Non-Bank Lending Market Perspective Q3 2020

Understanding the Alternative Lending Landscape

CEREBRO CAPITAL

TABLE OF CONTENTS

CITATIONS:

Butler, Kelsey. “How Private Credit Soared to Fuel Private Equity Boom.” Bloomberg.com, Bloomberg, 2019, www.bloomberg.com/news/articles/2019-09-22/how-private-credit-soared-to-fuel-private-equity-boom-quicktake

Federal Reserve Senior Loan Officer Survey, October 2020 https://www.federalreserve.gov/data/sloos/sloos-202010.htm

WHY ARE NON-BANKS IMPORTANT?

Non-bank lenders have existed for decades but were typically considered a last resort option for companies on the brink of failure. However, in the decade following the financial crisis, middle-market CFOs, business owners, and financial sponsors have been turning to non-bank lenders as a viable lending solution.

What caused the demand shift?

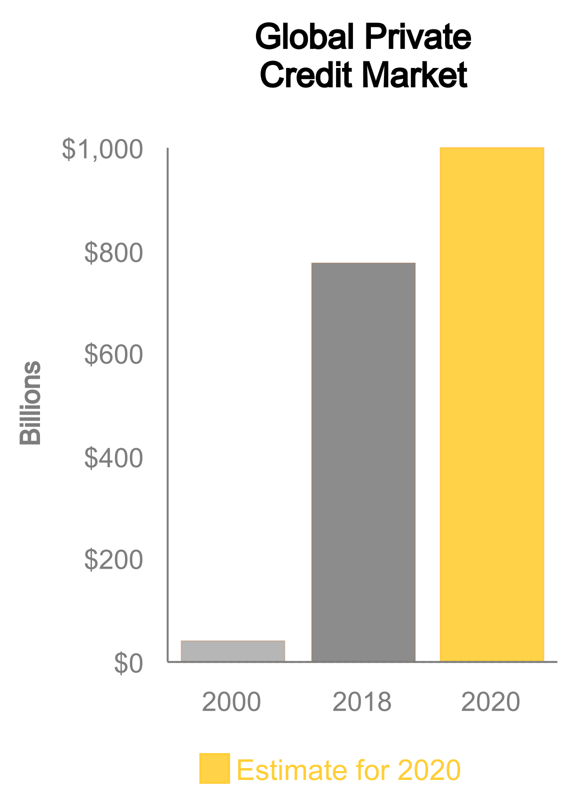
After the financial crisis abated, traditional banks faced increased regulatory scrutiny that resulted in tighter lending criteria. Credit committees declined more borrowers and reduced lending limits. Gone were the days when a long standing relationship could tip the scales for companies who were just outside the bank lending criteria. Many mid-market companies that were still performing well were left asking where to turn. Over the past decade, the vacuum created in the market was filled by a proliferation of non-bank lending. With an ability to provide credit in structures and amounts that traditional banks could not, these lenders experienced strong demand from well-performing firms willing to pay higher interest rates to ensure access to capital.

What helped alternative credit supply?

This demand was met by a strong supply of investment capital from institutional investors like pension funds and insurance companies. To help the economy recover faster, the Federal Reserve introduced low interest rate policy, which reduced the yield on traditional fixed income assets like treasuries and resulted in billions of dollars migrating to higher yield investments like direct lending.

In just the past two decades, "[global] private credit, which includes distressed debt and venture financing, has ballooned from $42.4 billion in 2000 to $776.9 billion in 2018. By one estimate, the total is likely to top $1 trillion in 2020."

- Bloomberg (Butler), September 2019



NON-BANK LENDING MARKET PERSPECTIVE Q3 2020

> **"Top middle-market CFOs should be regularly evaluating the expanding universe of corporate lenders, especially in times of economic volatility."**
>
> - Matthew Bjonerud, CEO, Cerebro Capital

Cerebro Capital connects mid-market borrowers to a breadth of lending options, including both bank and non-bank lenders. While commercial bank lending has been tracked over the past 25 years by the Federal Reserve, non-bank lending credit markets are not studied as consistently as commercial banks, leading to opacity in the alternative lending market. Cerebro launched a quarterly survey of non-bank lending activity for middle market commercial and industrial (C&I) loans that illustrates the perspectives of private credit lenders, also known as alternative lenders.

About the Survey

The survey included non-bank lending partners nationally and was conducted by Cerebro as a complement to the Federal Reserve's Senior Loan Officer Opinion Survey on Bank Lending Practices, also released quarterly. Cerebro hopes to shed light on this $1 trillion industry that is now approaching one-third the size of commercial bank lending. Furthermore, our findings provide insights on the impact that the current economic environment is having on lending markets

COMMON TYPES OF NON-BANK LENDERS

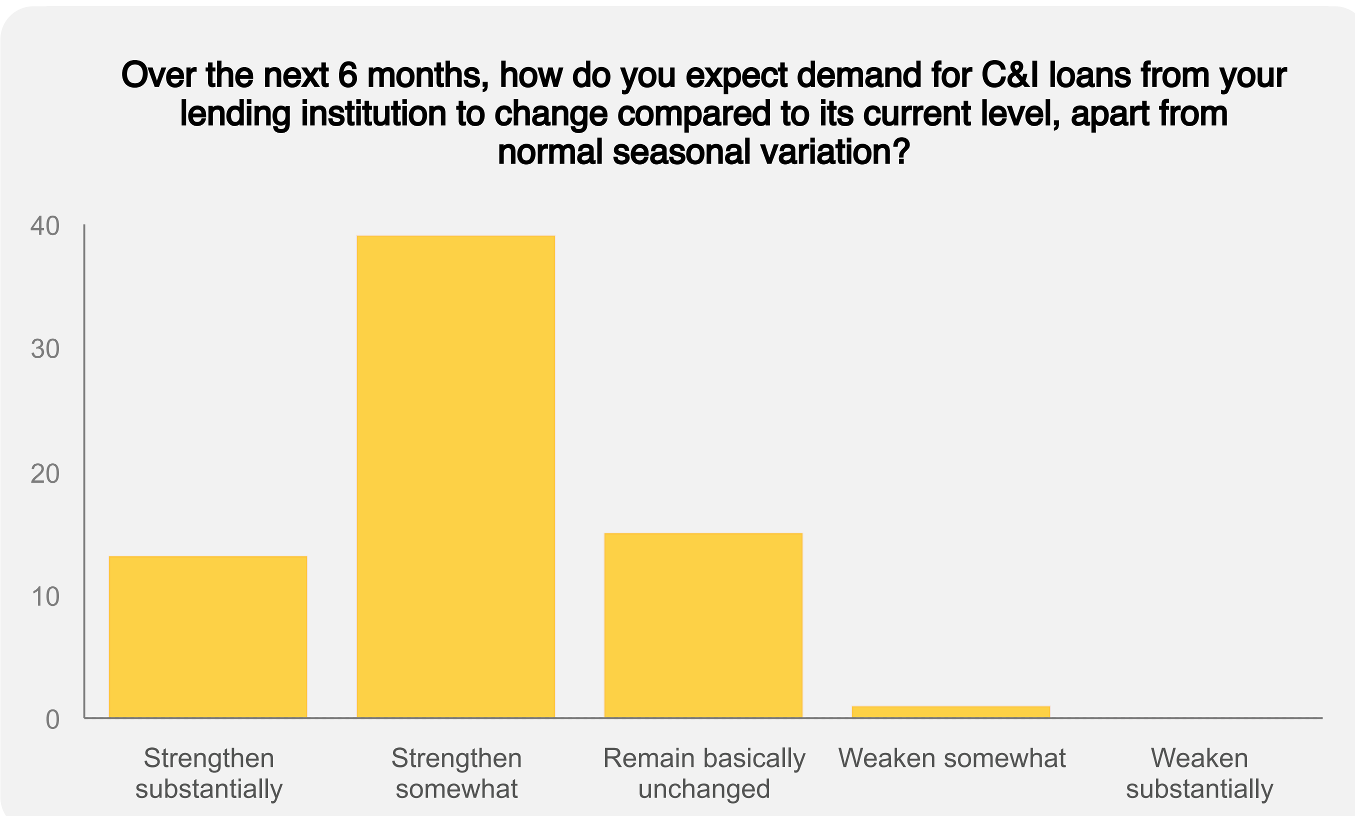
- **VENTURE DEBT FUNDS**
- **ASSET-BASED LENDERS**
- **MEZZANINE FUNDS**
- **SBICS & BDCS**
- **PRIVATE DEBT FUNDS**

Non-bank lenders from Cerebro Capital's lender network were surveyed in October 2020. Cerebro's lender participation exceeded the number of participants in the Federal Reserve's Senior Loan Officer Survey of the same period by 10%. Participating lenders represented over $335 billion in combined assets managed, with a primary lending focus of loan sizes from $2 million to $100 million. Participants included some of the oldest and largest non-bank lenders in the U.S., including private and publicly traded firms.

NON-BANK LENDING KEY FINDINGS

Borrower demand for non-bank alternatives is surging.

76% of non-bank lenders expect loan demand to strengthen over the coming months as borrowers leave commercial banks in search of relaxed covenants and flexible loan structures.



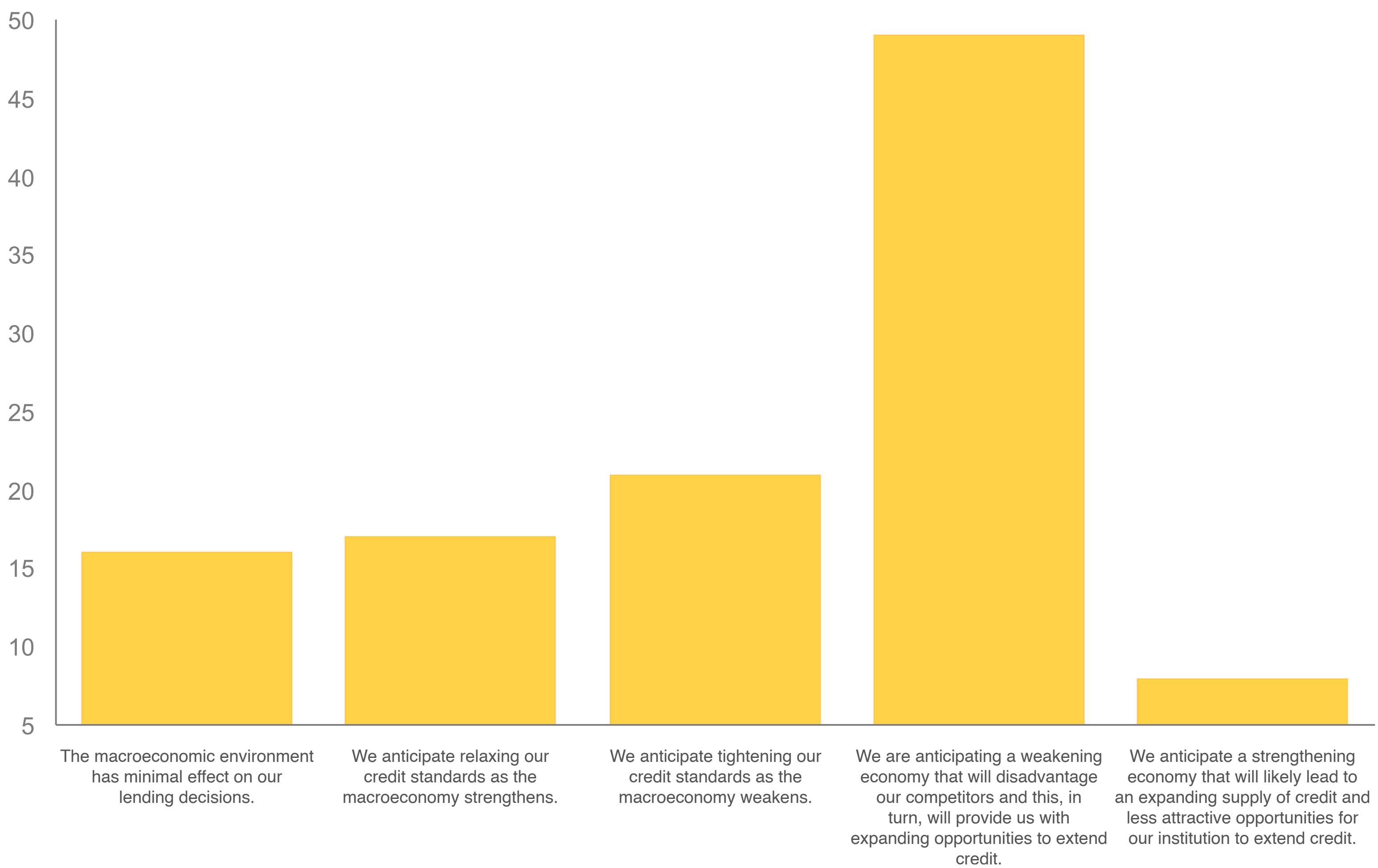
Survey conducted by Cerebro Capital in October 2020. N = 68

NON-BANK LENDING KEY FINDINGS

Macroeconomic conditions are creating an even bigger opportunity for alternative lenders.

With 63% of non-bank lenders anticipating a weakening economy that will disadvantage competitors and provide more opportunities for them to lend, non-bank lenders are seizing the opportunity to land deals with strong middle-market companies.

Looking ahead over the next six months, how are changes in the macroeconomy likely to impact your lending business? Please check all that you feel apply:

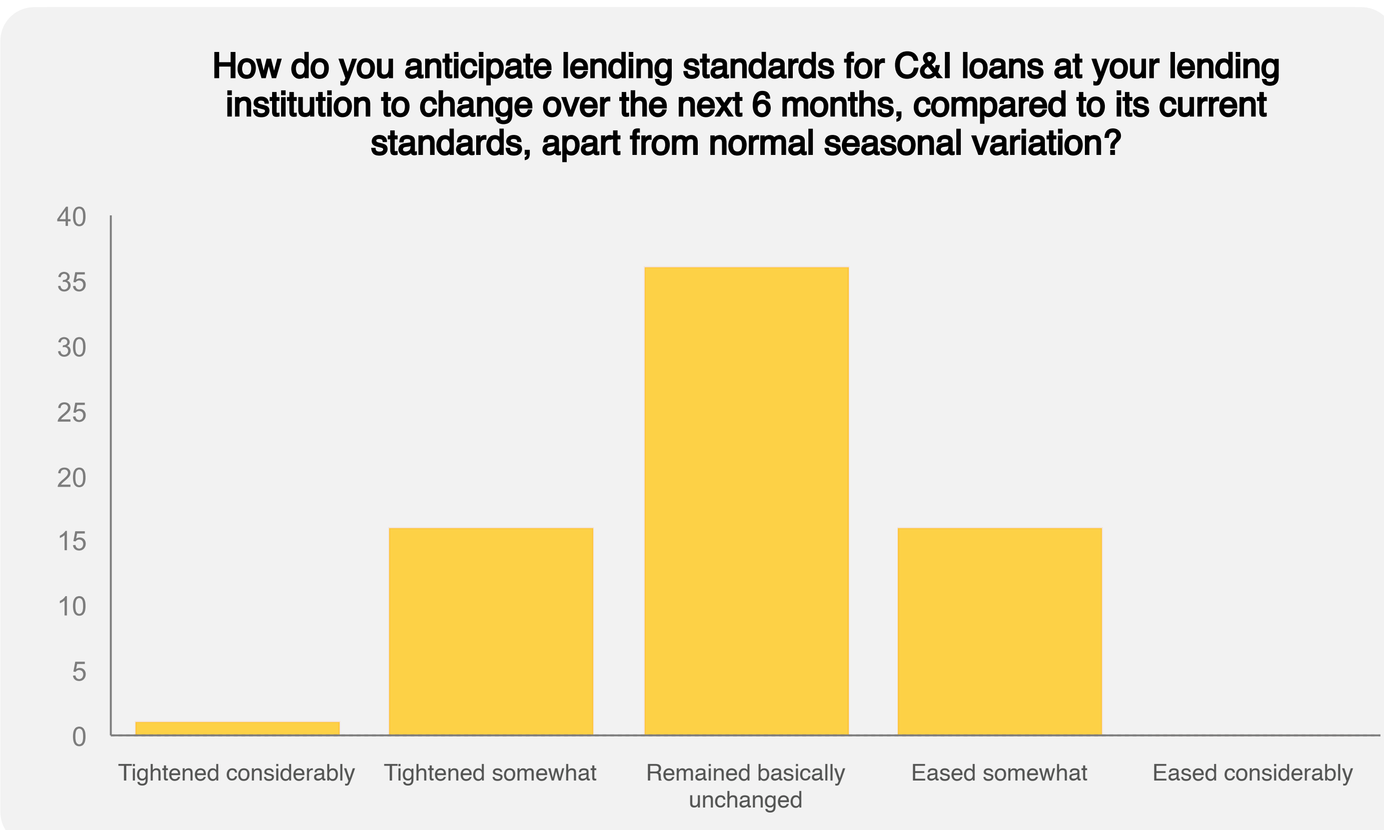


Survey conducted by Cerebro Capital in October 2020. N = 68

NON-BANK LENDING KEY FINDINGS

Some lenders anticipate tightening credit standards, while others may look to ease standards.

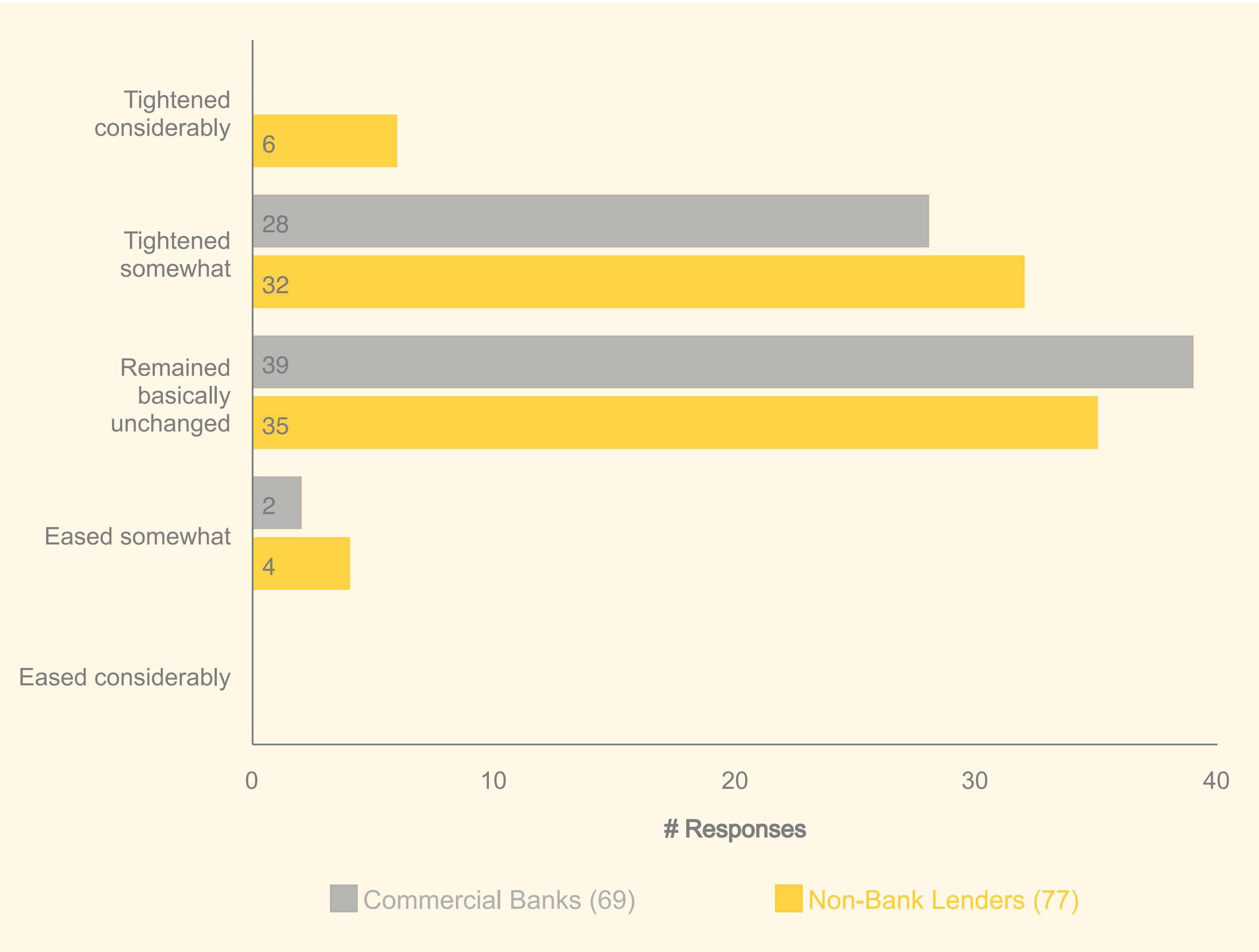
One-quarter of lenders anticipate tighter lending standards in the coming months ahead, potentially due to weakened economic conditions, while other lenders are anticipating easing standards to win new business.



Survey conducted by Cerebro Capital in October 2020. N = 69

Q3 2020 SURVEY RESPONSES

1. Looking back over the past three months, how have your lending institution's credit standards changed for C&I loans?



Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

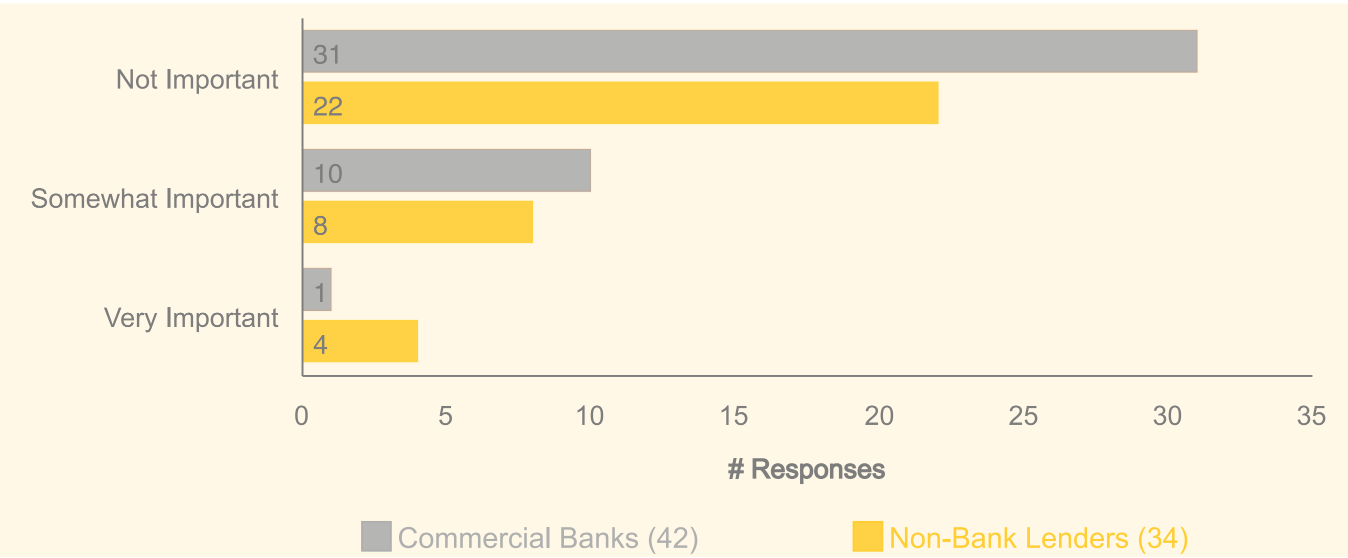
Corresponding Federal Reserve Question

"Over the past three months, how have your bank's credit standards for approving applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—to large and middle-market firms and to small firms changed?"

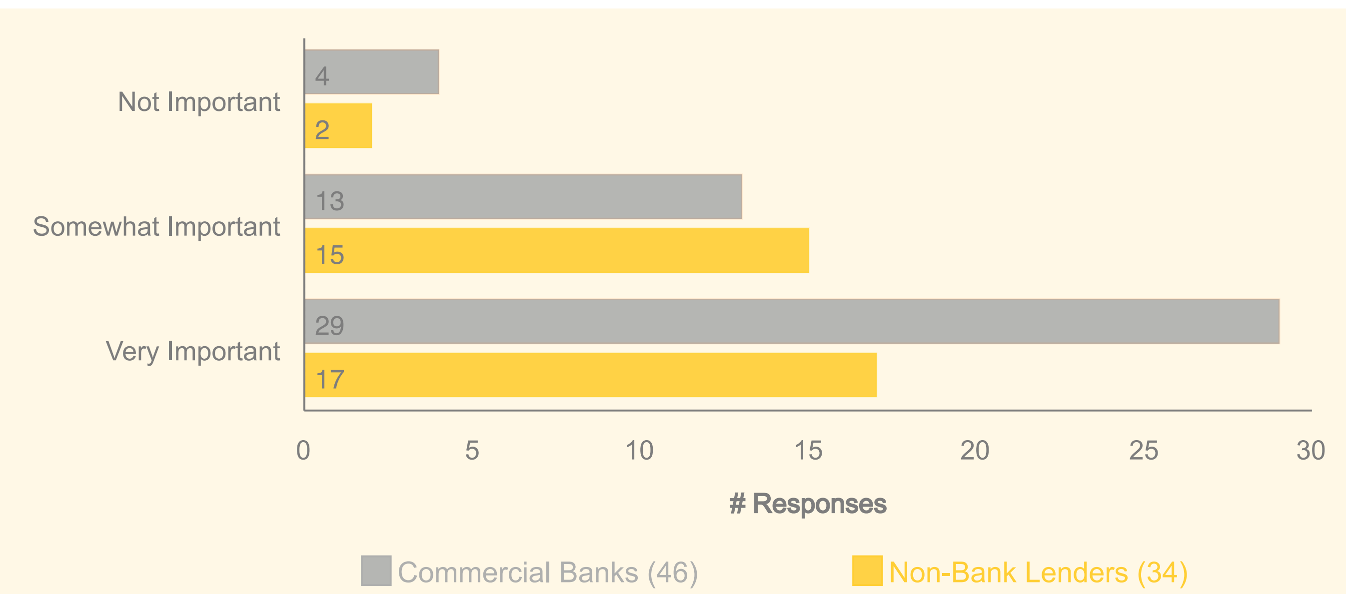
Q3 2020 SURVEY RESPONSES

1a. Because your lending institution has tightened its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Deterioration in your lending institution's current or expected capital position:



Less favorable or more uncertain economic outlook:



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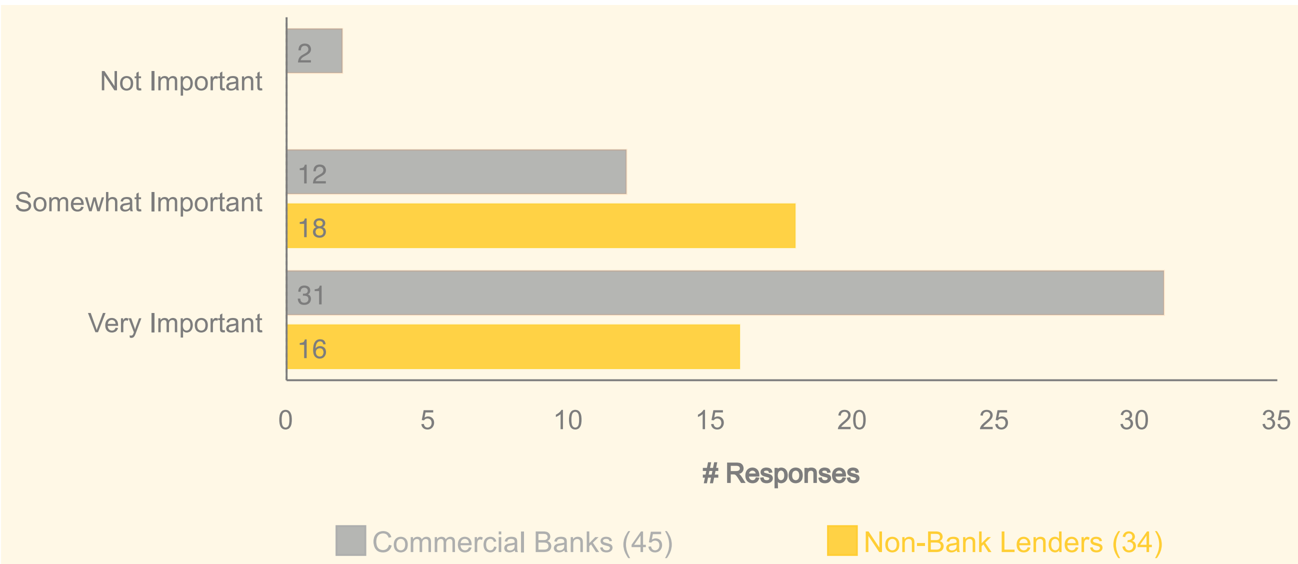
Corresponding Federal Reserve Question

"If your bank has tightened or eased its credit standards or its terms for C&I loans or credit lines over the past three months (as described in questions 1 and 2), how important have been the following possible reasons for the change? Possible reasons for tightening credit standards or loan terms."

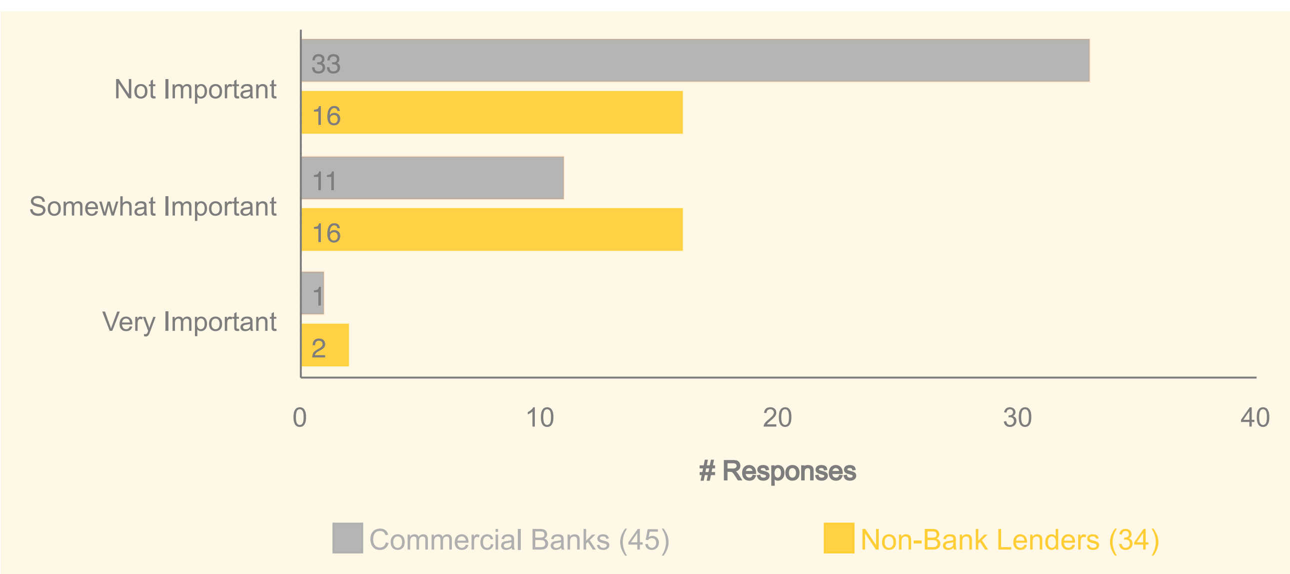
Q3 2020 SURVEY RESPONSES

1a. Because your lending institution has <u>tightened</u> its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Worsening of industry-specific problems:



Less aggressive competition from other lenders (other financial intermediaries or the capital markets):



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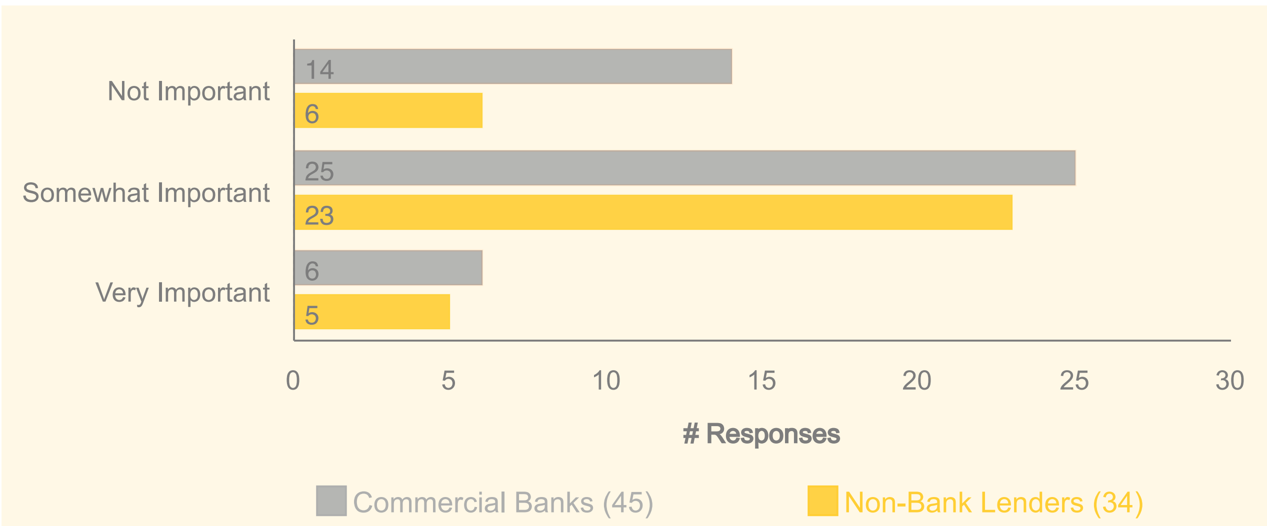
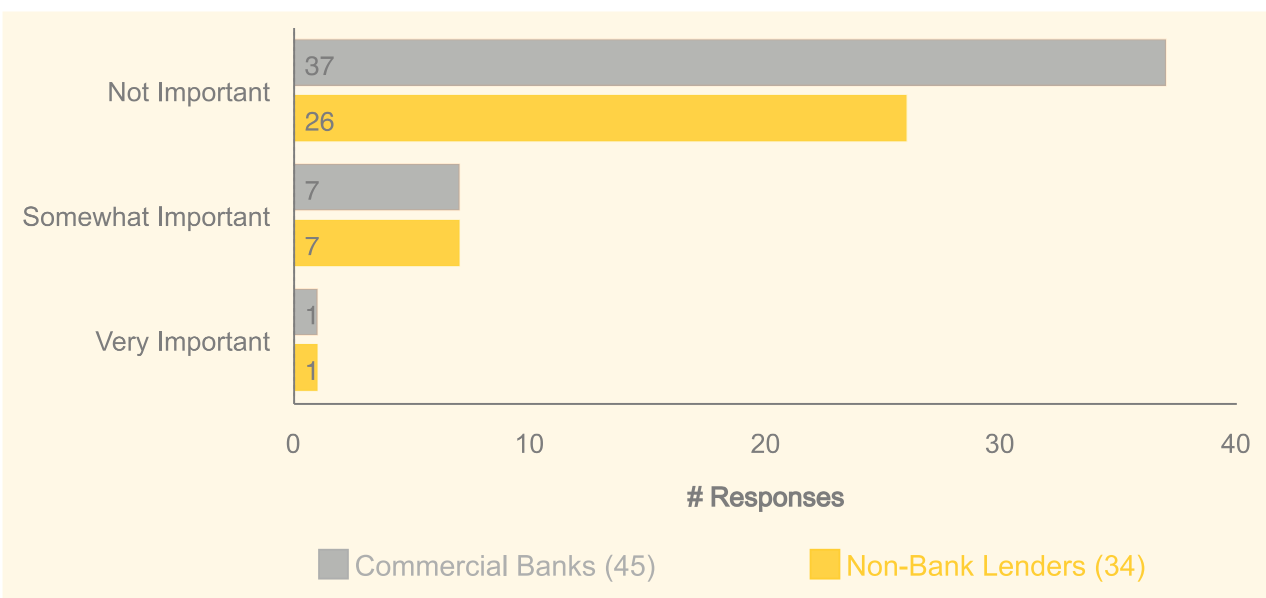
Q3 2020 SURVEY RESPONSES

1a. Because your lending institution has <u>tightened</u> its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Reduced tolerance for risk:



Decreased liquidity in the secondary market for these loans:



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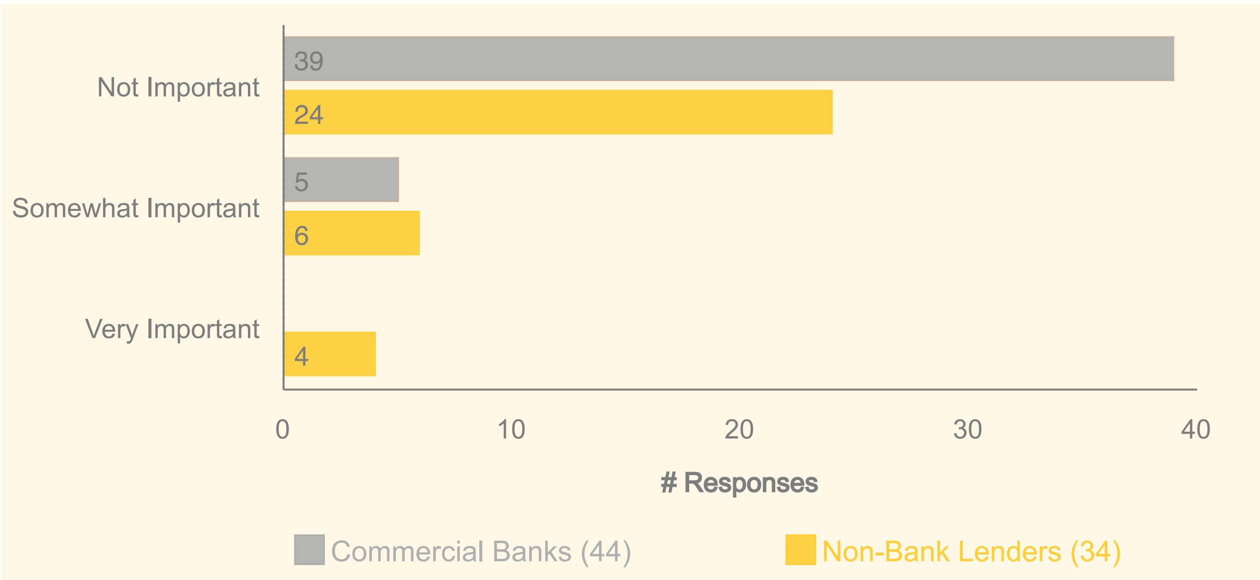
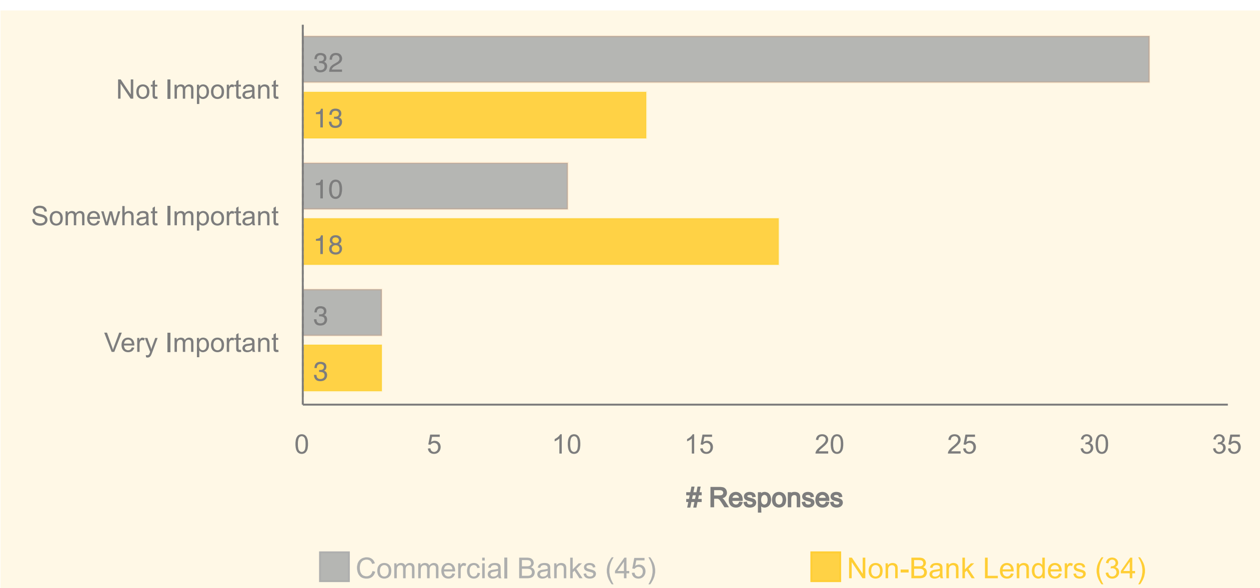
Q3 2020 SURVEY RESPONSES

1a. Because your lending institution has <u>tightened</u> its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Deterioration in your lending institution's current or expected liquidity position:



Increased concerns about the effects of legislative changes, supervisory actions, or changes in accounting standards:



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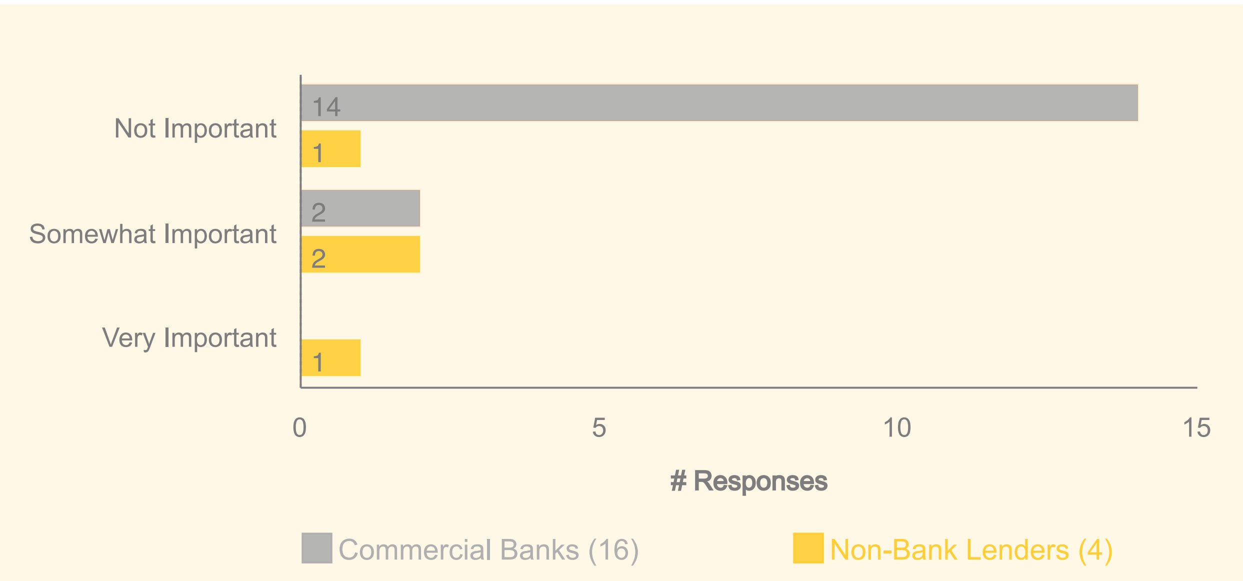
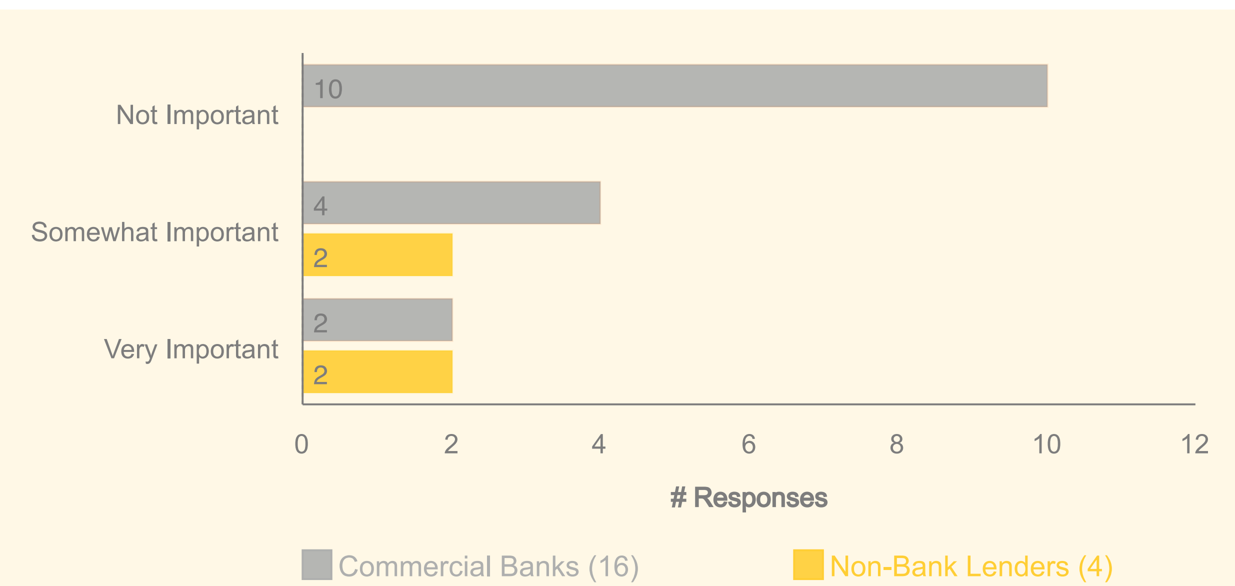
Q3 2020 SURVEY RESPONSES

1b. Because your lending institution has <u>eased</u> its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Improvement in your lending institution's current or expected capital position:



More favorable or less uncertain economic outlook:



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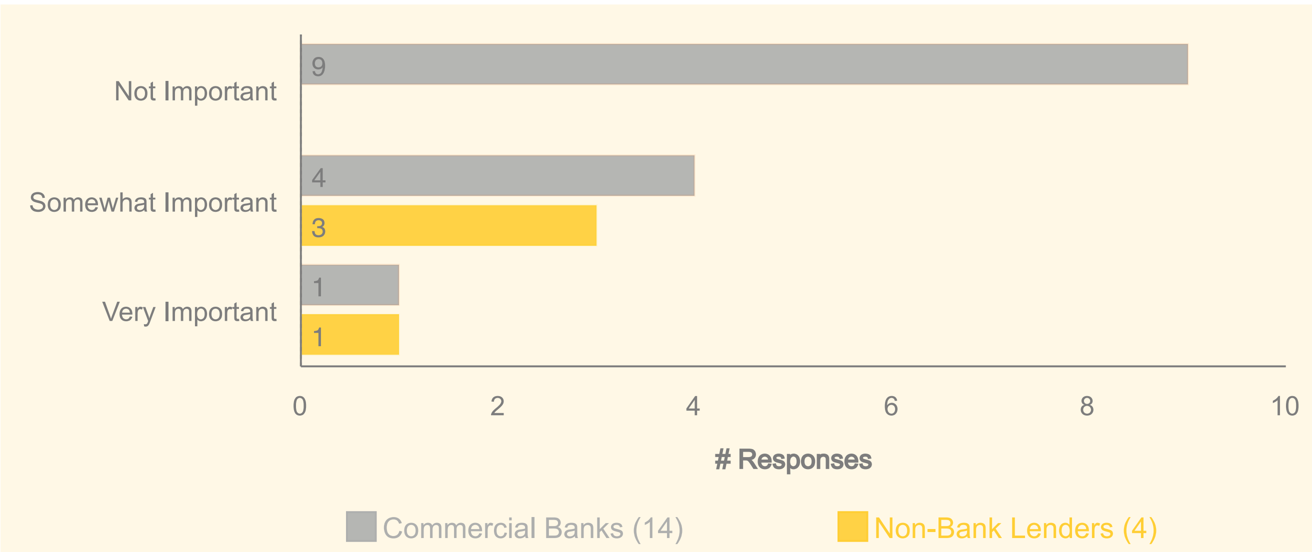
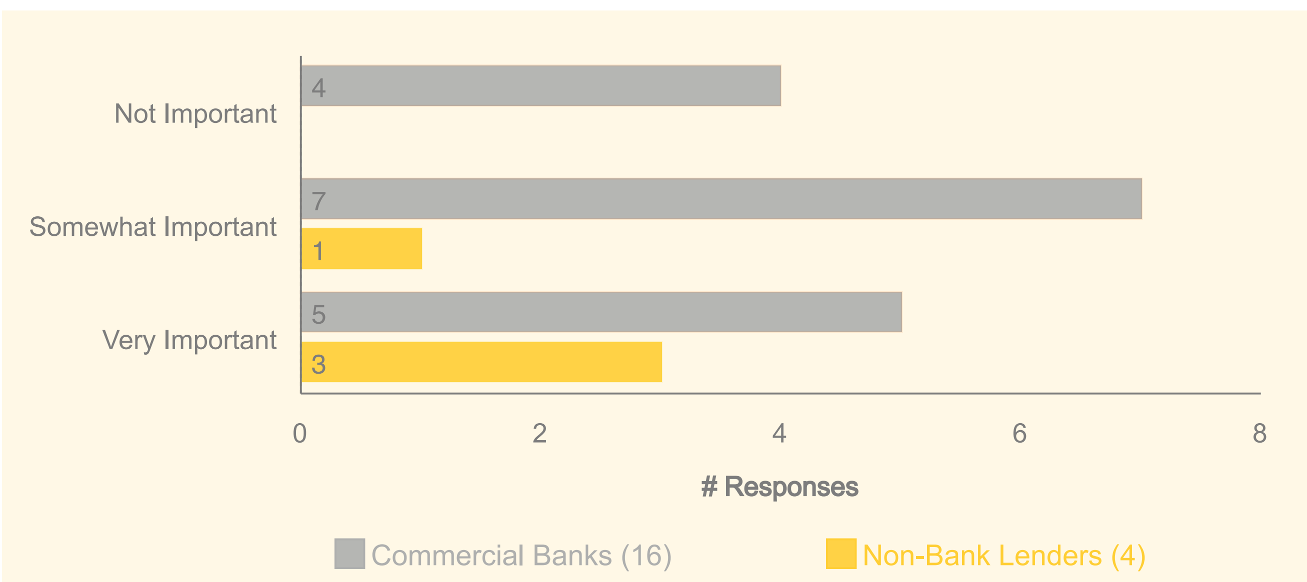
Q3 2020 SURVEY RESPONSES

1b. Because your lending institution has eased its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Improvement in industry-specific problems:



More aggressive competition from other lenders (other financial intermediaries or the capital markets):



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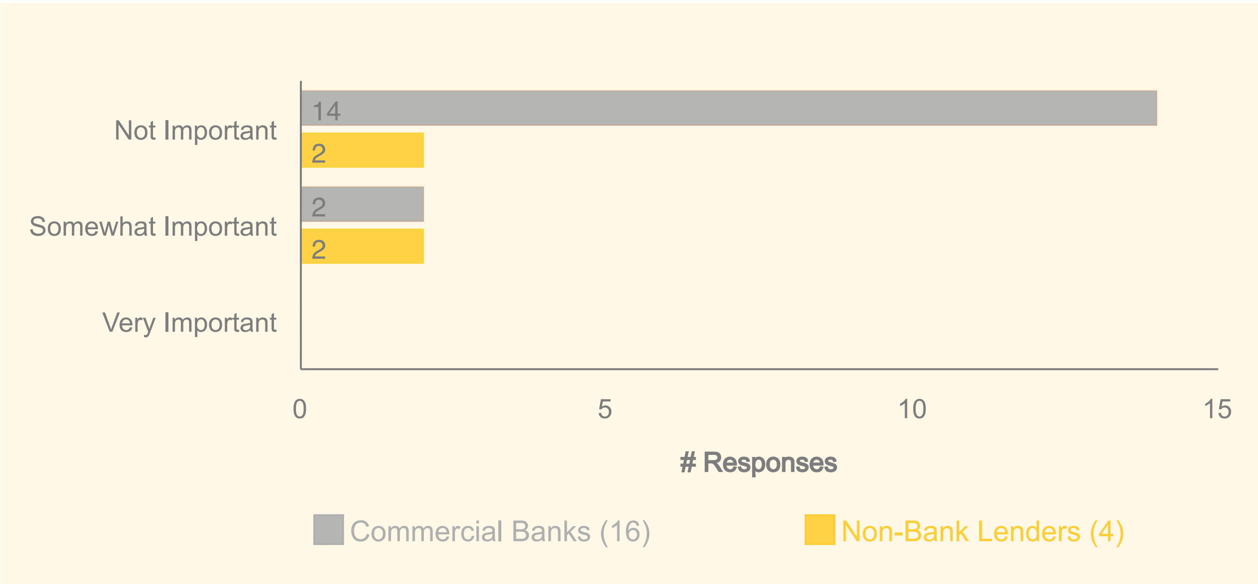
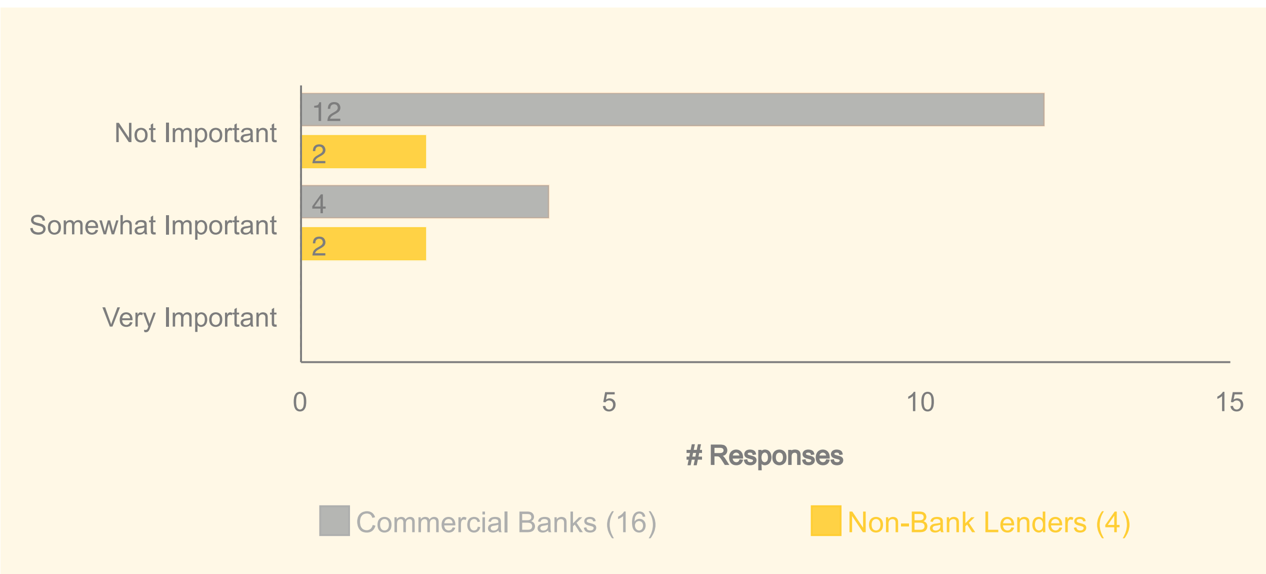
Q3 2020 SURVEY RESPONSES

1b. Because your lending institution has <u>eased</u> its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Increased tolerance for risk:



Increased liquidity in the secondary market for these loans:



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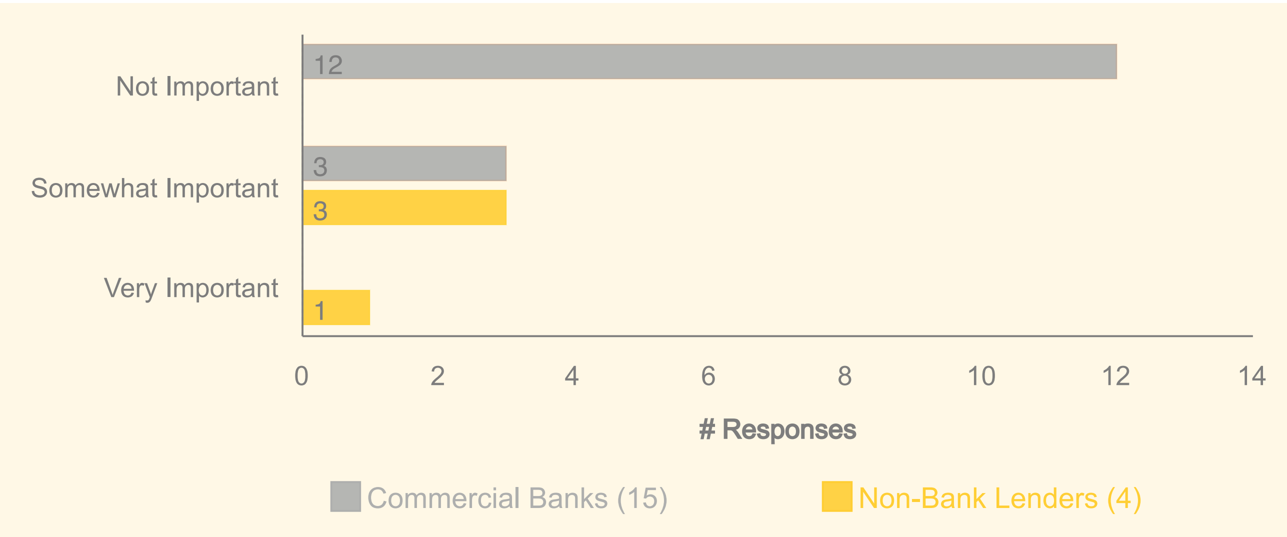
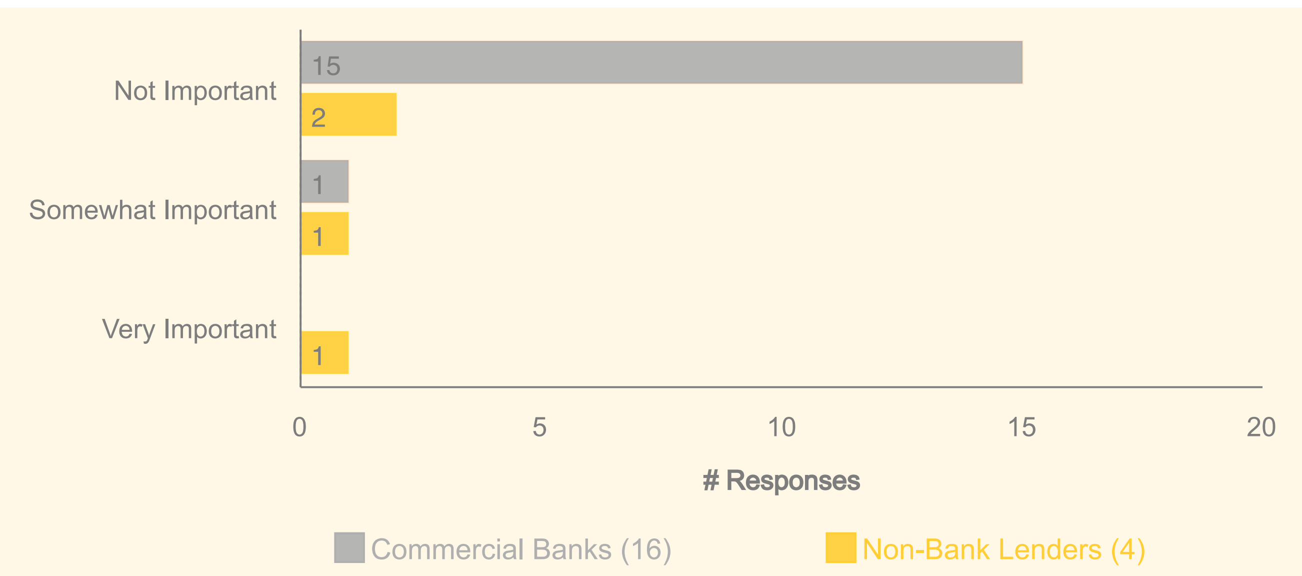
Q3 2020 SURVEY RESPONSES

1b. Because your lending institution has <u>eased</u> its credit standards for C&I loans over the past three months, how important have the following possible reasons been for the change?

Improvement in your lending institution's current or expected liquidity position:



Reduced concerns about the effects of legislative changes, supervisory actions, or changes in accounting standards:



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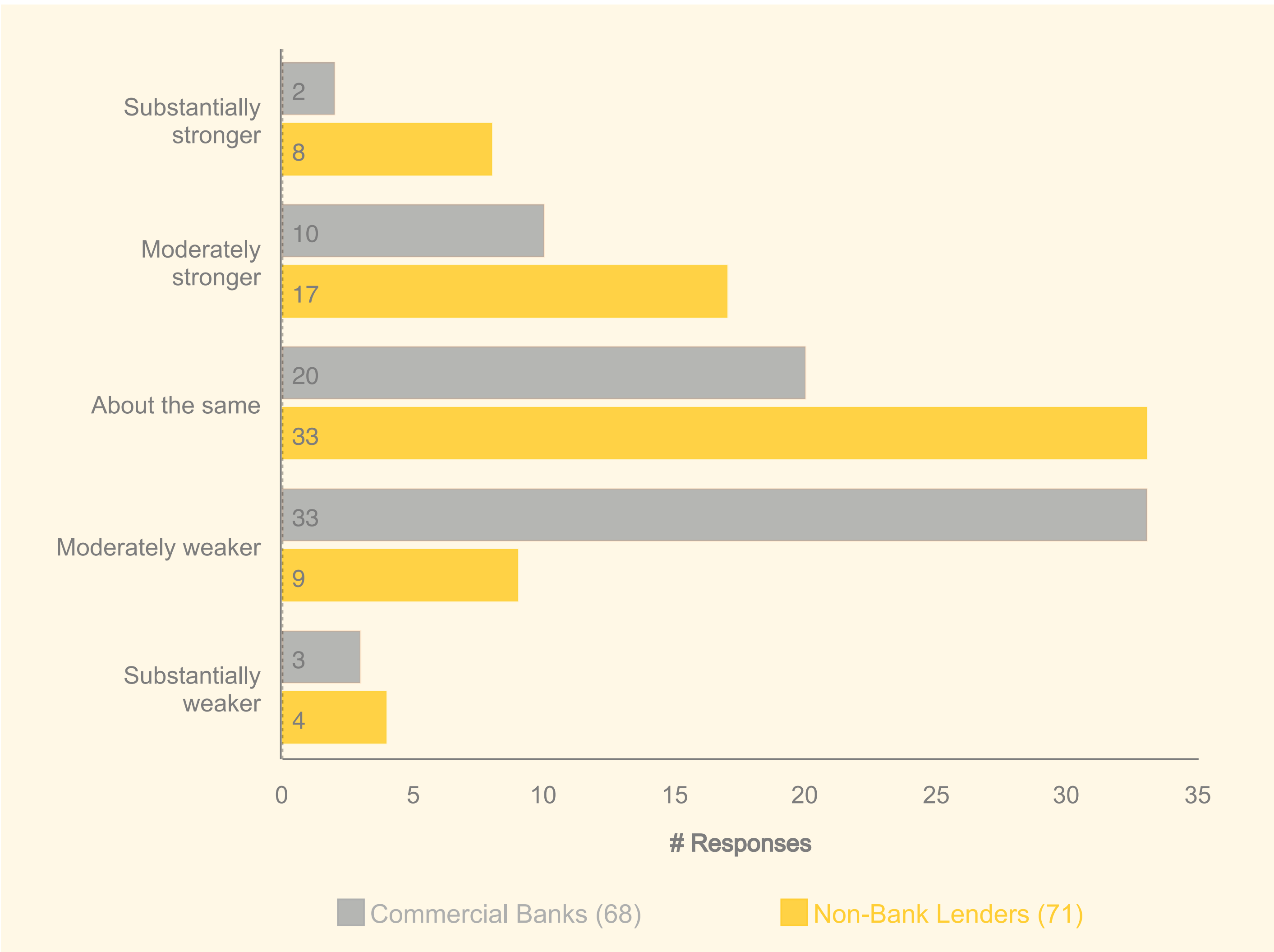
Q3 2020 SURVEY RESPONSES

2. Looking back over the past three months, how has demand for draws on existing C&I term loan commitments and/or draws on (existing) lines of credit changed?



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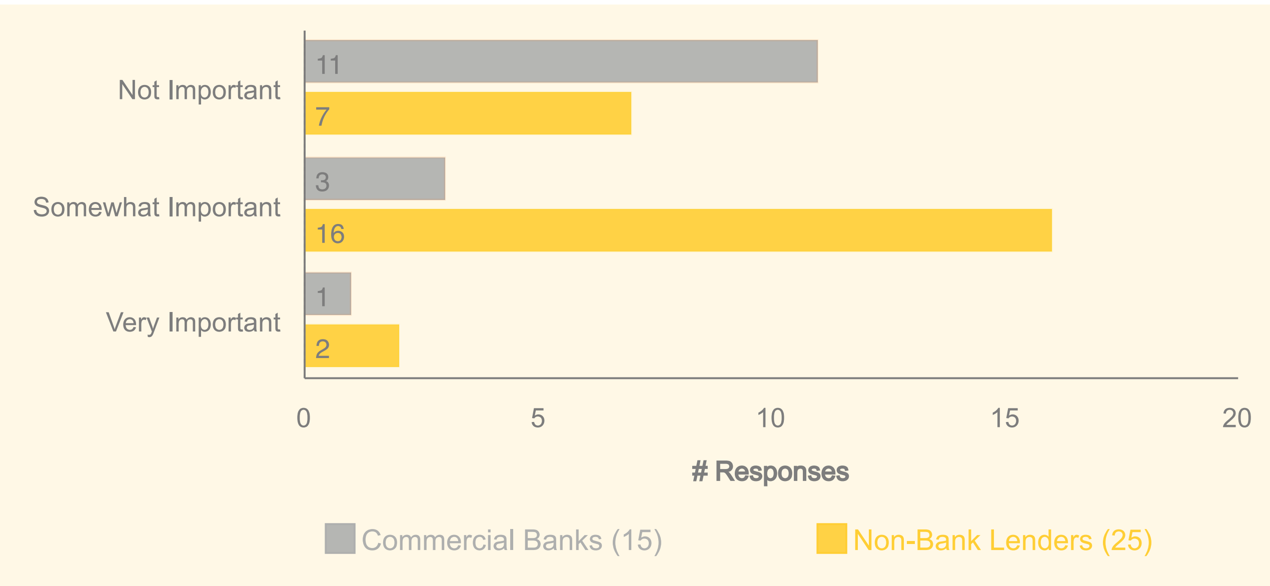
Corresponding Federal Reserve Question

"Apart from normal seasonal variation, how has demand for C&I loans changed over the past three months? (Please consider only funds actually disbursed as opposed to requests for new or increased lines of credit.)."

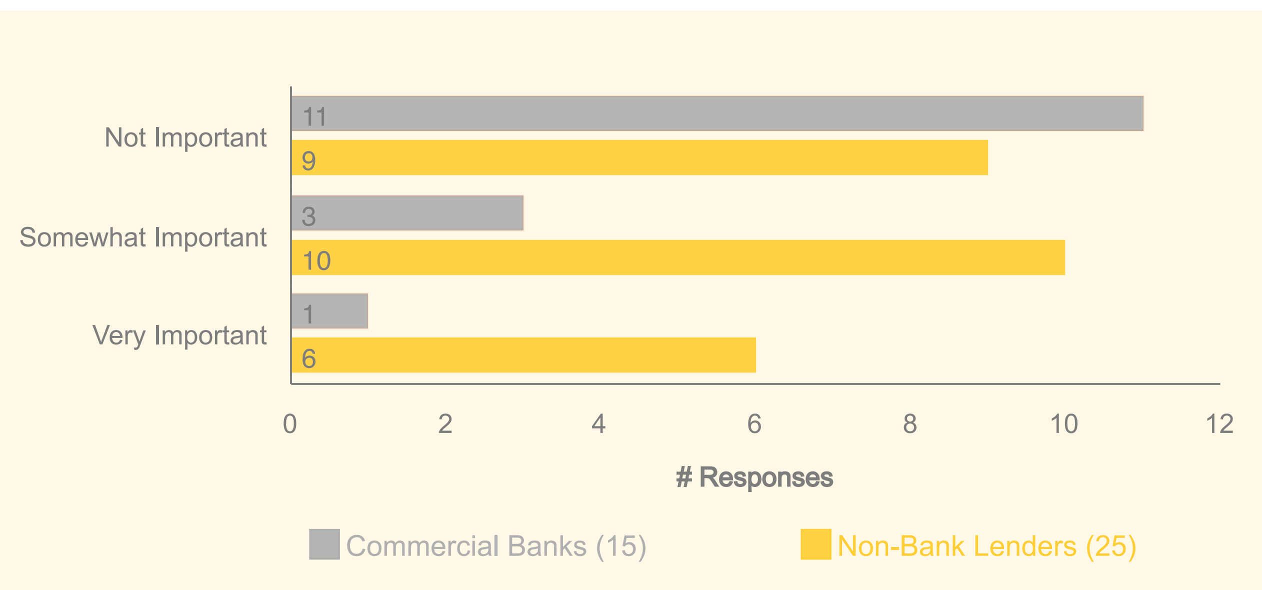
Q3 2020 SURVEY RESPONSES

2a. If demand for C&I loans has strengthened over the past three months, how important have the following possible reasons been for the change?

Customer inventory financing needs increased:



Customer accounts receivable financing needs increased:



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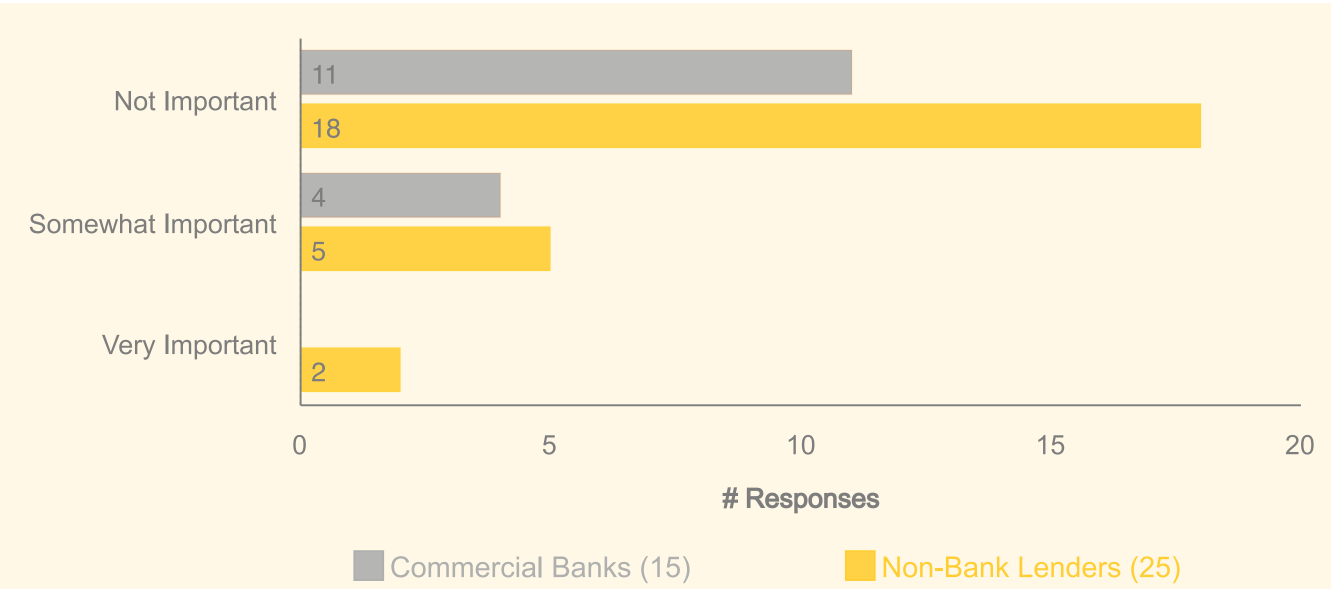
Corresponding Federal Reserve Question

"If demand for C&I loans has strengthened or weakened over the past three months (as described in question 4), how important have been the following possible reasons for the change? If stronger loan demand (answer 1 or 2 to question 4A or 4B), possible reasons."

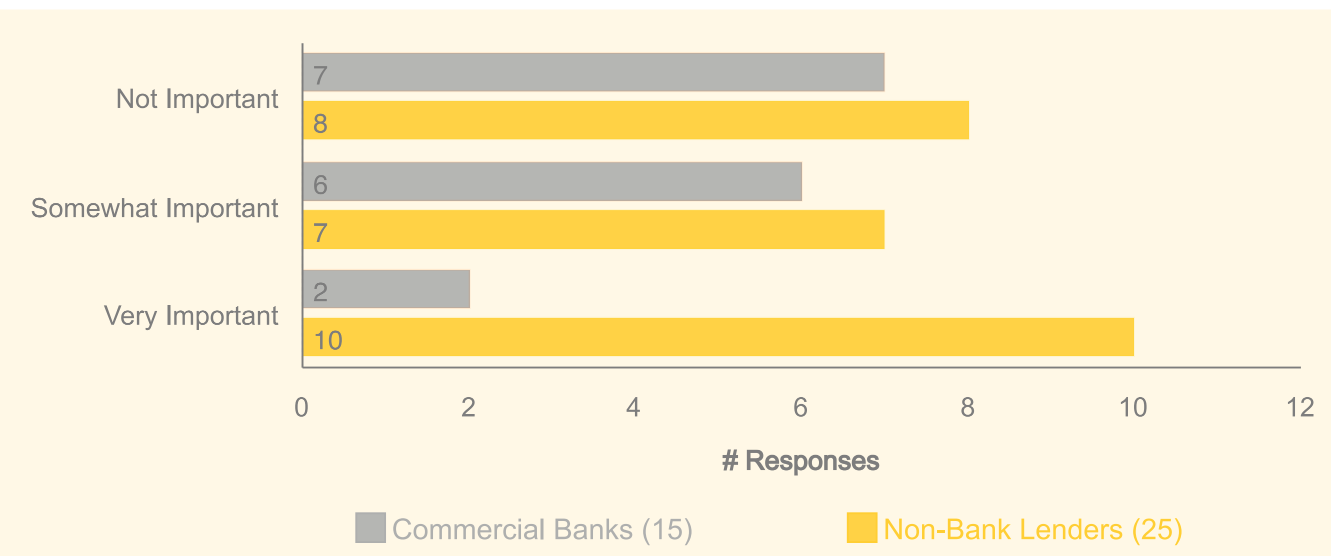
Q3 2020 SURVEY RESPONSES

2a. If demand for C&I loans has <u>strengthened</u> over the past three months, how important have the following possible reasons been for the change?

Customer investment in plant or equipment increased:



Customer internally generated funds decreased:



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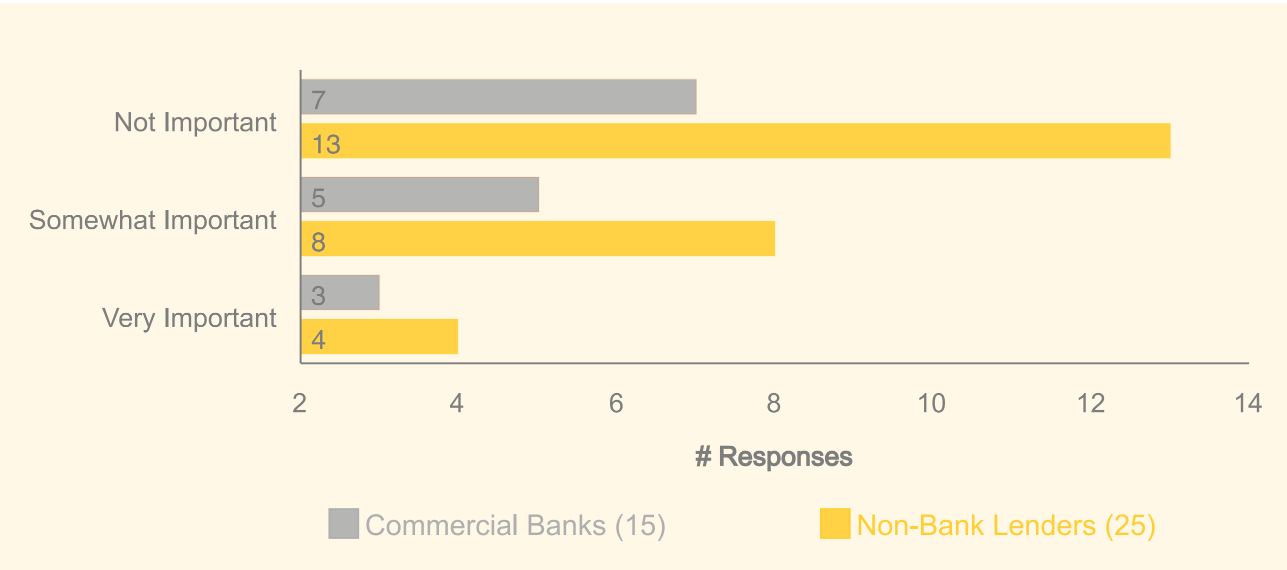
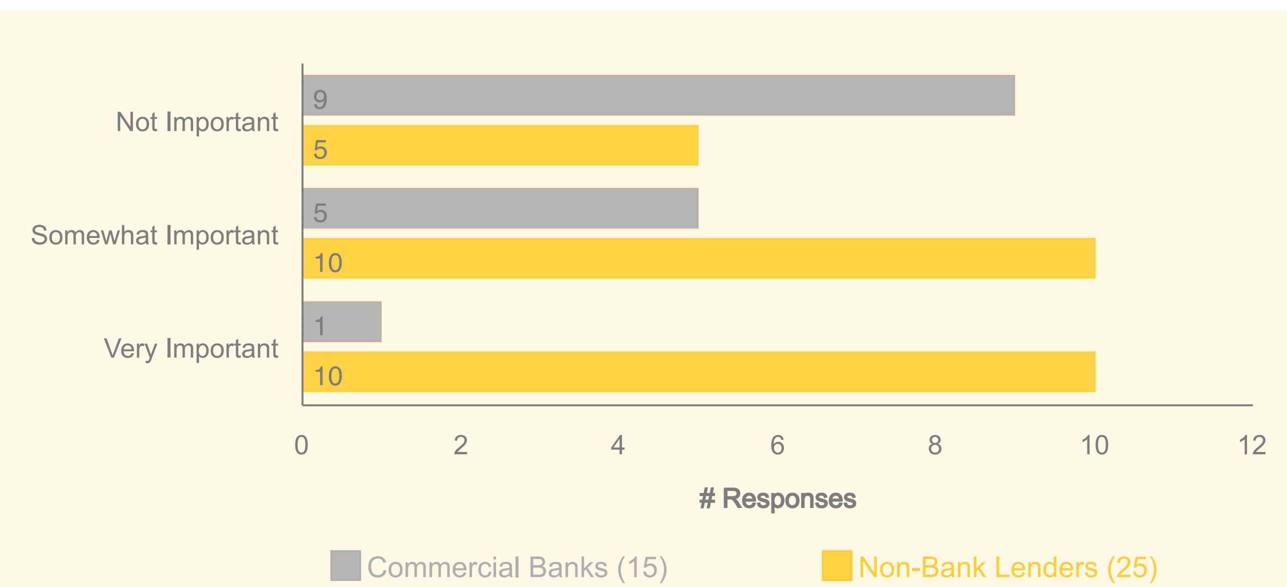
2a. If demand for C&I loans has strengthened over the past three months, how important have the following possible reasons been for the change?

Customer merger or acquisition financing needs increased:



Customer borrowing shifted to your lending institution from other lender sources because these other sources became less attractive:



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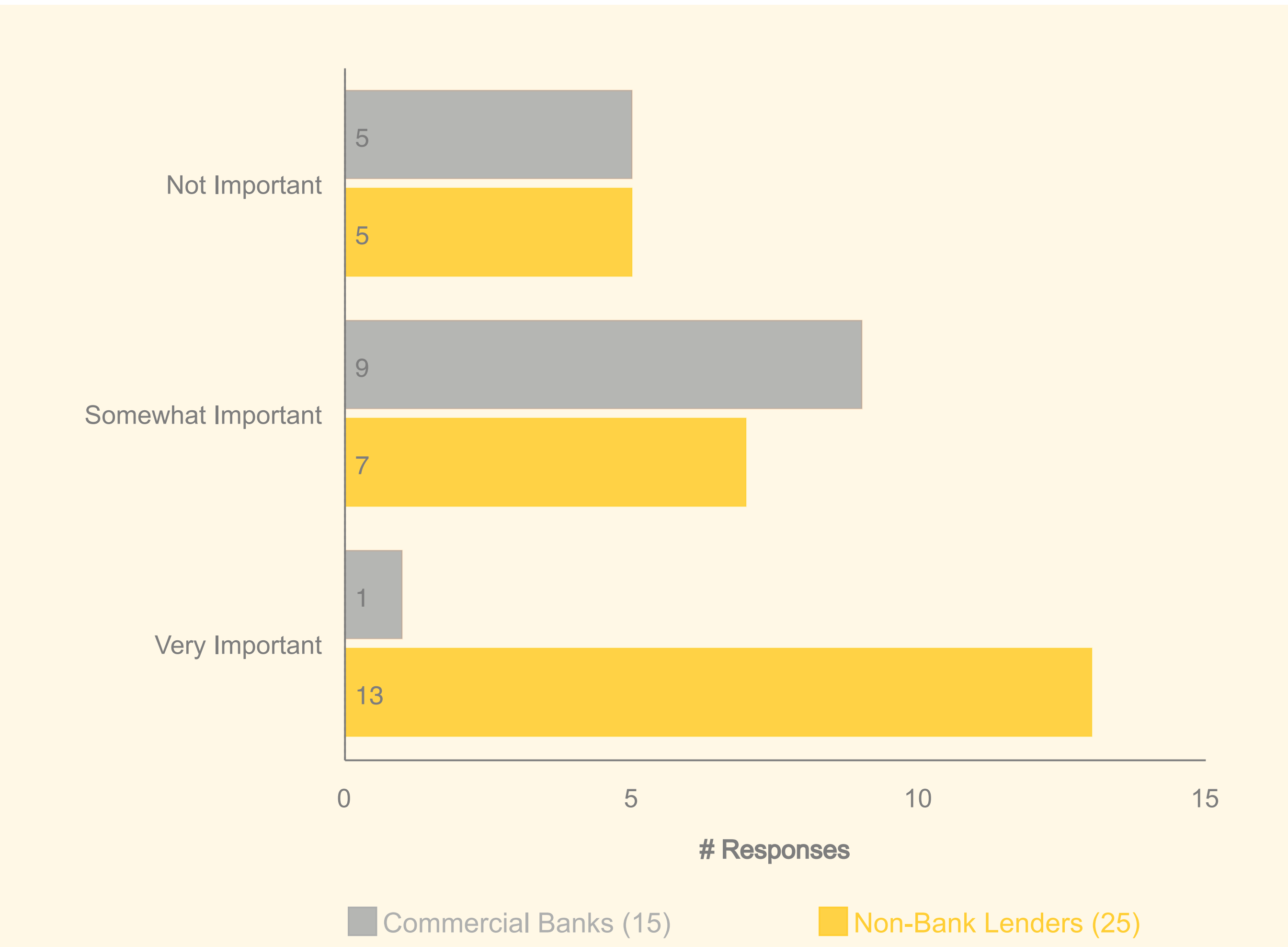
2a. If demand for C&I loans has strengthened over the past three months, how important have the following possible reasons been for the change?

Customer precautionary demand for cash and liquidity increased:



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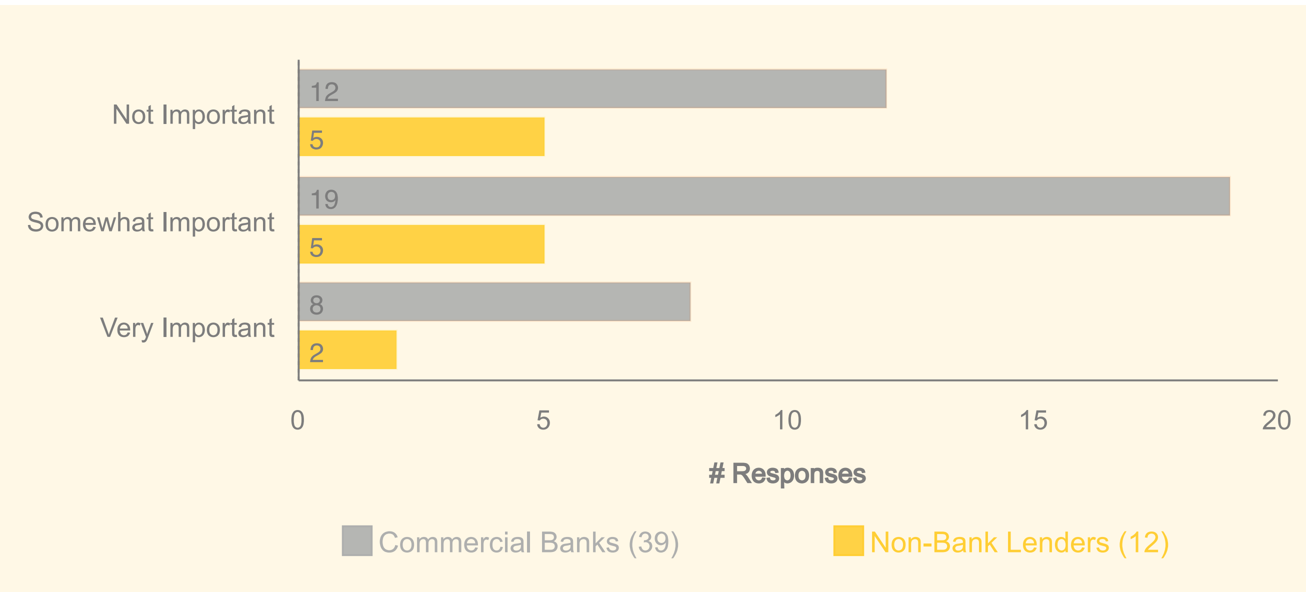
2b. If demand for C&I loans has weakened over the past three months, how important have the following possible reasons been for the change?

Customer inventory financing needs decreased:



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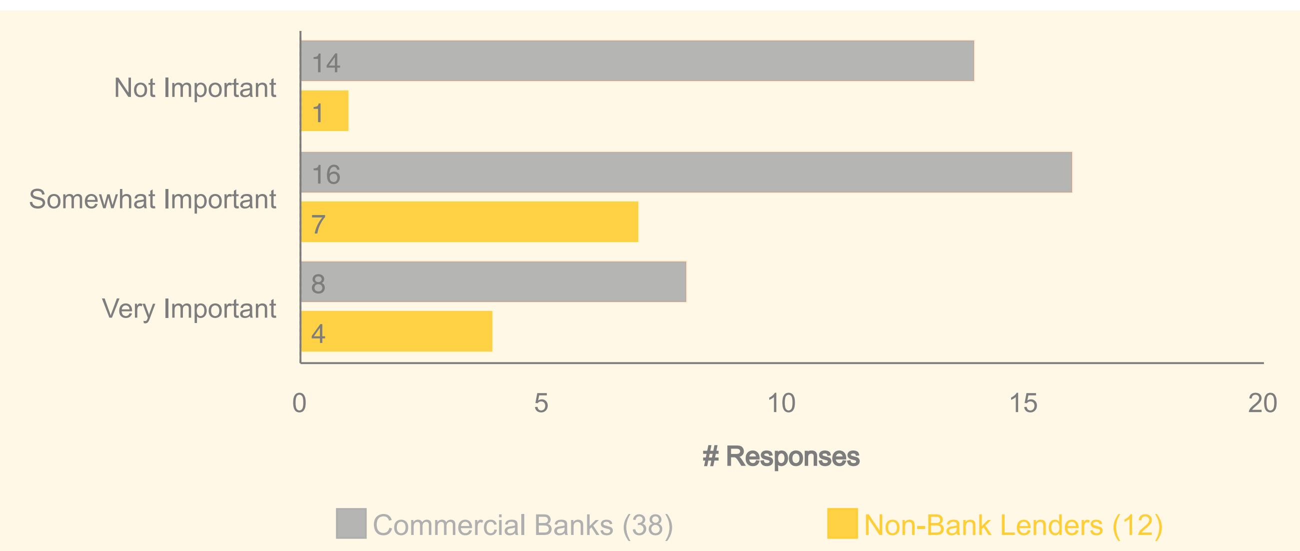

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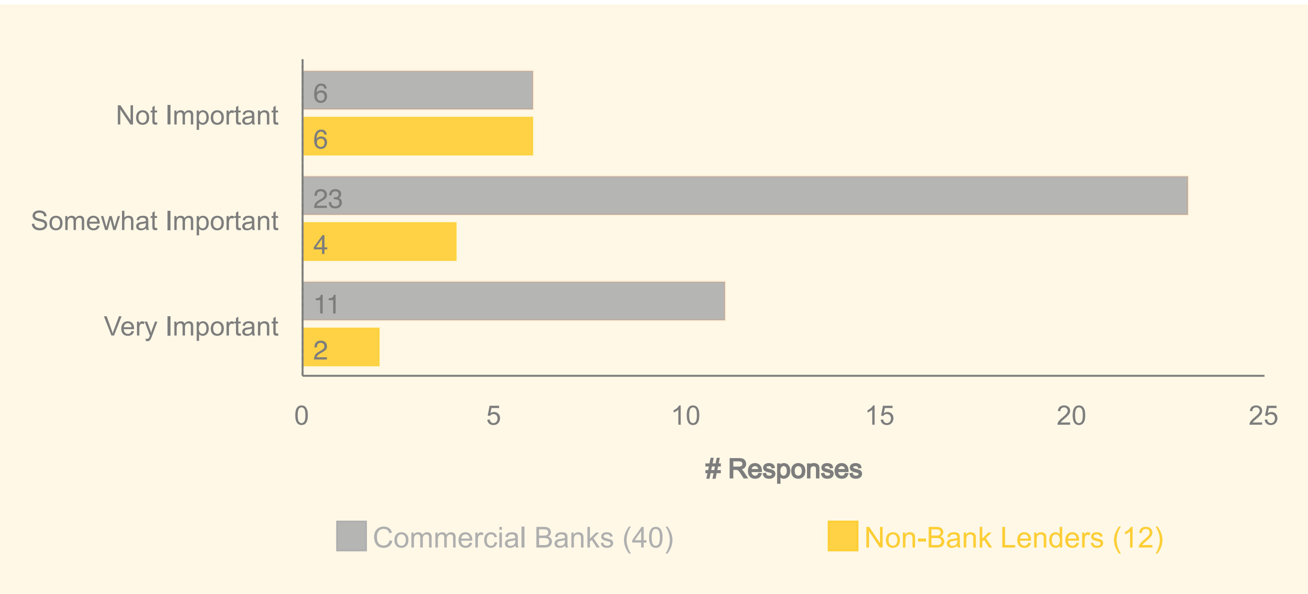
Customer investment in plant or equipment decreased:



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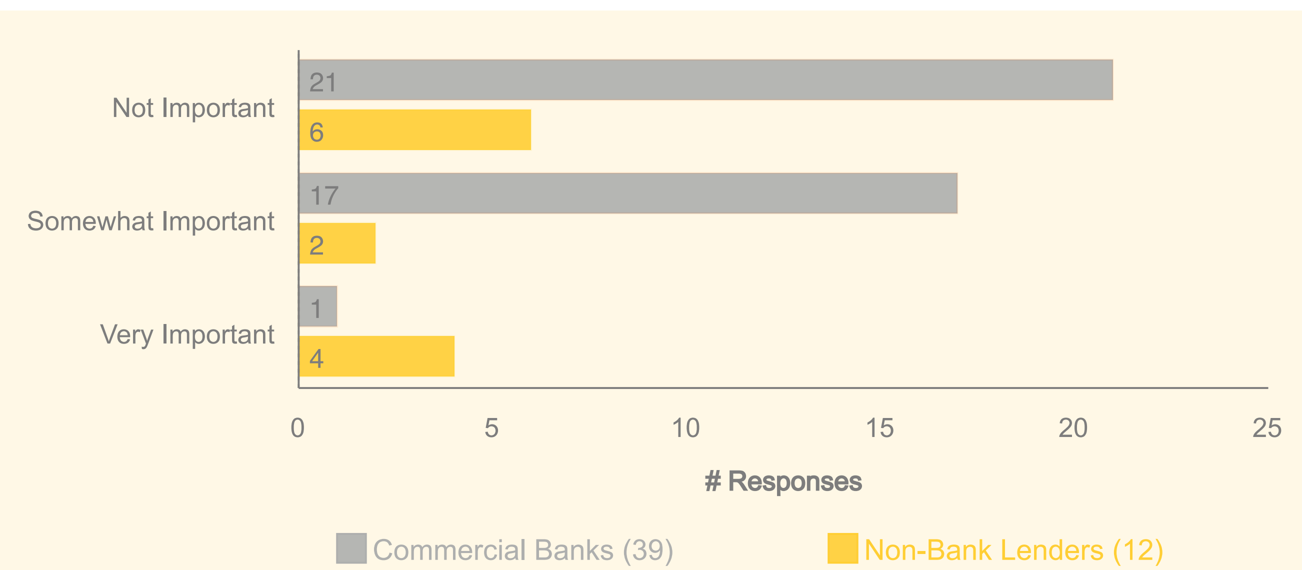

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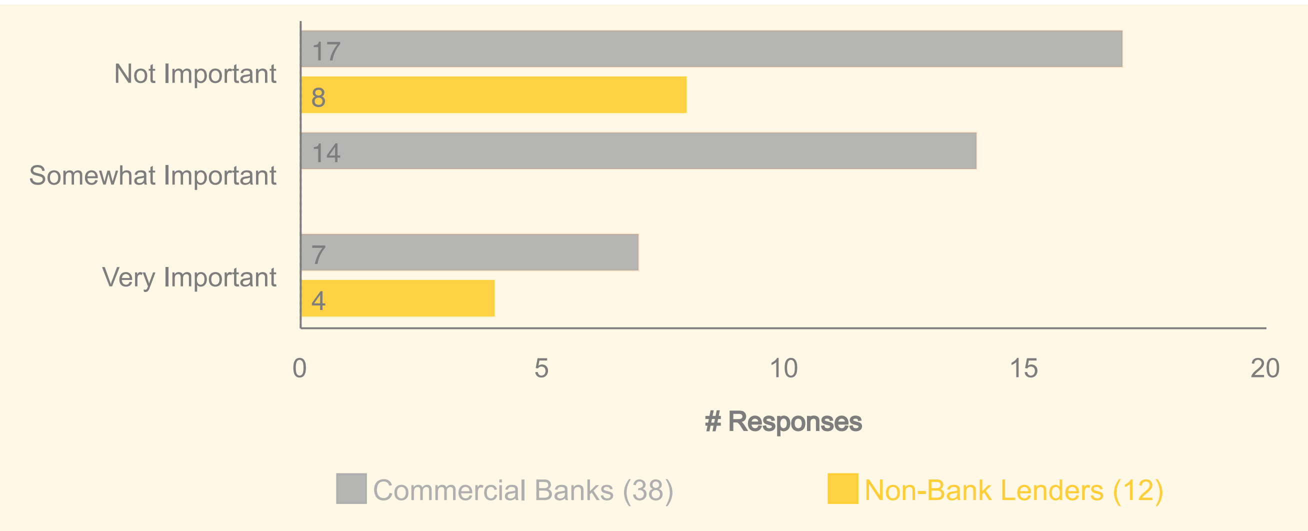
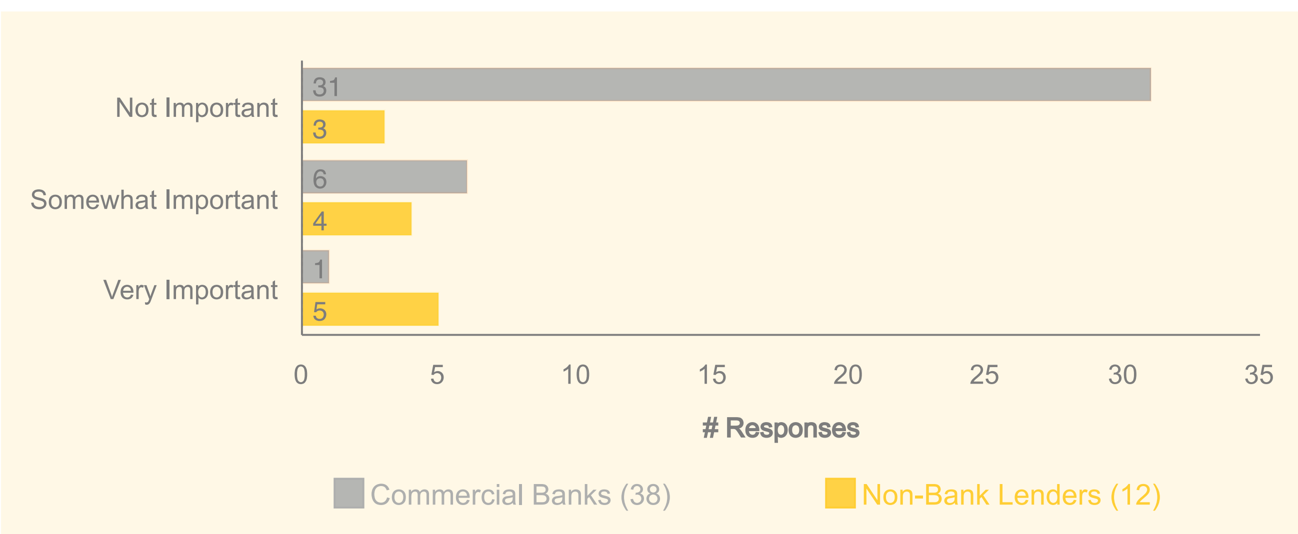


Customer borrowing shifted from your lending institution to other lender sources because these other sources became more attractive:



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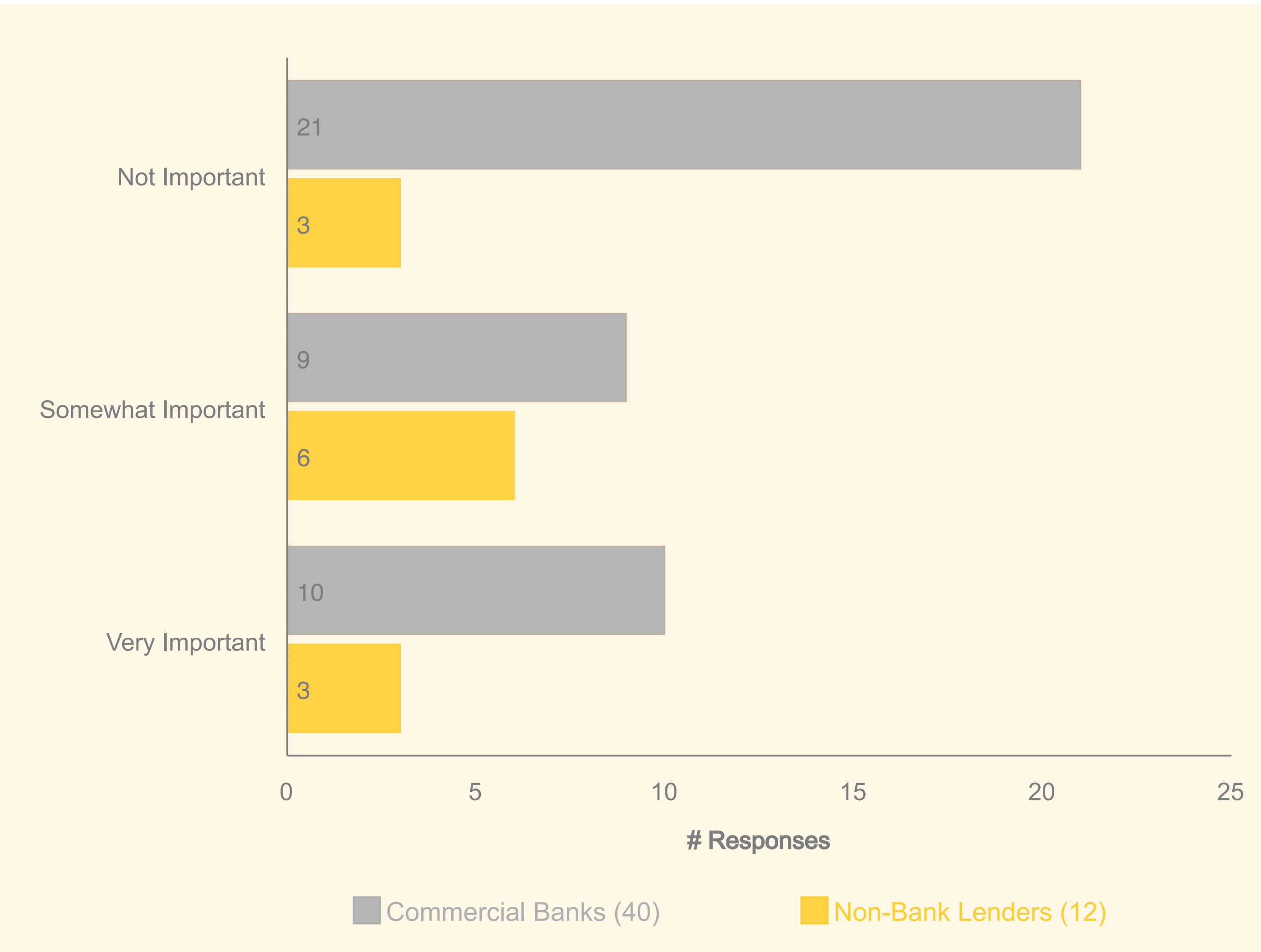

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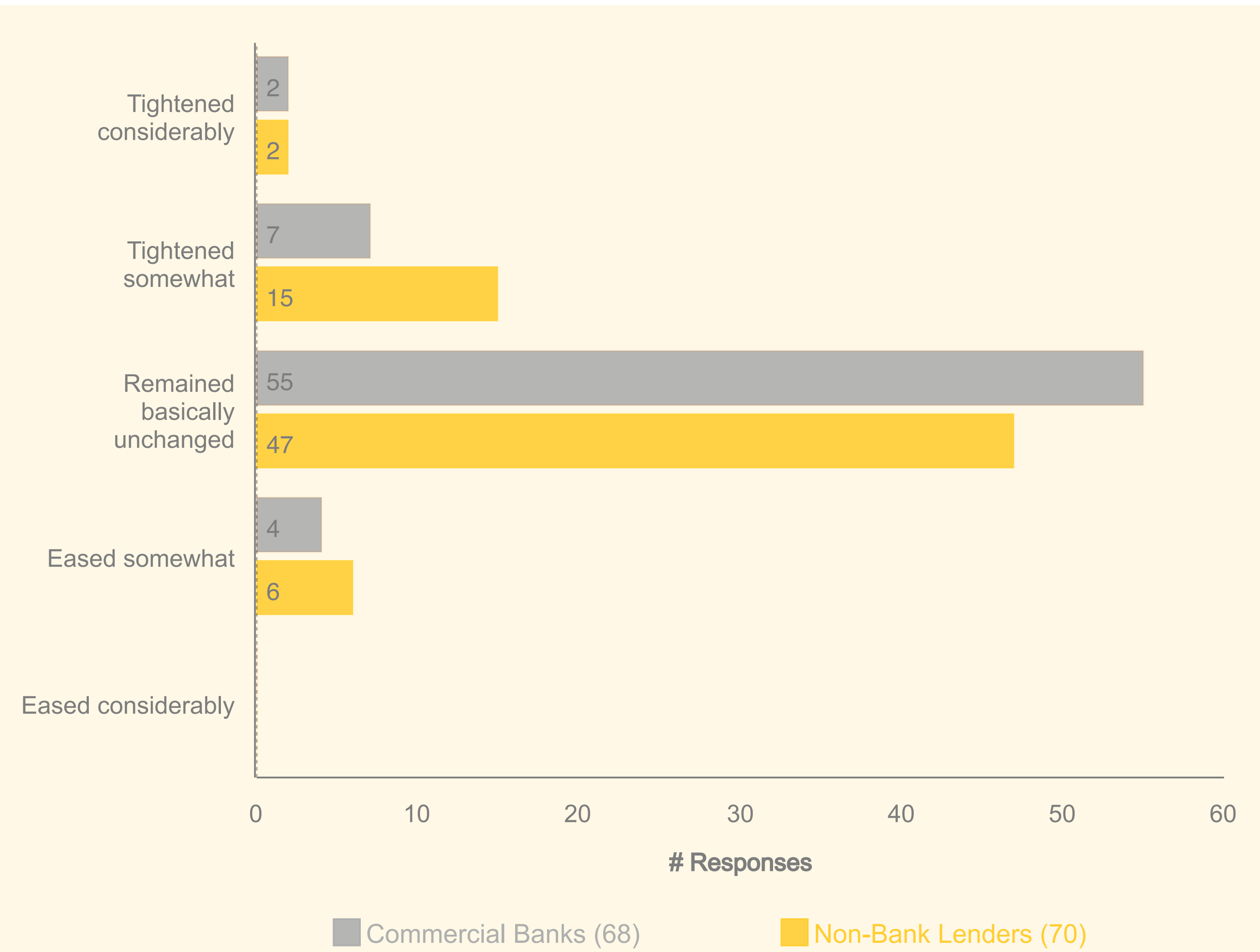
Q3 2020 SURVEY RESPONSES

3. Looking back over the past three months, for applications for C&I loans that your lending institution is currently willing to approve, how have the terms of those loans changed?

Maximum size of loans:



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Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

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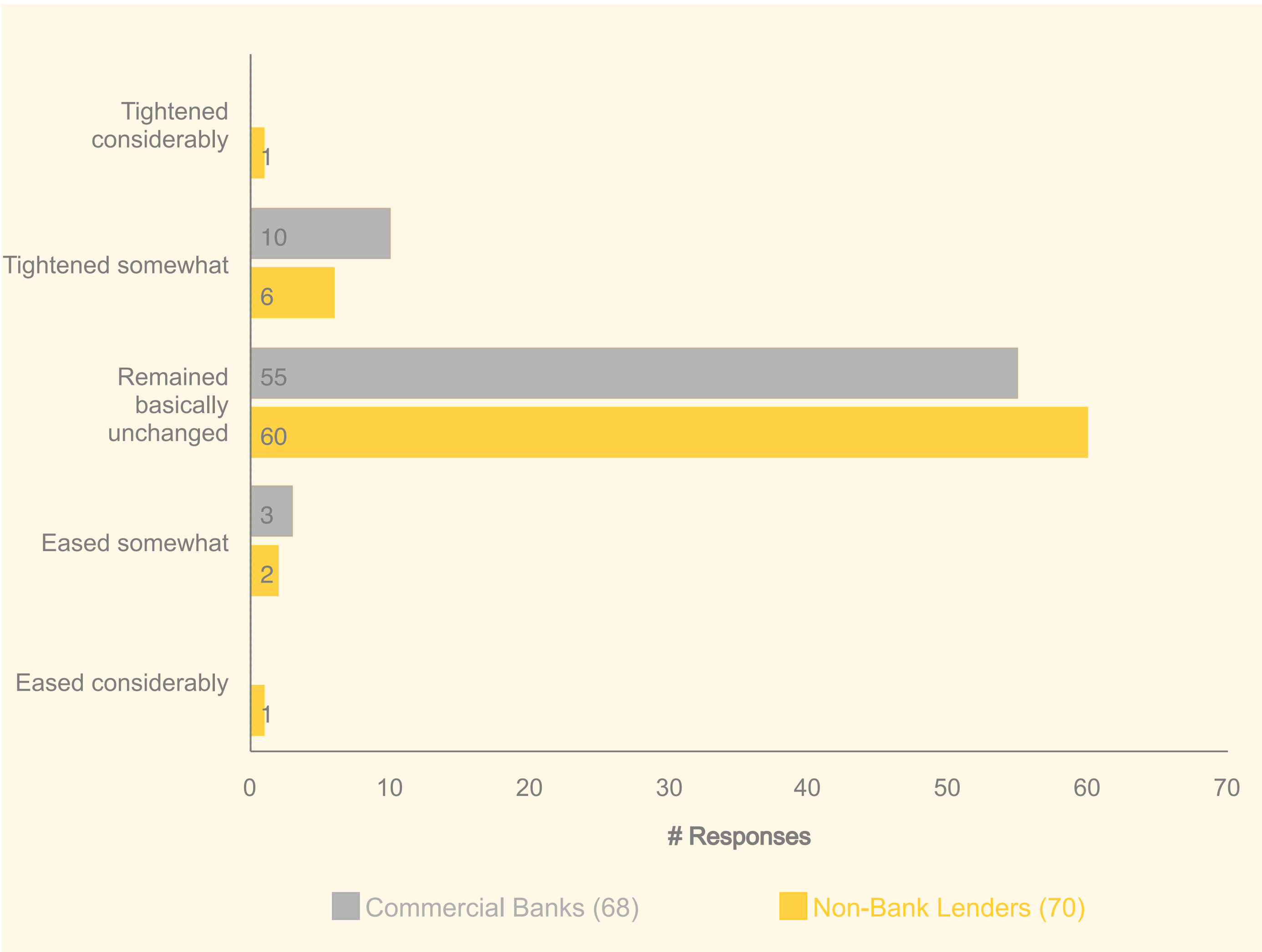
Maximum maturity of loans:



Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

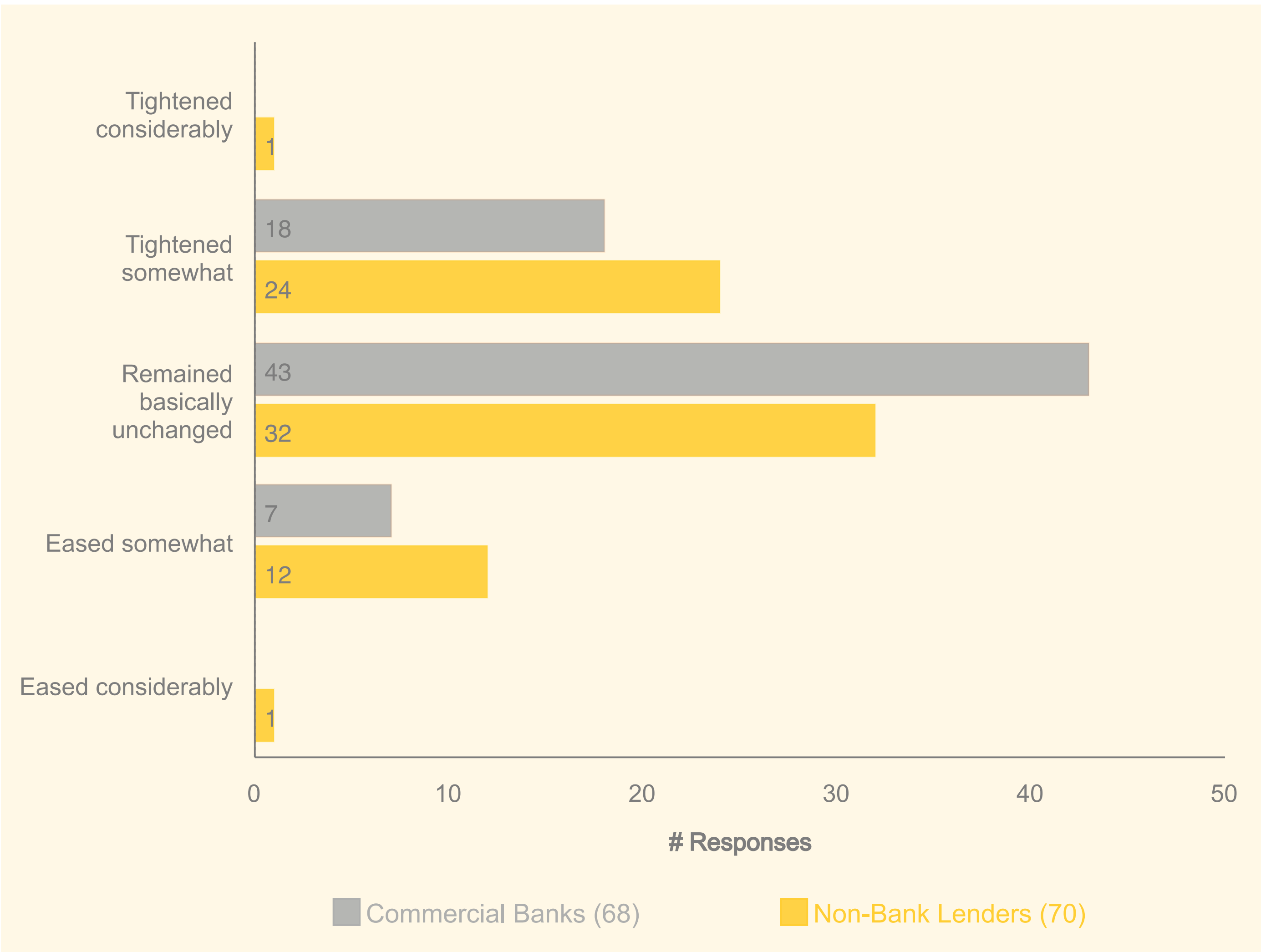
Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

Q3 2020 SURVEY RESPONSES

3. Looking back over the past three months, for applications for C&I loans that your lending institution is currently willing to approve, how have the terms of those loans changed?

Costs of loans:



Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

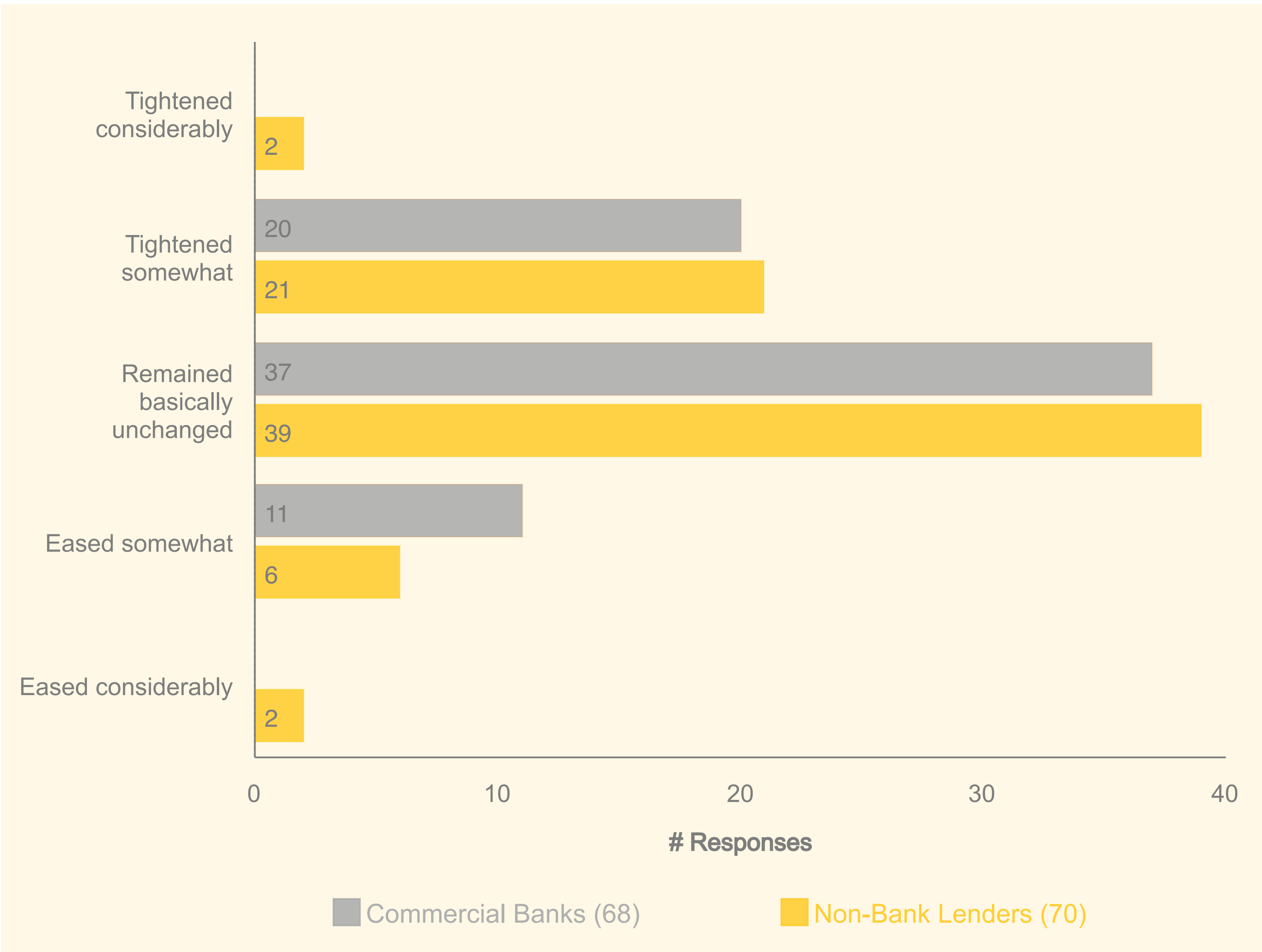
Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

Q3 2020 SURVEY RESPONSES

3. Looking back over the past three months, for applications for C&I loans that your lending institution is currently willing to approve, how have the terms of those loans changed?

Spreads of loan rates over your lending institution's cost of funds (wider spreads=tightened, narrower spreads=eased):



Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

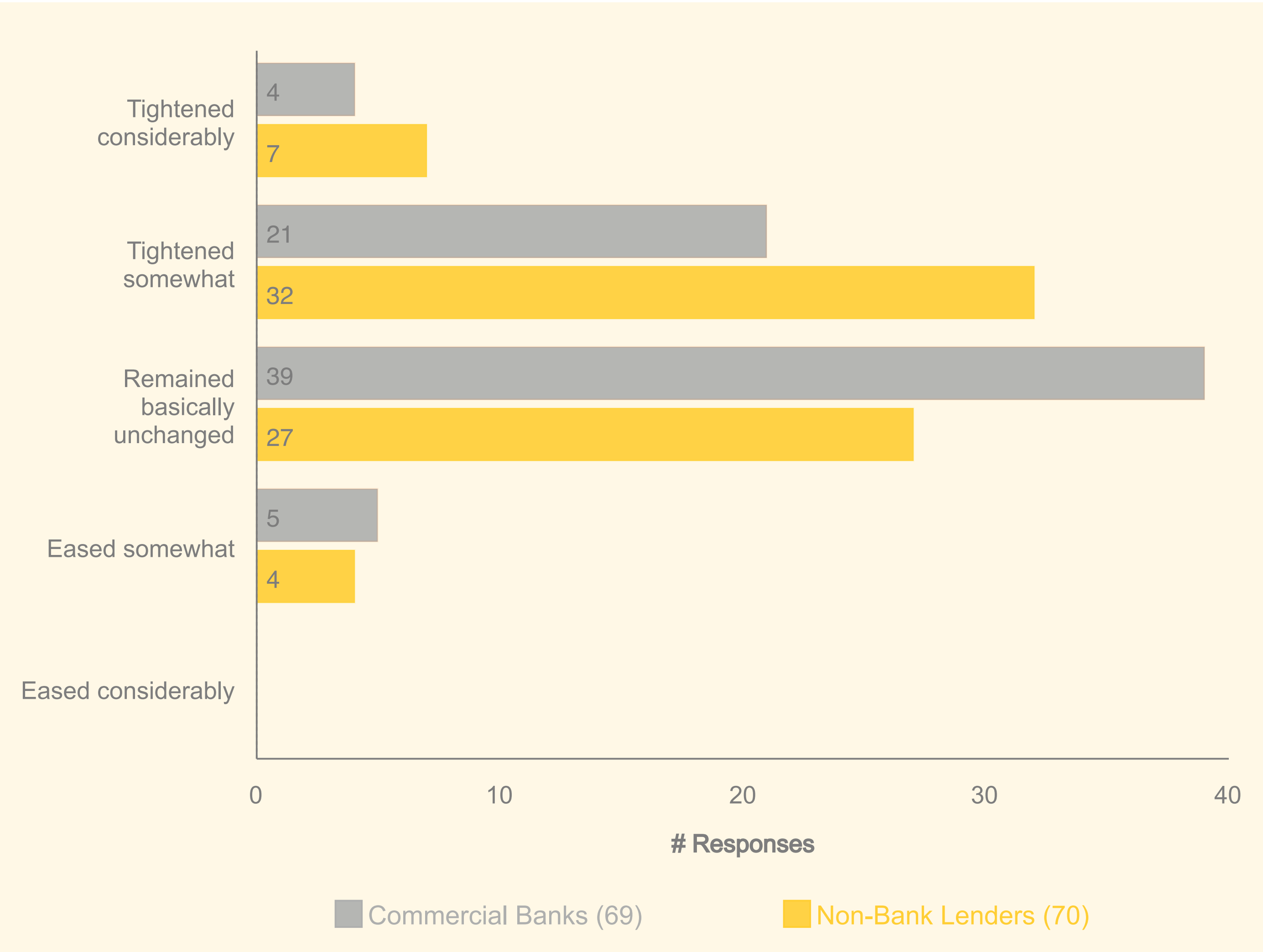
Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

Q3 2020 SURVEY RESPONSES

3. Looking back over the past three months, for applications for C&I loans that your lending institution is currently willing to approve, how have the terms of those loans changed?

Premiums charged on riskier loans):



Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

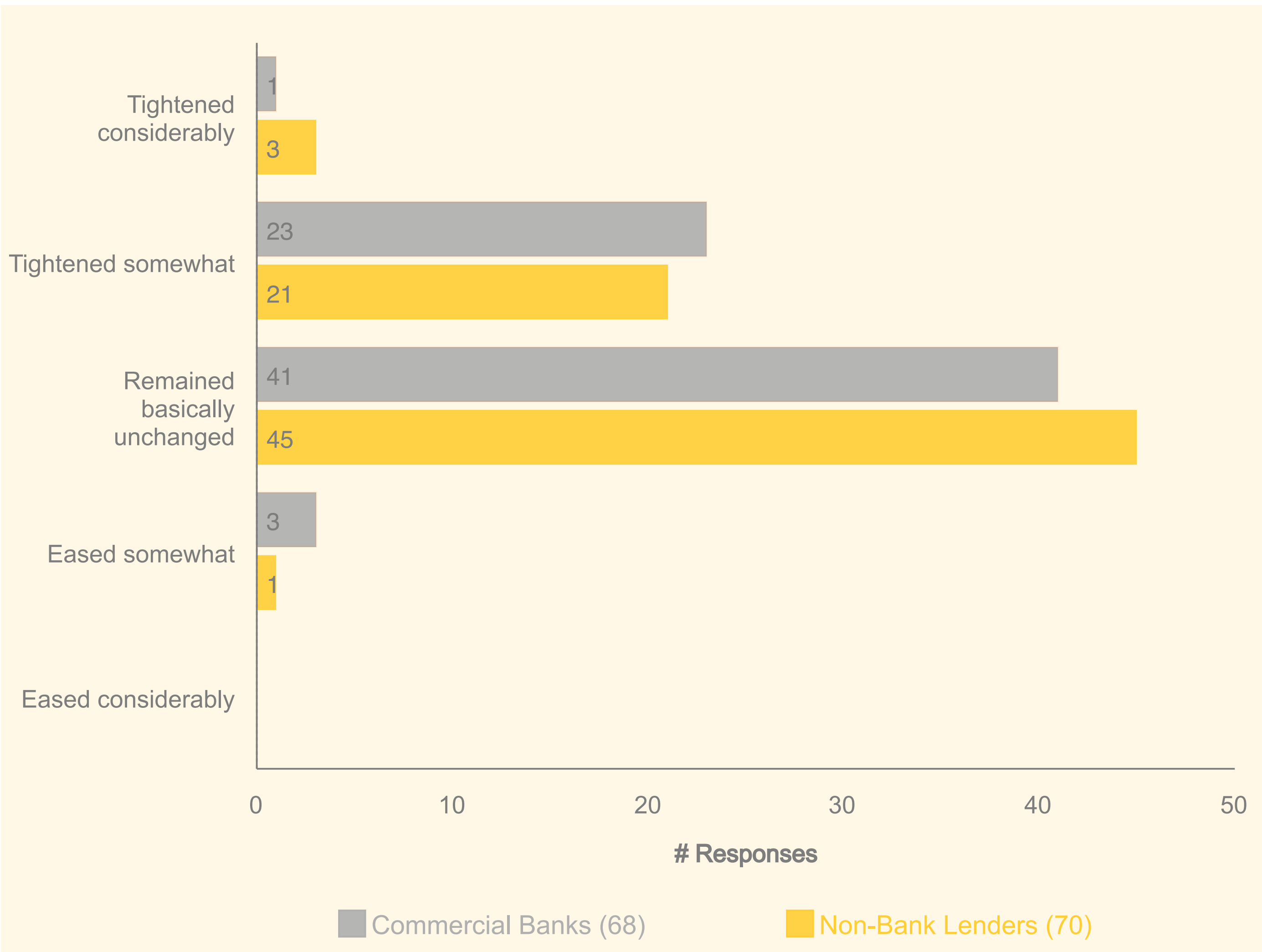
Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

Q3 2020 SURVEY RESPONSES

3. Looking back over the past three months, for applications for C&I loans that your lending institution is currently willing to approve, how have the terms of those loans changed?

Loan covenants:



Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

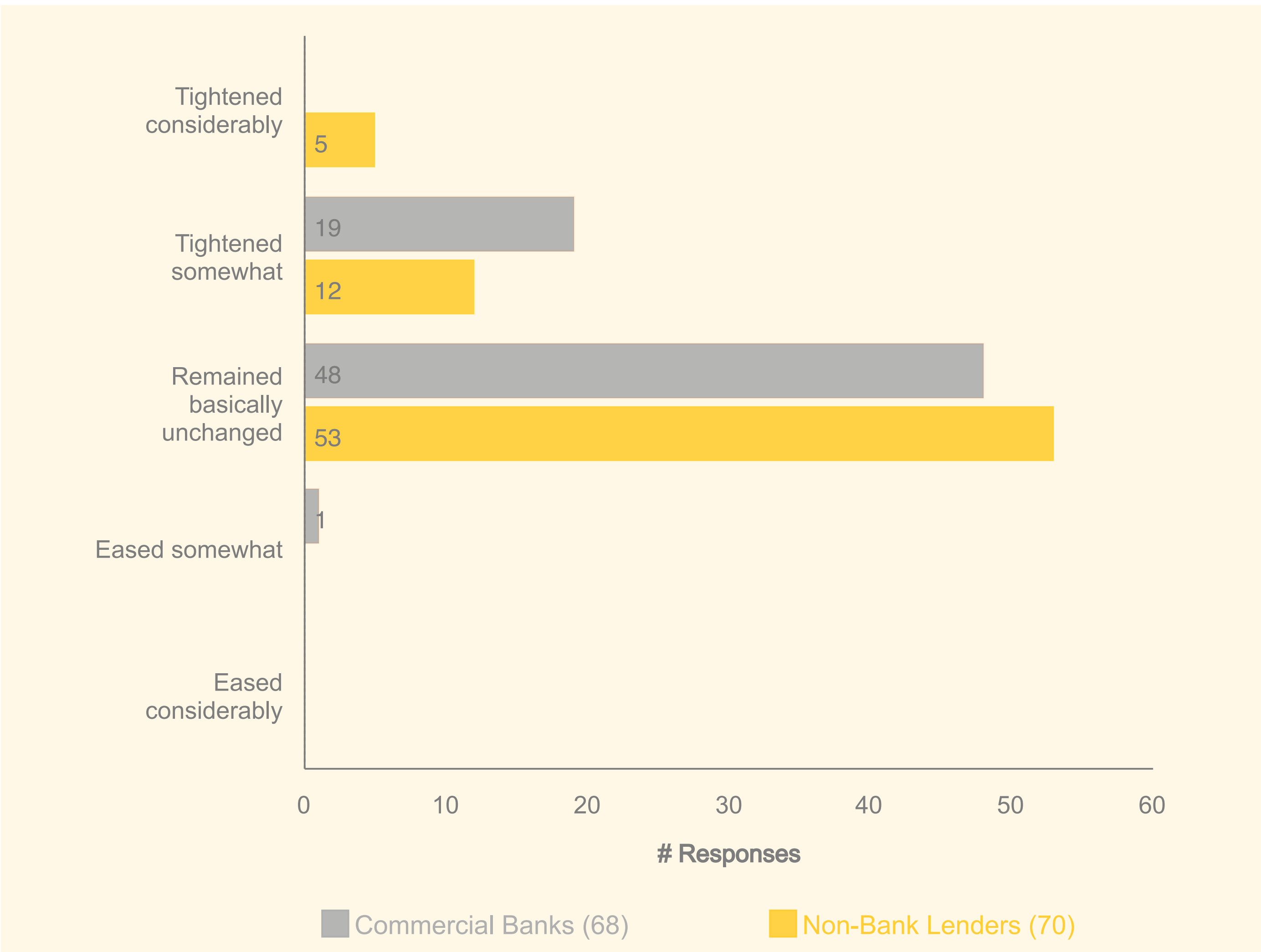
Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

Q3 2020 SURVEY RESPONSES

3. Looking back over the past three months, for applications for C&I loans that your lending institution is currently willing to approve, how have the terms of those loans changed?

Collateralization requirements:



Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

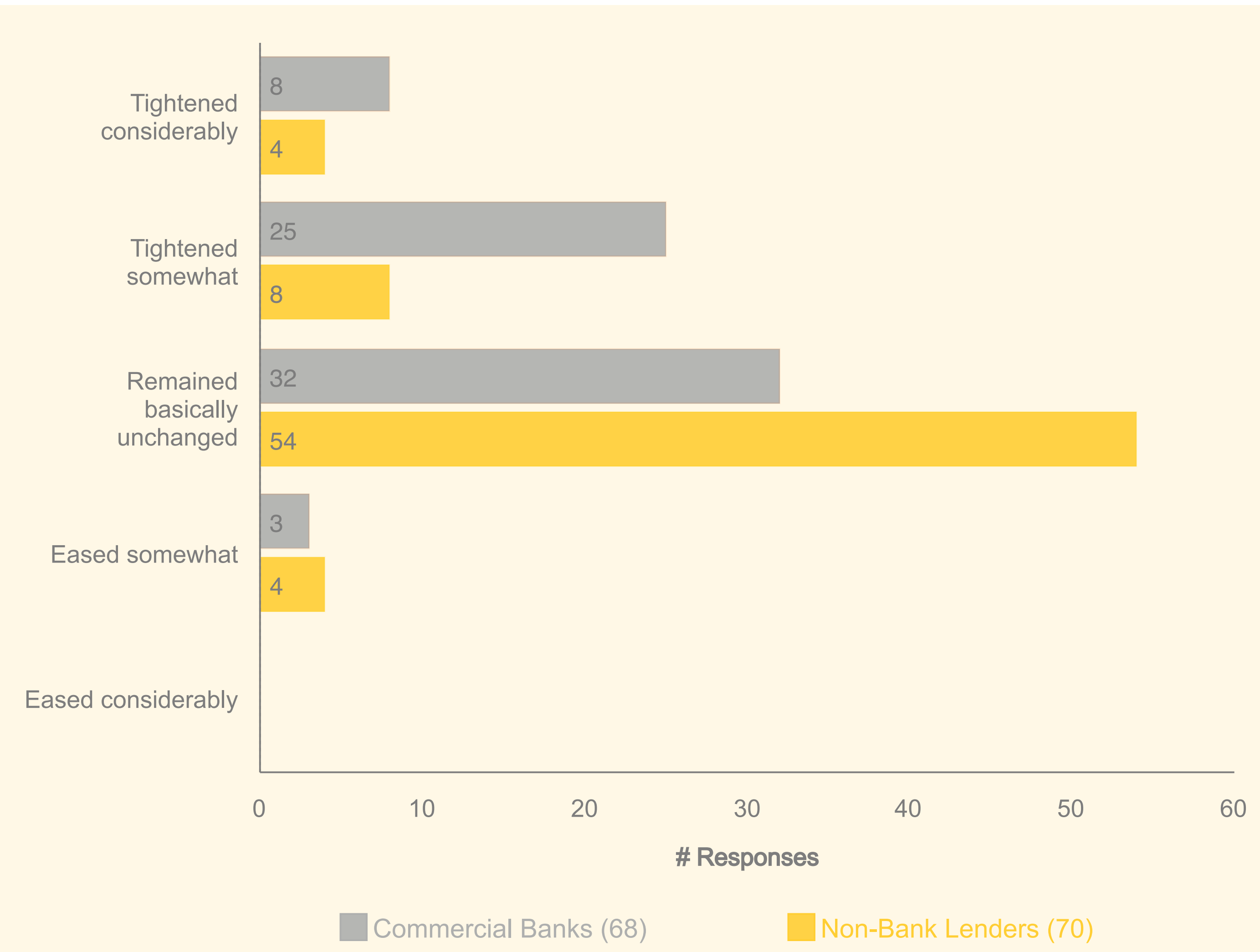
Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

Q3 2020 SURVEY RESPONSES

3. Looking back over the past three months, for applications for C&I loans that your lending institution is currently willing to approve, how have the terms of those loans changed?

Use of interest rate floors (more use=tightened, less use=eased):



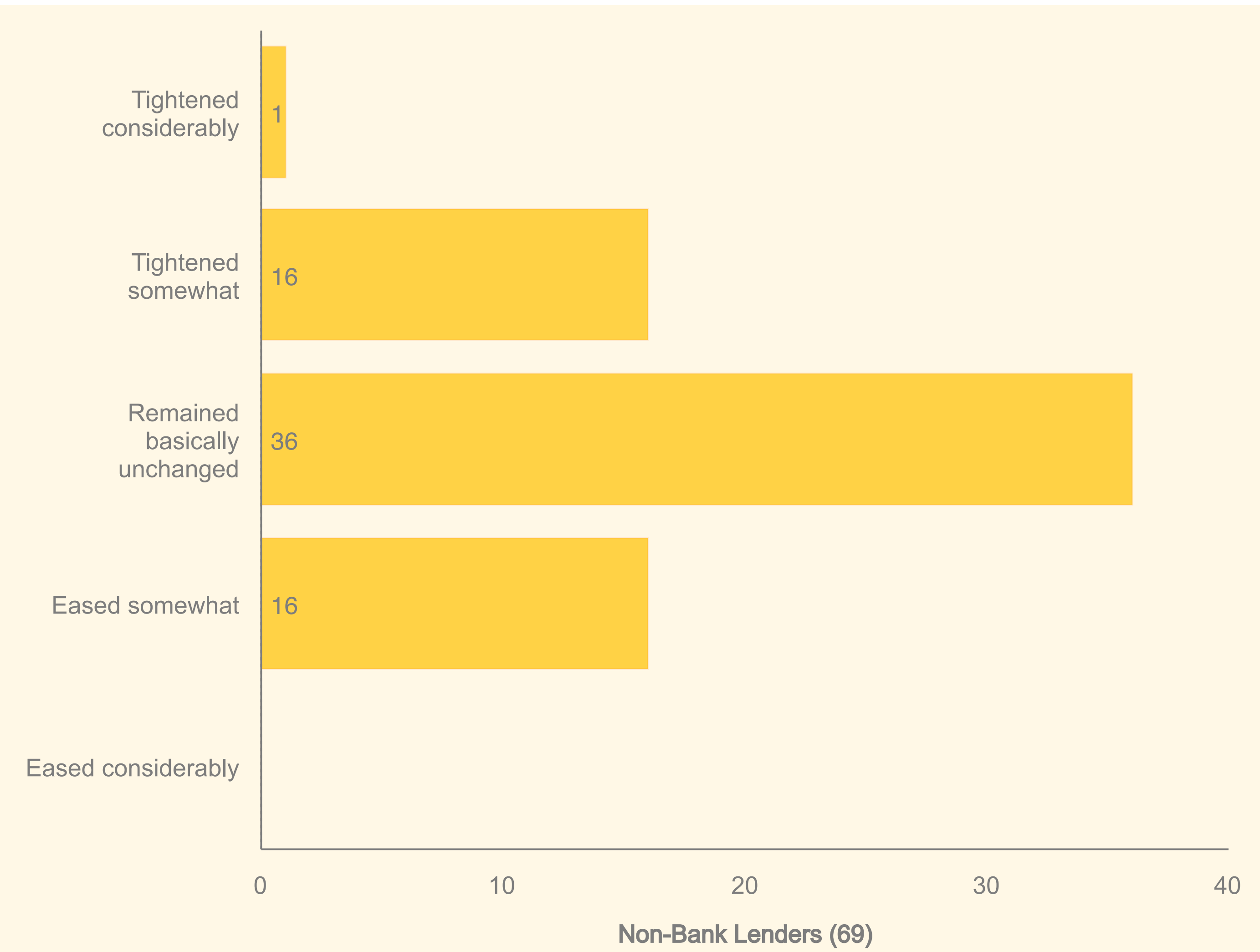
Commercial Bank data is sourced from the Federal Reserve Senior Loan Officer Survey, October 2020

Corresponding Federal Reserve Question

"For applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—from large and middle-market firms and from small firms that your bank currently is willing to approve, how have the terms of those loans changed over the past three months?"

Q3 2020 SURVEY RESPONSES

4. How do you anticipate lending standards for C&I loans at your lending institution to change over the next 6 months, compared to its current standards, apart from normal seasonal variation?

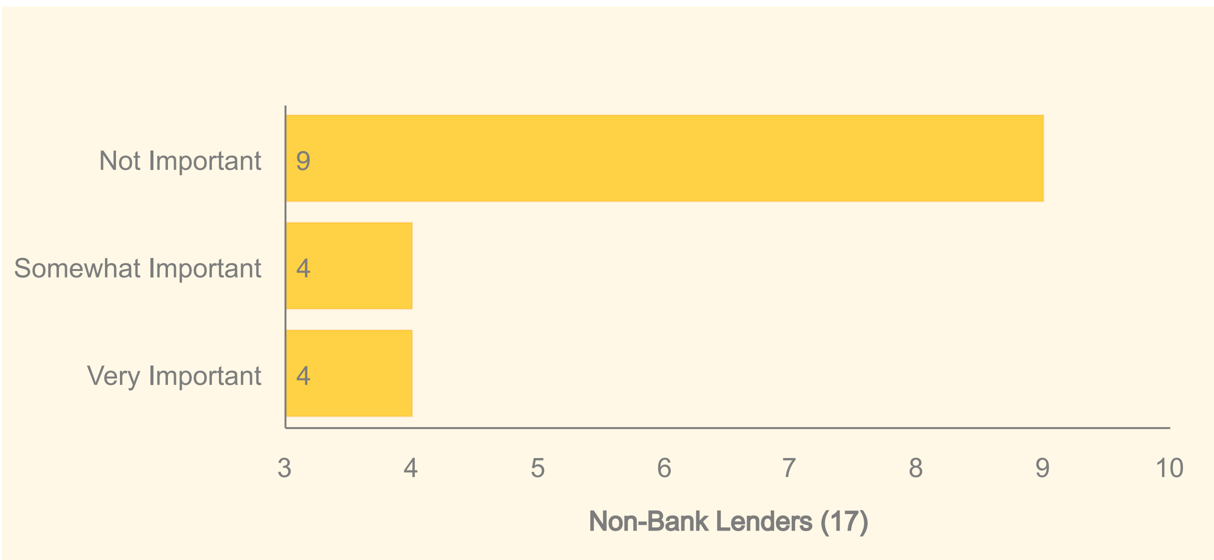


Corresponding Federal Reserve Question
No similar question asked in 3Q20.

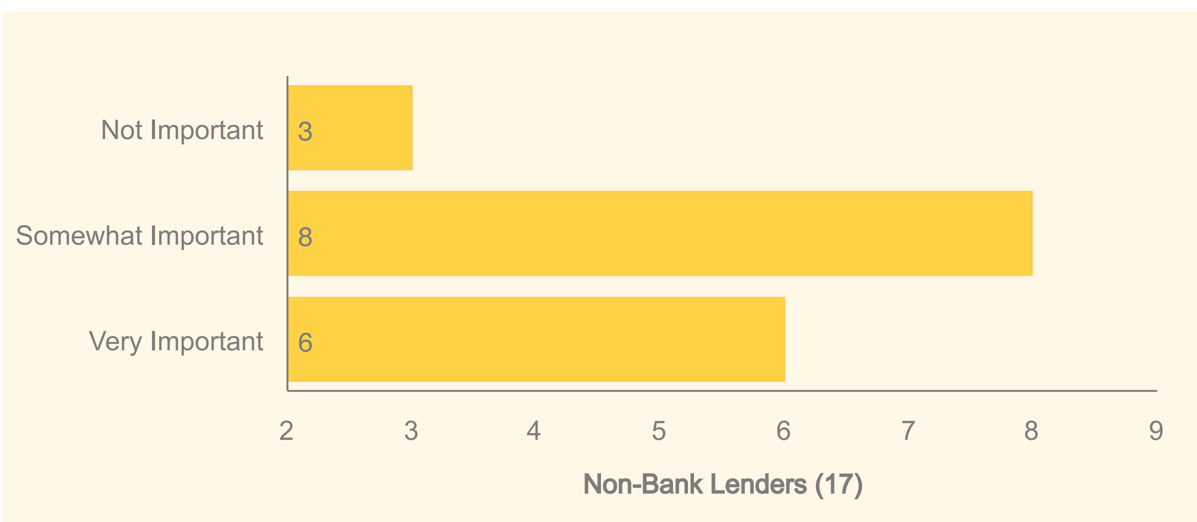
Q3 2020 SURVEY RESPONSES

4a. If you expect your lending institution to tighten its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

Expected deterioration in your lending institution's capital or liquidity position):



Expected deterioration in collateral values:

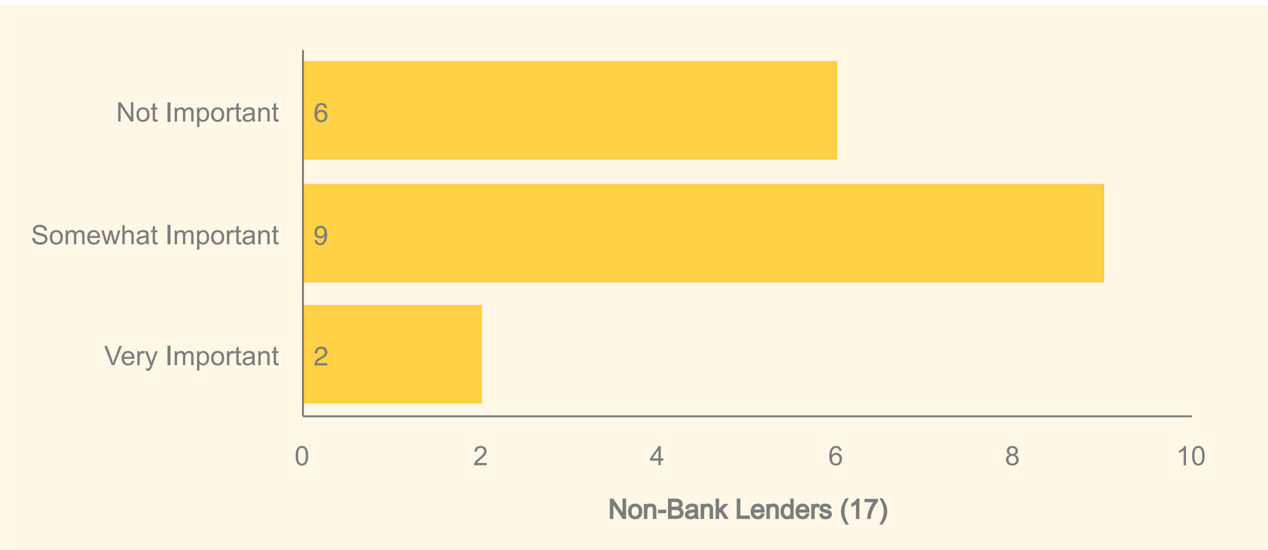


Corresponding Federal Reserve Question
No similar question asked in 3Q20.

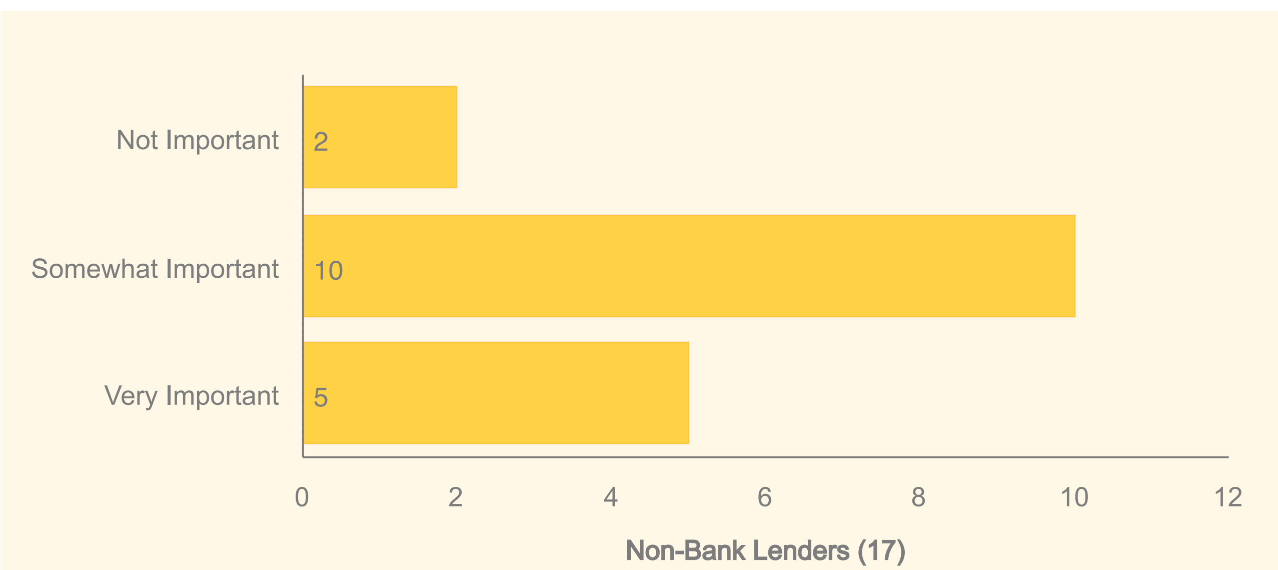
Q3 2020 SURVEY RESPONSES

4a. If you expect your lending institution to <u>tighten</u> its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

Expected reduction in competition from other lenders:



Expected reduction in risk tolerance:

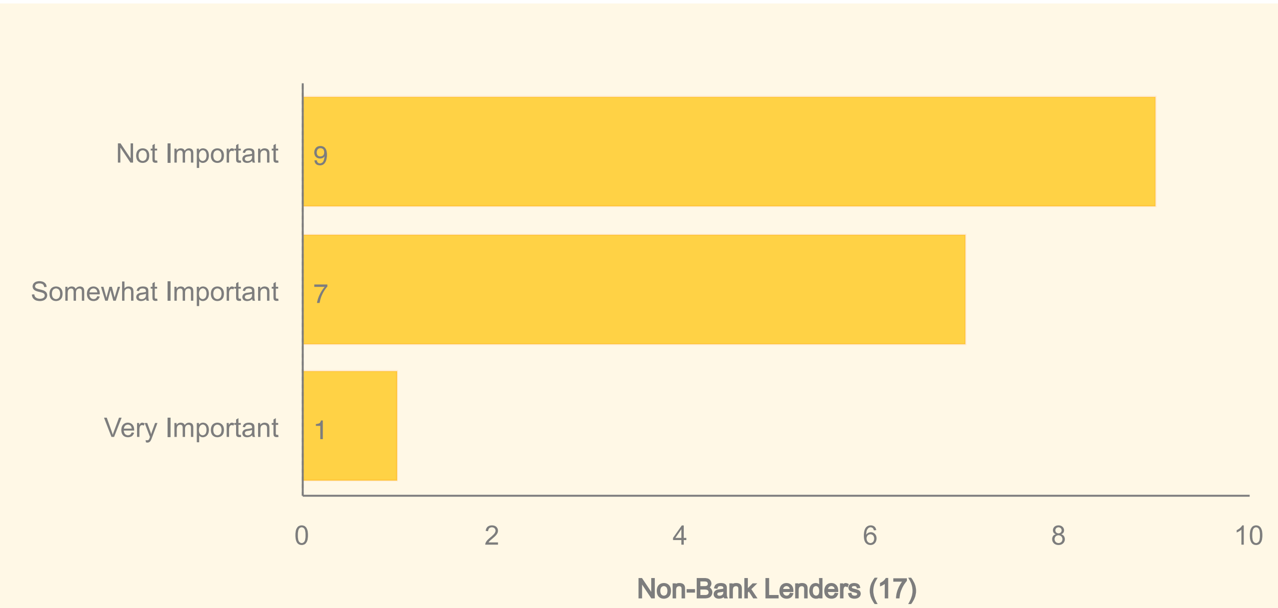


Corresponding Federal Reserve Question
No similar question asked in 3Q20.

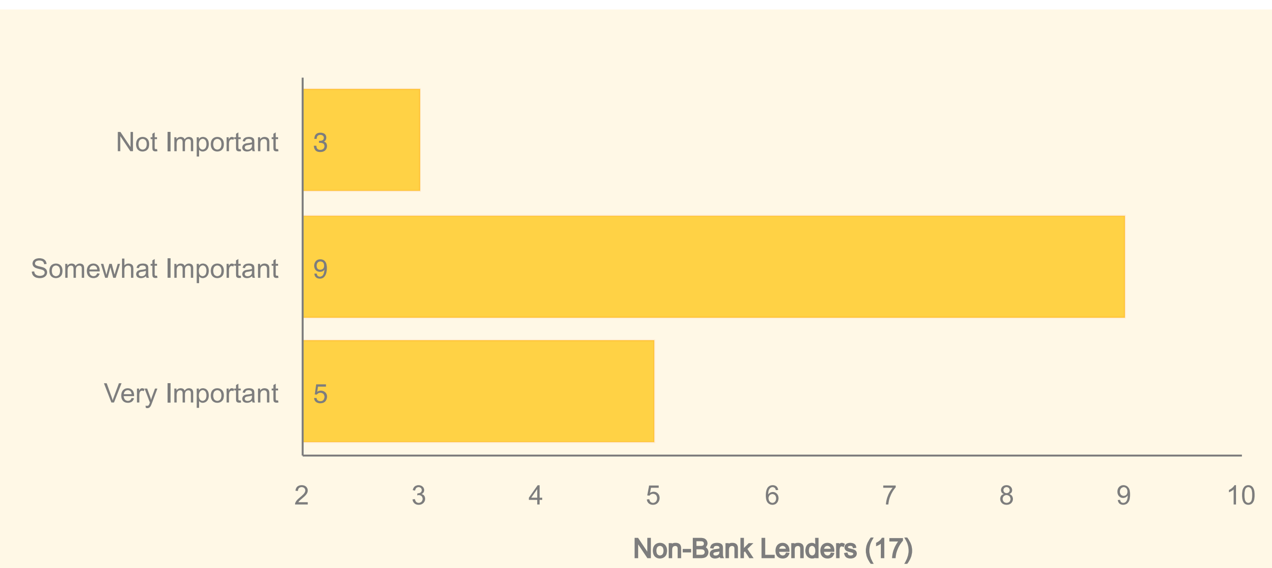
Q3 2020 SURVEY RESPONSES

4a. If you expect your lending institution to tighten its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

Expected reduction in ease of selling loans in secondary market:



Expected deterioration in credit quality of loan portfolio:

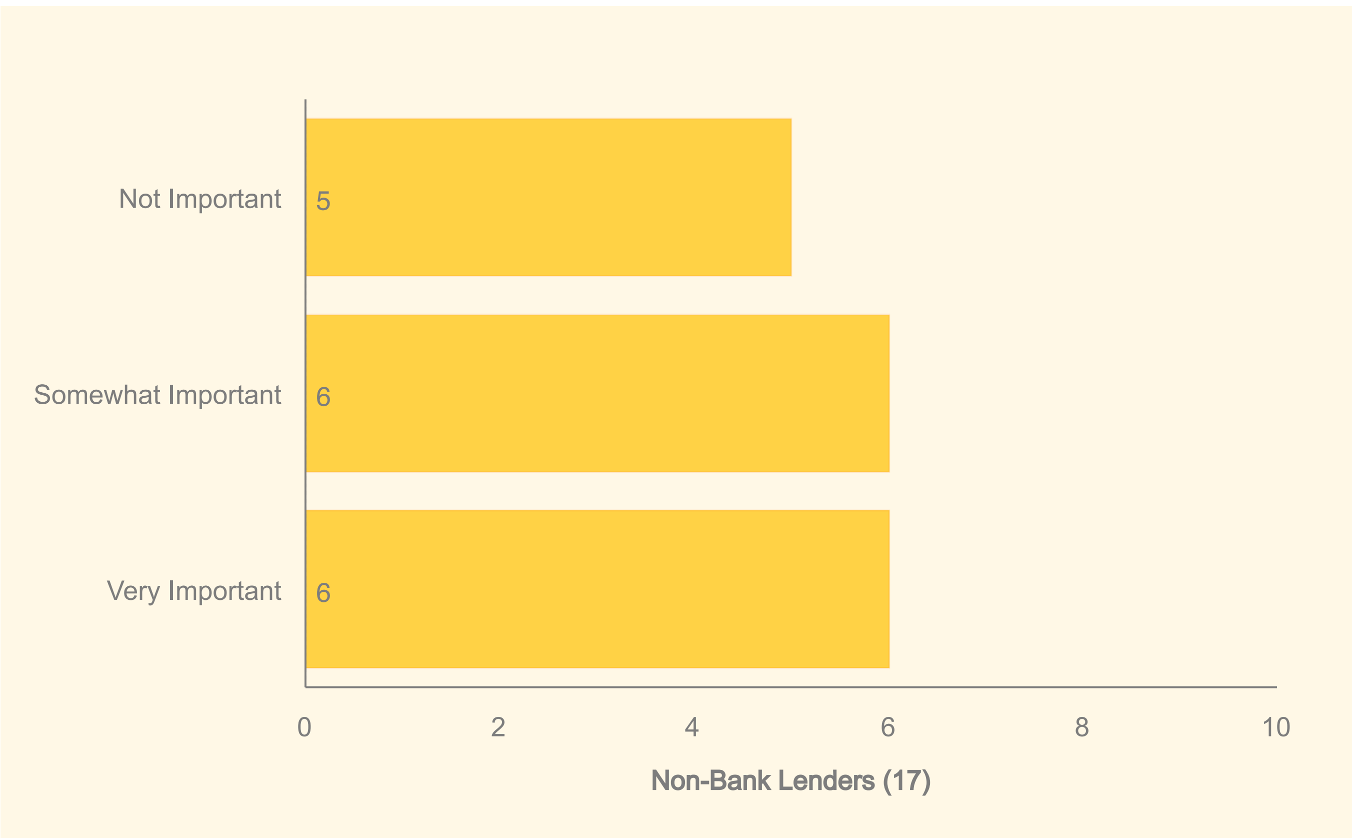


Corresponding Federal Reserve Question
No similar question asked in 3Q20.

Q3 2020 SURVEY RESPONSES

4a. If you expect your lending institution to tighten its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

Increased concerns about the effects of legislative changes, supervisory actions, or changes in accounting standards:

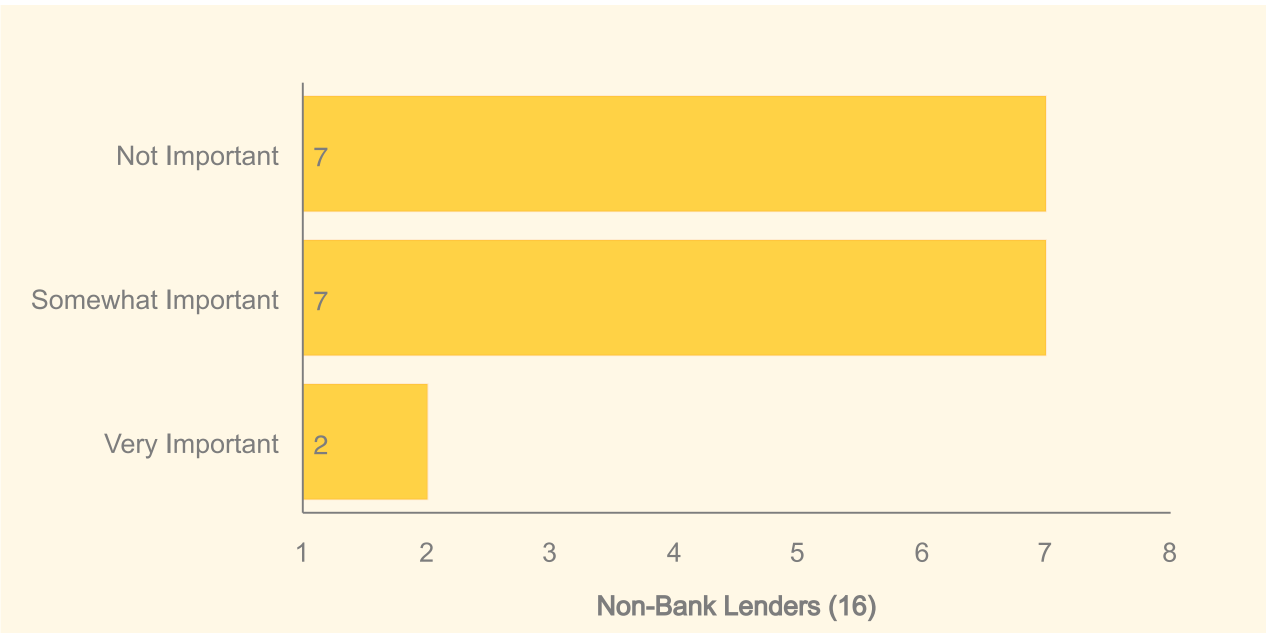


Corresponding Federal Reserve Question
No similar question asked in 3Q20.

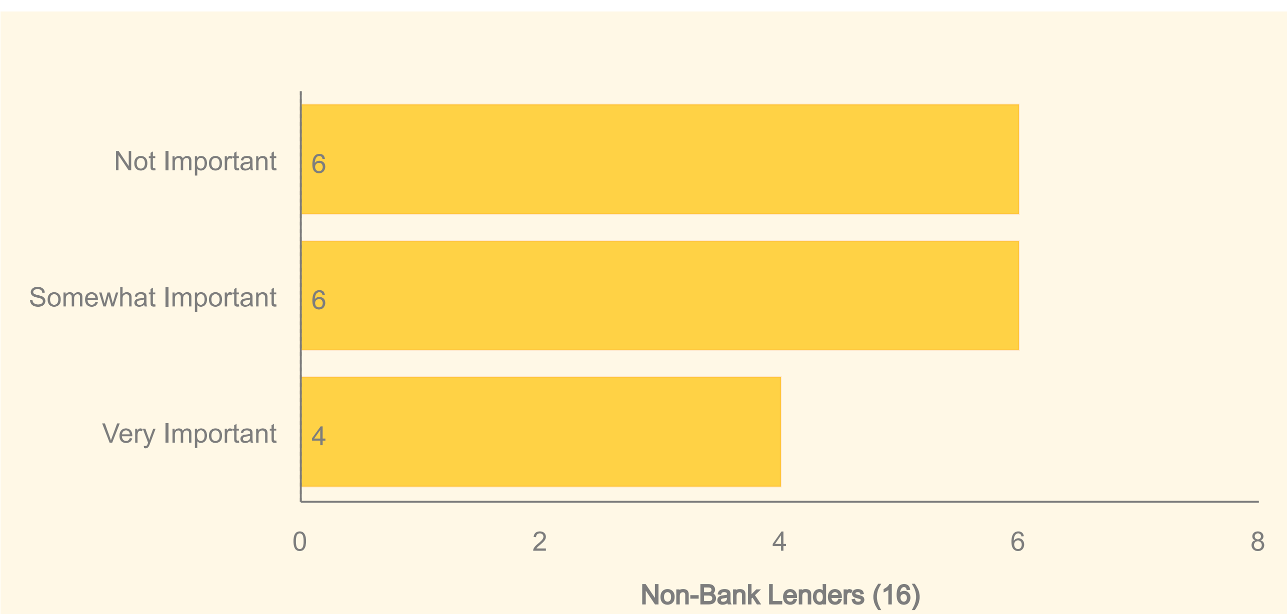
Q3 2020 SURVEY RESPONSES

4b. If you expect your lending institution to <u>ease</u> its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

Expected improvement in your lending institution's capital or liquidity position:



Expected increase in collateral values:

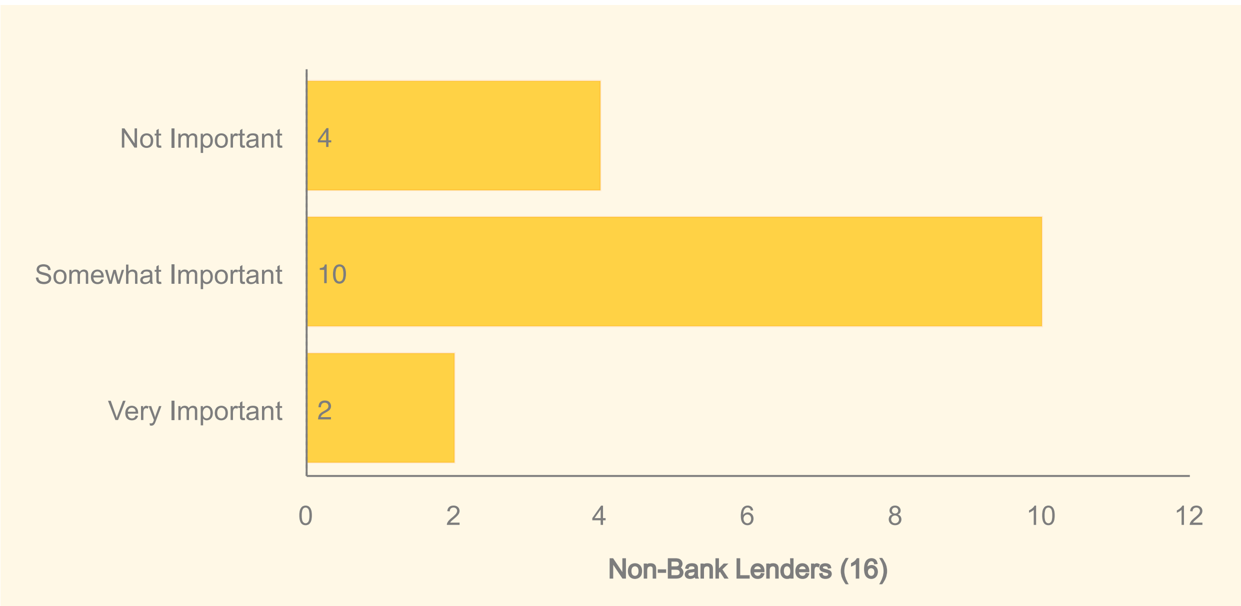


Corresponding Federal Reserve Question
No similar question asked in 3Q20.

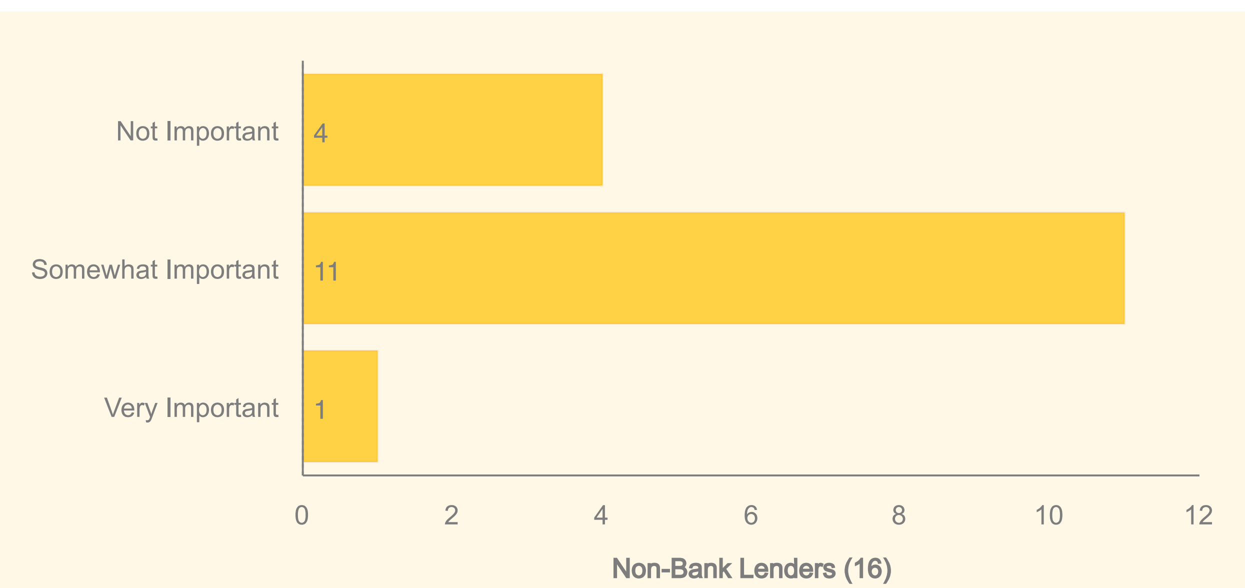
Q3 2020 SURVEY RESPONSES

4b. If you expect your lending institution to <u>ease</u> its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

Expected increase in competition from other lenders:



Expected increase in risk tolerance:



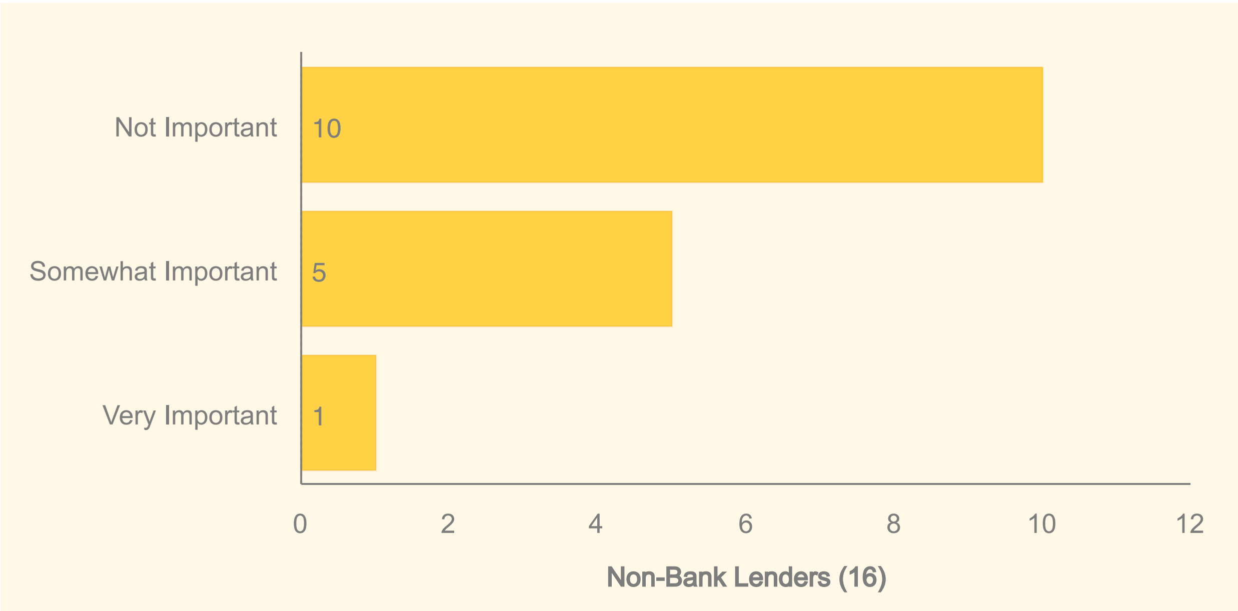
Corresponding Federal Reserve Question

No similar question asked in 3Q20.

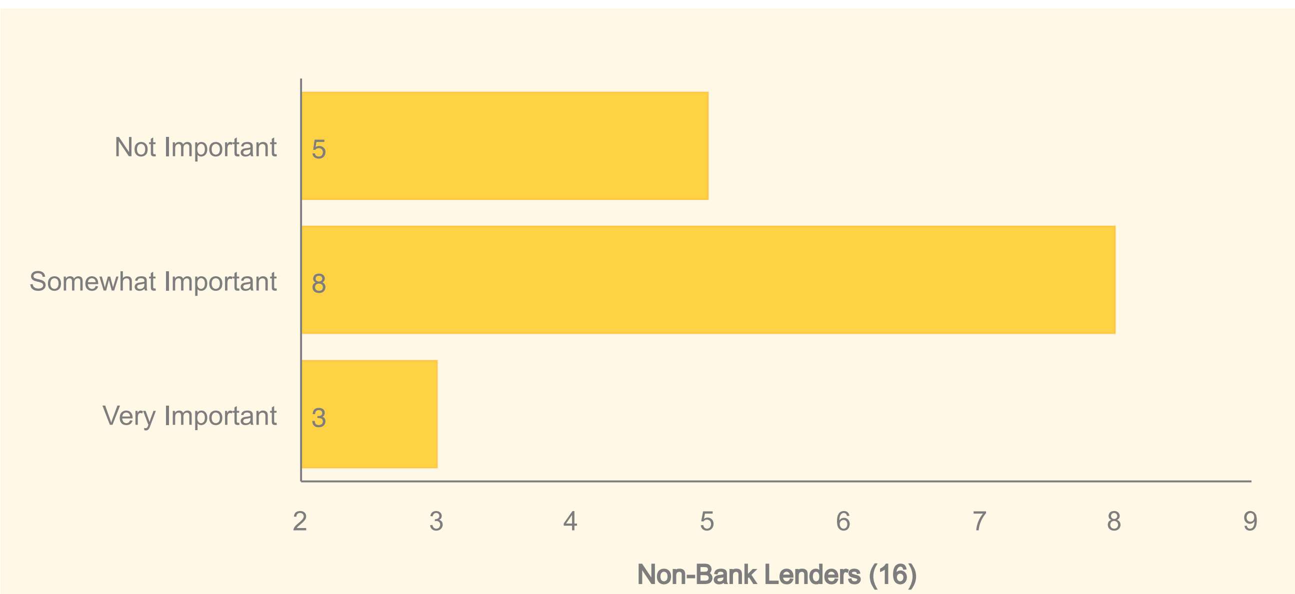
Q3 2020 SURVEY RESPONSES

4b. If you expect your lending institution to ease its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

Expected increase in ease of selling loans in secondary market:



Expected improvement in credit quality of loan portfolio:

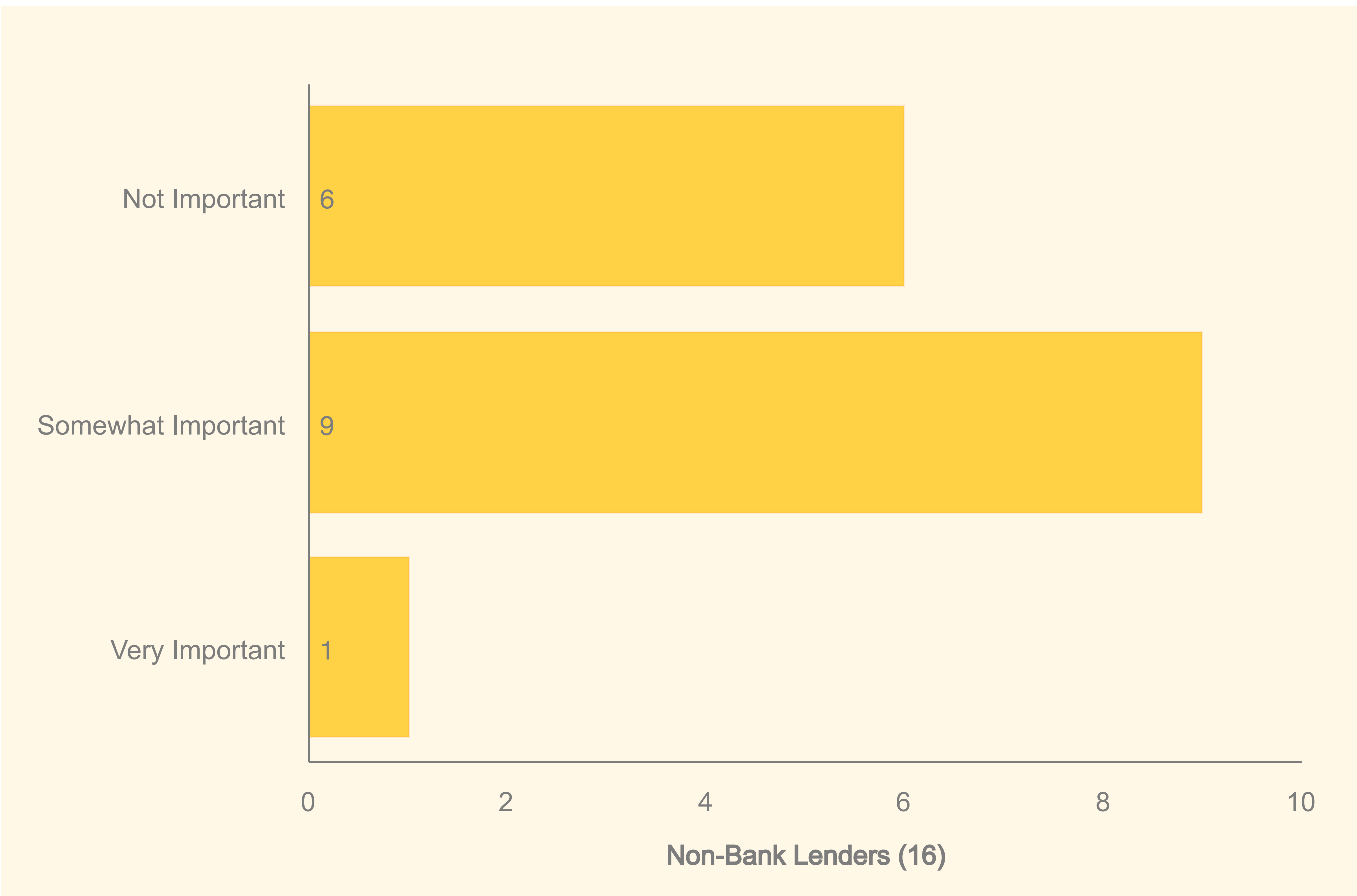


Corresponding Federal Reserve Question
No similar question asked in 3Q20.

Q3 2020 SURVEY RESPONSES

4b. If you expect your lending institution to ease its credit standards for C&I loans, how important are the following possible reasons for the expected change in standards?

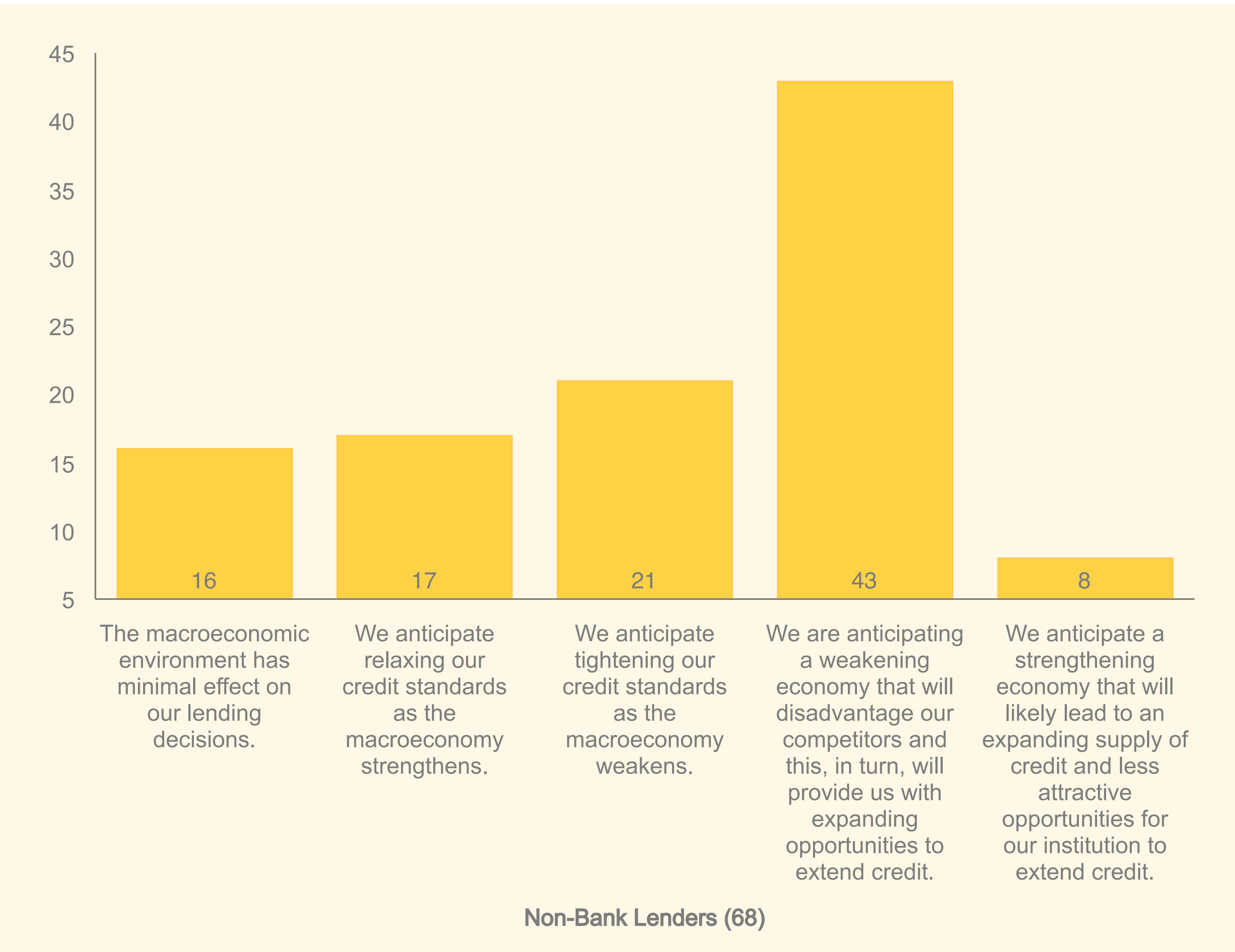
Reduced concerns about the effects of legislative changes, supervisory actions, or changes in accounting standards:



Corresponding Federal Reserve Question
No similar question asked in 3Q20.

Q3 2020 SURVEY RESPONSES

5. Looking ahead over the next six months, how are changes in the macroeconomy likely to impact your lending business? Please check all that apply:

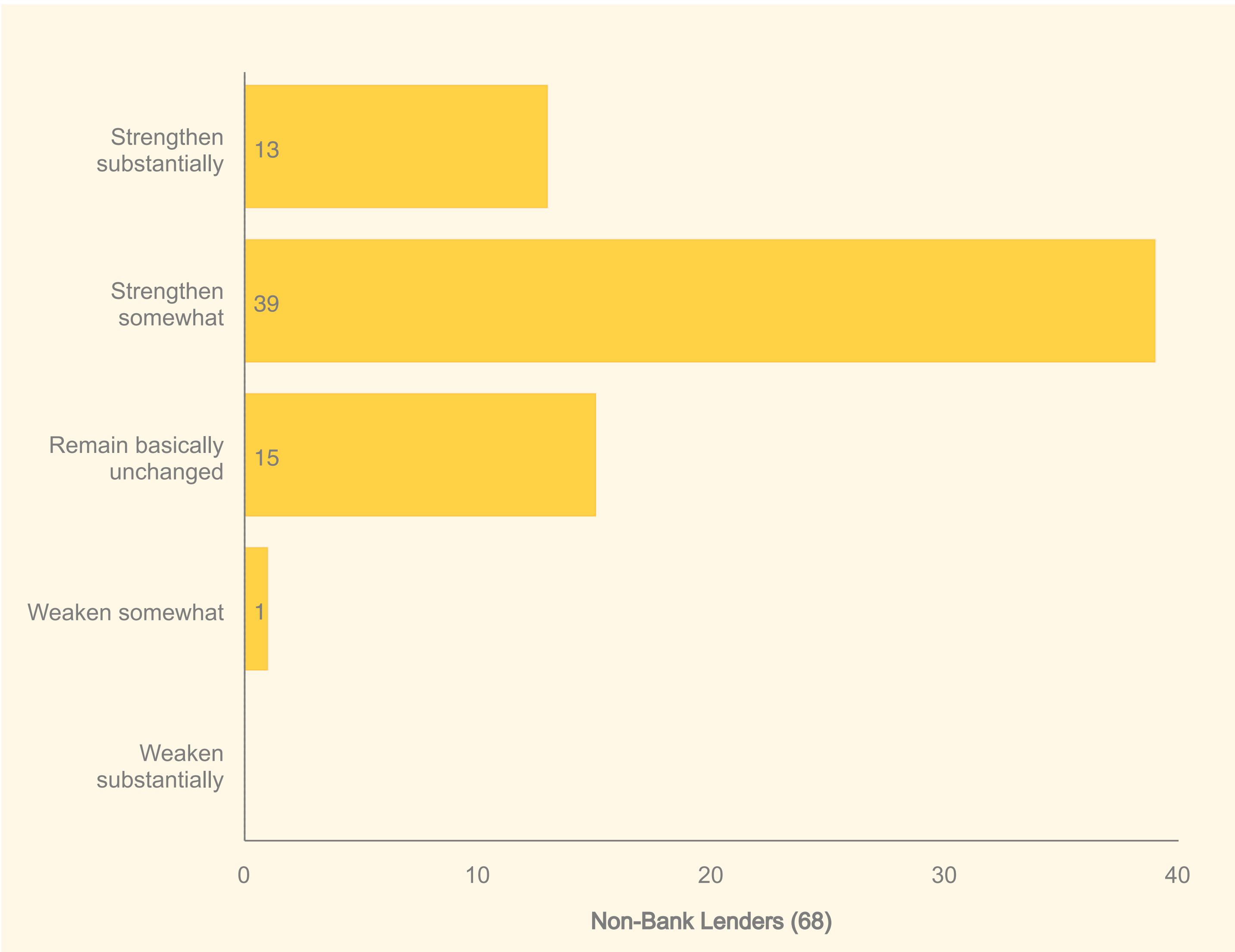


Corresponding Federal Reserve Question

No similar question asked in 3Q20.

Q3 2020 SURVEY RESPONSES

6. Over the next 6 months, how do you expect demand for C&I loans from your lending institution to change compared to its current level, apart from normal seasonal variation?

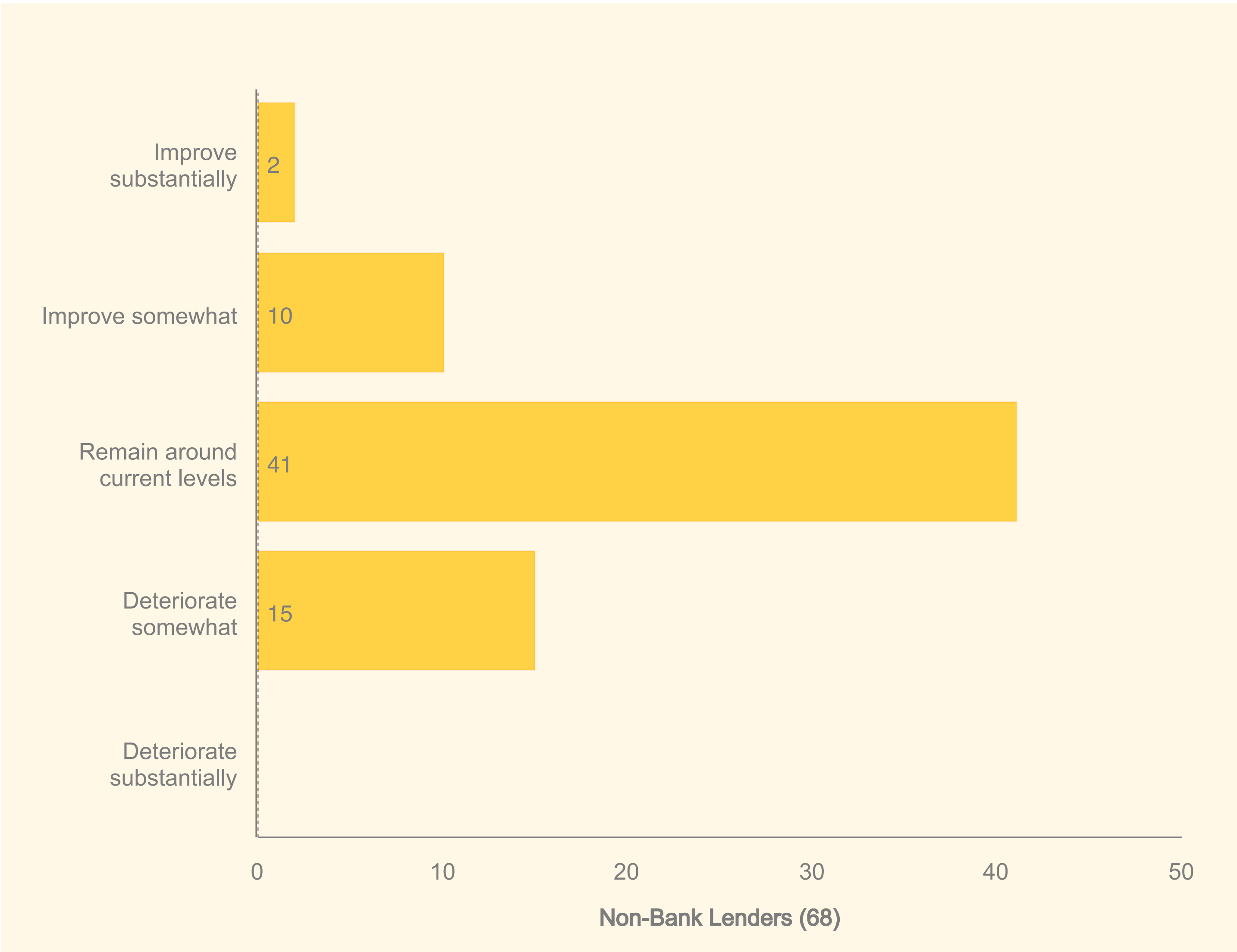


Corresponding Federal Reserve Question

No similar question asked in 3Q20.

Q3 2020 SURVEY RESPONSES

7. Over the next 6 months, what is your outlook for delinquencies and charge-offs on your lending institution's C&I loans?



Corresponding Federal Reserve Question
No similar question asked in 3Q20.

ABOUT CEREBRO CAPITAL

Debt Placement Innovated

Cerebro Capital offers the only data-driven matching algorithm for middle-market corporate borrowers and commercial lenders. Combining the power of technology, streamlined processes, and transactions team expertise, Cerebro offers the greatest certainty that your company will find the right lending partner in the market.

Benefits of the platform include:

- 800+ BANK & NON-BANK LENDERS
- MATCHING ALGORITHMS
- MANAGED RFP PROCESS
- CONFIDENTIALITY & DATA SECURITY
- TRANSACTION & LOAN EXPERTS
- SUCCESS-BASED FEE MODEL

Powered by over 800 bank and non-bank lenders, Cerebro Capital is a data-driven platform purposefully designed to democratize access to credit markets by connecting corporate borrowers and lenders to source corporate loans ranging from $2 million to $100 million. Cerebro has created a holistic corporate loan management solution designed to revolutionize the way borrowers, lenders, intermediaries and stakeholders manage corporate debt. **Contact Cerebro**