PRIVATE EQUITY NEWS

Cross-border financings: what to expect in 2022

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After a resounding 2021, which broke all imaginable deal activity metrics, many in the market are asking familiar questions about what to expect of 2022. Will global insolvency move to the fore as supra-national and government stimulus unwinds? Will deal fatigue impact transactions? Will inflation stem the behemoth credit markets? Or will the vast amount of dry powder across equity and debt markets (and all flavour of products in between) continue to rule strong and drive M&A growth across global markets, pandemic or no pandemic.

Hit the highs

Early indications of 2022 suggest that markets remain very strong with a positive outlook for deal flow and, even if certain indicators do not hit the highs of 2021, we can expect certain themes to drive unprecedented growth in 2022.

One theme we have seen through the market over the past three years, across both sides of the Atlantic, is that size matters. The greater availability of liquidity in both the equity and credit markets has meant increasing capacity to finance deals outside of the syndicated lending market, which has in turn played strongly into the hands of direct lenders.

Even if US rates move as commentators expect in 2022, given that interest rates remain historically low, the net effect on lending markets which impose dollarfloors will be minor. And still, competition to provide financing across verticals and industries has reached a fevered pitch. Indeed, for a number of deals, price is not proving to be the key driver, as evidenced by the resurgence of covenant-lite unitranche deals, particularly in Europe.

We have seen both larger funds being raised and more variety of fund types and structures, allowing a more flexible approach to, and wider availability of, financing at higher amounts and higher multiples. As if there were a need to bolster any funding gaps, we have seen "special situations" monies be deployed efficiently toward new growth investments and private equity LPs seeking opportunities to provide direct co-investment equity.

While size can be key for any individual deal, it is also needed to institutionalise lending relationships in the buy-and-build space – another theme that is strong and will continue to grow in prevalence. We have seen greater sophistication in strategies to identify targets (particularly on a cross-border basis or within verticals) which can add meaningful synergies (and even multipliers), cost-savings and growth potential.

Grow in sophistication

Diligence processes increasingly utilise artificial intelligence and automation to maximise market efficiency, and, if one considers the growing number of players with a proven track record focusing on integration support for management teams and utilising dedicated operating partners, we expect private equity investments to grow in sophistication. Long-term financing needs will need to be addressed at deal inception, even for relationship players and particularly for cross-border structures where choosing one credit market over another may have meaningful cost and operational implications.

Another theme we can expect to continue into 2022 is sectoral growth. While we may expect the energy sector to face difficulties, particularly in light of macroeconomic events, those might be more temporary or localised and may well lead to M&A consolidation and carve-out opportunities.

Conversely, tech and healthcare platforms remain at the forefront of investor confidence. Adjacent businesses, such as education tech, health tech, digital health and tele-health, will continue to receive strong support from the equity and debt markets, particularly given the continued focus on balancing working arrangements with personal priorities and the scientific advances that drive retail and wholesale results.

Finally, pre-Ebitda/revenue financings will undoubtedly attract significant attention and competition among investors, in light of the pure growth potential, which is very likely to be heightened by cross-border buy-and-build opportunities and synergies with established platforms.

As such, there are no early indicators that we are at a distinct crossroads in the cross-border financing markets. There are clear efficiencies that did not exist 10 years ago, and we have withstood a global pandemic, global geopolitical issues such as Brexit and global political changes which many thought it would be highly destructive towards the financing markets.

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Weather the storm

Those impediments may not yet have reached conclusion, but their darkest days appear to be behind us. There will undoubtedly be more challenges to overcome, but our cross-border financing markets seem well placed to weather those storms.

We can therefore expect confidence to continue, even if there are periods where deal volume does not quite reach the unique 2021 levels that exceeded the expectations of even the most bullish of market participants. While markets at all levels of the capital structure are particularly focused on growth, they must accept that a continuation, or even a reduction, of 2021 levels might properly yield higher than pre-pandemic activity levels.

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