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EIF Private Debt Survey 2021:
Private Debt for SMEs – Market Overview

EIF and University of Trier Entrepreneurial Finance Seminar

Private Debt for SMEs in Europe

10 March 2022

Market Overview

Desk Research

This overview provides data from publicly available resources about private debt funds.
As data sources, the databases ‘Pitchbook’, ‘Preqin’, and ‘Private Debt Investor’ as well as information available from private equity and private debt associations, fund managers websites, and general web research were used.

European Market Overview

Investment Focus

585

private debt funds in the European market

72% invest **exclusively** in Europe

- Europe has a developing ecosystem of private debt funds that is getting stronger and revolves around funds that predominantly invest in Europe.
- The European ecosystem of private debt funds has approximately €311B assets under management.
- 29% of the private debt funds focus on growth-oriented firms.

Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Summary

- Currently 585 private debt funds are active in the European market. 28% of these funds invest globally and Europe is only one segment of their fund.

- 97% of funds with available data focus on small or mid cap portfolio companies. Their preferred average loan size lies in the range of €9M - €45M.

The publicly available data for private debt funds remains rare or even poor. Our desk research is unable to answer detailed underlying questions regarding the forces in the private debt market.

Therefore, our following market survey provides unique insights into the European private debt market that helps to increase the transparency of the market for the public!

Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Market Overview

Survey

The EIF PD Survey

Number of Respondents

146

from 22 countries

51% supported by the EIF

Assets under Management

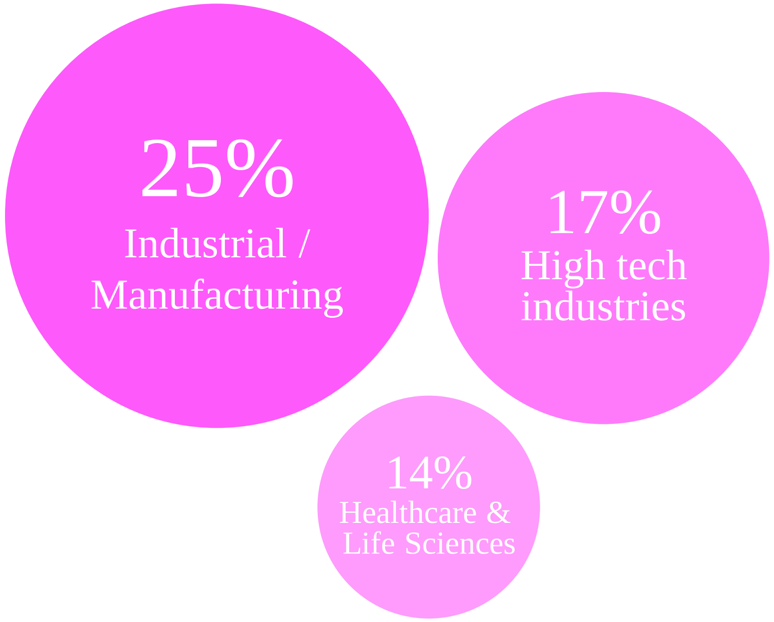
Median:
€501M - €1,000M

Target Market Segment by Portfolio Company Revenue

Median:
€51M - €100M

Top Sectors

(Most important sector named by funds)



Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Geographic Focus

Most important European countries

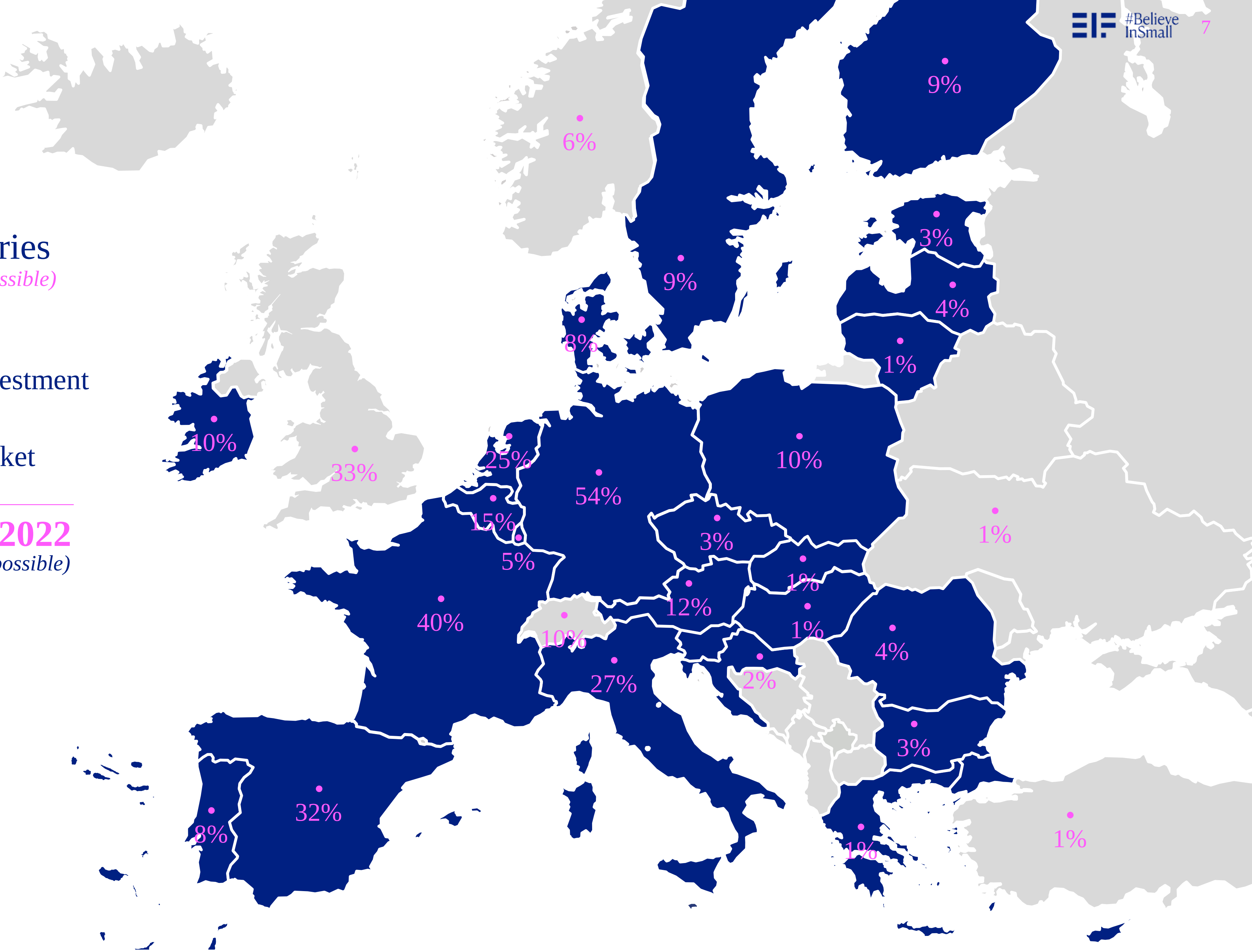
(indicated in % by respondents, multiple selection possible)

- 97% invest in Europe
- 57% have their main country of investment in the EU
- Germany is the most important market

Highest Market Potential by 2022

(indicated in % by respondents, multiple selection possible)

1. Germany *(58%)*
2. France *(42%)*
3. Spain *(41%)*
4. Netherlands *(35%)*
5. Italy *(35%)*



Source: *EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm*

Industry Focus

Private Debt Funds focus equally on both asset-heavy and asset-light industries

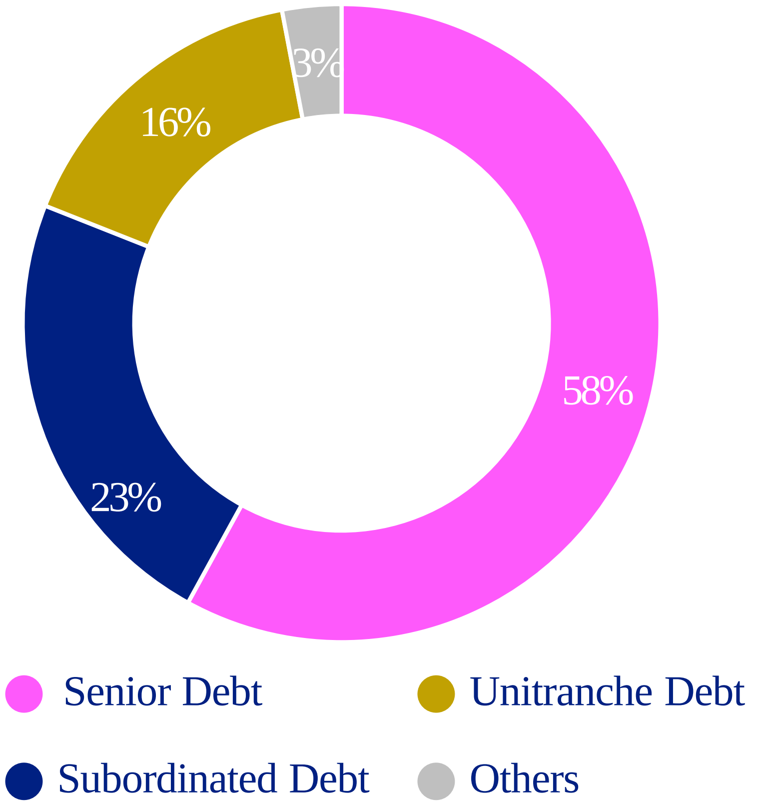
73% Industrial/Manufacturing	**62%** High-Tech Industries	**60%** Healthcare and Life Sciences
47% Consumer Products	41% Media and Telecommunications	27% Beverage/Food/Tobacco
23% Energy and Utilities	22% Retail and Wholesale	19% Banking/Finance/Insurance

(Q: Please select up to 5 of the most important industries in which your firm invests in private debt.)

Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

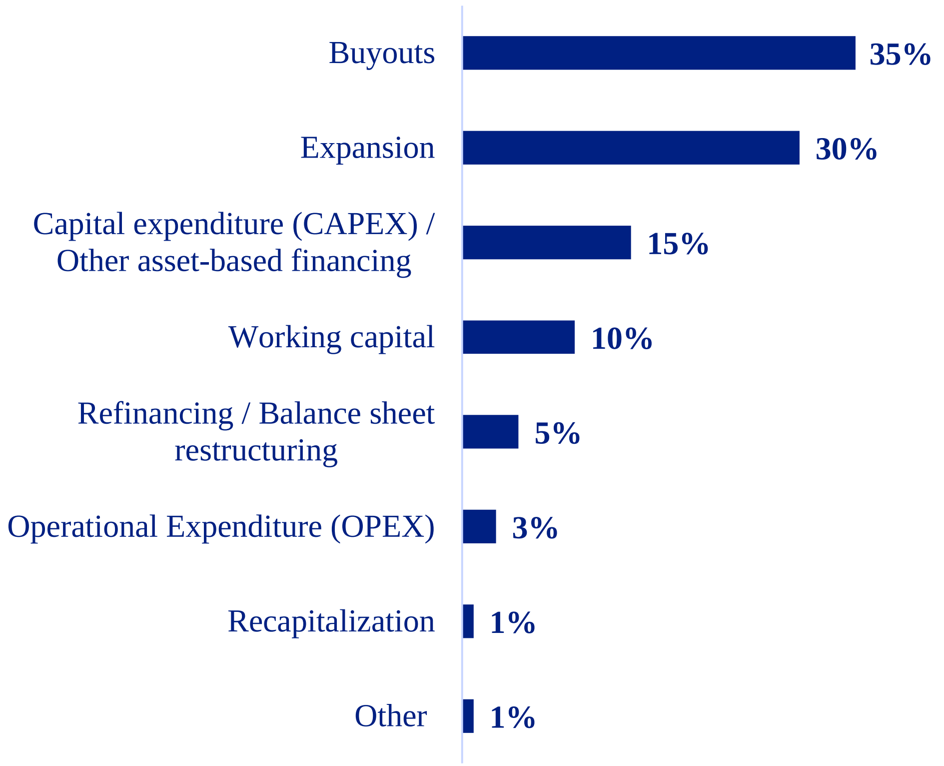
Strategy & Loan Characteristics

Debt Strategy

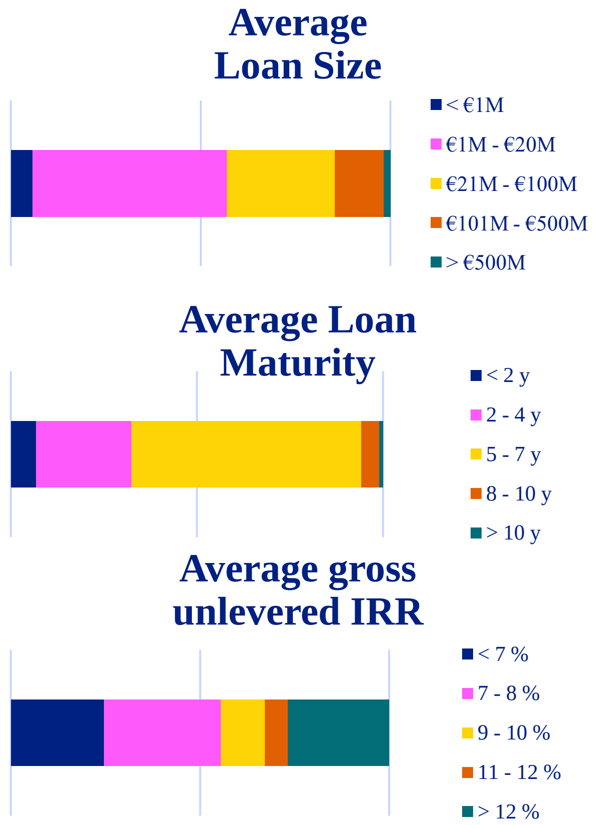


Most Important Loan Purpose

(indicated in % by respondents)



Loan Characteristics



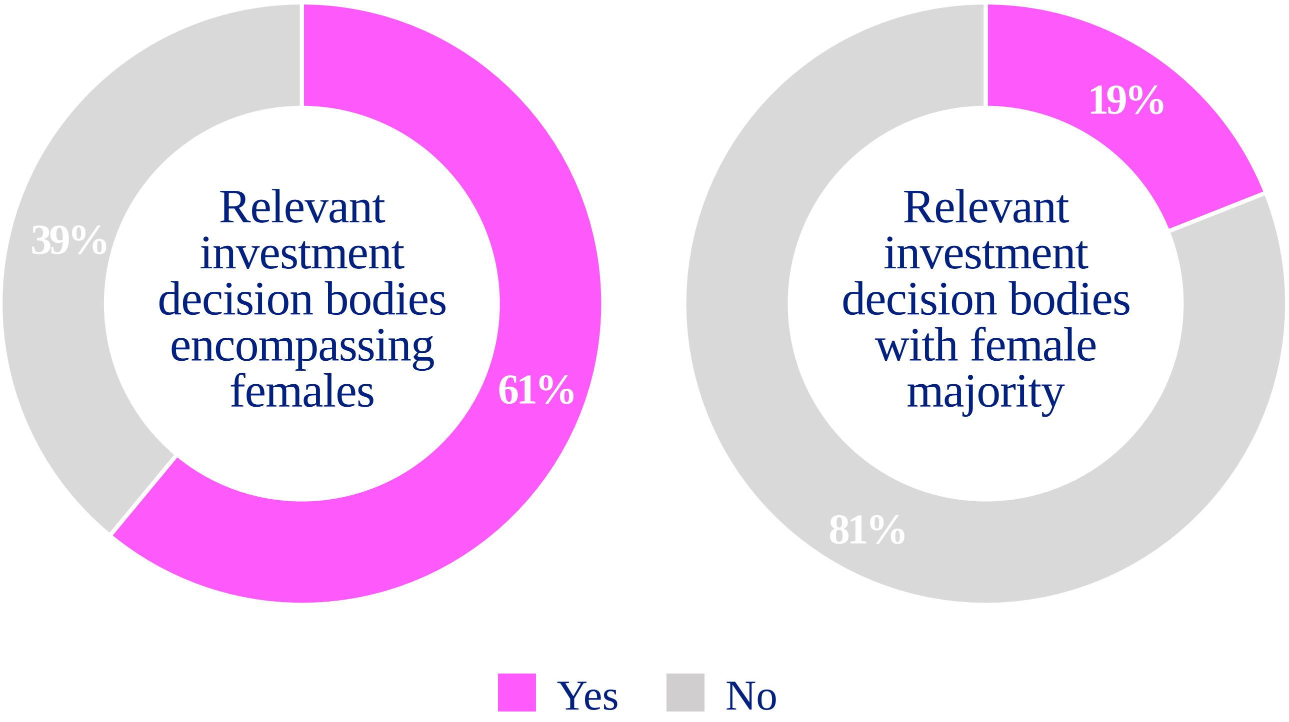
ESG Challenges and Female Representation

Biggest Challenges in Implementing an ESG Strategy

(indicated in % by respondents, multiple selection possible)

1.	Quantifying ESG information/Developing ESG-related KPIs	82%
2.	Comparability of ESG information across companies	57%
3.	Clarity of ESG analytical and reporting framework	46%
4.	Greenwashing	43%
5.	Costs associated with gathering and assessing ESG information	31%

Female Representation at Fund Level



Note: ESG considerations featured prominently in the EIF Private Debt Survey. A dedicated EIF Working Paper is going to be published soon.

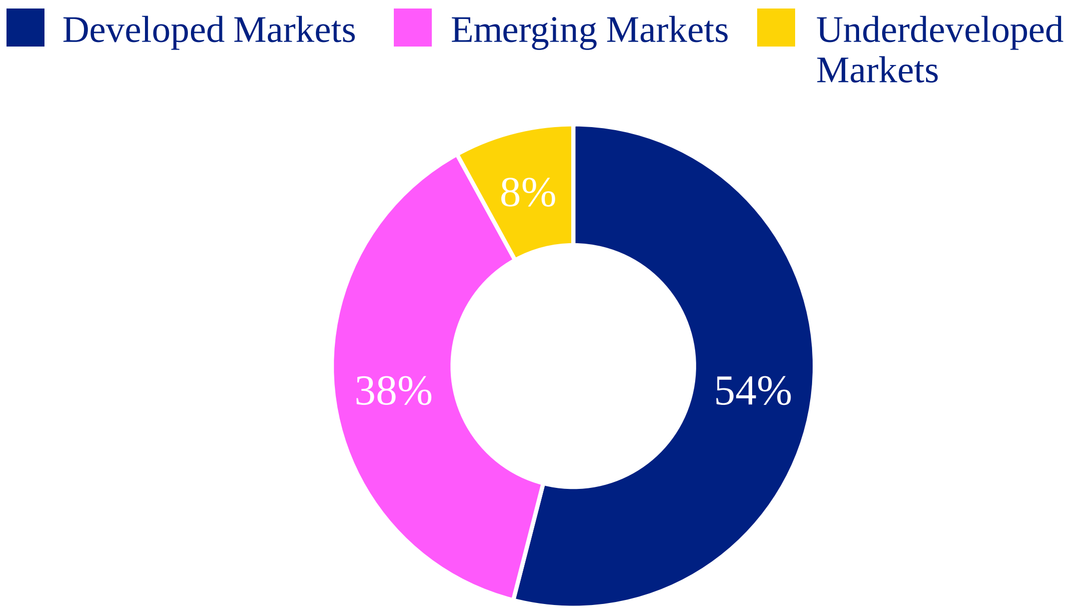
Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Market Split: Geographic

Developed (debt fund) markets: Germany, France, United Kingdom
Emerging (debt fund) markets: Italy, Spain, Netherlands, Belgium, Ireland, Nordics
Underdeveloped (debt fund) markets: Eastern Europe

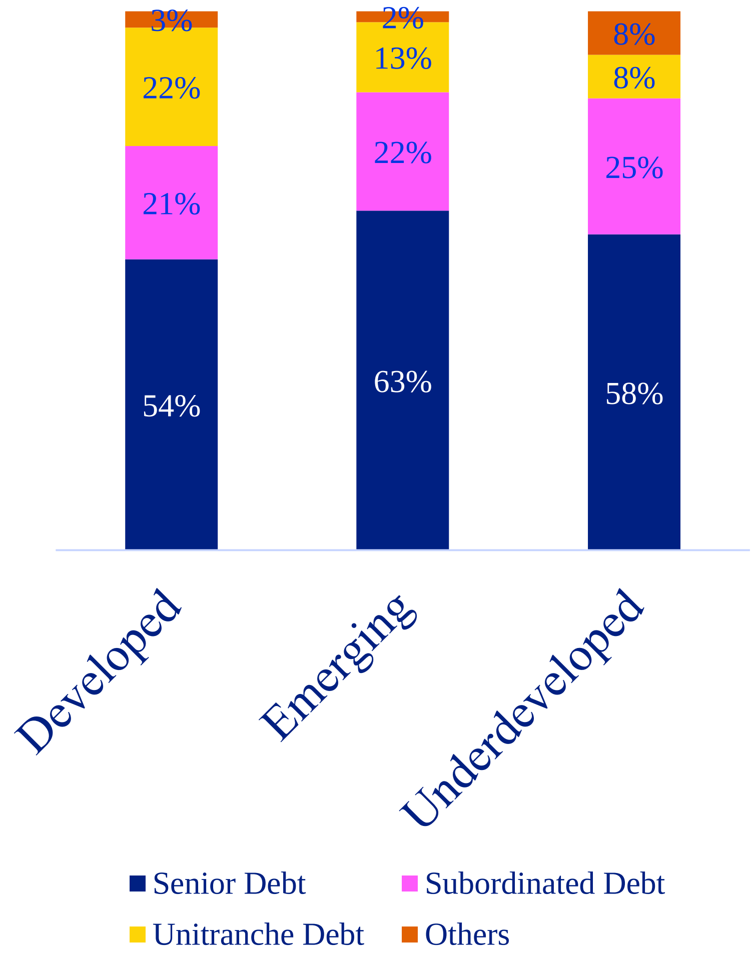
Geographic Distribution

Overview of Respondents by Market



- **Developed debt fund markets:** Germany, France, United Kingdom
- **Emerging debt fund markets:** Italy, Nordics, Spain, Belgium, Netherlands, Ireland
- **Underdeveloped debt fund markets:** Eastern Europe

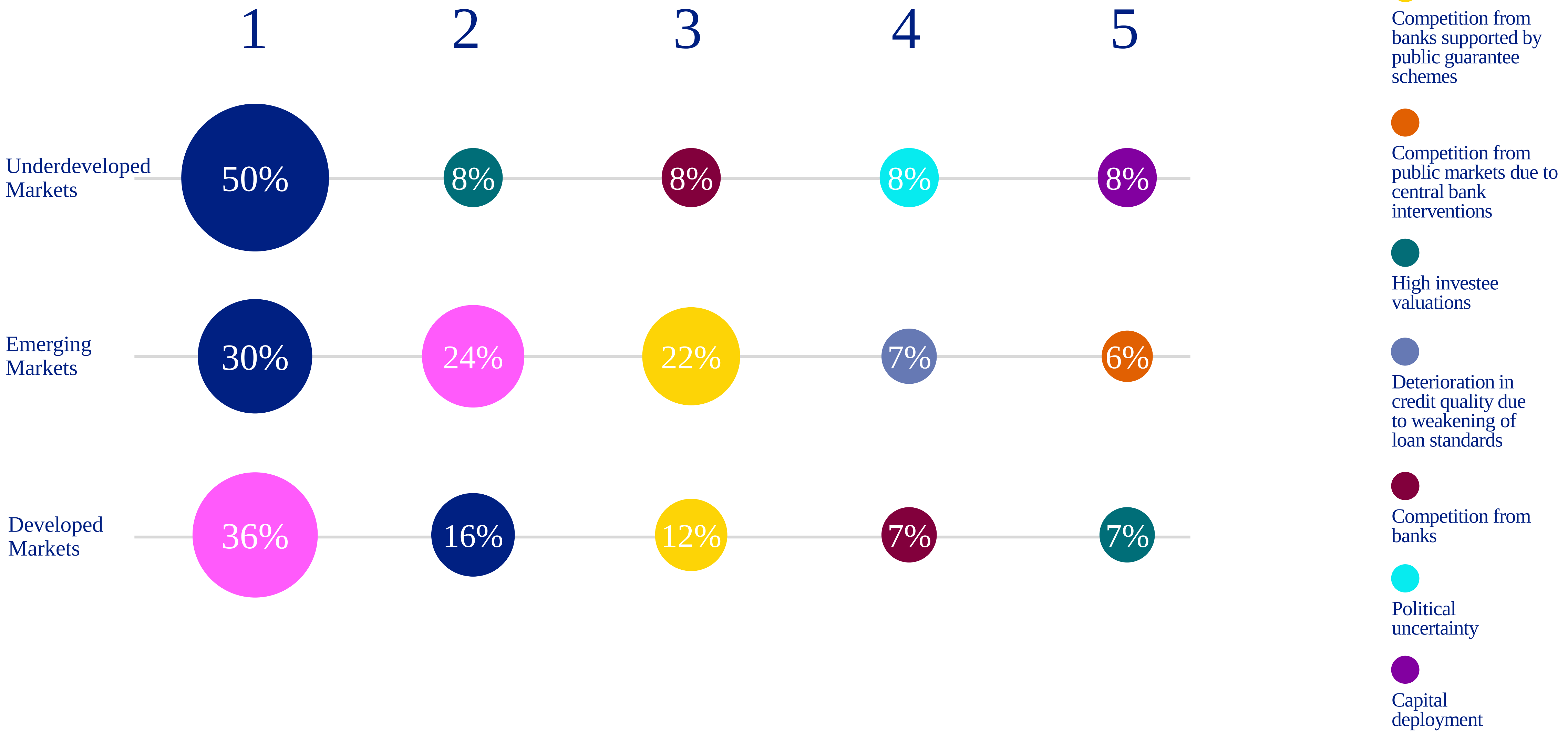
Private Debt Strategy



Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Challenges in PD business

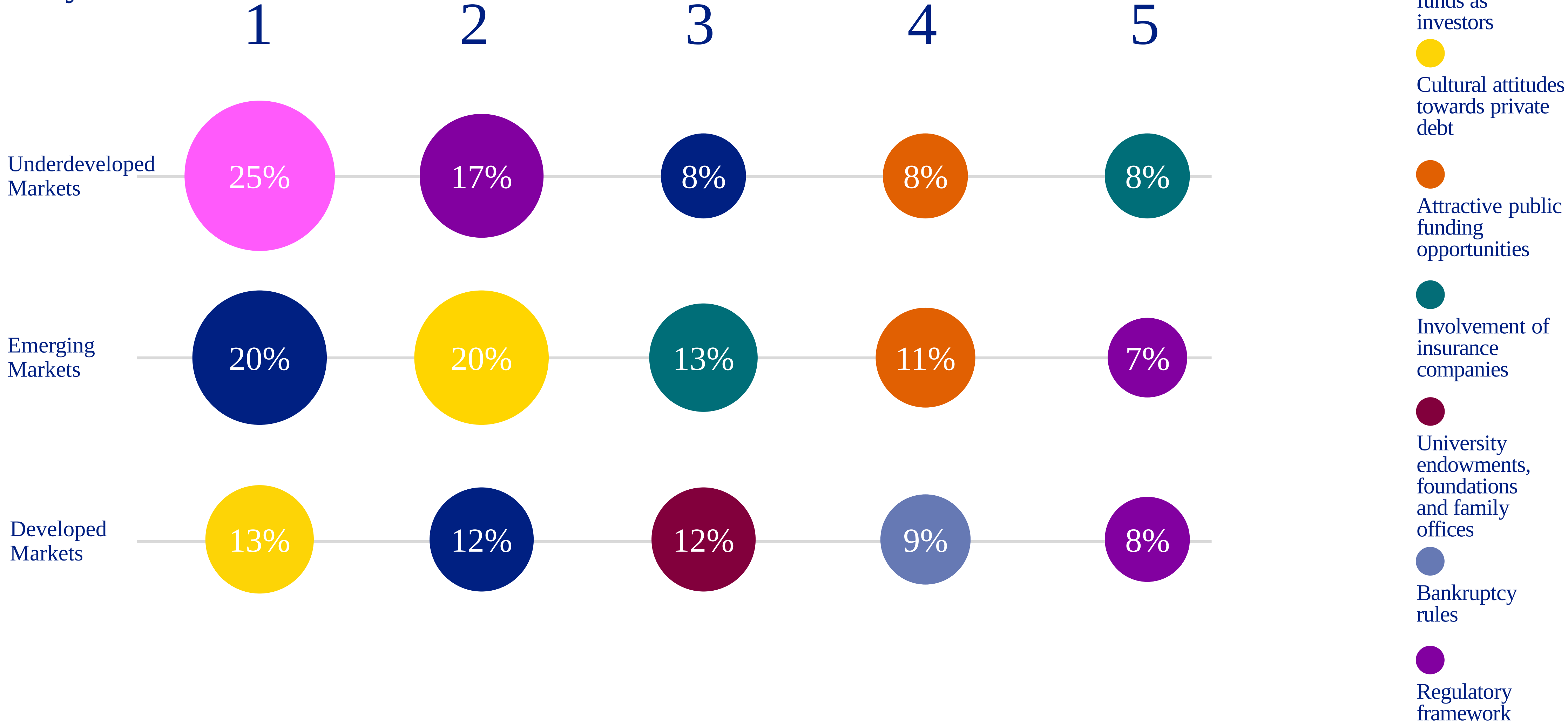
Largest challenges that can harm the growth of the PD sector



Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Underdeveloped Elements

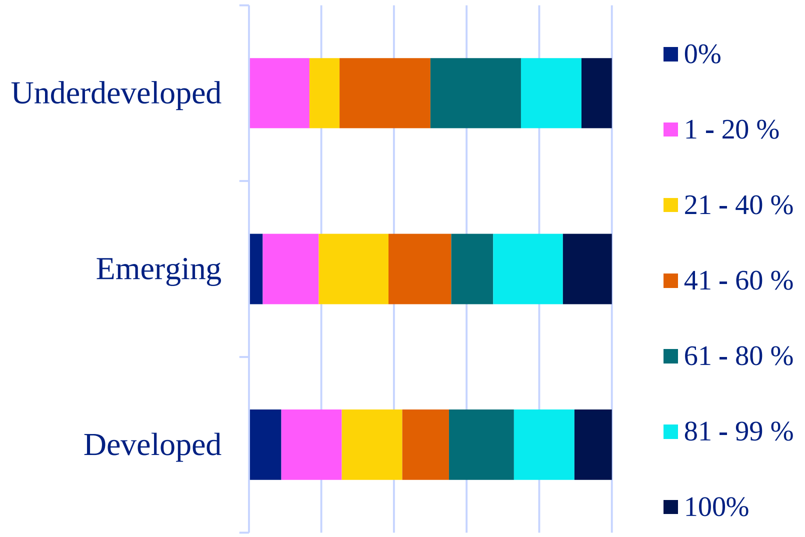
The largest elements that are helpful but underdeveloped in the local PD ecosystems



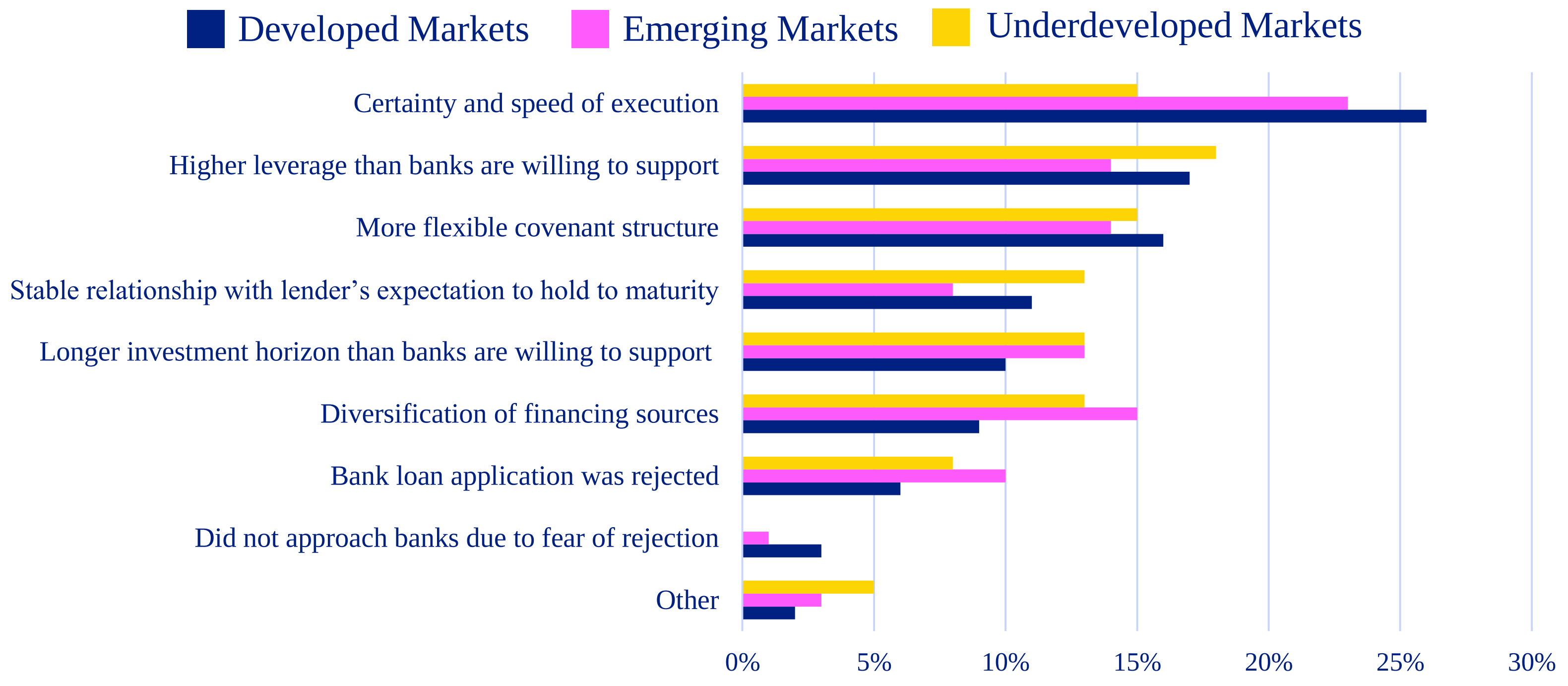
Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Bank Financing

Percentage of portfolio companies that would not have been able to get bank financing



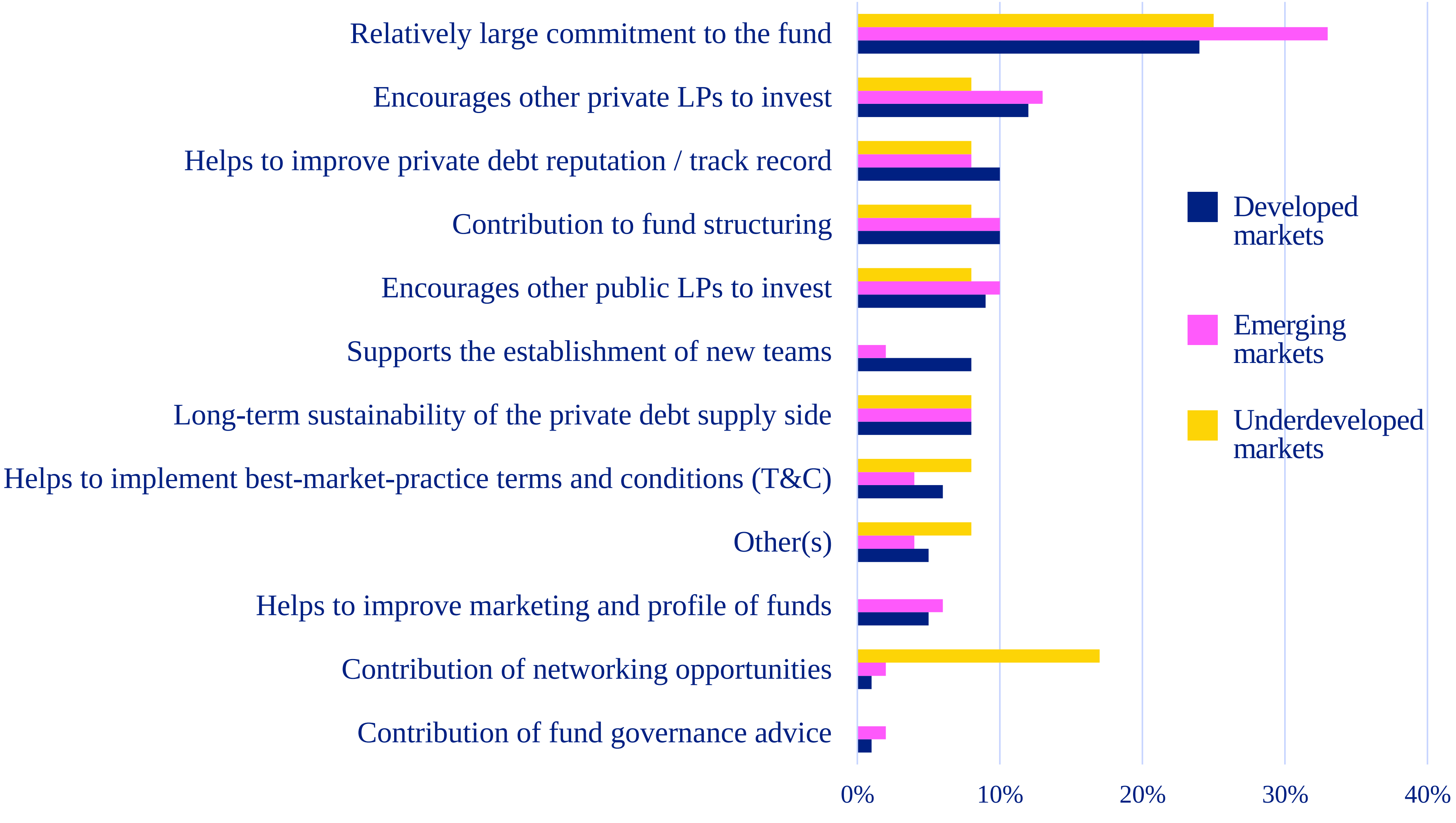
Reasons why firms choose private debt over bank debt



Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Governmental Support

Most important aspects of governmental support programs



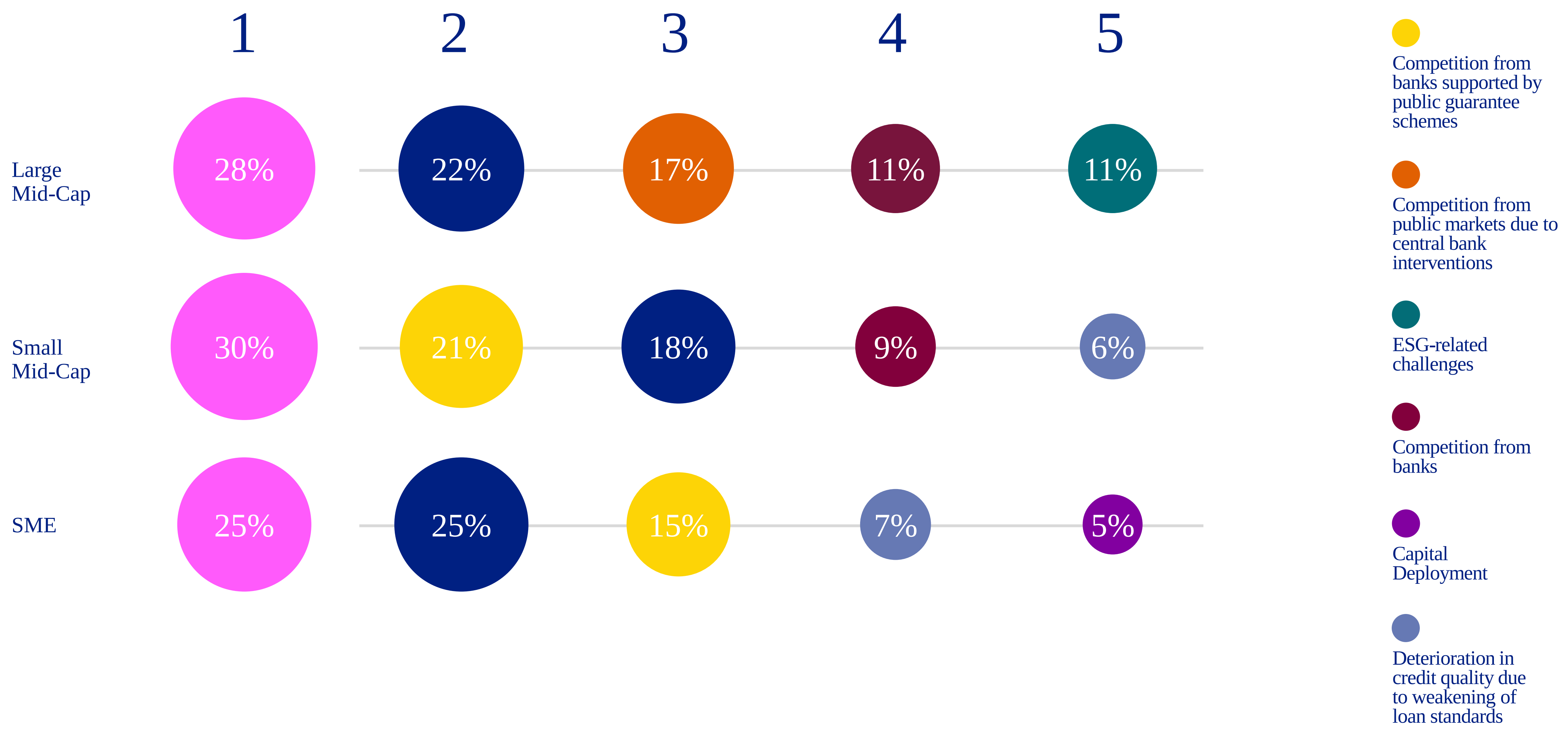
Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Market Split: Portfolio Company Size

SME: Funds that target portfolio companies with up to 249 employees
Small Mid-Caps: Funds that target portfolio companies with a number of employees in the range between 250-499
Large Mid-Caps: Funds that target portfolio companies with a number of employees in the range between 500-3,000

Challenges in the PD business

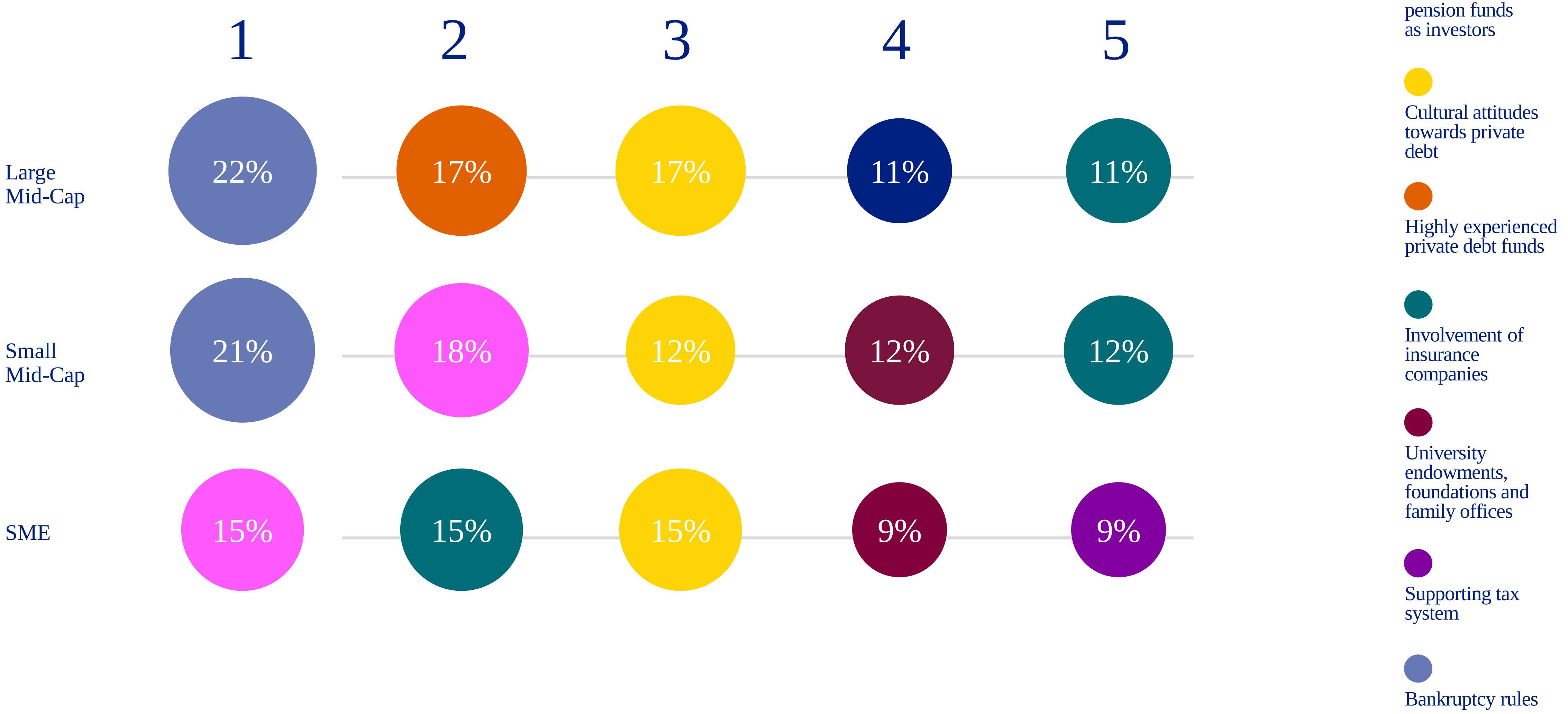
Challenges in the PD business by target sectors



Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

Underdeveloped Elements in the EU

Most underdeveloped elements that would support PD ecosystems



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Summary

Summary (i/ii)

- The publicly available data for private debt funds remains scarce. Our desk research is unable to answer all questions regarding the private debt market. Therefore, the *EIF Private Debt Survey* provides unique insights into the European private debt market that helps to increase the transparency of the market for the public.
- Private debt can be important to mitigate access to debt finance constraints, as (depending on the markets under consideration) 40-60% of PD fund portfolio companies would not have been able to get bank financing.
- The loan characteristics among funds that focus on mid caps and small caps are in line with expectations. Funds that focus on mid caps have more assets under management, larger loan sizes and lower targeted IRRs.
- The United Kingdom, France and Germany are the most developed debt fund markets in Europe. Northern and in particular Eastern Europe are less developed.
- PD funds and loan sizes are significantly smaller in underdeveloped and emerging European private debt markets compared to developed markets. Since the competition from PD funds is the largest challenge in developed markets, it is likely that developed markets' players will diversify beyond those markets, if transparency and PD ecosystems are properly developed.

Summary (ii/ii)

- Fundraising is one of the strongest challenges across the European PD markets. Different market segments lack the involvement of different investors. However, the absence of important investors seems equally important. Underdeveloped markets particularly lack the involvement of corporate investors, whereas emerging and developed markets miss the involvement of pension funds as investors. Considerable investment tickets are needed to support fundraising traction and development of new teams, in particular in underdeveloped and emerging markets.

- Bankruptcy rules, cross-border integration, and cultural attitudes towards private debt are seen as the most underdeveloped elements among PD investors. Public institutions need to investigate, how the EU might overcome these structural disadvantages for the private debt market, e.g. by contributing to the internationalisation of the LP investor base.

- The market sentiment in the private debt market is very positive (at the time the survey was conducted). However, the very positive outlook paired with concerns of high-investee valuations should be closely monitored to avoid bubble building.

Source: EIF Private Debt Survey 2021: Private Debt for SMEs – Market Overview. EIF Working Paper 2022/79. Available at: https://www.eif.org/news_centre/research/index.htm

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If we believe in small big things can happen

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Private Debt Funds and their Portfolio Companies

EIF and University of Trier Entrepreneurial Finance Seminar

"Private Debt for SMEs in Europe"
(March 10th, 2022)

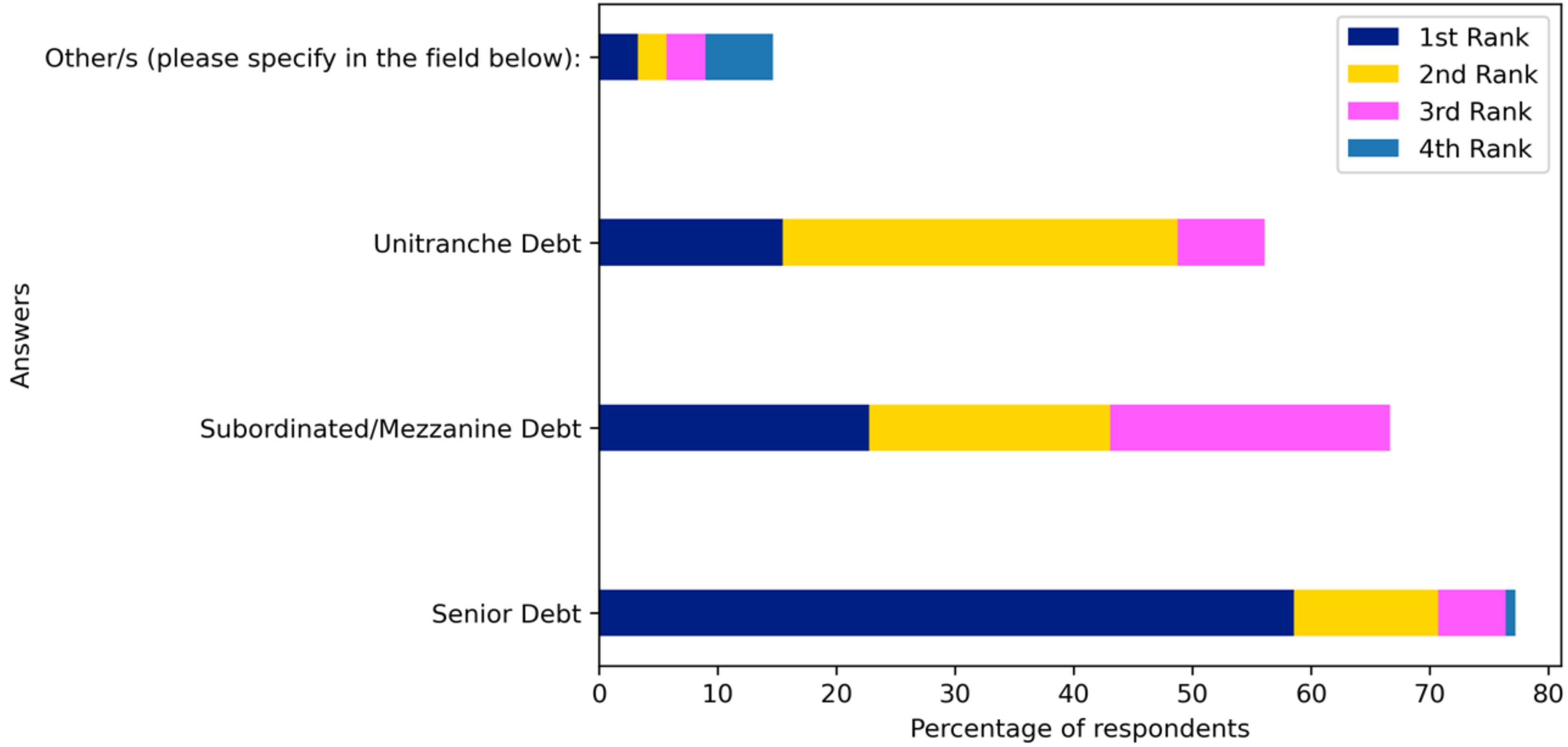
Prof. Dr. Jörn Block

Agenda

- PD-lending strategy and loan characteristics
- Sourcing, selection, and due diligence
- PE-sponsored deals
- Private debt versus bank loans
- Post investment activity

PD-lending strategy and loan characteristics

Capital structure



Question: Please select the most important capital structure seniority of your portfolio companies for your PD business.

Lending strategy

Strategy	N (%)
Direct lending	142 (49.31)
Special situations	42 (14.58)
Real estate debt	23 (7.99)
Venture debt	21 (7.29)
Other/s (please specify in the field below):	20 (6.94)
Distressed debt	16 (5.56)
Infrastructure debt	16 (5.56)
Fund of Funds	8 (2.78)
Number of respondents (responses)	153 (288)

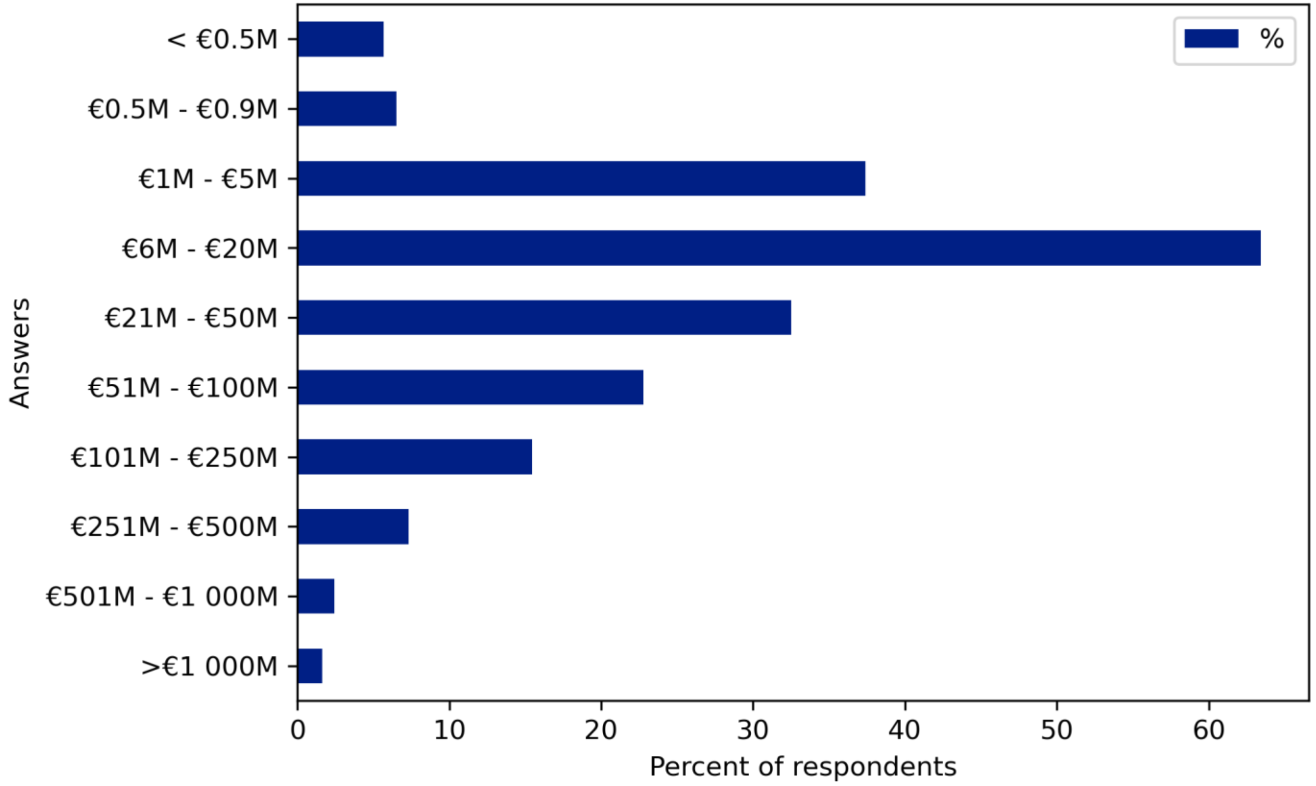
Question: Please select the most important capital structure seniority of your portfolio companies for your PD business.

Loan syndication

	Yes, with banks	Yes, with other DF			No
Syndicated loans provided (y/n)	**N (%)**	**N (%)**			**N (%)**
	29 (17.58)	38 (23.03)			85 (51.52)
Syndicated loans provided (%)	**Mean**	**Std. dev.**	**25%**	**50%**	**75%**
	37,36	29,72	15	30	50

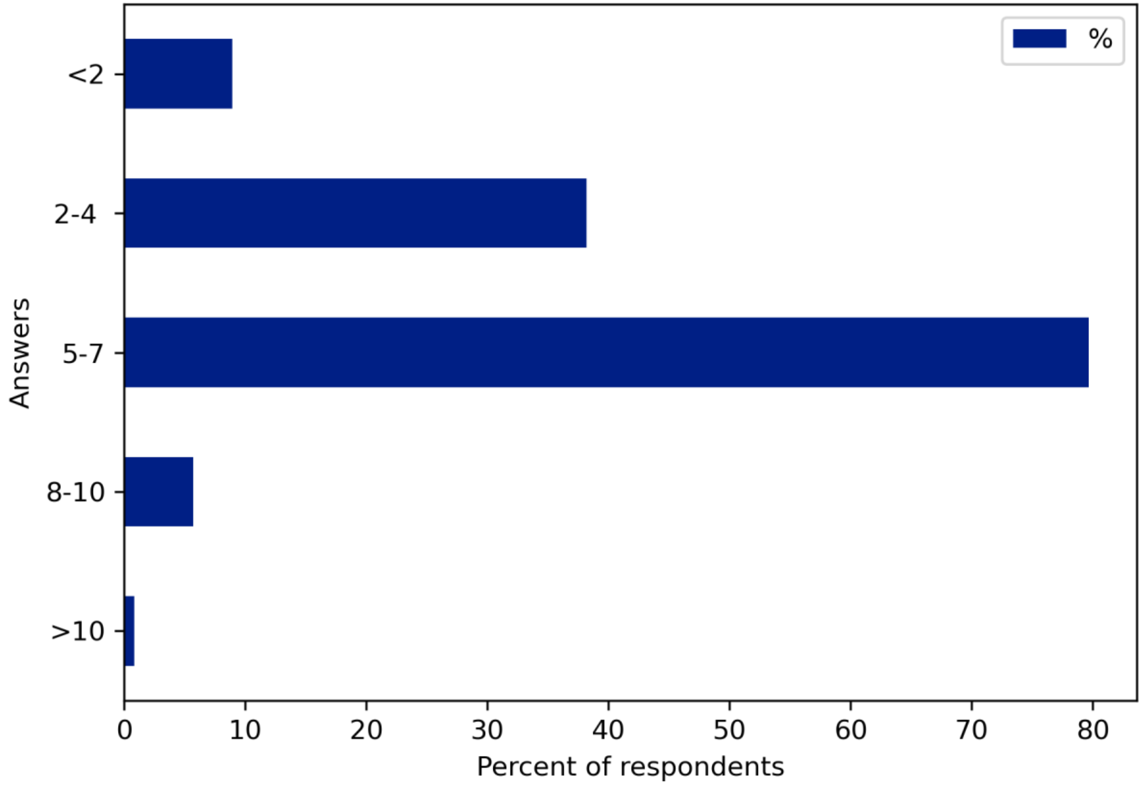
Questions: Do you provide syndicated loans? What percentage of your loans are syndicated? (%)

Loan size



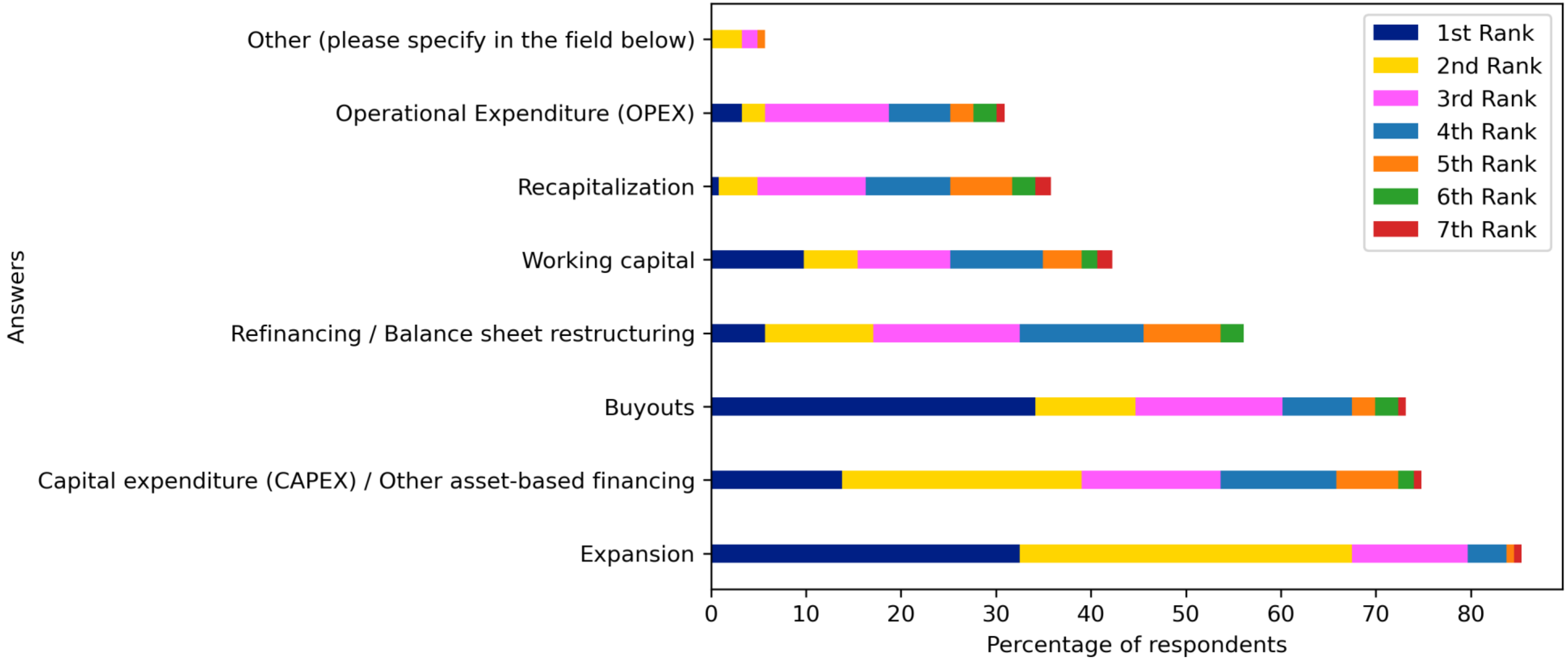
Question: What are the total average target loan sizes (in million €), where your fund is investing (including portions of the same loan provided by third parties alongside your fund)?

Loan maturity



Question: What is the typical loan maturity (in years), where your fund is investing?

Loan purpose



Question: What are your main loan purposes?

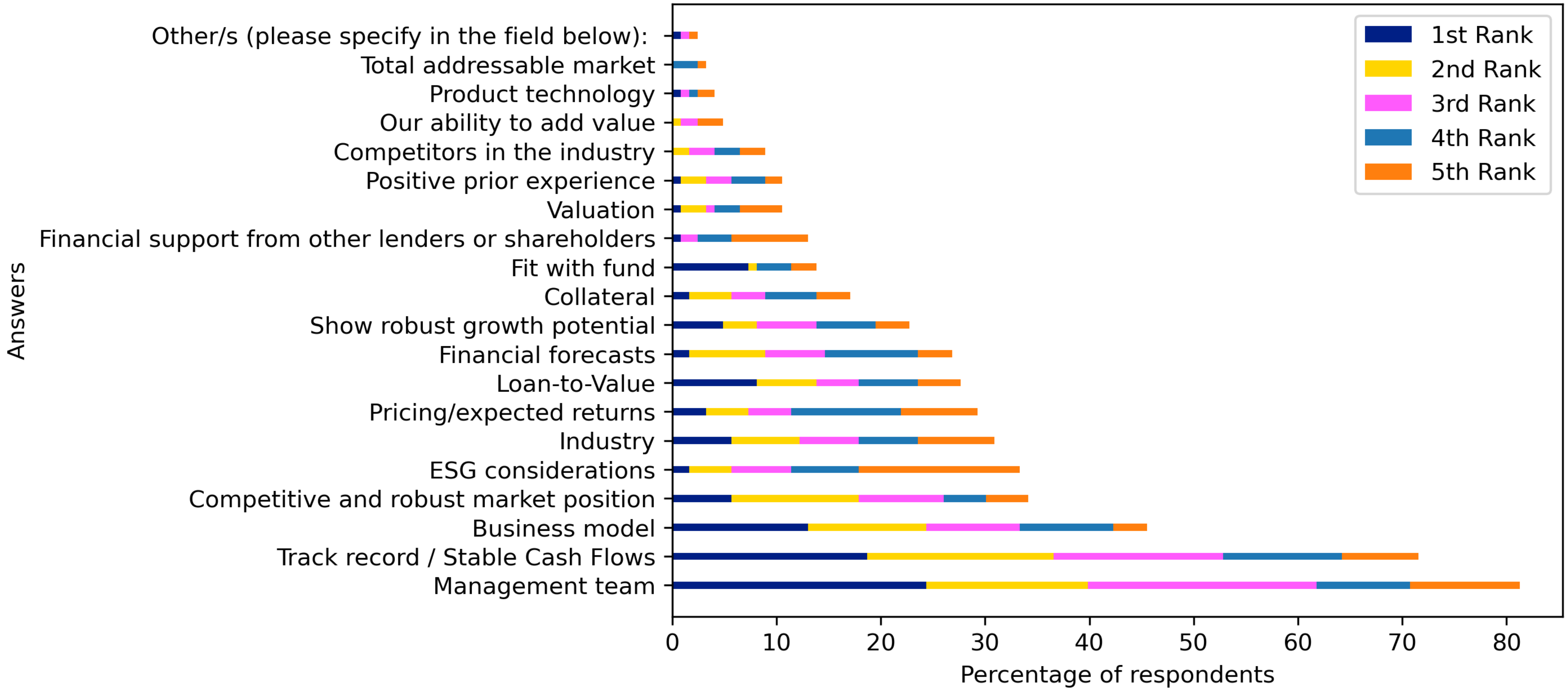
Sourcing, selection, and due diligence

Selection: industry

	Senior debt	Other PD
Industries	**N (%)**	**N (%)**
Industrial/Manufacturing	91 (17.57)	19 (14.50)
Healthcare and Life Sciences	73 (14.09)	17 (12.98)
High tech industries (e.g. software/IT)	72 (13.90)	20 (15.27)
Consumer Products	52 (10.04)	16 (12.21)
Media and telecommunications	47 (9.07)	15 (11.45)
Beverage/food/tobacco	32 (6.18)	8 (6.11)
Energy and Utilities	28 (5.41)	5 (3.82)
Banking/Finance/Insurance	25 (4.83)	4 (3.05)
Retail and wholesale	25 (4.83)	8 (6.11)
Construction and real estate	24 (4.63)	7 (5.34)
Transportation	18 (3.47)	3 (2.29)
Hotel/Gaming/Leisure	12 (2.32)	4 (3.05)
No clear sector focus	12 (2.32)	1 (0.76)
Other/s	7 (1.35)	3 (2.29)
Sovereign	0 (0)	1 (0.76)
Number of respondents (responses)	119 (518)	34 (131

Question: Please select up to 5 of the most important industries in which your firm invests in private debt.

Selection: most important criteria



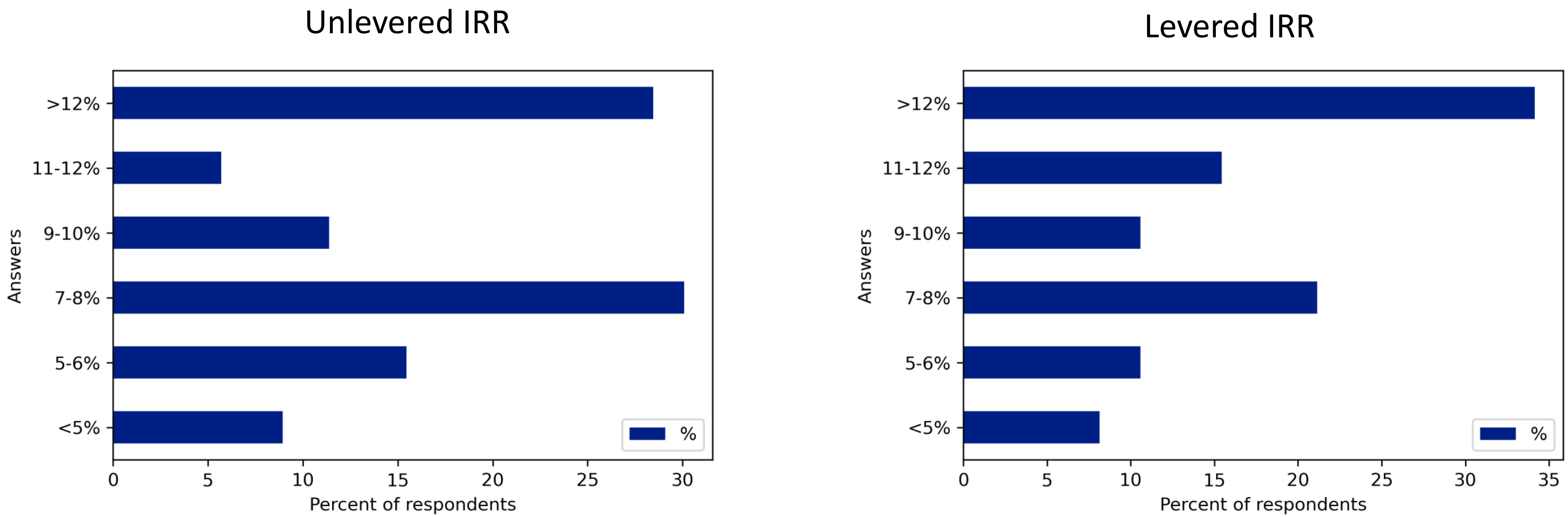
Question: Select up to 5 of the most important factors you consider when deciding whether to lend.

Selection: financial metrics used

Financial metrics	N (%)
None	1 (0.33)
Other/s (please specify in the field below)	17 (5.63)
NPV	24 (7.95)
Multiple of sales / earnings	57 (18.87)
Hurdle rate or IRR	74 (24.50)
Cash flow	129 (42.71)
Number of respondents (responses)	150 (302)

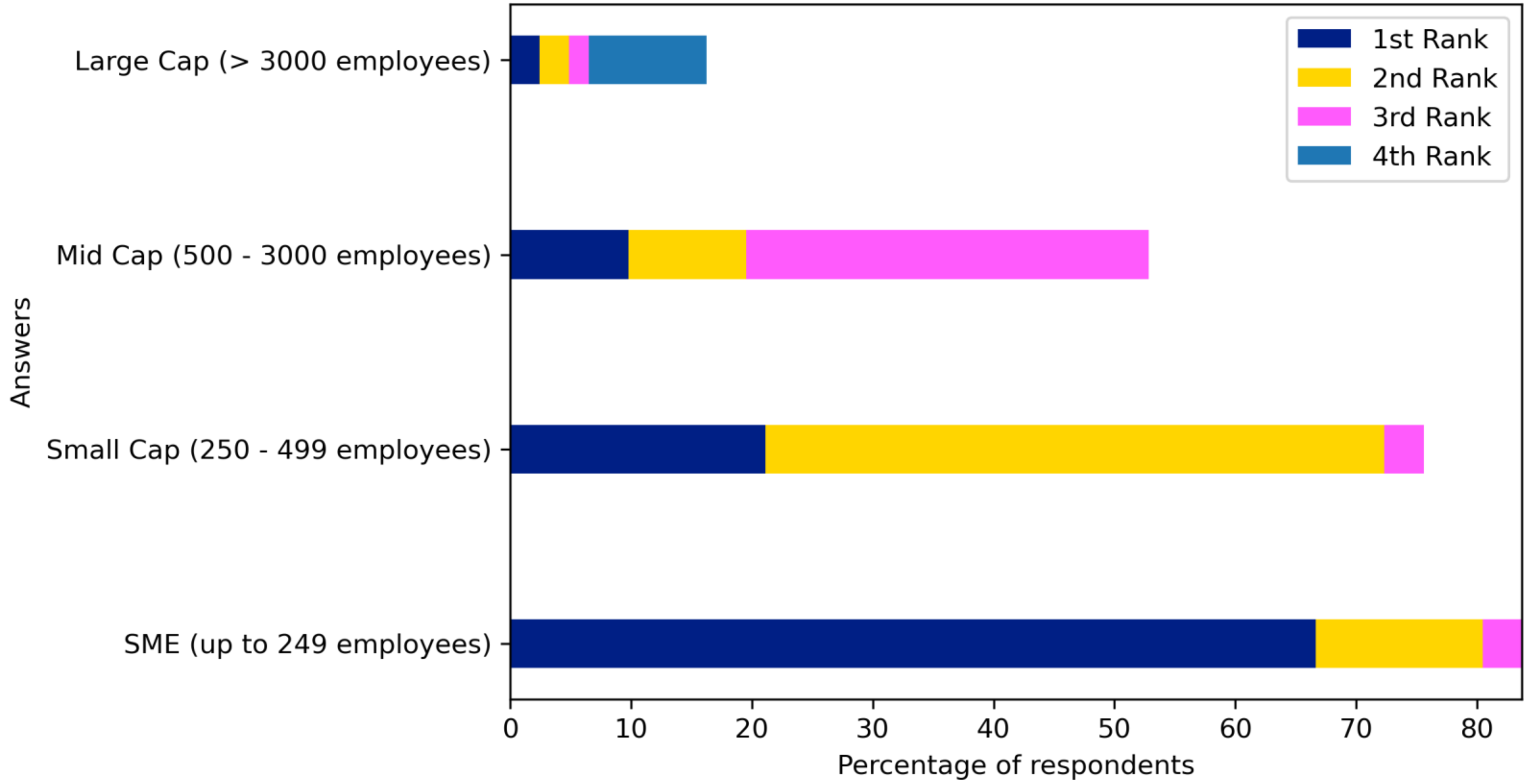
Question: What financial metrics do you use to analyze investments?

Target IRR



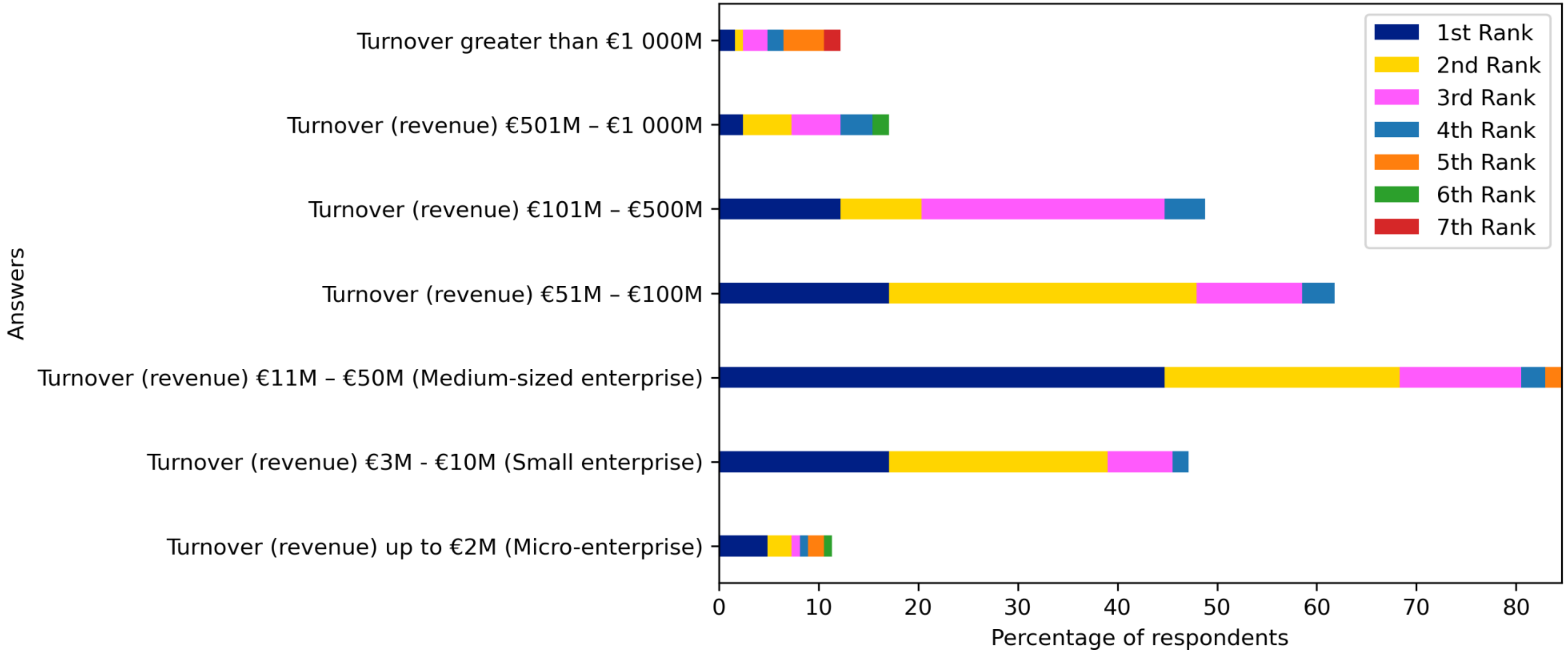
Question: What is your gross target (un)levered IRR in your companies' investments (%)?

Selection: firm characteristics (1/3)



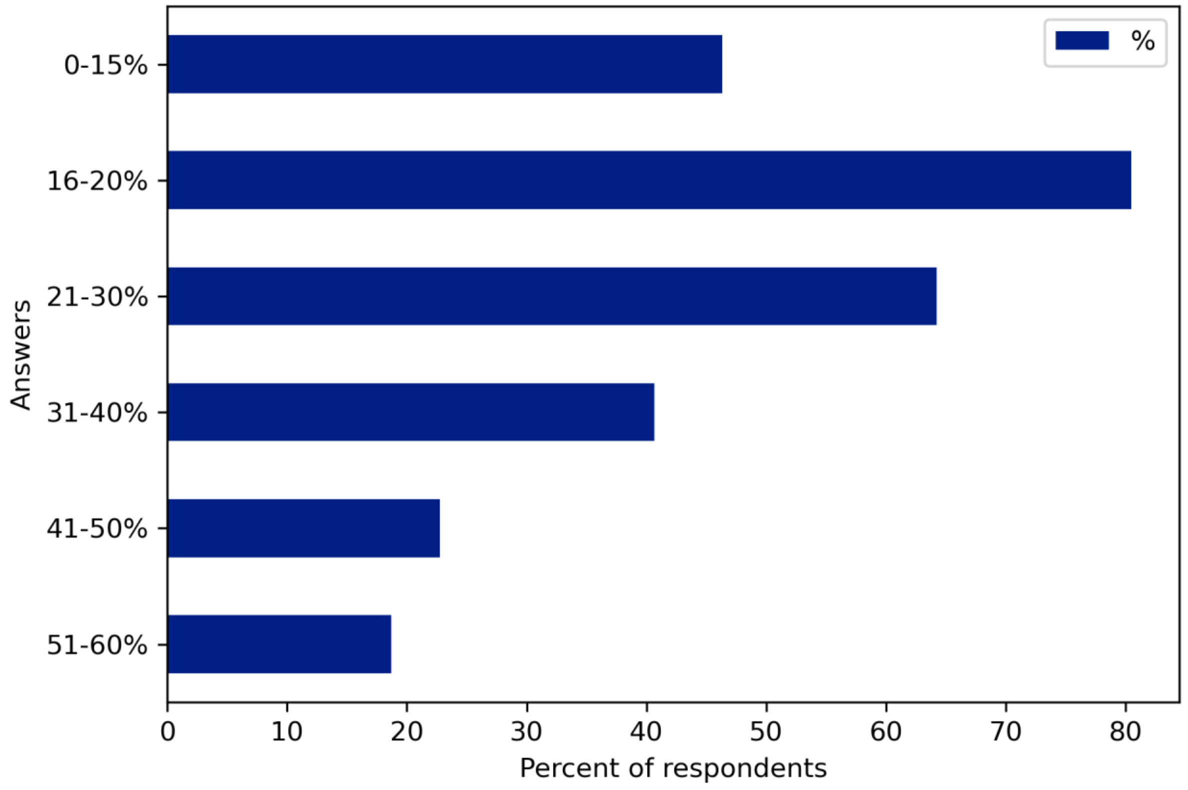
Questions: What are the corporate market segments in which you prefer to invest (enterprise size, by number of employees)?

Selection: firm characteristics (2/3)



Questions: What are the corporate market segments in which you prefer to invest (enterprise size, by turnover)?

Selection: firm characteristics (3/3)



Questions: What are the corporate market segments in which you prefer to invest (enterprise size, by EBIDA-margin)?

Due diligence outsourced?

Outsourcing	N (%)
Other/s	14 (5.22)
No	54 (20.15)
Yes, to accountants	63 (23.51)
Yes, to consultants	66 (24.63)
Yes, to lawyers	71 (26.49)
Number of respondents (responses)	149 (268)

Question: Do you outsource due diligence?

PE-sponsored deals

Importance of PE-sponsored deals

	Mean		Std. dev.		Median		25%		75%	
	Senior PD	Other PD	Senior PD	Other PD	Senior PD	Other PD	Senior PD	Other PD	Senior PD	Other PD
Total invested capital made up of sponsored deals	44.26	33.18	36.21	36.39	40	20	10	0	80	69

Question: What percentage of your total invested capital in (senior) PD is made up of sponsored deals?

Relative performance of PE-sponsored deals

Performance of sponsored deals compared to sponsor-less deals during COVID-19	N (%)
Far worse	5 (3.27)
Somewhat worse	9 (5.88)
Similarly	65 (42.48)
Somewhat better	20 (13.07)
Far better	8 (5.23)
I don't know	46 (30.07)

Question: How did sponsored deals perform compared to sponsor-less deals during the COVID-19 crisis?

Why PE-sponsored deals? (1/2)

Advantages of sponsored deals	**N (%)**
Other/s	25 (7.16)
Stronger recovery upon distress: PE sponsor's past turnaround experience / network of potential rescue lenders / dry powder liquidity	48 (13.75)
Lower monitoring costs: efficient division of monitoring enabled by PE sponsor's active governance role	51 (14.61)
Deal quantity: More opportunities in general due to the high amount of dry powder that PE firms are sitting on	67 (19.20)
Lending relationship: Repeated transactions with the same PE sponsor lowers information cost and provides a stronger pipeline of quality deal flow	67 (19.20)
Deal quality: Signaling based on PE sponsor reputation / track record	91 (26.07)

Question: What are the main advantages of sponsored deals compared to sponsor-less deals?

Why PE-sponsored deals? (2/2)

Synergies between private debt and private equity	**N (%)**
Higher Debt/Assets or Debt/Tangible Assets (i.e. more efficient collateral use)	35 (10.80)
More flexible financial covenants	91 (28.09)
More tailor-made negative covenants for operational flexibility	97 (29.94)
Higher Debt/EBITDA leverage (i.e. higher willingness to lend against cash flow)	101 (31.17)

Question: In your view, what is the greatest synergy that private debt provides to private equity (that banks cannot / can no longer provide)?

Concerns for sponsored deals

Concerns for sponsored deals	N (%)
Increased cash flow volatility from overinvestment	25 (11.21)
Other/s	28 (12.56)
Claim dilution from debt issuance / use of liens (due to the sponsor exerting debt contractual expertise)	38 (17.04)
Higher default probability due to high leverage typical of most buyouts	61 (27.35)
Low bargaining power in enforcing covenant rights (due to high reliance on the sponsor for deal origination)	71 (31.84)

Question: What are the main concerns for sponsored deals compared to sponsor-less deals?

Negative covenants

Negative covenants	Most important items for PD manager	Items that PE sponsors tend to most aggressively negotiate on
	N	N
Incremental debt	1 114	2 74
Liens	54	15
Investments	43	44
Payments	2 100	1 80
M&As and asset sales	91	57
Affiliate transactions	33	15
Prepayment restrictions	3 70	3 59

Question: Among the negative covenants listed below: 1) select those that are most important for you and 2) select those that PE sponsors tend to most aggressively negotiate on: ...

Financial covenants

Financial covenants		Most important items for PD manager		Items that PE sponsors tend to most aggressively negotiate on
		N		N
Debt / Assets or Equity		46		21
Measures of net worth		12		7
Measures of liquidity	2	69		25
Debt / EBITDA	1	118	1	85
Minimum EBITDA		30		14
Debt service / EBITDA		90		35
Lease payments		14		4
Dividend payout		51	2	61
Capital expenditure		47		25
EBITDA definition	3	68	3	59
Equity cure rights		31		50

Question: Among the financial covenants listed below: 1) select those that are most important for you and 2) select those that PE sponsors tend to most aggressively negotiate on …

Private debt versus bank loans

Why not a bank loan? (1/3)

Percentage of portfolio companies that would not be able to get bank financing	N (%)
0	10 (6.54)
1 - 20%	23 (15.03)
21 - 40%	25 (16.34)
41 - 60%	26 (16.99)
61 - 80%	26 (16.99)
81 - 99%	27 (17.65)
100%	16 (10.46)

Question: What percentage of your portfolio companies would not have been able to get bank financing in the absence of your financing?

Why not a bank loan? (2/3)

Reasons for not getting a bank financing	N (%)
Other/s	40 (11.24)
Cash flow is too low or unstable	43 (12.08)
Firms operating in niche sectors	54 (15.17)
Due diligence is messy due to less clean financials or a lack of sophisticated internal systems	65 (18.26)
Firm size is too small for bank syndication	75 (21.07)
Firm has low amount of tangible assets as quality collateral	79 (22.19)
Number of respondents (responses)	143 (356)

Question: Why do you think banks would not want to finance companies that are reliant on private debt?

Why not a bank loan? (3/3)

Reasons for choosing private debt over bank debt	**N (%)**
Did not approach banks due to fear of rejection	10 (1.87)
Other/s	15 (2.81)
Bank loan application was rejected	44 (8.24)
Stable relationship with lender's expectation to hold to maturity (vs bank originate-and-distribute model)	53 (9.93)
Longer investment horizon than banks are willing to support	60 (11.24)
Diversification of financing sources	61 (11.42)
More flexible covenant structure	81 (15.17)
Higher leverage than banks are willing to support	83 (15.54)
Certainty and speed of execution (vs long / uncertain bank syndication process)	127 (23.78)
Number of respondents (responses)	153 (534)

Question: Why do you think firms choose private debt over bank debt?

Post investment activity

Interaction with portfolio company

Frequency of interaction with portfolio companies	N (%)
Multiple times a week	8 (5.4)
Once a week	7 (4.7)
2-3 times a month	43 (28.9)
Once a month	65 (43.6)
Less than once a month	26 (17.4)
Never	0

Question: In the first six months after making an investment, how frequently do you interact with the management of a typical company in your portfolio?

Methods of monitoring

Methods of monitoring portfolio companies	**N (%)**
Other/s	9 (1.4)
Establish acceptable risk limits	41 (6.5)
(Re)grading of risk ratings	44 (7.0)
Conduct periodic stress tests and scenario analysis	55 (8.7)
Measure and monitor identified risks	101 (16)
Covenant checks	126 (19.9)
Updated financial statements	126 (19.9)
Periodic meetings with borrowers	130 (20.6)

Question: How do you monitor portfolio companies?

Distress resolution

Distress resolution	**N (%)**
Simple waiver without material intervention	79 (29.37)
Out-of-court renegotiation	75 (27.88)
Reorganisation regime (like Chapter 11 in the US)	46 (17.10)
Not relevant (no portfolio firm in distress)	45 (16.72)
Liquidation (like Chapter 7 in the US)	16 (5.95)
Other/s	8 (2.97)

Question: For those portfolio firms which are in distress, how is their distress resolved?

Appendix

Board membership

Board representation	N (%)			
	Portfolio company is sponsor-less	**Portfolio company is PE-sponsored or sponsor-less**	**Portfolio company is in distress**	**Portfolio company is in distress or not**
Yes, often and we actively intervene in the day-to-day business of the company	9 (6%)	19 (12%)	45 (29%)	9 (6%)
Yes, often as a passive participant	3 (2%)	26 (17%)	20 (13%)	27 (18%)
Yes, sometimes as an active participant	9 (6%)	20 (13%)	25 (16%)	21 (14%)
Yes, sometimes as a passive participant	20 (13%)	41 (27%)	20 (13%)	33 (22%)

Question: Do you sit on the board (advisory, supervisory, executive or similar committees) of your portfolio companies?

Loan purpose

Loan purpose	N (%)
Expansion	127 (20.85)
Capital expenditure (CAPEX) / Other asset-based financing	112 (18.39)
Buyouts	110 (18.06)
Refinancing / Balance sheet restructuring	87 (14.29)
Working capital	63 (10.34)
Recapitalization	57 (9.36)
Operational Expenditure (OPEX)	42 (6.90)
Other (s)	11 (1.81)
Number of respondents (responses)	153 (609)

Question: What are your main loan purposes?

Loan size and maturity

	Mean	Std. dev.	25%	50%	75%
Target loan size (in Million €)	70.17	148.95	13	13	75.5

Question: What are the total average target loan sizes (in million €), where your fund is investing (including portions of the same loan provided by third parties alongside your fund)?

	Mean	Std. dev.	25%	50%	75%
Loan maturity (in Million €)	5.10	1.96	3	6	6

Question: What is the typical loan maturity (in years), where your fund is investing?

Target IRR

	Mean	Std. dev.	25%	50%	75%
Levered IRR	9.55	3.36	7.5	9.5	13
Unlevered IRR	8.70	3.33	5.5	7.5	13

Question: What is your gross target (un)levered IRR in your companies' investments (%)?

Selection: profitability and firm characteristics

Profitability	Mean	Std. dev.	25%	50%	75%	min	max
ROI (%)	10.64	4.10	7.5	10	13.13	5	20
MOIC	1.38	0.17	1.2	1.4	1.48	1.15	1.7

Question: What is your required gross multiple / return for an investment (%)?

Loan repayment schedule

Repayment schedule	**N (%)**
Amortizing without initial grace period	17 (7.49)
Balloon	35 (15.42)
Amortizing with initial grace period	61 (26.87)
Bullet	114 (50.22)

Question: What is the typical repayment schedule?

Types of debt

Types of debt	N (%)
Term loan	131 (53.25)
Bond	56 (22.76)
Other asset-based lending	42 (17.07)
Revolving credit facility	17 (6.91)
Number of respondents (responses)	153 (246)

Question: Which types of debt do you offer?