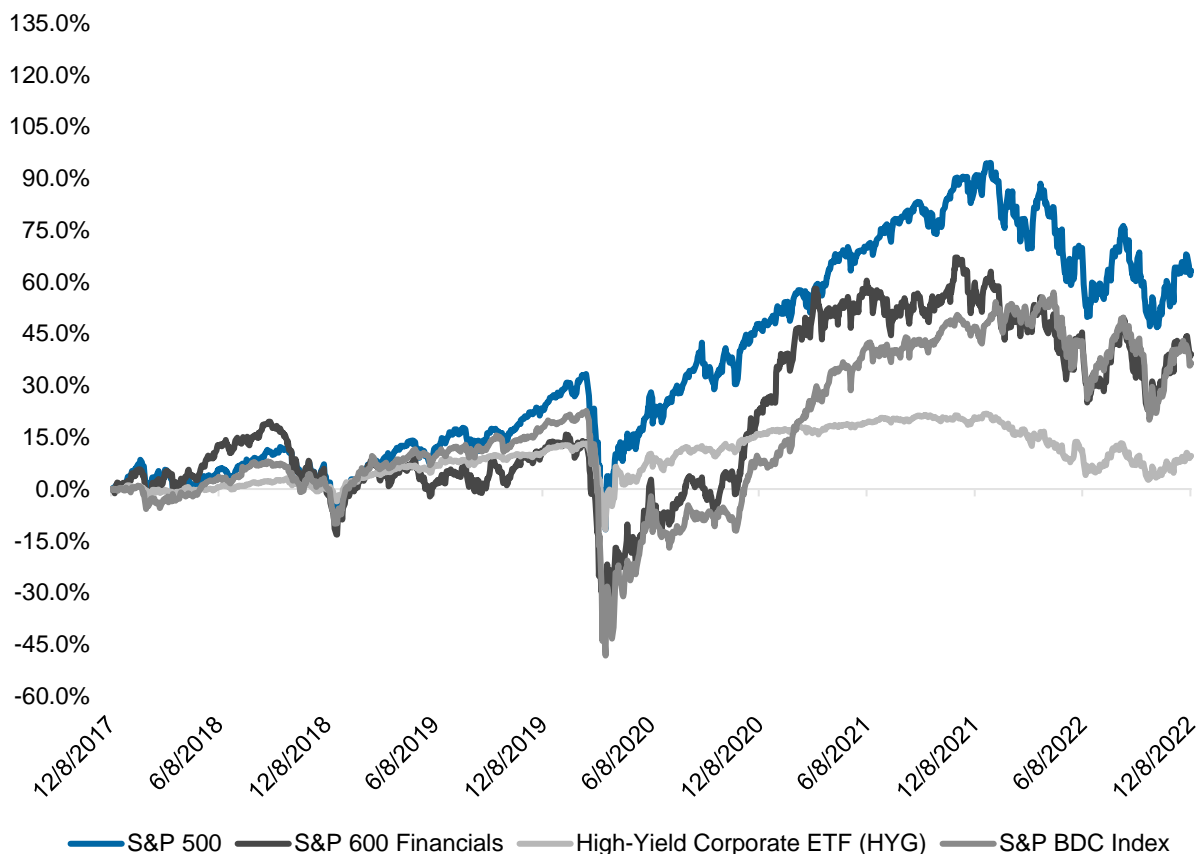
(3) Ranges represent the 25th, 50th, and 75th percentile of new loans for each respective quarter. Excludes outliers.

Maturity of LIBOR-Based Debt Securities for BDC Portfolio Companies by Year⁽¹⁾ (principal in \$ millions)



Cumulative Total Return (%) as of December 8, 2022

	1 Year	5 Years
S&P 500	-1.9%	79.7%
S&P 600 Financials	-9.1%	48.4%
High-Yield Corporate ETF (HYG)	-7.7%	11.3%
S&P BDC Index	7.0%	33.9%



Source: Advantage Data, Bloomberg.

(1) Represents the principal balance of maturities for debt securities with a LIBOR component for all BDCs tracked by Advantage Data.

Publicly Traded BDC Market Snapshot

(Dollars in millions, except per share data)

Company Name	Ticker	Market Cap.	Price at 12/8/2022	Price/52-Wk High	LTM Price Change	Price as a Multiple of NAV	LTM ROA	LTM ROE	Div. Yield	Debt/Equity
Large Cap										
Ares Capital Corp.	ARCC	\$ 9,811.03	\$ 18.96	82%	-10.5%	1.02x	5.9%	9.0%	10.1%	1.3x
FS KKR Capital Corp.	FSK	\$ 5,311.50	\$ 18.77	80%	-10.4%	0.74x	3.2%	2.8%	13.5%	1.3x
Owl Rock Capital Corp.	ORCC	\$ 4,828.27	\$ 12.26	80%	-13.4%	0.83x	5.4%	7.6%	10.8%	1.2x
Blackstone Secured Lending Fund	BXSL	\$ 3,950.42	\$ 23.28	61%	-31.5%	NM	NM	NM	NM	NM
Prospect Capital Corp.	PSEC	\$ 2,858.91	\$ 7.19	80%	-14.5%	0.72x	5.6%	6.0%	10.0%	0.5x
Main Street Capital Corp.	MAIN	\$ 2,835.99	\$ 36.71	80%	-18.2%	1.42x	8.2%	12.5%	8.1%	1.0x
Golub Capital BDC, Inc.	GBDC	\$ 2,242.15	\$ 13.12	81%	-15.0%	0.88x	4.4%	6.0%	10.1%	1.2x
Hercules Capital, Inc.	HTGC	\$ 1,768.43	\$ 13.70	72%	-17.4%	1.30x	3.6%	3.2%	14.9%	1.1x
Goldman Sachs BDC, Inc.	GSBD	\$ 1,493.37	\$ 14.53	71%	-24.2%	0.97x	4.0%	5.7%	12.4%	1.4x
Sixth Street Specialty Lending, Inc.	TSXL	\$ 1,472.28	\$ 18.18	75%	-22.3%	1.11x	6.1%	8.0%	9.5%	1.1x
Oaktree Specialty Lending Corp.	OCSL	\$ 1,278.12	\$ 6.97	89%	-6.6%	1.03x	2.9%	2.3%	10.3%	1.1x
New Mountain Finance Corp.	NMFC	\$ 1,277.36	\$ 12.66	90%	-7.6%	0.96x	5.9%	8.5%	10.1%	1.5x
Mean				78%	-16.0%	1.00x	5.0%	6.5%	10.9%	1.15x
Mid Cap										
Barings BDC, Inc.	BBDC	\$ 937.04	\$ 8.61	76%	-21.9%	0.76x	3.0%	1.8%	11.1%	1.1x
Bain Capital Specialty Finance, Inc.	BCSF	\$ 836.73	\$ 12.96	80%	-14.8%	0.76x	5.4%	7.7%	11.1%	1.2x
SLR Investment Corp.	SLRC	\$ 811.73	\$ 14.82	76%	-19.6%	0.81x	2.0%	0.6%	11.1%	1.1x
MidCap Financial Investment Corp.	MFIC	\$ 793.92	\$ 12.13	87%	-5.2%	0.79x	4.2%	4.5%	11.6%	1.5x
BlackRock TCP Capital Corp.	TCPC	\$ 731.33	\$ 12.66	87%	-6.3%	0.90x	6.0%	8.7%	10.1%	1.2x
Carlyle Secured Lending, Inc.	CGBD	\$ 717.55	\$ 13.97	93%	1.7%	0.81x	7.0%	11.4%	12.5%	1.1x
CION Investment Corp.	CION	\$ 563.69	\$ 10.17	67%	-22.2%	0.63x	5.3%	6.1%	12.2%	1.0x
Capital Southwest Corp.	CSWC	\$ 576.95	\$ 17.84	66%	-29.4%	1.08x	6.7%	10.3%	12.8%	1.3x
PennantPark Floating Rate Capital Ltd.	PFLT	\$ 515.13	\$ 11.36	79%	-11.0%	0.98x	2.8%	0.7%	10.0%	1.3x
Mean				79%	-14.3%	0.83x	4.7%	5.8%	11.4%	1.21x
Small Cap										
Fidus Investment Corp.	FDUS	\$ 460.64	\$ 18.85	89%	4.8%	0.97x	11.5%	17.6%	10.6%	NM
Gladstone Investment Corp.	GAIN	\$ 447.01	\$ 13.45	78%	-21.3%	1.01x	7.9%	9.5%	9.8%	0.6x
TriplePoint Venture Growth BDC Corp.	TPVG	\$ 446.67	\$ 12.66	69%	-29.5%	1.00x	3.2%	1.3%	11.7%	1.1x
Crescent Capital BDC, Inc.	CCAP	\$ 413.27	\$ 13.38	69%	-24.0%	0.66x	4.0%	4.2%	12.3%	1.1x
PennantPark Investment Corp.	PNNT	\$ 387.43	\$ 5.94	74%	-14.3%	0.66x	0.3%	-4.0%	11.1%	1.2x
Trinity Capital Inc.	TRIN	\$ 368.23	\$ 10.47	52%	-40.4%	0.76x	6.2%	6.0%	17.2%	1.2x
Gladstone Capital Corp.	GLAD	\$ 346.76	\$ 9.87	77%	-14.8%	1.09x	5.5%	6.3%	8.5%	1.1x
Horizon Technology Finance Corp.	HRZN	\$ 344.80	\$ 13.06	79%	-18.0%	1.12x	6.0%	7.1%	10.5%	1.2x
Saratoga Investment Corp.	SAR	\$ 309.76	\$ 26.03	88%	-11.4%	0.92x	4.8%	4.9%	10.4%	1.8x
WhiteHorse Finance, Inc.	WHF	\$ 300.07	\$ 12.91	80%	-16.7%	0.87x	5.3%	6.0%	11.4%	1.3x
BlackRock Capital Investment Corp.	BKCC	\$ 271.42	\$ 3.74	85%	-6.5%	0.82x	4.6%	4.5%	10.7%	0.8x
Stellus Capital Investment Corp.	SCM	\$ 261.72	\$ 13.39	94%	2.8%	0.94x	4.3%	7.5%	10.2%	2.2x
Portman Ridge Finance Corp.	PTMN	\$ 210.44	\$ 21.90	86%	-11.6%	0.84x	0.7%	-4.0%	12.2%	1.4x
Monroe Capital Corp.	MRCC	\$ 191.31	\$ 8.83	75%	-21.3%	0.85x	2.8%	-0.2%	11.3%	1.3x
Oxford Square Capital Corp.	OXSQ	\$ 155.92	\$ 3.13	71%	-23.3%	0.94x	-12.6%	-30.2%	13.4%	1.1x
Medallion Financial Corp.	MFIN	\$ 151.51	\$ 6.83	68%	17.8%	0.53x	4.1%	14.4%	4.7%	5.0x
OFS Capital Corp.	OFS	\$ 140.76	\$ 10.51	78%	-3.6%	0.77x	4.4%	3.8%	11.4%	1.9x
First Eagle Alternative Capital BDC, Inc.	FCRD	\$ 130.16	\$ 4.35	91%	-2.7%	0.85x	-4.3%	-16.5%	10.1%	1.4x
SuRo Capital Corp.	SSSS	\$ 106.25	\$ 3.75	27%	-71.0%	0.48x	-34.5%	-39.9%	0.0%	0.3x
Great Elm Capital Corp.	GECC	\$ 75.92	\$ 9.99	48%	-46.0%	0.79x	-5.6%	-31.3%	18.0%	1.5x
PhenixFIN Corp.	PFX	\$ 74.68	\$ 34.00	79%	-18.7%	0.58x	-1.5%	-5.9%	0.0%	0.6x
Silver Spike Investment Corp.	SSIC	\$ 61.96	\$ 9.97	65%	NM	0.73x	1.2%	1.2%	0.0%	NM
Logan Ridge Finance Corp.	LRFC	\$ 58.80	\$ 21.69	82%	-5.7%	0.60x	-1.8%	-11.6%	0.0%	NM
Investcorp Credit Management BDC, Inc.	ICMB	\$ 56.98	\$ 3.96	69%	-20.0%	0.61x	3.2%	1.0%	13.1%	1.6x
Rand Capital Corp.	RAND	\$ 37.68	\$ 14.60	78%	-14.1%	0.65x	0.1%	-0.4%	4.1%	NM
Equus Total Return, Inc.	EQS	\$ 21.90	\$ 1.62	60%	-31.9%	0.60x	0.0%	0.0%	0.0%	NM
Firsthand Technology Value Fund, Inc.	SVVC	\$ 7.79	\$ 1.13	25%	-71.8%	0.20x	-78.4%	-87.9%	0.0%	NM
Mean				72%	-19.7%	0.77x	-2.2%	-5.1%	8.6%	1.42x
High				94%	17.8%	1.42x	11.5%	17.6%	18.0%	4.96x
Mean				75%	-17.7%	0.84x	0.8%	-0.3%	9.7%	1.30x
Median				78%	-15.0%	0.83x	4.1%	4.5%	10.6%	1.21x
Low				25%	-71.8%	0.20x	-78.4%	-87.9%	0.0%	0.33x

Source: S&P Capital IQ.

Note: As of December 8, 2022.

NM refers to not meaningful.

ROA = (Net Change in Net Assets + Interest Expense)/Average Net Assets.

ROE = Net Change in Net Assets/Average Equity.

About Portfolio Valuation and Fund Advisory Services

Houlihan Lokey's Portfolio Valuation and Fund Advisory Services practice is a leading advisor to many of the world's largest asset managers, who rely on our strong reputation with regulators, auditors, and investors; private company, structured product, and derivative valuation experience; and independent voice. We value illiquid assets on behalf of hundreds of hedge funds, private equity firms, financial institutions, corporations, and investors. We rapidly mobilize the right team for the job, drawing on our expertise in a wide variety of asset classes and industries along with our real-world transaction experience and market knowledge from our dedicated global Financial and Valuation Advisory business.

Our Service Areas



Our Office Locations





Houlihan Lokey is the trusted advisor to more top decision-makers than any other independent global investment bank.

Corporate Finance

2021 M&A Advisory Rankings All U.S. Transactions		
Advisor	Deals	
1 Houlihan Lokey	301	
2 Goldman Sachs	285	
3 JP Morgan	282	
4 Jefferies	199	
5 Morgan Stanley	185	

Source: Refinitiv.

No. 1 U.S. M&A Advisor

Top 5 Global M&A Advisor

Leading Capital Markets Advisor

Financial Restructuring

2021 Global Distressed Debt & Bankruptcy Restructuring Rankings		
Advisor	Deals	
1 Houlihan Lokey	63	
2 Rothschild	38	
3 Moelis	34	
4 PJT Partners	33	
5 Lazard	24	

Source: Refinitiv.

No. 1 Global Restructuring Advisor

1,500+ Transactions Completed Valued at More Than \$3.0 Trillion Collectively

Financial and Valuation Advisory

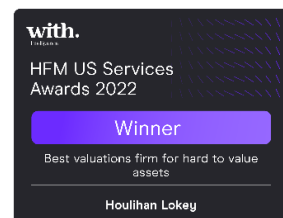
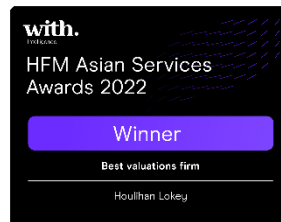
2002 to 2021 Global M&A Fairness Advisory Rankings		
Advisor	Deals	
1 Houlihan Lokey	952	
2 JP Morgan	890	
3 Duff & Phelps, A Kroll Business	882	
4 Morgan Stanley	602	
5 BofA Securities	531	

Source: Refinitiv. Announced or completed transactions.

No. 1 Global M&A Fairness Opinion Advisor Over the Past 20 Years

1,000+ Annual Valuation Engagements

Awards



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