Birds-Eye View on Private Debt Markets

Q2 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 Infrastructure Debt	180 – 350 bps	●●●○○	●●●●○
Junior Infrastructure Debt	425 – 750 bps	●●●●○	●●●●○
Mortgage Debt	100 – 200 bps	●●●○○	●●●●○
Senior Real Estate Debt	140 – 330 bps	●●●●○	●●●●○
Whole Loan Real Estate Debt	475 – 675 bps	●●●●○	●●●●○
Mezzanine Real Estate Debt	675 – 1,525 bps	●●●●○	●●●●○
Senior Corporate Debt	275 – 400 bps	●●●○○	●●●○○
Senior Government Risk Related Transport Debt	175 – 280 bps	●●●●○	●●○○○
Senior Commercial Transport Debt	225 – 350 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

- The Real Estate sector again remained strong in Q1 2022. Although the world is still being influenced by more than one crisis at the same time, this was not yet reflected on the German Real Estate investment market in Q1 2022 with a dynamic transaction volume of EUR 24bn. This is an increase of +43% compared to Q1 2021. Investors invested almost 50% of the quarterly result in German office properties in the first quarter and about half of the total transaction volume falls to the Top 7 cities.
- The turnaround in interest rates, which led to higher financing costs, is thereby not reflected in the Real Estate market or has already been priced in or overlaid by other developments. In addition, historically speaking, valuation of Real Estate properties shows a higher correlation to real interest rates rather than nominal interest rates[4]. In the logistics sector, the average prime yield across the regions fell by a further seven bps to 2.96%, while city centre commercial properties remain unchanged at 2.91%. In contrast, office properties in the Top 7 German cities are slightly more expensive at 2.62% yield.
- The European Real Estate investment volumes posted the second strongest Q1 ever. In terms of Q1 2022 performance, the highlights were the institutional capital's focus on the European Real Estate market and the record levels of investment recorded in the industrial sector: Norway (+993%), Spain (+402%), Germany (+112%), Italy (+93%), the Netherlands (+15%) and the UK (+13%) all reported first quarter highs.
- The transaction volume of global Infrastructure and energy transactions stood at USD 235bn at the end of the first quarter of 2022, up from USD 156bn during the same period one year prior. The increase in transaction volume was realized despite a drop in the number of transactions from 672 in Q1 2021 to 637 in Q1 2022. Sector wise, telecommunications was the best performing segment in the first quarter with transactions totaling at USD 55bn, almost quadrupling transaction activity compared to Q1 2021 and reaching a market share of 23%. Similarly, transport displayed a strong start to the year with total transaction volume reaching USD 53bn (YoY: +231%) and a market share of 23% in Q1 2022. Debt markets have remained robust during the first quarter of 2022 with debt volume reaching USD 104bn for the period (YoY: +7.2%).
- In Europe, the Infrastructure market demonstrated a strong start to the year, featuring 306 Infrastructure transactions in Q1 2022 with a total volume of USD 76bn. This compares to 288 transactions with a total volume of USD 54bn in Q1 2021, constituting an increase of +6% and +30% in deal count and transaction volume, respectively. The continuing trend of decarbonization and digitalization kept the deal flow high, despite of geopolitical turbulences. High investment and capital needs offer investors interesting market opportunities, especially in the Unitranche and Junior financing market with developers and sponsors facing the everlasting field of tension between active pipeline and limited capital to develop their various projects.
- The Aviation sector continued to recover with industry-wide revenue passenger kilometres (RPKs) increasing by 76% (YoY) compared to March 2021 and up 2.8% versus February 2022. In terms of capacity available seat kilometres (ASKs) grew 46% (YoY). The significant recovery of international air traffic is apparent looking at the isolated figures compared to March 2021. RPKs grew by 285% for international flights in March 2022 and APKs by 132%.
- The impact from the war in Ukraine on air travel remains very limited overall. Even travel within Europe as well as travel between Asia and Europe remains strong. The closure of the Ukrainian airspace, accounts only for roughly 3.3% of total air passenger traffic in Europe, and for 0.8% of total traffic globally, as per 2021 according to IATA.

[4] For further information we can provide a more detailed presentation on the influence of changing interest rates in Real Estate Debt.

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Tactical Portfolio Allocation[5]

- Our Tactical Portfolio Allocation model currently covers seven Private Debt asset classes across different seniorities.
- Similarly to Q1 2022, the strongest asset classes in Q2 2022 are Transportation Mezzanine and overall Infrastructure Debt. The asset class with the lowest score is Transportation Senior.
- Although macro liquidity scores increased during this quarter, overall macro scores decreased further in Q2 2022 due to significantly lower consumer confidence. However, our expert opinion in Terms of Deal Quality, Pricing and Strategic Attractiveness generally improved.
- The continuous decline in financial scores is mainly driven by the historically low illiquidity premiums, slightly compensated by rising risk appetite. The increase in liquid benchmarks indicates a higher credit risk, which is balanced by more attractive liquid spreads.
- The score for Transportation Mezzanine continues to rank among the first places among our observed sectors, whereas Transportation Senior scores continue to deteriorate for the second quarter in a row. This shift is mostly due to the scores for expert opinion, which remained strong for the Mezzanine tranche, but declined for the Senior tranche.
- In the Real Estate Debt sector, the Senior score catches up to the Mezzanine tranche. This is due to the changes in the expert opinion. While the rating slightly declined for Real Estate Mezzanine, a significant improvement in Real Estate Senior scores could be observed.
- Overall Infrastructure Debt scores remain steady compared to Q1 2022. The Senior Score is mostly influenced by the strong increase in liquid spreads, in combination with a less substantial decrease in credit risk compared to Infrastructure Mezzanine and other asset classes. The Mezzanine score benefits from the increased expert opinion.
- The score for Corporate Direct Lending shows a slight decrease, mostly due to the lower consumer confidence in addition to the drop in the liquid benchmark development.

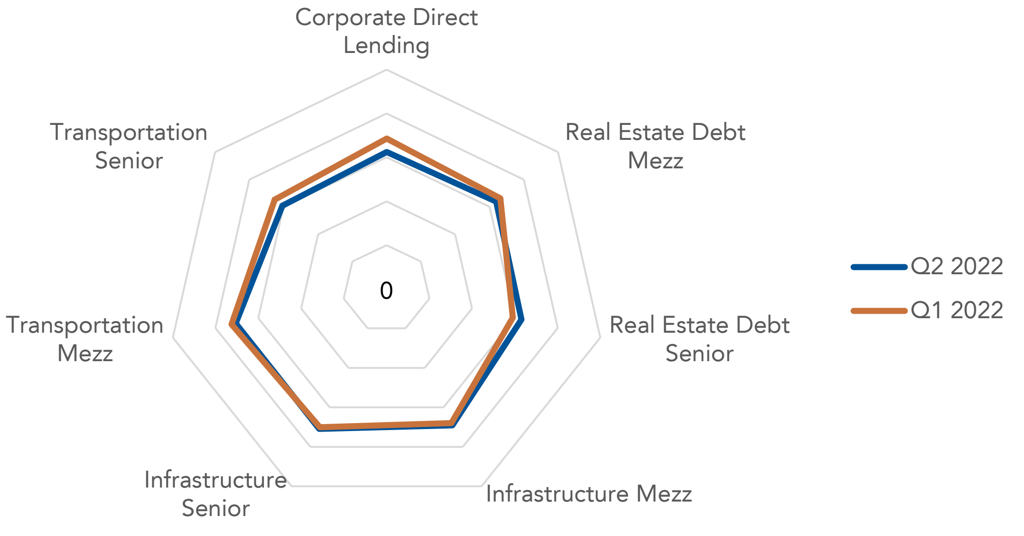

Figure 2: Assessment of selected Private Debt asset classes
Source: Prime Capital Research

[5] **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 March 2022 amounts to 100bps, below the 15th percentile of the historic spread distribution, and is associated with grade 1. 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.

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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