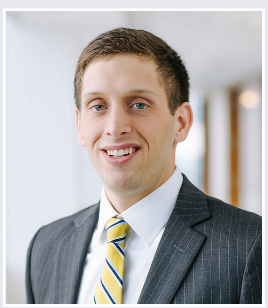
Strength Through the Storm

JENNIFER DZWONCHYK
Vice President
Twin Brook Capital Partners

Jennifer is a Vice President at Twin Brook, leading an underwriting team focused on the structuring, diligence, negotiation, execution, and management of investments across a range of industries.



TONY MAGGIORE
Vice President
Twin Brook Capital Partners

Tony is a Vice President and senior member of Twin Brook's special situations team, focusing primarily on restructurings and distressed investments.

AS WE HEAD INTO THE FINAL QUARTER OF 2020, TWIN BROOK CAPITAL PARTNERS' JENNIFER DZWONCHYK AND TONY MAGGIORE DISCUSS WORKING WITH LOWER MIDDLE MARKET COMPANIES AND THEIR PRIVATE EQUITY SPONSORS OVER THE PAST SEVERAL MONTHS AND THE AMAZING RESILIENCE MANY OF THESE BUSINESSES HAVE EXHIBITED IN THE FACE OF UNPRECEDENTED CHALLENGES.

How are most middle market companies doing in comparison to the early days of the pandemic?

TONY: Generally, I'd say companies are doing better than initially anticipated. If you had asked how we thought businesses would hold up during the early days of the COVID-19 outbreak and ensuing economic shutdown, our expectations likely would have been more negative than the actual results. When it came to weathering that environment, government assistance programs helped, but I think that many lower middle market companies' demonstrated abilities to preserve cash, cut costs, and be operationally nimble in the face of an unprecedented and everchanging situation have been key.

While uncertainty absolutely persists, I think it has declined in comparison to a few months ago. We saw that early results provided a clearer picture of how shutdowns, supply chain disruptions, and other challenges had impacted businesses – improving visibility around how companies were managing through the pandemic – and, in many cases, navigating those difficulties included putting plans and initiatives in place that have made those companies better equipped to mobilize in the face of a COVID-19 resurgence or similar crisis in the future.

Are there some companies or industries that appear to be withstanding the challenges brought on by COVID-19 better than others?

JENNIFER: Some types of companies and industries have definitely fared better than others. I think they generally fall into one of four categories, the first being companies that are thriving in this environment. We've seen this include subscription-based and other services focused on at-home or remote operations, as well as businesses that provide services or products for which there is a specific need in the face of a pandemic. The second bucket consists of businesses that we believe will likely be impacted by a longer-term economic shift but have generally fared relatively well thus far – such as those in the general industrial space – as they've sought to align cost structures where possible and are closely monitoring demand in this unique economic environment. The third group includes those that were hit hard by temporary shut downs but have experienced V-shaped recoveries, as they quickly bounced back once pandemic-related lockdown measures were lifted and they were able to reopen. We found this to be the case with many healthcare companies. Lastly, you have what I would say is a smaller basket of businesses that are struggling and facing significant, lasting impacts, like those that are focused on travel or events.

As we look at what has contributed to companies being able to work through this, I think much of it has been driven by management teams, many of which have made a lot of sacrifices and tough decisions – with the support of their operationally-focused private equity sponsors – aimed at protecting and ensuring a path forward for their businesses. We've seen this include managing cost structures and finding ways to reduce fixed costs, maintaining a hyperfocus on cashflow and enacting cash preservation strategies, and making adjustments based on geographies, as we've seen the pace of reopening and rules vary from state to state.

What role have private equity sponsors played when it comes to middle market companies seeking to navigate this environment?

TONY: I think private equity firms have been critical partners for their portfolio companies during this time, especially in the lower middle market. We believe our sponsor clients have a wealth of operational expertise and – in many cases – have helped their portfolio companies navigate multiple cycles, so over the past few months, they've been a key resource for businesses as they seek to manage and make timely decisions about costs and cashflow. The operating partner support and guidance that these sponsors provide their management teams – offering insight on best practices gleaned from their historical experience or what they are seeing across their broader portfolio – has, in our opinion, been invaluable. Furthermore, when required in the face of tougher situations, we've seen a number of sponsors step up to support the liquidity of a business, and that support – whether it be through a direct injection of capital or help securing financing – has often been key to those companies weathering this storm.

JENNIFER: I'd add that, in our experience, sponsors have also been very important when it comes to working with lenders. At Twin Brook, we have always been focused on building deep sponsor relationships, and – in many cases – members of our team have been partnering with our private equity clients for 15-20+ years. We believe that experience working hand-in-hand on multiple transactions and through numerous situations has fostered a level mutual of trust and open line of communication that have been particularly key over the past few months, as they've helped us proactively support borrowers and allowed for greater flexibility when it comes to generating solutions for any issues that may arise.

In this environment, has Twin Brook's approach to working with sponsors and borrowers changed?

JENNIFER: Since inception, Twin Brook's strategy has been about more than just providing capital and closing deals; we are focused on being a dedicated lending partner that is there to serve our private equity sponsors and their lower middle market portfolio companies through periods of both growth and distress. Core to nearly every aspect of our approach is a commitment to consistency and reliability – as reflected in the design of our teams, our underwriting process, and our portfolio management – and that has absolutely remained unchanged.

I think how we construct our teams is unique and has certainly proved to be very helpful in this environment. At Twin Brook, the team that underwrites a new opportunity stays with that account for the life of the credit. We believe that team continuity affords a seamless experience and greater surety of execution for our borrowers and their sponsors, while also better positioning us to support them and manage the credit within our portfolio on an ongoing basis.

TONY: Regular communication with our borrowers, their management teams, and their sponsors about all parts of their businesses – whether it be daily, weekly, or monthly – has long been a staple of our approach. We believe these frequent interactions and the higher-quality, more timely information they provide help us maintain a deep knowledge of these companies and what impacts them and is central to our active monitoring of credits. The consistency of these interactions has not changed over the past few months; sponsors and borrowers have continued to proactively communicate and provide us with the right information, which supports our ability to identify potential issues early on and work together to address them.

What do you think the experiences of the past few months have highlighted?

TONY: Building on what Jennifer noted earlier, I think this situation has shined a light on the value of relationships – whether they be between lenders, sponsors, or borrowers. Back in March, when the outbreak of COVID-19 took hold in the U.S., many middle market companies suddenly found themselves in uncharted waters. In that environment, we saw that having trusted partners that understood your business, knew how you operate and could therefore act nimbly and calmly, and that were there to support you as you navigated the complexities of the moment and sought to prepare for the events of tomorrow was certainly meaningful. Establishing deep relationships takes substantial time and effort, so I think those that had them in place going into this were grateful they did.

JENNIFER: I think this has also demonstrated the importance of having the right management team in place. In the lower middle market, private equity sponsors are often building portfolio company management teams almost from scratch, and those teams have continued to impress us. We've seen them – with the support of their sponsors – be steadfast in the face of great uncertainty, act decisively, and make the changes necessary, even when tough, to adapt. Because of this, I believe many companies are coming out of the past few months better positioned for both the challenges and opportunities of the future. ■