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Birds-Eye View on Private Debt Markets

Q1 2022

Private Debt is an important and growing segment of financial markets for institutional investors. Prime Capital's quarterly Birds-Eye View on Private Debt Markets aims to provide a concise assessment of market trends and pricings, which due to their private nature, are necessarily less transparent than public fixed income. We hope this publication will be helpful to investors in Private Debt.

We estimate current spreads based on the wide range of transactions we observe in **our** course of business. Due to heterogeneity of obligors, credit qualities, structural features, security packages, etc. a certain level of abstraction and significant degree of judgement is required to arrive at estimates, which, as such, reflect a good deal of expert opinion. It is also to reflect this heterogeneity that we report spread ranges rather than point estimates. In addition, we put current spreads in historical perspective, based on our past estimates, as well as provide projections of future spread developments. These projections, enriched by Prime Capital's Private Debt Portfolio Management team's qualitative assessments, provide the basis for our Tactical Portfolio Allocation, which is reported at the end of the document. The Market Trends section both reports significant events and serves as a basis for the qualitative assessment.

Pricing[1]

	Current Spread	LTM[2]	NTMe[3]
Senior Infra Debt	180 – 330 bps	●●●○○	●●●●○
Junior Infra Debt	425 – 700 bps	●●●●○	●●●●○
Mortgage Debt	100 – 200 bps	●●●●○	●●●●○
Senior Real Estate Debt	140 – 300 bps	●●●○○	●●●●○
Whole Loan Real Estate Debt	450 – 650 bps	●●●○○	●●●○○
Mezzanine Real Estate Debt	650 – 1,500 bps	●●●○○	●●●○○
Senior Corporate Debt	300 – 425 bps	●●●○○	●●●○○
Senior Government Risk Related Transport Debt	200 – 300 bps	●●●●○	●●○○○
Senior Commercial Transport Debt	250 – 375 bps	●●●○○	●●○○○
Mezzanine Transport Debt	500 – 700 bps	●●●●○	●●●●○

Figure 1: Pricing of selected Private Debt asset classes

Source: Prime Capital Research

Strong increase in spread ●●●●●
Strong decrease in spread ●○○○○

[1] **Pricing Methodology:**
The assessment of asset class pricing of the last and next twelve months is represented by the traffic-light system and based on Prime Capitals opinion and ranges from 0 to 5, where 0 indicates a strong decrease and 5 indicates a strong increase of spreads. A value of 3 indicates stable market spreads.
[2] Last twelve months
[3] Next twelve months expectation

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Market Trends

- Total Real Estate Volume in Germany has exceeded EUR 100bn in 2021 which is up by more than 30% compared to 2020. The German Top 7 cities accounted for approximately two thirds with a total transaction volume of over EUR 70bn. Office and residential investments represented c. 70% of the total investment volume, followed by Logistics, Retail and mixed-use assets.
- Despite continuous risks due to global political and economic developments, prime yields continued to decline in Q4 2021, especially for Food-anchored Retail properties, with yields falling by 40 bps compared to Q4 2020. This is mostly caused by increased prices in the asset class. Similarly, Logistic properties have proven to be value winners of 2021 with yields being 35 bps lower than yields in Q4 2020. However, premium Office properties continue to be the most expensive products, with yields decreasing to 2.64% across German Top 7 cities.
- In 2021, over 40% of investments in the European Commercial Real Estate market stemmed from foreign investors, largely driven by European and US investors, accounting for 43% and 31% of cross-border investments, respectively. Investments from Asia seem to be still impacted by the pandemic. While they accounted for 20% of cross-border investments back in 2019, Asian Pacific investors stood at only 8% and Middle Eastern investors at only 4% of cross-border investments in 2021.
- The deal volume in the global infrastructure market continued its strong development in Q4 2021 and surpassed the USD 900bn threshold in FY 2021. With a deal volume of USD 923bn in total, FY 2021 stands massive 22% higher than pre-pandemic levels of FY 2019. Whilst the sectors Energy, Renewables and Transport still make up two thirds of total transaction volume, the Telecommunication sector shows continuously increasing activity, especially in the European markets. In line with overall transaction volume compared to pre-Covid-19 levels in 2019, debt financing increased by c. 20% with 56% of deal value financed. As in previous quarters, classical bank financing remains as primary source for debt for about 80% of total infrastructure debt volume.
- In Europe, value can still be found in telecommunication projects, with a significant share of 23% of the market being allocated towards this sector in FY 2021. The macro trend of digitalization has materialized in the infrastructure market, with the market share in Telecoms increasing from 11% in 2019 to before mentioned levels in 2021. Whilst the market has been mainly dominated by greenfield projects in the previous years (e.g. fibre roll-out and Data Centers), an increasing number of refinancings is currently coming to market. This provides for an interesting market opportunity for institutional investors, especially with regards to risk mitigation as well as capital deployment.
- During the fourth quarter and the year 2021 overall, air-travel recovery continued gradually despite disruptions from the Delta and Omicron variant. In the absence of Omicron, results would have probably been even stronger and bookings for near-future travel less impacted during the last quarter of 2021. According to IATA, industry-wide revenue passenger-kilometers (RPKs), an indicator of global passenger demand, were 45% below pre-crisis levels of December 2019, while available seat-kilometers (ASKs) recorded a 38% decline compared to 2019.
- Aircraft leasing companies have shown resilience, with a market share of 50% (vs. owned aircraft) and making up 60% of new aircraft deliveries in 2021. This is further emphasized as the last quarter of 2021 has marked one of the busiest quarters within the last three years in terms of lessor capital markets activity, with an issuance of USD 24.5 bn. It has to be noted though that the majority of volume is attributed to AerCaps issuance of USD 21 bn, in order to fund the Gecas acquisition.

Tactical Portfolio Allocation[4]

- Our Tactical Portfolio Allocation model currently covers seven Private Debt asset classes across different seniorities.
- In Q1 2022, the strongest asset class is Transportation Mezzanine and Infrastructure Senior. The asset class with the lowest score is Real Estate Senior.

[4] **Tactical Portfolio Allocation Methodology:**
The asset class specific grades describe the asset class specific investment environment relative to historic observations.
Grades range from 0 to 5, where 0 indicates that the current investment environment compares to the worst observed historic outcomes and a value of 5 indicates a historically attractive investment environment. A value of 3 indicates historic medians.
Grades are derived from 5 sub-categories:
Macroeconomic survey data, financial market variables, liquid benchmark proxies, pipeline and expert opinion.
Each sub-category is comprised of several variables. For each variable we define a grade based on the comparison of current realization versus percentiles of historic distribution of this variable. E.g. the PCAG illiquidity premium in December 2021 amounts to 121bps, between the 25th and 35th percentile of the historic spread distribution, and is associated with grade 2. To obtain grades associated with the 5 sub-categories, we take the average across all individual variable grades associated with the respective category. The final grade is the average of the 5 sub-categories.

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- Compared to Q4 2021, overall macro scores decreased in Q1 2022 driven by falling consumer confidence and overall worsening sentiment. Lower financial scores are mainly driven by falling macro risk appetite and declining illiquidity premiums, whereas expert opinion generally improved.
- Generally speaking, scores for Junior/ Mezzanine financing tended to improve, while Senior scores moved more heterogeneous, with improvement in Infrastructure, but declines in Transportation and Real Estate.
- While the overall score for Transportation Mezzanine remains strong in the new year, securing the first rank among our observed sectors again, the score for Transportation Senior decreases. This shift is mostly due to the very strong increase on the liquid benchmark rating for the Mezzanine tranche, in combination with a decreasing score in expert opinion for the Senior tranche.
- In Real Estate Debt the Mezzanine score in Q1 2022 surpasses the Senior score again, which fell back to its Q3 2021 scoring, after temporarily ranking higher than the Mezzanine tranche in Q4 2021. This is, similarly as for the Transportation sector, based on the significant increase on the liquid benchmark rating, as well as an improved expert opinion for Mezzanine. Meanwhile decreasing scores for pipeline and expert opinion for the Senior tranche support this observation.
- Infrastructure Debt shows continuous improvements again in both, Senior and Junior debt. Although financial market scores continue to decrease in both Infrastructure tranches, the remaining sub-categories remain on an equal or improved rating compared to Q4 2021. The only exception can be seen in liquid benchmarks ratings, with a slight decrease for Infrastructure Senior financing.
- The score for Corporate Direct Lending shows a slight increase, mostly due to the improved liquid benchmark development. Expert assessments remain above the historic average, which could indicate a market with interesting targets if you are selective.

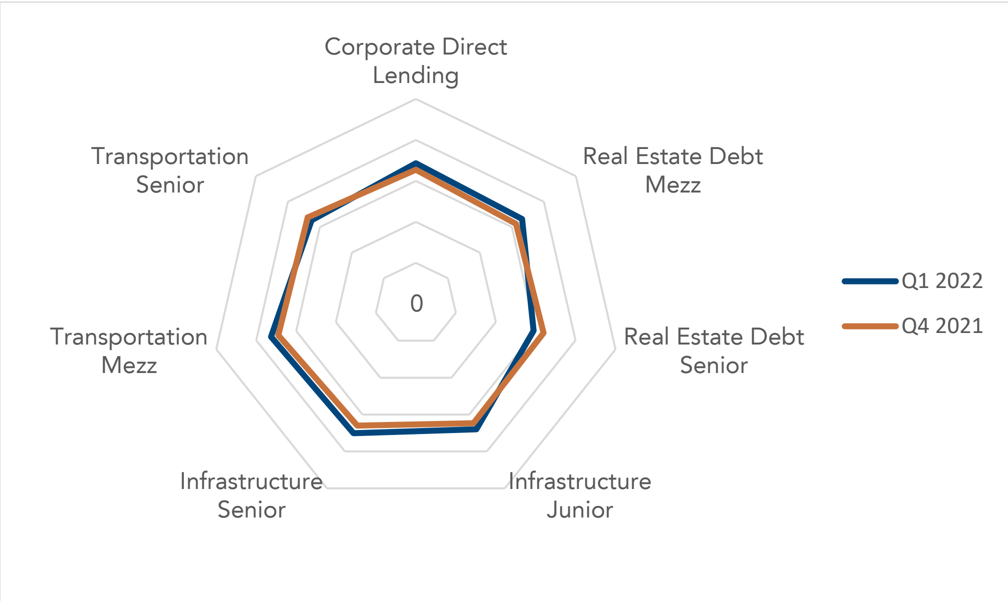

Figure 2: Assessment of selected Private Debt asset classes
Source: Prime Capital Research

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About Prime Capital's Private Debt Team

Prime Capital's Private Debt Team manages in excess of EUR 2bn across asset classes for institutional investors. The Team invests in Infrastructure Debt, Real Estate Debt, Transport Debt and Corporate Lending. We expect significant further asset growth in these areas, while providing satisfactory risk adjusted returns to our predominantly institutional investors.

Further information about Prime Capital AG can be found at www.primecapital-ag.com

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Prime Capital Private Debt Expertise

> Investment and Portfolio Management, advice and support for direct investments, portfolio strategy and sector allocation

> Managed accounts and funds with investment expertise in various jurisdictions and markets

> Unique "multi-channel sourcing" with access to transactions via direct lending, bank and advisor sourcing on the basis of longstanding relationships to market leading sponsors, equity funds and banks

> Independent Risk Management function to improve sustainable investor yield

> Investments in Senior and Junior/ Mezzanine debt, global as well as local investment strategies

> Holistic integration of ESG risks in the investment process

> Specific ESG related strategies

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