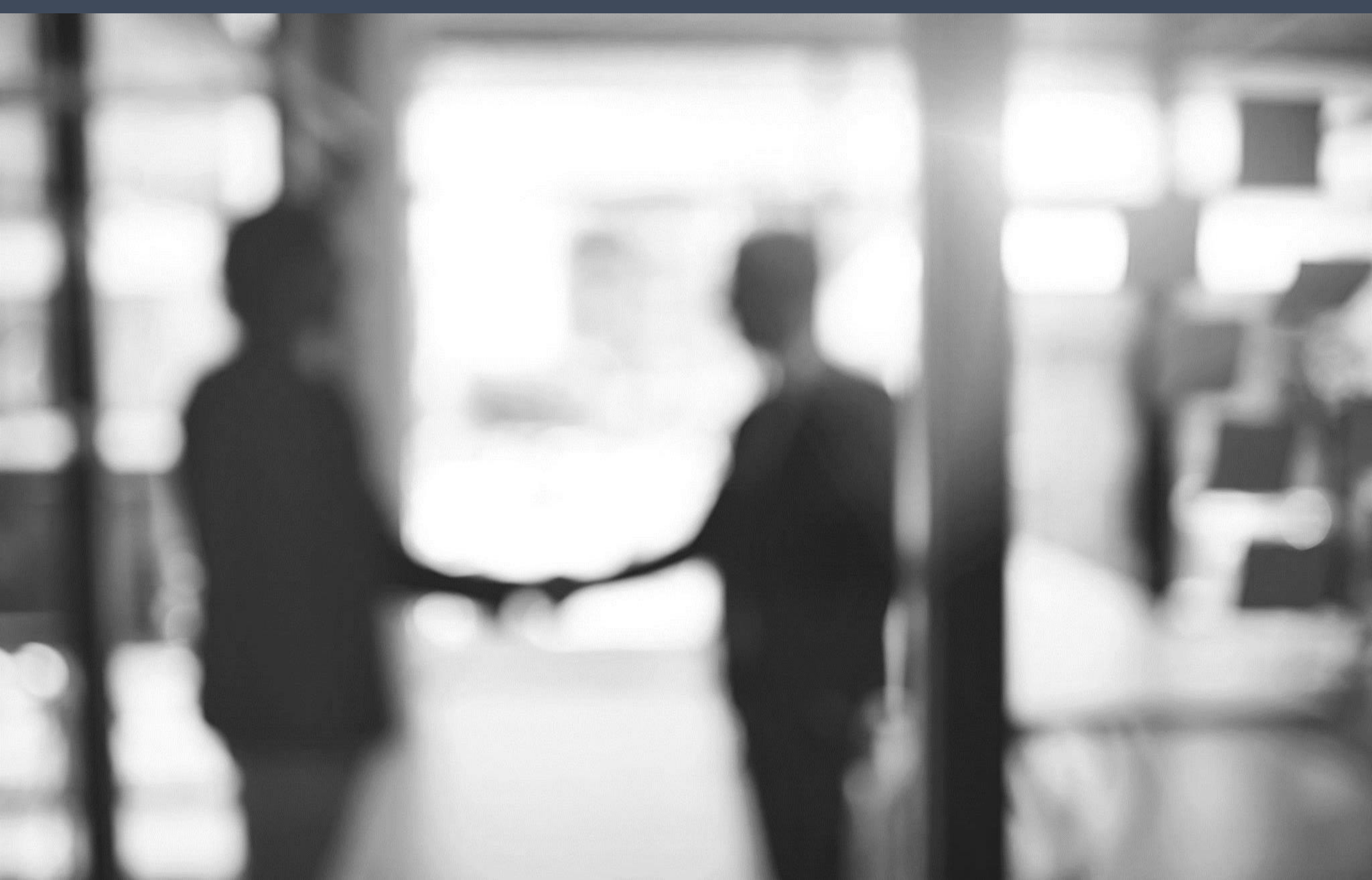
gamBIT
CORPORATE FINANCE

Debt Capital Markets

Gambit Review

February 2024



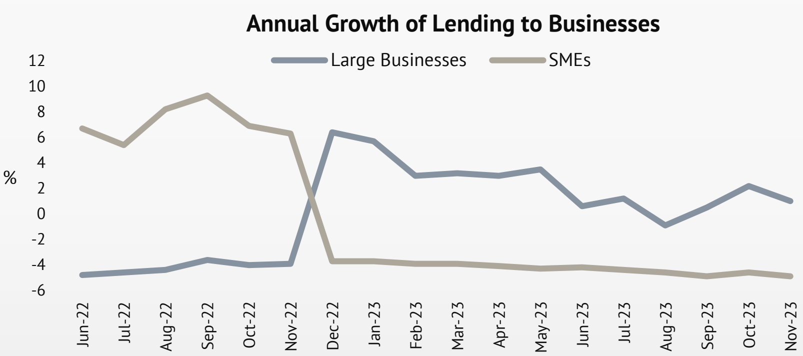
Executive Summary

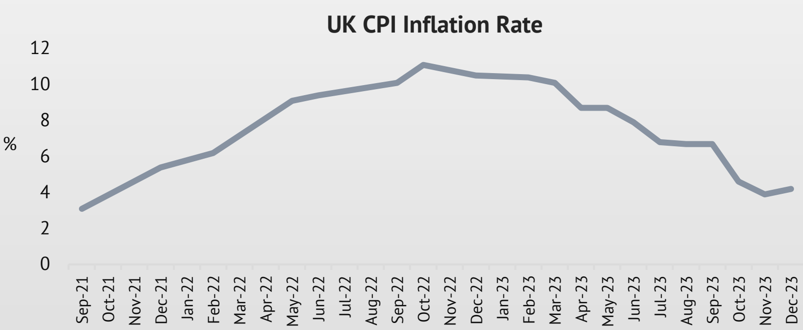
gamBIT CORPORATE FINANCE

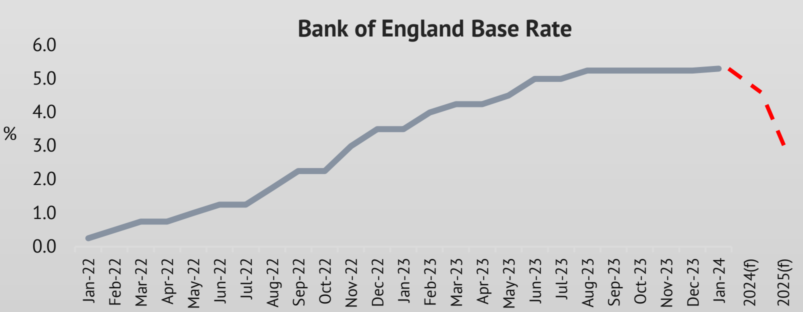
Jason Evans
Partner, Debt Advisory

Jason Evans is the partner that leads Gambit's Debt Advisory team. Prior to joining Gambit, Jason was Regional Director for Lloyds Banking Group, heading up the regional corporate banking team in the mid-market and working with businesses with turnover between £10m and £750m. During his 32-year career, Jason has held various senior roles, including Divisional Head of Leveraged Finance for HSBC.

He is an Associate of the Securities and Investment Institute, holding an advanced corporate finance qualification from the Institute of Chartered Accountants in England and Wales (ICAEW). Jason has also been voted "Corporate Banker of the Year" on a number of occasions at the Insider Dealmaker Awards and more recently has won a number of debt advisory awards.



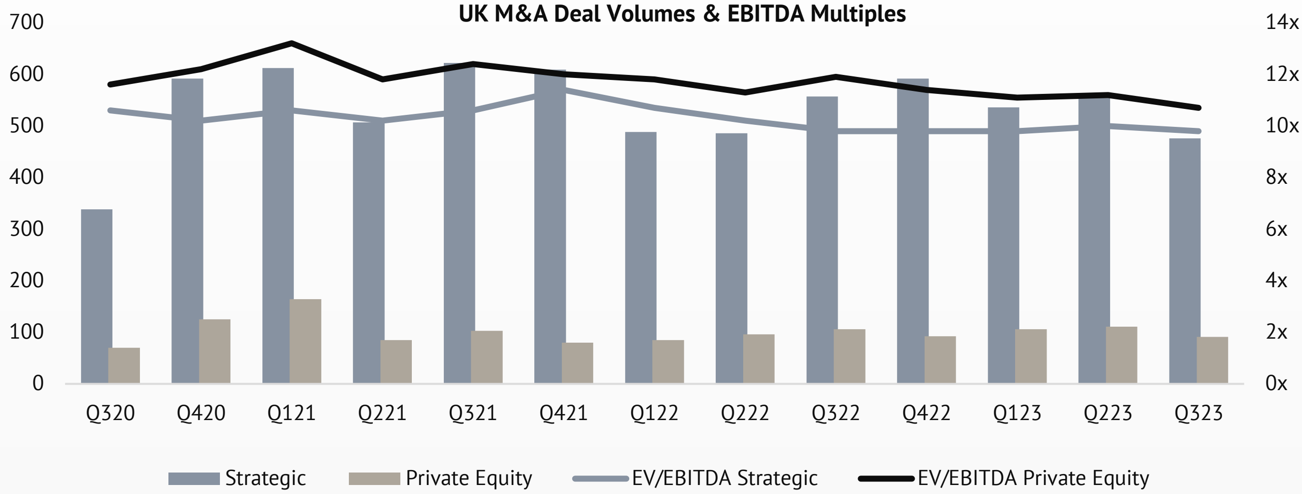




Source: Gambit analysis, Bank of England and ONS

- As dynamic geopolitical conditions and a restrictive credit environment remain, with the average cost of new borrowing increasing from an effective rate of 6.9% in October 2023 to 7.0% in November 2023, the growth rate of borrowing to SMEs further contracted to -4.9% in November 2023.
- Financial institutions continue to dictate the terms, scrutinising covenant headroom, challenging sensitivity scenarios and focusing on EBITDA 'add-backs'.
- Even with higher interest expenses impacting the leverage profiles of businesses, there is optimism that the global outlook is improving with inflationary pressures softening.
- Despite a 0.1% uptick in December 2023, there has been a clear downward trajectory in the cost of capital as inflation has fallen from a peak of 11.1% in September 2023 to 4.2% in December 2023.
- As a result, the Bank of England has held base rates at 5.25% since August 2023 and Capital Economics forecasts that base rates will soften to 4.75% in 2024 and 3% in 2025.
- In this current climate, it is essential for borrowers to leverage the expertise of experienced corporate finance advisors to be well-prepared for discussions with financial institutions.

M&A & Credit Markets



Overview & Outlook

- M&A deal volumes decreased by 15% from Q223 to Q323, with the number of executed transactions softening from 670 to 576.
- This downturn in M&A transaction volumes and values is largely attributable to the macroeconomic landscape and turbulence of public markets and the dynamics of larger, 'jumbo' transactions.
- The UK M&A mid-market remains resilient, with deal volumes higher than the ten-year average and volumes and values in line with pre-pandemic levels despite the significantly higher cost of capital environment compared to 2019.
- Product diversification and transformative tech continue to drive M&A activity as firms look to spread risks in an uncertain macroeconomic environment and further digitalise operations to remain competitive.
- As inflationary expectations soften, cost of capital is anticipated to improve and with a General Election looming, we forecast an uptick in M&A transaction volumes in 2024.
- Leveraging the expertise of a knowledgeable debt advisor to support a quality proposal to present to the most relevant funder audience, is key to achieving a successful fundraise in this dynamic market.

Valuation Multiples

- Strategic and private equity EV/EBITDA valuations proved resilient despite historically high levels of cost of capital, remaining above 9.8x for the whole of 2023.
- Well-capitalised consolidators in the UK mid-market are continuing to execute transactions, paying premiums for quality assets characterised by high scability, low capital intensity, disruptive potential and high-income visibility.
- Given the improving economic outlook and given private equity consolidators being eager to deploy their $2.5bn of accumulated 'dry powder', we expect an uplift in EV/EBITDA valuations in 2024.

Source: Gambit analysis, ONS and S&P

Debt Market Trends

Leveraged Finance

- $70bn of leveraged loans were issued in Q323, the highest quarterly issuance since Q122, particularly underpinned by buy-out and acquisition-related financing transactions, as both borrowers and lenders have become optimistic about the macroeconomic outlook and central bank rate cuts.

- As leveraged loan issuance exhibited an uptick in Q323, pricing spreads softened and borrowers took advantage of the 'window of opportunity' to undertake refinancings, dividend recaps and 'amend-to-extend' transactions.

- We expect that issuance volumes of leveraged loans will continue to increase in 2024, particularly accelerated by private credit firms facilitating refinancings and extensions for borrowers addressing upcoming maturities.

Typical Pricing Spreads

	Senior Cash Flow	Unitranche	Subordinated
Jan-24	4.50% - 6.50%	6.50% - 8.75%	10.25% - 13.50%
Dec-23	4.75% - 6.75%	6.75% - 9.00%	10.50% - 13.50%
Jan-23	4.75% - 7.00%	7.00% - 9.25%	10.50% - 13.50%

- The firmer credit environment induced by the Bank of England's 'hiking cycle' has increased pricing spreads across a broad range of lending products since H222.

- Pricing spreads have eased a little in comparison to Q123 but remain historically inflated, suggesting that the UK continues to be a 'lenders' market', with funders dictating terms, scrutinising covenant headroom, modelling sensitivity analysis and focusing on EBITDA 'add-backs'.

- However, despite the macroeconomic uncertainty which pervaded H123, inflation is gradually receding and there is a widespread consensus that the Bank of England base rate may have peaked in September 2023.

- In this more challenging fundraising environment, leveraging the expertise of a knowledgeable debt advisor to support a quality proposal to the most relevant funder audience will be key in achieving an optimal outcome.

Source: Bank of England, Weil and Gambit analysis

Alternative Credit Options

Private Credit

- Given significant increases in the cost of capital during the first half of 2023, private credit deployment slowed, however, with improving economic sentiment deal flow has returned (and particularly lower mid-market), albeit with increased emphasis on quality of earnings and due diligence.

- Whilst private credit continues to be a key debt source for mid-market M&A activity, mainstream banks have reengaged, albeit generally with less complex lower leverage/risk structures in transactions.

- Private credit firms are prioritising lending to companies in non-cyclical sectors such as healthcare and technology, characterised by strong recurring revenue flows, diverse customer bases with low levels of churn and significant prospects for future growth. Indeed, for such opportunities, there is a very healthy debt appetite to be found.

- The private credit market is poised for significant growth, particularly underpinned by refinancing mandates as $1.4tr of leveraged loans are set to mature over the next two years.

- With many financial institutions having been cautious to deploy funds in 2023, there will be heightened pressure to put capital to use in 2024.

Asset Based Lending (ABL)

- ABL is business funding that is secured by assets such as accounts receivable, inventory, equipment or property, rather than being secured by future cash flows.

- Agreements can have fewer restrictions than cash flow loans, including less stringent eligibility criteria, fewer restrictions on the use of funds and limited financial covenants.

- ABL is an alternative credit option that has seen significant growth in recent years. Growth has particularly accelerated since 2020, with committed ABL volumes reaching record highs of $900bn in 2022, as ABL houses have been able to 'fill the gap' in place of traditional banks that have adopted stricter lender practices since the pandemic-induced economic downturn.

- Over the next decade, the ABL market is expected to experience sustainable growth of 5% - 7% per year. Forecast growth in ABL lending is underpinned by:

  - Loans being secured against a more diverse collateral base, with more 'exotic' assets such as intellectual property now featuring.

  - A larger number of sector specialist lenders with heightened expertise and understanding of the risk profiles of their respective fields.

  - The relatively low cost of capital seen with ABL solutions, potentially augmented with subordinated debt.

Source: Gambit analysis, Weil, Pitchbook

Gambit Corporate Finance

gamBIT CORPORATE FINANCE

Jason Evans

Partner, Debt Advisory

Office:	+44 (0) 845 643 5500
Mobile:	+44 (0) 772 544 6741
Email:	jason.evans@gambitcf.com

Harrie Thorrington

Manager, Debt Advisory

Office:	+44 (0) 845 643 5500
Email:	harrie.thorrington@gambitcf.com

Oscar Webb

Analyst, Debt Advisory

Office:	+44 (0) 845 643 5500
Email:	oscar.webb@gambitcf.com

Gambit Corporate Finance acted as lead advisor to veezu. on its refinancing from Santander TRESMARES CAPITAL — gamBIT CORPORATE FINANCE

Gambit Corporate Finance provided strategic advice to the **British and Irish Lions** — gamBIT CORPORATE FINANCE

Gambit Corporate Finance acted as lead advisor to SPECTRA Group on its fundraising from NatWest — gamBIT CORPORATE FINANCE

Gambit Corporate Finance acted as lead advisor to THE RIDER FIRM.CC on its fundraising from Santander — gamBIT CORPORATE FINANCE

Gambit Corporate Finance acted as lead advisor to CREO MEDICAL on raising debt facilities from BARCLAYS — gamBIT CORPORATE FINANCE

Gambit Corporate Finance acted as lead advisor to the management of outsource on its management buy-out with funding from Close Brothers — gamBIT CORPORATE FINANCE

Gambit Corporate Finance

Established in 1992, Gambit Corporate Finance is an independent corporate finance boutique specialising in advising private and public organisations on mid-market transactions in the UK and overseas. With offices in London and Cardiff, Gambit is widely recognised as a market leader in corporate finance advice having built up detailed industry knowledge and an enviable track record in deal origination and execution.

www.gambitcf.com

Corporate Finance International

Gambit is the exclusive UK shareholder of CFI, a global partnership of mid-market investment banks and corporate finance advisory firms. With over 250 professionals located in 30 offices throughout the world, CFI members specialise in cross-border acquisitions, disposals, capital raising, and related services. CFI is Ranked number 17 in Europe and number 25 globally by Thomson Reuters for transactions valued up to €200m.

www.thecfigroup.com