

# Insights

## How TCP Assesses Private Credit Investment Opportunities

October 2023

### Corporate Private Credit Has the Potential to Provide Strong Risk/Return Profile in a Higher for Longer Interest Rate World

During 2023, inflationary pressures have eased from multi-decade highs but remain elevated at above-target levels. Central banks are committed to containing inflation and interest rates are likely to stay higher for longer. Against this backdrop, corporate private credit has the potential to provide an attractive risk/return profile.

We believe that Private Credit will continue to benefit in a world of high benchmark interest rates with its floating-rate yield profile, whilst our security position and strong lender protections aim to offer low volatility against a backdrop of an uncertain economic outlook.

We take a closer look at one of our recent transactions to illustrate how we approach deal selection and underwriting – the foundations of constructing a portfolio that provide investors with consistent cash returns and downside protection.<sup>1</sup>

### TCP's Differentiated Origination Capability: How Did We Originate the Deal?

The investment involved providing debt financing to facilitate the merger of two of the market leading debt collection businesses to create the second largest player in Australia. The business provides agency collection services (not purchasing debt ledgers) on behalf of clients that include major government departments (such as the ATO and Services Australia) and blue-chip corporates (such as major telcos).

TCP was able to secure the investment opportunity due to the strength and experience of the team that enjoy key competitive advantages in originating high quality investments:

**Deep market relationships:** TCP team members had a long-standing relationship with the Sponsor, and had provided financing for the business previously. This familiarity provided the Sponsor and the Borrower comfort in approaching TCP to provide the financing. It also demonstrates our differentiated origination capabilities, with the ability to generate proprietary deal flow via our long-standing market relationships

**Speed and certainty of execution:** Through our previous dealings with the Sponsor and our strong reputation in the market, the Borrower had confidence that TCP would deliver the financing in a timely manner and provide certainty for the transaction, in what was a tight deal timeline

Once mandated on the financing, TCP was able to lead the execution of the financing which provided us with the ability to negotiate the appropriate terms and conditions.

## **TCP's Rigorous Due Diligence: What Did We Like About the Deal?**<sup>1</sup>

### *A leading, defensive business with strong management team:*

- Top 2 external debt collection business in Australia with a high quality management team and supported by experienced Sponsor
- Anti-cyclical industry as debt collection activities would actually increase if there was a significant economic downturn or recession
- High barriers to entry given regulatory requirements on operational processes
- Diversified, blue-chip client base including government departments, telcos, and insurers, often with multi-decade long relationships

### *Significant equity buffer:*

- Private Equity Sponsor contributed significant equity capital of two-thirds of the overall capital structure, which means there is a large buffer sitting underneath our senior secured debt investment
- Moderate leverage (Debt/EBITDA) off a structural low point in earnings (given collection activity had effectively been turned off during the Covid period)

### *Strong cash flow generation:*

- Stable earnings base with minimal capex and low working capital requirements underpins high free cash flow generation
- Increasing demand for debt collection services in an economic downturn
- Strong debt serviceability with more than four times interest cover

### *Capital preservation via downside protection:*

- Senior Secured ranking and all asset security ensures that we get repaid first
- Two maintenance financial covenants providing an early warning trigger for any earnings deterioration (Net Leverage Ratio and Interest Coverage Ratio)
- Documentation protections including cash flow sweeps and restrictions on ability to make acquisition and disposals, and not allowing distributions to shareholders until leverage has been reduced

### *Attractive, consistent yield:*

- Deal is priced with an all-in current yield of >10.0% given relatively low levels of competition from other lenders in this segment of the market
- Consistent cash income from Borrower via quarterly interest payments
- Interest rate is floating rate, providing an inflation hedge, with capital value not at risk from duration risk

## **TCP's Risk Management Process: How Are We Monitoring the Deal?**

The TCP Investment Committee meets on a monthly basis to review the performance and rating/valuation of every investment in the portfolio.

Consequently, we have been carefully monitoring the performance of the investment on a monthly basis using updated financial information from the Borrower and various industry updates. To date, the investment has performed in-line with our expectations and remains compliant with all covenants.

## **Potential Benefits of Private Credit for Investors**

TCP has built a diversified portfolio of defensive, cash generative credits that share many of the characteristics discussed above in the TCP Private Debt Income Fund.

The Fund offers investors stable cash income with an attractive risk-return profile, strong investor protections, low correlation with public markets whilst the floating return profile provides a natural hedge against inflation / interest rate movements.

Our outlook for Private Credit is constructive as the "higher-for-longer" interest rate environment will enable lenders such as TCP to demand higher returns, lower leverage and tighter terms and conditions.

## About Tanarra Credit Partners

Tanarra Credit Partners (“TCP”) is an Asia-Pacific private credit specialist with offices in Sydney, Melbourne, Wellington and Hong Kong. TCP’s senior investment team has 100 years of combined global credit markets experience.

Since inception in 2017, TCP has grown to manage over \$780 million of investor capital and has an excellent record of originating and structuring leveraged finance transactions across the Asia-Pacific region.

TCP is the credit vertical of Tanarra Group, diversified alternative asset investment firm, headquartered in Australia, with A\$3 billion in assets under management.

### Tanarra Credit Partners Senior Management



**Peter Szekely**  
Managing Partner



**Graham Lees**  
Managing Director



**Peter Han**  
Managing Director

## For more information about the TCP Private Debt Income Fund, speak to a GSFM Account Manager:

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1. Past performance should not be taken as an indicator of future performance. returns are not guaranteed.

Equity Trustees Limited (“Equity Trustees”) (ABN 46 004 031 298), AFSL 240975, is the Responsible Entity for the TCP Private Debt Income Fund (“the Fund”). Equity Trustees is a subsidiary of EQT Holdings Limited (ABN 22 607 797 615), a publicly listed company on the Australian Securities Exchange (ASX: EQT).

The Investment Manager for the Fund is Tanarra Credit Partners Pty Ltd (“TCP”) ACN 114 164 331, as an authorised representative of Tanarra Capital Australia Pty Ltd (ACN 114 164 331) AFSL No. 290098. This publication has been prepared by TCP to provide you with general information only. In preparing this information, we did not take into account the investment objectives, financial situation or particular needs of any particular person. It is not intended to take the place of professional advice and you should not take action on specific issues in reliance on this information. Neither TCP, Equity Trustees nor any of its related parties, their employees or directors, provide and warranty of accuracy or reliability in relation to such information or accepts any liability to any person who relies on it and each such person disclaims all responsibility and liability for any loss or damage in relation to this document (including without limitation, liability for negligence). Past performance should not be taken as an indicator of future performance. You should obtain a copy of the Product Disclosure Statement before making a decision about whether to invest in this product.

In making any investment decision in relation to the Fund, each prospective investor should consider whether the investment is suitable to its own individual circumstances, and is urged to consult with its own qualified advisors with respect to the legal, tax, regulatory, financial and accounting consequences of investing in the Fund.

No person guarantees the performance of the Fund, a rate of return from the Fund, or the repayment of capital from the Fund. A purchase of interests in the Fund will involve a high degree of risk due, among other things, to the nature of the Fund’s investments. Any forward-looking statements included in this document may prove to be inaccurate and should not be relied upon as indicative of future matters. There can be no guarantee that targets or objectives set out in this document will be met.

TCP Private Debt Income Fund’s Target Market Determination is available <https://swift.zeidlerlegalservices.com/tmds/ETL4900AU>. A Target Market Determination describes who this financial product is likely to be appropriate for (i.e. the target market), and any conditions around how the product can be distributed to investors. It also describes the events or circumstances where the Target Market Determination for this financial product may need to be reviewed.