

E X P E R T Q & A

*Mid-market services businesses are relatively insulated from the effects of trade policy and represent attractive opportunities for private capital, argue Churchill Asset Management's **Mat Linett** and **Jason Strife***



A safe haven

Q What are your expectations regarding dealflow for the remainder of 2025? And how are both the junior and senior lending markets likely to be impacted with regard to terms?

Mat Linett: Expectations were high at the end of last year. The feeling was that a flood of dealflow was about to be unleashed. Then, as we entered 2025, sentiment shifted more towards cautious optimism. Now, given the geopolitical situation and all the noise around tariffs, the mood has tempered.

There is significant capital sitting on the sidelines that needs to be deployed, but only deals involving truly superior companies with well-defined market share and strong pricing power, in bulletproof sectors, will get completed – at least until there is greater clarity around trade policy.

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With regard to terms, our markets tend to lag slightly, so we haven't seen the immediate widening of spreads that has taken place in the broadly syndicated loan market. However, if this kind of market volatility continues, we expect spreads to widen and terms to continue to move in favour of direct lenders.

Jason Strife: I completely agree. The distributions we saw in our private equity business last year pointed to a very active 2025. We are now net sceptics regarding the prospect of new deals coming to market in the near term.

The good news is that even if new leveraged buyouts fail to be consummated at the level previously predicted,

refinancing opportunities are likely to remain strong. Historically, our deployment has been approximately 70 percent focused on new buyouts and 30 percent on recapitalisations, but we've seen a reversal in those statistics over the past six months.

Q Are some strategies more protected from the threat of tariffs than others?

ML: We focus exclusively on the mid-market segment. US companies in this space overwhelmingly tend to sell domestically, providing insulation from any retaliatory tariffs. We also tend to focus on service businesses that are not importing input goods, which also provides insulation against the proposed US tariffs.

To the extent that tariffs create demand destruction, everyone would be impacted by them in some way. But

focusing on companies providing services within the US provides a degree of protection, at least from the direct impact of any tariff regime.

JS: I would add that private equity owners are very good at taking an offensive position – they have a four-to-six-year window in which to create value and they have therefore been extremely proactive when it comes to responding to tariffs. The challenge, of course, is that policy decisions change so quickly. We had private equity owners calling us within a week with plans to pivot strategy to combat the tariffs contained in the first wave of announcements from President Donald Trump, which have since been unwound. That lack of consistency is not a productive environment for anyone.

Q Against that backdrop, how are you approaching underwriting new deals?

JS: We are turning up the dial on certain aspects of due diligence and focusing on services businesses that are insulated from cost pressures. We are also seeing opportunities to back low-cost leaders in markets that might face cost pressures, but where any resulting price increases are unlikely to impact that company's leadership position.

ML: Brand equity is also key. Some companies have proven pricing power. We have, after all, been dealing with inflation for a number of years, which has given us good insight into those companies and industries that are able to weather this kind of environment.

I would add that while we are, of course, extremely focused on the impact of tariffs right now, we always factor in the possibility of recession during our holding period. Having said that, anything with cyclicalities is currently off the table. We are also looking at attachment points to make up for some of the current uncertainty and to ensure that risk-adjusted returns are commensurate with the opportunity.

“Only deals involving truly superior companies in bullet-proof sectors will get completed, until there's greater clarity”

MAT LINETT

Q Which sectors or subsectors do you deem to be particularly resilient?

ML: Managed service providers would be one example. These are companies handling the cloud and cybersecurity for small and medium-sized enterprises. They have strong recurring revenue attributes, good pricing power and, as a service, they will not be affected by tariffs. Private equity firms are extremely active in this space and scaled providers are in demand. There are also routes to exit in the unlikely event that a company gets into trouble.

We have also had considerable success with accounting platforms, as well as engineering and consulting service providers, which are particularly attractive to investors.

Q How would you describe LP appetite for private capital in this environment?

JS: We are seeing strong appetite for junior capital right now. There are good return opportunities in that middle part of the balance sheet, which are only becoming more apparent given the number of companies requiring additional duration and fresh capital to reset capital structures and support growth plans. Meanwhile, secondaries activity has exploded as a counterbalance to muted primary activity. Investors are gravitating towards platforms that offer complementary strategies and create origination synergies.

ML: Private debt can really shine as an asset class during periods of dislocation in capital markets. We saw that play out during covid-19 and we are seeing it again now. Private equity firms can rely on private debt funds to be there when required and investors rely on the historically stable cashflows that private debt can offer.

Q Are there any product adjacencies that you believe to be particularly interesting right now?

JS: Our value proposition has always been to exploit as many product opportunities to service mid-market private equity clients as possible, and there are a couple more opportunities that I believe could be attractive. The first is an extension of our existing junior capital business; I would not describe it as opportunistic or distressed investing because that implies a misalignment with the private equity owner. Instead, I would describe it as a capital solutions business where we would use our platform's flexibility to alleviate pressure on an asset's capital structure.

Most of what we do within our junior capital business today involves high-performing assets, but following this strategy would mean targeting the next tier down – namely, businesses that may have been owned by private equity for one too many years. This strategy would target fundamentally good businesses that have underperformed for one reason or another and need duration through a capital structure solution.

There are now more than 10,000 companies owned by private equity and a proportion of those businesses will inevitably need more time to generate value, so we see this as a long-term opportunity regardless of the macro environment. ■

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