**Market Update**

**SPP’s Middle Market Leveraged Cash Flow Market At A Glance**

<table>
<thead>
<tr>
<th>Deal Component</th>
<th>September '17</th>
<th>August/July '17</th>
<th>September '16</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cash Flow Financial</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Debt multiples</td>
<td>$10.0MM EBITDA 2.75x-4.00x</td>
<td>$10.0MM EBITDA 2.75x-4.00x</td>
<td>$10.0MM EBITDA 2.50x-3.50x</td>
</tr>
<tr>
<td>Total Debt Limit</td>
<td>$7.55MM EBITDA 3.25x-4.50x</td>
<td>$7.55MM EBITDA 3.25x-4.50x</td>
<td>$7.55MM EBITDA 3.00x-4.00x</td>
</tr>
<tr>
<td>Multiple</td>
<td>$10.0MM EBITDA 3.50-5.00x</td>
<td>$10.0MM EBITDA 3.50-5.00x</td>
<td>$10.0MM EBITDA 4.50-5.00x</td>
</tr>
<tr>
<td><strong>Senior Cash Flow</strong></td>
<td>$20.0MM EBITDA 4.50x-6.00x</td>
<td>$20.0MM EBITDA 4.50x-6.00x</td>
<td>$20.0MM EBITDA 4.00x-5.50x</td>
</tr>
<tr>
<td><strong>Pricing</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Bank</td>
<td>$&lt;10.0MM EBITDA L+5.50%-8.00%</td>
<td>$&lt;10.0MM EBITDA L+5.50%-8.00%</td>
<td>$&lt;10.0MM EBITDA L+6.00%-8.00%</td>
</tr>
<tr>
<td><strong>Second Lien Pricing</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Avg)</td>
<td>$&lt;7.55MM EBITDA L+7.00%-12.00% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+7.50%-12.00% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+8.00%-11.00% floating (0.50%-1.00% floor)</td>
</tr>
<tr>
<td><strong>Subordinated Debt Pricing</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Bank</td>
<td>$&lt;10.0MM EBITDA L+10.00%-13.00%</td>
<td>$&lt;10.0MM EBITDA L+10.00%-13.00%</td>
<td>$&lt;10.0MM EBITDA L+10.00%-13.00%</td>
</tr>
<tr>
<td><strong>Unitranche Pricing</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Bank</td>
<td>$&lt;10.0MM EBITDA L+12.00%-14.00%</td>
<td>$&lt;10.0MM EBITDA L+12.00%-14.00%</td>
<td>$&lt;10.0MM EBITDA L+11.00%-14.00%</td>
</tr>
<tr>
<td><strong>Minimum Equity Contribution</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lenders</td>
<td>$&lt;7.55MM EBITDA L+7.00%-12.00% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+7.50%-12.00% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+8.00%-10.00% floating (0.50%-1.00% floor)</td>
</tr>
<tr>
<td><strong>Equity Co-Investment</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lenders</td>
<td>$&lt;10.0MM EBITDA L+6.00%-7.50% floating (0.50%-1.00% floor)</td>
<td>$&lt;10.0MM EBITDA L+6.50%-8.00% floating (0.50%-1.00% floor)</td>
<td>$&lt;10.0MM EBITDA L+7.00%-8.50% floating (0.50%-1.00% floor)</td>
</tr>
<tr>
<td><strong>Recap Liquidity</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lenders</td>
<td>$&lt;20.0MM EBITDA L+12.00%-20.00% floating (0.50%-1.00% floor)</td>
<td>$&lt;20.0MM EBITDA L+12.00%-20.00% floating (0.50%-1.00% floor)</td>
<td>$&lt;20.0MM EBITDA L+12.00%-20.00% floating (0.50%-1.00% floor)</td>
</tr>
<tr>
<td><strong>Story Receptivity</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lenders</td>
<td>$&lt;7.55MM EBITDA L+8.50%-9.50% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+8.50%-9.50% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+8.00%-9.00% floating (0.50%-1.00% floor)</td>
</tr>
<tr>
<td><strong>Tone of the Market</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lenders</td>
<td>$&lt;7.55MM EBITDA L+9.50%-10.50% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+9.50%-10.50% floating (0.50%-1.00% floor)</td>
<td>$&lt;7.55MM EBITDA L+9.00%-10.00% floating (0.50%-1.00% floor)</td>
</tr>
</tbody>
</table>

---

**Cash Flow Financial**

- Debt multiples range from $10.0MM to $20.0MM EBITDA, with multiples ranging from 2.75x to 5.00x.
- Total debt limit is set at $7.55MM EBITDA, with multiples ranging from 3.25x to 5.00x.

**Pricing**

- Non-bank financing is available at a range of EBITDA multiples, from $<10.0MM to $<15.0MM EBITDA.
- Second lien pricing is set at $<7.55MM EBITDA L+7.00%-12.00% floating, with a floor of 0.50%-1.00%.
- Subordinated debt pricing starts at $<7.55MM EBITDA L+12.00%-14.00%.

**Market Update**

- Recap liquidity remains strong going into the fall, though a clear preference seems to be forming for sponsored deals over non-sponsored issuers. Most aggressive leverage rates and terms have generally been found outside the commercial banking community, but banks are still bidding on a competitive basis.
- The market continues to be exceedingly forgiving for sponsored deals, with a wide range of pricing and leverage terms available. Recap opportunities abound in this market, especially in light of increased valuation multiples and higher enterprise valuations. The distinction between recaps and other deals is clear, with common and subordinated preferred capital readily available from insurance companies, credit opportunity funds, and a larger more sophisticated, domestic and foreign family office network.
- Lenders still want sponsors to have substantive skin in the game, which translates to a 30.0%-40.0% base level of equity (this level is inclusive of any rollover). As a general proposition, non-sponsor equity of less than 20.0% will not attract the best terms (though may still get done). There is no dearth of additional capital available to cover for potential equity shortfalls from both equity and debt providers.
- The market for non-controlling equity continues to build and far exceeds the more parochial historical family office and other deals. As of this writing, one-month Libor is over 1.00%, so it is in large part academic, yet lenders are still looking for some downside protection.

**Check out SPP online: http://sppcapital.com/**
Unwind

The Federal Open Markets Committee continues to move closer to unwinding its $4.5 trillion balance sheet held since the financial crisis. The minutes from the July FOMC meeting indicate that several committee members wanted to initiate the unwind, but were outnumbered by others who insisted on pushing the discussion to the September meeting. Minneapolis Fed president Neel Kashkari has been perhaps the most vocal of all FOMC members on this issue. He was the lone dissenter at the June meeting (when the Fed funds rate was last raised), insisting to focus instead on the balance sheet and push off rate rises while labor markets and inflation measures improved.

Federal Reserve Chair Janet Yellen spoke following the annual central bank meeting at Jackson Hole, Wyoming to reaffirm her support for the financial regulations established in the wake of the financial crisis. Ms. Yellen's term as Fed Chair is set to end in February of next year, and speculation is rampant regarding President Trump's intention to reappoint her for another term (or potentially opting instead for his chief economic advisor, Gary Cohn). The President's most recent pronouncements suggest he is still intent to make good on his campaign promises and dismantle a number of financial regulations during his tenure (having described Dodd-Frank in the past as a "disaster"). Chair Yellen may have four more meetings with the FOMC before her term is finished, and will have to move swiftly to establish a framework for balance sheet alleviation that can be sustained long term.

The combination of another North Korean missile launch, their subsequent nuclear test, the havoc induced by Hurricane Harvey, weaker than expected employment gains in August, and continued anemic inflation have pushed investors to further discount the probability of additional rate hikes in 2017. CME Fed Funds Futures prices currently estimate a 63.5% chance of the FOMC maintaining interest rates through the rest of the year, and a 35.7% probability that they are raised by 25 basis points.

Below is a quick recap of this month’s key economic releases:

- **Employment Data Weak**
  - The most recent employment report from the Bureau of Labor Statistics showed lower than expected gains in non-farm payrolls and a slight uptick in the unemployment rate. Non-farm payrolls rose by 156,000, lower than the expected mark of 180,000. The unemployment rate rose to 4.4%, up 0.1% from July, despite the participation rate remaining at 62.9%. Annualized change in average hourly earnings remained the same from July at 2.5%. On a more positive note, additions to manufacturing payrolls was four times higher than expected, with August posting 36,000 additions to the sector.

"I think I need to cool off
I'm feeling super nova
I think he finna blow up
I think he finna blow up

I catch wind and throw shade
I shed light and I find hate
Yeah lights on, my mind off
Is it bad time, oh my my my my my

Oh my, I've been working all week
No lie, can't sleep and I don't why (and I don't know why)
I'm just tryna unwind
I'm just tryna unwind
I'm just tryna unwind
I'm just tryna unwind

"Unwind" - Healy

**Conference Board’s Consumer Confidence Index**

**Non-Farm Payroll Employment (Seasonally Adjusted)**

**Unemployment Rates (U-3 and U-6)**

**Implied Probability of Rate Hikes for Rest of 2017**
• **Consumers Remain Confident** – The Conference Board’s consumer confidence index enjoyed a strong August, with the most recent estimation for the figure measured at 122.9, up from 120.0 in July. The primary driver was the Present Situation component, which jumped from 145.4 to 151.2, its highest mark since 2001. The report shows that significantly more consumers believe that business conditions are “good” (32.5% to 35.4%) and fewer are saying that conditions are “bad” (13.5% to 13.1%). Short and long term optimism levels were tempered, with the Expectations component ticking up 1 point to 104.

• **Q2 GDP Revised Upwards** – A solid second quarter mark of 2.6% annualized GDP growth was upgraded to 3.0% growth in the preliminary report from the Bureau of Economic Analysis. Estimated growth of 3.3% in consumer spending shown in this revision was a major driver for the strong overall figure. Non-residential investment was also noted by the BEA as a main contributor, holding at a strong 6.9% annualized growth for the quarter. Overall government spending decreased on the quarter by a greater margin than originally estimated. Estimates for Q3 growth are somewhat bullish, with the GDPNow forecast predicting a seasonally adjusted rate of real GDP growth of 3.1% for Q3.

• **Personal Income Climbs, PCE Falls** – After a disappointing June, the Personal Income and Outlays report from the BEA showed considerable growth in personal income, which was up 0.4% in July. Disposable personal income and personal consumption expenditures were both 0.3% higher on the month as well. The core PCE price index (PCE less food and energy) fell from 1.5% to 1.4% on the month, potentially disappointing news for an FOMC keenly focused on the inflation measure.

• **ISM Manufacturing and Non-Manufacturing Indices Stronger in August** – The Institute for Supply Management’s recent Report on Business showed greater than expected strength in manufacturing, with its PMI index eclipsing expectations. The index’s boost to 58.8 (up from 56.3 in July) was aided by higher levels of production, inventories, order backlog, and maintained strength in new orders. This is the index’s highest mark since 2011. The ISM’s non-manufacturing index missed expectations but grew stronger in August with a mark of 55.3, up 1.4 points from a weak July report.

• **The Housing Market Continues to Decelerate** – Both new and existing home sales were weaker in July, which coincided with higher prices. Existing home sales were estimated at an annualized rate of 5.44 million in July, down 1.3% month-over-month. New home sales fell by a mark of 39,000 on the month to an annualized level of 571,000. Both have enjoyed relatively strong figures in recent months stemming from a stock market surge and interest rates remaining suppressed.

**Private Market Update:**

After holding leverage tolerances and credit spreads static for July and August, SPP is back in a tightening mode in September.

Our non-bank lending spreads for companies with less than $10 million of EBITDA have been tightened by 100 basis points (with the range dropping from 6.5%-8.0% to 5.5%-8.0%), while credit spreads for companies with more than $15 million of EBITDA have been reduced by 50 basis points on the upper band (from 4.5%-6.5% to 4.5%-6.0%). We are also tightening the lower end of the pricing band for companies with less than $7.5 million of LTM EBITDA for both unitranche and second lien note spreads by 0.5%, bringing the range to 7.0%-12.0%.

This most recent reduction in spreads is a testament to the increased competition in the lower middle market for assets, specifically among non-bank lenders (BDCs, commercial finance companies, credit opportunity funds and insurance companies). As the role of commercial banks continues to decline in middle market leveraged finance, non-bank lenders have rushed in to fill the vacuum by driving pricing to more competitive levels and offering more competitive terms and conditions.
According to the most recent quarterly report of the Federal Deposit Insurance Corporation (FDIC), total net loans by FDIC insured institutions grew only 3.7% from a year earlier; that is down from the 6.7% year-over-year growth in loans posted in June of 2016. While this may seem like a boon to the non-bank lending community, it has also created greater competition in an ever growing non-bank lending community comprised of BDCs, CLOs, credit funds and insurance companies. While commercial banks controlled roughly 30.0% of the primary investment market in 2005, that stake has declined to less than 5.0% today. Meanwhile, the number of non-bank direct lending funds has grown to 145 as of July 2017. This mark is more than twice the amount of private funds created for mezzanine securities (which currently stands at 60), and greater than all private mezzanine, distressed debt, and special situations funds combined.

The most significant byproduct of the greater competition is pricing. As indicated above, pricing of middle market asset has continued to compress throughout the year. The tighter loan spreads have also put increased pressure on the profitability of BDCs. In fact, the publically traded BDC index ETF dropped from a high of 23.70 in May of this year to approximately 21.25 in mid-August. As of August 5, approximately 74.0% of publically traded BDCs are trading at a discount to their net asset value (NAV), and more than 20.0% of publically traded BDCs are trading below 80.0% of their NAV.

In addition to tighter spreads, the increased competition by non-bank lenders has led to greater tolerances for leverage. According to S&P Market intelligence, average debt multiples of middle market loans have swelled to more than 5.9x, a full turn above the 4.9x average debt multiple recorded in 2015.

The increased competition for assets, lower pricing and higher leverage multiples have certainly had an impact on deal flow. While the numbers have still not been tabulated in the middle market, market participants contacted by SPP indicate that deal flow has dramatically increased through the summer months. August has been one of the most active months in all of 2017 for SPP, with more deals being reviewed in August than in June and July combined. If last month is any indication, the fourth quarter of 2017 is shaping up to be one of the busiest on record, and conventional wisdom suggests that the sheer amount of deal flow will force investors to be more selective in asset allocation.

The takeaway is quite dear for any issuer contemplating financing in 2017—those that get in the market first will be the greatest beneficiaries of the excess liquidity conditions.

**Contact SPP Today**

Please feel free to call any of the professionals at SPP Capital to discuss a particular financing need, amendment, or restructuring situation, or just to get a little more color on the market. You don’t need an imminent or market-ready deal to call us. Our hope is that you use SPP as your go-to resource for any information, analysis, and review of potential transactions.

For your smaller capital needs, SPP’s direct lending platform, SPP Mezzanine Partners, is currently investing in senior, second lien, mezzanine, and unitranche instruments ranging from $5 to $15 million. We focus on established lower middle market companies with proven business models, stable cash flows and strong management teams.

Stefan Shaffer  
Managing Partner  
212.455.4502

**DISCLAIMER:** The "SPP Leveraged Cash Flow Market At-A-Glance" and supporting commentary is derived by the anecdotal experience of SPP Capital Partners, LLC, its specific transactions, discussion with issuers, lenders and investors consistent with its standard operating practices. Any empirical data specifically derived by third parties, or intellectual property or opinions of third parties are expressly attributed when utilized. The factual information provided has been obtained from sources believed to be reliable, but is not guaranteed as to accuracy or completeness. All data, facts, tables or analyses provided by Governmental or other regulatory bodies are deemed to be in the public domain and not otherwise expressly attributed herein. SPP Capital Partners, LLC is a member of FINRA and SIPC. This information represents the opinion of SPP Capital and is not intended to be a forecast of future events, a guarantee of future results or investment advice. It is not intended to provide specific advice or to be construed as an offering of securities or recommendation to invest.

To unsubscribe to this email, please click [here](#).  
To request to be added to our distribution list, please click [here](#)
**SUPPORTING DATA**

- **Historical Senior Debt Cash Flow (x EBITDA)**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing cash flow for different EBITDA ranges: 
    - Less than $7.5MM EBITDA
    - $7.5MM to $10MM EBITDA
    - Greater than $10MM to $20MM EBITDA

- **Historical Total Debt Limit (x EBITDA)**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing debt limits for different EBITDA ranges:
    - Less than $7.5MM EBITDA
    - $7.5MM to $10MM EBITDA
    - Greater than $10MM to $20MM EBITDA

- **Historical Senior Cash Flow Pricing (Bank)**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing pricing for different EBITDA ranges:
    - Bank Lower Bound
    - Bank Upper Bound

- **Historical Senior Cash Flow Pricing (Non-Bank)**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing pricing for different EBITDA ranges:
    - NB Lower Bound (<$10)
    - NB Upper Bound (<$10)
    - NB Lower Bound (>$15)
    - NB Upper Bound (>$15)

- **Historical Minimum Equity Contribution**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing equity contribution for different EBITDA ranges:
    - Lower Bound
    - Upper Bound

- **U.S. PE Middle Market Deal Flow by Quarter**
  - Source: PitchBook
  - Graph showing deal flow over time by quarter and year:
    - Deal Value ($B)
    - # of Deals Closed

- **Historical Second Lien Pricing**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing second lien pricing for different EBITDA ranges:

- **Historical Subordinated Debt Pricing**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing subordinated debt pricing for different EBITDA ranges:
    - Lower Bound
    - Upper Bound

- **LIBOR Floor Pricing**
  - Source: SPP's "MIDDLE MARKET LEVERAGE CASH FLOW MARKET AT A GLANCE"
  - Graph showing LIBOR floor for different EBITDA ranges:
    - Lower Bound
    - Upper Bound