# THE RISE OF PRIVATE DEBT IN AUSTRALIA:
## A BOOST FOR THE FUTURE OF CORPORATE LENDING

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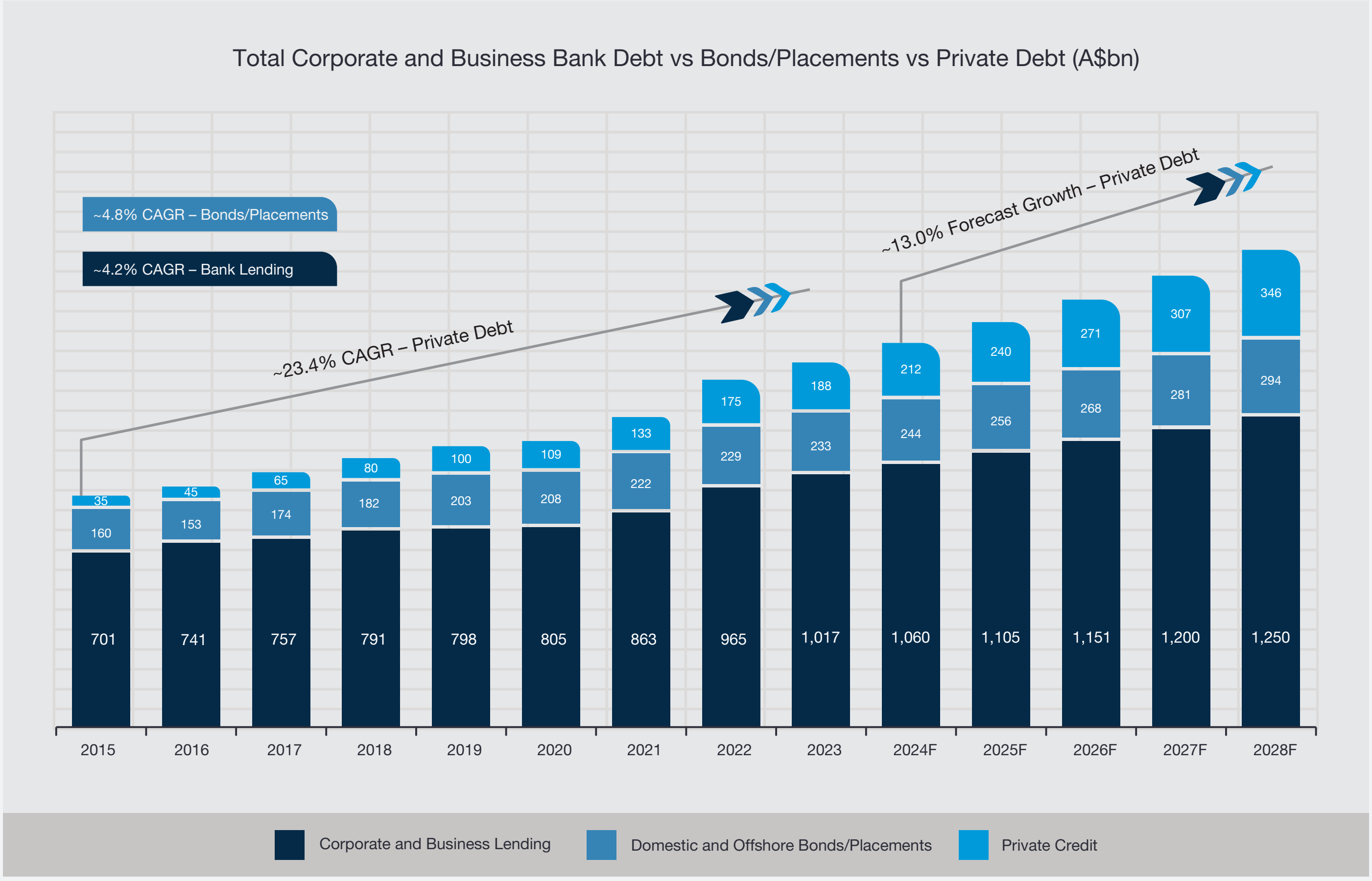
In the first half of 2024, we've witnessed a stream of positive news stories regarding the latest private debt deals, the establishment of new private debt funds, and the consolidation of several existing private debt fund managers in the Australian market. These developments clearly indicate the impressive growth and maturing of the private debt market in recent years in Australia.

Over the past decade, the private debt market has shown remarkable growth, consistently outpacing the broader corporate lending market. The chart below illustrates the rapid expansion of private debt during this period and its promising future potential. Using the midpoint of current Blackrock and Preqin growth estimates of 13 percent per annum, private debt could reach close to $350 billion in Australia and account for about 18 percent of total corporate lending in the next five years. This should propel private debt to surpass our corporate bond market in size, with banks retaining their key role in Australian corporate lending and holding the largest share.




Source: RBA, Bloomberg, Private Placement Monitor, EY, Blackrock, Preqin Future of Alternatives 2028

This is great news for Australian companies with an ever-increasing number of bank and private debt options available for them to access. While it can be daunting to compare private debt against existing markets that they are more familiar with, along with the challenge of working their way through the long list of active lenders, this increased borrower choice is a positive development.

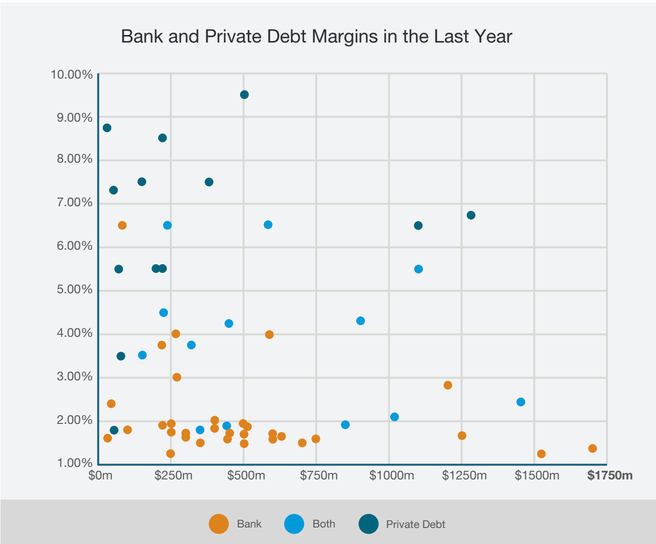
While it's important to tailor the comparison to the specific needs of each business and approach it independently, we have explored three key areas for comparing private debt and bank debt. This should help contribute to the ongoing debate about choosing the right market for your needs.

# Comparing Private Debt and Bank Debt - Three Key Areas

## 1. The recent experience in credit margins

In 2024, we've experienced robust demand from lenders, competitive pricing and keen interest to participate in the opportunities available. While the traditional view has been that companies can secure the best pricing from bank and bond markets and utilize private debt for greater leverage, flexibility, or speed of execution, this perspective is evolving.

From inspecting a wide range of bank and private debt deals in Australia in the chart below, we observe that each source of debt funding has its competitive advantages, albeit with an increasing overlap where both sources can lend on common or similar terms.



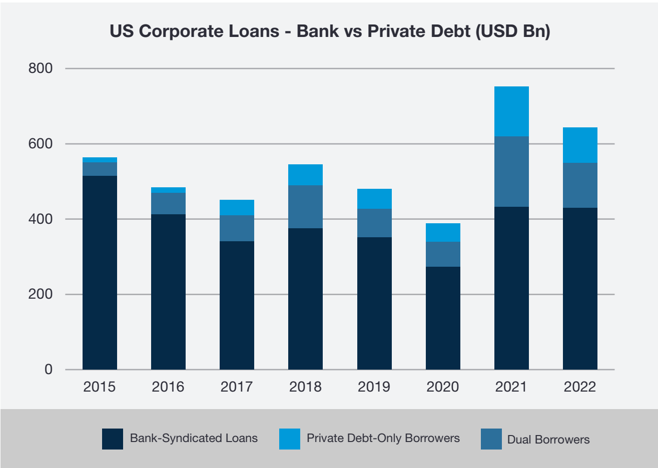


Source: Loanconnector, Debtwire, AFR, ASX Releases

This indicates that pricing tends to be consistently lower in the bank market and in a wider range in the private debt market. However, as institutional capital becomes more abundant, private debt lenders are expected to offer tighter pricing in more situations. This trend is expected to continue as both bank and private debt capital are drawn to larger and better-rated financings, especially while base rates remain elevated and total returns are at current levels.

## 2. Market competitors or complementary solutions?

In coming years, it will also be important to keep an eye on the relationship between banks and private debt lenders as competition remains high. An interesting observation from the chart below on the US market is that while private debt lending has grown quickly, the largest increase was for companies that have both private debt and bank debt in their funding structures.




Source: Private Debt versus Bank Debt in Corporate Borrowing 2024 Report (US)

Already in the Australian market, we are seeing a similar trend for the increased use of dual bank and private debt loan structures, including:

a) Unitranche, Term Loan B, Direct Private Debt funding lines sitting alongside working capital, asset finance, hedging and transactional facilities from banks

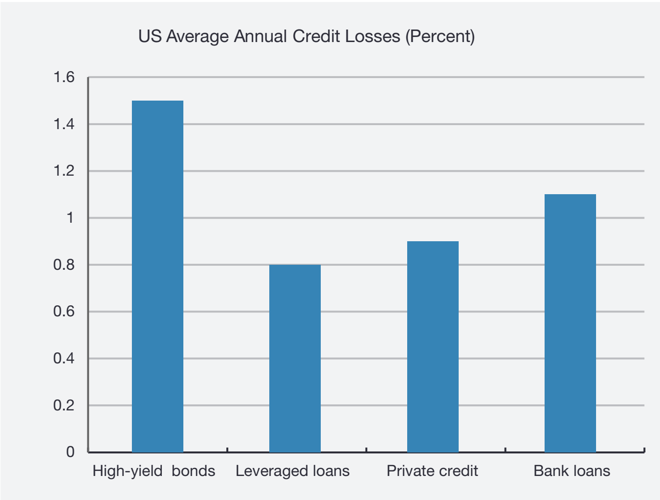
b) Large institutional syndicated loans with both bank and private debt lenders, currently mostly with sub-investment grade profiles but likely to increase in investment grade lending over the coming years

c) Debt structures where banks provide the senior or corporate debt, and private debt lenders provide junior debt or asset- or project-specific debt facilities, in each circumstance where the private lender steps in to fund beyond the appetite of banks

One significant advantage of banks and private debt lenders complementing each other this way instead of always competing is that it provides a broader range of mergers and acquisitions (M&A), growth, project finance, and debt restructuring funding options to choose from.

## 3. Sharing the risk as problems emerge

Another important area for comparison is how problem loan and default levels differ during an economic downturn, and how banks and private debt lenders respond in these circumstances. We have already seen both perform relatively well through COVID-19 and the interest rate rises over the last two years. However, this may change in the near term given the current economic headwinds.




Sources: Cliffwater, Fitch Ratings, Preqin, IMF and between 2013 and 2022.

One indication of the potential outlook here is the credit loss record in the US over the past decade, as illustrated in the chart above, showing there is a small variation across private debt, leveraged loans, and bank debt over this period. Recently, news reports have predicted an increase in loan and covenant default rates in private debt. However, historical data in the US indicates similar actual loss levels across the respective markets once loans are reset, restructured and recovered.

While we might observe different results in Australia due to our very low level of problem loans in recent years, it is too early to make definitive conclusions until we see these trends play out over a full economic cycle. Moreover, under these circumstances, there could also be a resurgence in the high-yield segment of the private debt market, as these lenders provide capital to companies that are highly leveraged or require greater flexibility, for example assisting in filling the bid-ask spread on M&A transactions and enabling a refinance to facilities with more covenant headroom.

## An Expanded Range of Lending Options for Australian Companies

By reviewing the three key areas of comparison between banks and private debt lenders and the levels of market growth seen in recent years, it is likely that both will have plenty of opportunities to play an important role in funding Australian companies in coming years. Even if the market sizing and share in five years' time differs to the current forecasts, there is no doubt that we will see a wide range of options and solutions for companies to consider. Healthy competition across all segments will also benefit the broader economy by supporting a wider range of M&A, growth and corporate funding needs.

## How A&M Can Help

A&M Debt Advisory helps companies to plan, select, source, negotiate and amend debt facilities across a range of debt markets and funding structures. Debt markets are more sophisticated and more complex than ever before. The A&M Debt Advisory team supports borrowers in navigating those markets and is well equipped to support its private equity and corporate clients through the economic cycle, providing high value-add advice on debt raising, capital structure optimisation and navigating challenging situations.

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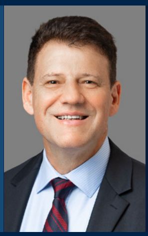

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With over 10,000 people providing services across six continents, we deliver tangible results for corporates, boards, private equity firms, law firms and government agencies facing complex challenges. Our senior leaders, and their teams, leverage A&M's restructuring heritage to help companies act decisively, catapult growth and accelerate results. We are experienced operators, world-class consultants, former regulators and industry authorities with a shared commitment to telling clients what's really needed for turning change into a strategic business asset, managing risk and unlocking value at every stage of growth.

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