



A PARADIGM SHIFT FOR EUROPEAN DEBT

May 2023



Private debt funds are filling the gap left by bank retrenchment, says Sandrine Richard, Head of private debt at Generali Investments Partners*

How would you describe the current mid-market private debt opportunity across Europe?

The markets that we focus on in France, Germany, Italy and Spain are changing deeply. Starting with covid, then the geopolitical situation, the weaknesses in the global banking system, higher inflation, energy prices and interest rates, we have seen a paradigm shift that has created opportunities and points of attention for debt funds and investors. Investing in private debt implies floating rate notes, so increases in base rates are benefiting investors.

Because it is not listed, private debt aims to offer protection against volatility. Private credit also has a key role in supporting the economy and SMEs, while providing protection via lender-friendly documentation, notably financial covenants, which is even more key in the current environment.

As the banks have stepped back from corporate lending that has enabled private debt funds to fill a gap. Banks do have less capacity to lend and their clients still need access to capital, so there is a good opportunity for us to work not in competition but in collaboration with bank lenders. We need to continue to be selective.

Your private debt fund targets SMEs across Europe. What makes SME borrowers attractive, and how can investors tap into the best businesses in this segment?

The direct private debt fund is targeting SMEs in continental Europe, with the option of more opportunistic investments in the UK. The fund focuses on senior secured debt in the most protected part of the capital structure, given the evolution of the market and the challenging macroeconomic environment.

This fund will invest only in floating notes, protecting investors from the increased rates. With an Article 8 classification under the EU's Sustainable Finance Disclosure Regulation (SFDR), the fund

will target companies that are willing to make ESG commitments. The metrics will be bespoke, so that the ESG support can be targeted to the needs of each company. The SME space is attractive from an investor perspective because of the sheer number of opportunities – there are 11.8 million SMEs in our four markets alone, according to European Commission Eurostat data. That volume allows us to be selective, while also providing diversification for

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investors because these companies are unlikely to be listed. Because the finance for each business is small, these are typically bilateral loans which again reduces the potential for overlaps within investor portfolios.

Because direct lenders are in dialogue with shareholders and management teams, they can be long-term financial partners in the development of the business. On ESG, that dialogue puts us in a better position to agree and deliver on a collaborative approach.

Lastly, SMEs are attractive because there is less competition in that space from private debt, with fewer players than there are in the upper mid-cap space.

How does the opportunity set vary across geographies? Where are the most attractive places to deploy capital today?

We see opportunities in all four of the markets that we target through our direct private debt fund. We are a little bit more cautious on the UK, because we think the Brexit impact is not yet fully known. In France private debt is now an option considered by all corporates looking for financing of leveraged buyouts or acquisitions. In Germany, unitranche has been very successful in the last 18 months.



Sandrine Richard

Head of private debt at
Generali Investments Partners*

Sandrine brings to Generali Investments over 25 years of investment and business development experience in the European asset management industry.

Sandrine joins from Muzinich, where she steered the European and French senior secured and private debt strategy in senior leadership roles, contributing to launching and managing private debt funds with robust ESG processes. Prior to that, she covered senior roles at AXA AM, including leading the private debt investment team, and at Exane.

Sandrine holds CESGA (Certified ESG Analyst), CAIA (Chartered Alternative Investment Analyst) and CFAF (Centre de Formation à l'Analyse Financière) certifications, in addition to having achieved an Independent Administrator Executive Master from EM LYON, and a diploma from the Institut Supérieur de Gestion (ISG) Business School.

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Generali European Direct Private
Debt Fund #1

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Italian banks are still active but in the last six months we have seen some senior and mezzanine transactions and are starting to see small unitranche deals. The Spanish market is smaller and quite mature in terms of the different financing options, whether that is bank-only, banks and private debt, senior and mezzanine or unitranche. There are lots of options for Spanish borrowers.

How can lenders build a resilient 'all-weather' approach into their European portfolios in the current macroeconomic environment?

The benefit of closed-end funds in private debt is that we have time to invest. Usually we have three years, so we don't have to hurry and can adjust the pace of capital deployment with our understanding of the risk-return ratio. Having that time allows us to be selective, to conduct deep analysis of investment opportunities and negotiate the best documentation for all parties.

Monitoring is also important to that all-weather approach, ensuring we keep in close dialogue with the company to anticipate and respond when performance erodes. Having local investment teams

in our markets helps with that selection, analysis and monitoring of investments and reduces risk.

Our investment teams and committees also have expertise outside of private debt, so they can share that knowledge to help us build insights on industries, macros and trends that support our selectivity.

Finally, as an Article 8 fund, how do you support SMEs on their ESG journeys? What are the biggest challenges with this for a manager today?

The ESG philosophy is to help portfolio companies enhance their ESG processes. We strongly believe that if a company has better awareness of their ESG strengths and objectives, that creates additional value for investors by developing businesses which promote certain environmental or social characteristics with a greater capacity to repay their debt at par. In order to do that, we leverage ESG regulation and lean on the support and expertise of the PE firm and management team to integrate ESG into the day-to-day business.

Our contribution starts with an analysis of the non-financial aspects of the company to understand their intentions, based on discussion with the sponsor, management team, our investment team and our ESG team at Generali. That multi-party approach helps define and implement the ESG objectives during the investment phase.

During the period that we hold the portfolio companies, our contribution is to offer analysis from external ESG experts based on a short annual questionnaire that monitors progress and shows what still needs to be done. We also track quantifiable KPIs to ensure compliance with our proprietary sustainability due diligence evaluation.

For SMEs, we believe it is really important that we provide support and leverage our capabilities to help management teams – we are all still at the beginning of this journey and collecting the data is a challenge, as is coordinating all the different requests for data from counterparties around the business. The regulatory environment is not yet completely robust and stable, but as it matures these issues will be overcome.

Investment Objective

The Compartment will aim to realise attractive risk-adjusted returns, providing stable income, by investing primarily in euro denominated floating senior secured loans or bonds made to, or issued by European small and mid-sized businesses in accordance with the terms of this Supplement and the requirements of the RAIF Law. The Fund is not a guaranteed product. There is no guarantee that the investment objective will be reached or that investors will reach a return on capital. Investors may risk losing part or all their initial investment (risk of capital loss).

Risks

Risks related to the investment strategy of the compartment: Acquisition of debt through novation via transfer certificate, assignment and participation; Investment in small to medium sized entities; Fixed-income instruments; Lender liability risk; Liquidity in the market for loans; Risks associated with private debt securities; Private debt terms; Unregistered securities; Market risk. General risks of investment: Economic risk; Interest rate risk; Foreign exchange risk; Credit risk; Volatility; Counterparty risk; Operational risk. Please refer to the Risk section of the Issuing Document of the fund for more details about the risks.

ESG Information

SFDR class: Article 8 of Regulation (EU) 2019/2088 on sustainability reporting in the financial services industry. This sub-fund promotes environmental and/or social characteristics, it does not have as its objective a sustainable investment. **ESG strategy:** The Compartment invests with priority in debt instruments issued by Target Companies whose economic activities are in line with certain environmental and/or social characteristics inspired by the UN SDGs such as, for example, mitigating climate change, sustainable use and protection of water resources, creating and maintaining decent employment, protecting human rights and communities, and/or promoting diversity and inclusion. **ESG policy:** Debt instruments amounting to at least 80% of the Total Committed Debt Amount will, at the time of their initial assessment in the Sustainability Due Diligence, have to meet the minimum ESG Rating threshold determined by the Investment Manager for the Compartment. **Promoted criteria:** The "Compartment Exclusions" excludes investments in Target Companies which are involved in unethical business activities such as, for example, (a) serious or systematic human rights violations and/or severe environmental damages, (b) cases of gross corruption and (c) controversial business sectors. **Binding elements of the selection process:** Debt instruments amounting to at least 80% of the Total Committed Debt Amount will have to meet the minimum ESG Rating threshold determined by the Investment Manager for the Compartment. Each Target Company will be screened according to the Compartment Exclusions. **Methodological limits:** Based on the available information collected during the Sustainability Due Diligence, the Investment Manager will assign an overall average rating to each Target Company ("ESG Rating"). Such ESG Rating will, due to the nature of the debt instruments and the limited availability of data, be based on quantitative and qualitative considerations made by the Investment Manager for the individual Target Company. For more information about the ESG criteria, approach, binding elements of the selection process, and methodological limits, please refer to the Issuing Document and its SFDR Pre-contractual disclosure (Annex 1 to Appendix D).

Important Information

This marketing communication is related to **Generali Direct Private Debt Fund**, a Luxembourg partnership limited by shares (société en commandite par actions) qualifying as a reserved alternative investment fund (fonds d'investissement alternatif réservé) formed under the laws of the Grand Duchy of Luxembourg pursuant to the law dated 23 July 2016 on reserved alternative investment funds ("RAIF Law"), and its Sub-Fund **"European Direct Private Debt Fund 1"**, altogether referred to as "the Fund". This marketing communication is intended **only for professional investors** in Italy, France, Austria, Germany and Spain, the countries where the Fund is registered for distribution and where the AIFM is registered for distribution under the AIFMD Directive 2011/61/EU. **It is not intended for retail investors, nor for U.S. Persons** as defined under Regulation S of the United States Securities Act of 1933, as amended.

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