Deerpath expands the direct lending mindset and fan club

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Christopher Faille • August 26, 2021

Deerpath Capital Management has successfully filled the lending void left by banks in recent years by creating a safe, market-neutral strategy for global institutional investors, according to Managing Director Reed Van Gorden.

Specifically, Deerpath provides customized cash flow based on senior debt financing to lower middle-market companies across a wide range of industries, filling the space left by reluctant bankers.

Reed Van Gorden (provided)

Even before the global financial crisis 13 years ago, banks were often reluctant to lend money directly to firms found in Deerpath's purview.

That crisis sucked even more air out of that space. Further, over the subsequent recovery, Dodd-Frank, Basel III, and the updated U.S. guidance on leveraged lending all helped direct banks to the larger businesses, contributing to the neglect of the mid-market.

Some of this was likely unintended by the drafters of the relevant documents. Dodd-Frank, for example, included the Volcker rule, which limited banks' exposures to equity positions in private equity and hedge funds. Banks could still lend to those funds so long as there were no equity features to the debt instrument. But the rule limited the flexibility of banks in this area and created an enhanced opportunity for non-bank lenders to increase their capital offerings to the PE funds.

Direct lending, Van Gorden emphasized, is a very demanding business. "Players that have longevity in the market have a competitive advantage."

Founded in 2007 by Gary Wendt, James Kirby, and John Fitzgibbons, Deerpath has offices in New York (the headquarters), Chicago, Fort Lauderdale, Houston, Boston, and California. Its investment products include first lien senior secured loans, revolvers, stretch senior, unitranche loans, and some equity positions.

Van Gorden said that the "lower middle market" may be understood as "the range of roughly $5 to $20 million in EBIDTA, or between $50 and $100 million in enterprise value."

Why the gap? "Banks are not set up to underwrite deals that come through their regional teams, regional teams focus on ABL deals that conform to a borrowing base," Van Gorden said. "I can get on the phone with the Investment Committee same day in order to approve a deal."

It is precisely this ability to get the necessary information, on a ground-up micro level, or the reliability of its lenders, that allows Deerpath to produce market neutral returns: that is, returns that are not dependent on where a macro-economy is in the business cycle.

Deerpath's portfolio industries include communications, energy and natural resources, healthcare, and manufacturing. The three principals and co-founders (Wendt, Kirby, Fitzgibbons) came together because they realized, as Van Gorden explained, that "there was a great opportunity within the lower middle market to offer safe loans that would produce superior returns for investors."

Tas Hasan, partner and chief operating officer of Deerpath, expressed his view that European institutions are interested not only because of the resilience and growth of the asset class as a whole but because they see the U.S. market as the most mature in direct lending.

"If you want to be a real investor in direct lending you have to have an allocation in the U.S.," Hasan said.

On May 12, Deerpath announced the closing of its Fund 5, which at $1.1 billion was Deerpath's largest fundraising in Europe and Asia thus far. It gained more than 50 new limited partners from around the globe.

The institutions that invested were, in this order: pensions (both public and private), insurers, and asset managers.

A lot of the large pension funds, insurers, and asset management firms that have large allocations in fixed income are eyeing new strategies. In turn they are ripe for the opportunity Deerpath offers – better quality companies that are the top of the capital structure and higher yields, in comparison with bonds, and the bottom of that structure.

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