

Pemberton pinpoints European mid-market opportunity for global clients



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Susan Barreto November 2, 2020

The unprecedented trends of 2020 continue to inspire investors, especially in the direct lending space in Europe where banking consolidation and regulations have pushed the opportunity for lending into historic levels.

Specifically, September and October represented the biggest pipeline of leveraged loan deals in Pemberton's six-year history.

Helping matters is that default rates

as of last month were running about 50% of that of the U.S., according to Simon Drake-Brockman, founder and managing partner at Pemberton, which is among the largest European private credit platforms, backed by Legal & General Group Plc.

"Historically direct lending was thought of as the place where banks couldn't go, but that is not the case today," added Drake-Brockman, who worked at RBS prior to launching Pemberton in 2011.

The firm's assets have grown to \$10 billion offering investors access to its sponsored and non-sponsored direct lending investments for growth companies across Europe. Drake-Brockman's assessment is that the opportunity for direct lending in Europe is there is little doubt that it will be on the rise over the next five years.

Notably the markets between the U.S. and Europe couldn't be more divergent. Overall, the European debt platform totals \$250 billion, while in the U.S. its totals \$700 billion.

In the U.S. the lending industry has been growing since the 1990s and largely grew out of mergers of the big banks, observed Drake-Brockman. In the U.S., 90% of the lending market is deals done by funds and 10% banks. Meanwhile in Europe it is 35% funds and the rest is banks, he added.

"So you have a natural growth opportunity that is a transfer of assets out of banking and into institutional funds that are driven by investors hunting for yield," he said of the European potential, adding that while there are more than 200 lenders in the U.S., in Europe the top two firms account for half of the overall market. Pemberton with a shorter track record has been ranked third in the line-up.

In the U.S., the market has been massive and driven by high quality firms, but the story of the U.S. economy has been one of an expectation for slower growth. Increasingly firms are becoming active in the space and the terms Pemberton have seen are weak and lack controls as a lender, he said.

Increasingly foreign investors are looking to get into Europe with capital coming from Canada, U.S. and Australia.

In its latest step in its strategic expansion into the U.S. and Canadian market, Pemberton announced the appointment of Scott Hamilton to the newly created role of managing director for North American business development. He will lead institutional client coverage and consultant relations for Pemberton's European private debt strategies in the U.S. and Canada.

Previously, Hamilton was managing director of institutional distribution at Alcentra.

"It's exciting to be joining Pemberton at this inflection point in the European direct lending market," Hamilton said. "With its highly experienced team, platform scale and dual-track credit process, Pemberton has come through this economic downturn on a strong footing, and as a leading provider of corporate debt solutions across Europe."

During the COVID-19 pandemic, Pemberton has been very targeted in its lending. For instance in the airline industry, they have focused on the servicing of plans and military and private jets, which have done well despite commercial airline shutdowns. And over the last 10 years, Drake-Brockman said the firm has learned how easily technology can make products obsolete.

In September, Pemberton supported private equity giant Advent International's acquisition of a majority stake in Hermes UK, a consumer delivery company that works with U.K. retailers to deliver millions of parcels. Such an investment is a perfect COVID-related lending strategy.

Hermes has been hiring and the recruitment drive reflects the increased demand creating by people shopping online during the lockdown, and the continued growth in the sector.

Pemberton's investment was via its mid-market debt strategy.

"Pemberton's platform was purpose-built to support companies with strong growth potential and sponsors with unrivalled expertise in furthering their portfolio companies' ambitions," said Eric Capp, head of UK at Pemberton. "Hermes UK and Advent International are both perfect examples of this, and we are excited to provide capital to help Hermes UK pursue further investment in future growth and technology."

Pemberton is focused on 'new economy' lending with an eye on first tier supply chain companies and areas such as food manufacturing, business services, pharma, technology and education, according to Drake-Brockman.

In general, Pemberton creates 7-year bullet loans that on average have a life span of three years as the company is usually acquired before the end of the loan.

Pemberton's returns vary by strategy. Its senior secured fund has BB risk and yields 6% annually. The mid-market lending fund has single B corporate bond risk and via four to five times leverage is expected to earn 8% to 9% annually. Lastly, the strategic credit offering includes complex financing or mezzanine debt and yields 14%. That offering is viewed as an alternative to hedge funds and private equity yields.

More importantly, Pemberton relies on an internal credit rating model system that would be on par with something implemented at any global bank. The model has been signed off by one of the leading regulators in Europe and over a 20-year time period has had a predictability rate of 70%, according to Drake-Brockman.

The sophisticated model has meant that the level of loan information Pemberton collects is sizable.

"I think one of the reasons we have had such a positive experience in Europe is because not only have we been able to have the ability to underwrite and source loans, but to also have the information on the loans," Drake-Brockman added.



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