



# Resilient Lending Structures in an Uncertain Market

## I. Key Investment Practices

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## More Dry Powder, Looser Terms

The direct lending market is now \$1.4 trillion,<sup>1</sup> as large as the US leveraged loan market, and is expanding as a result of bank retrenchment over the past decade, successful fundraising and sustained conviction in the asset class from both new and existing investors.

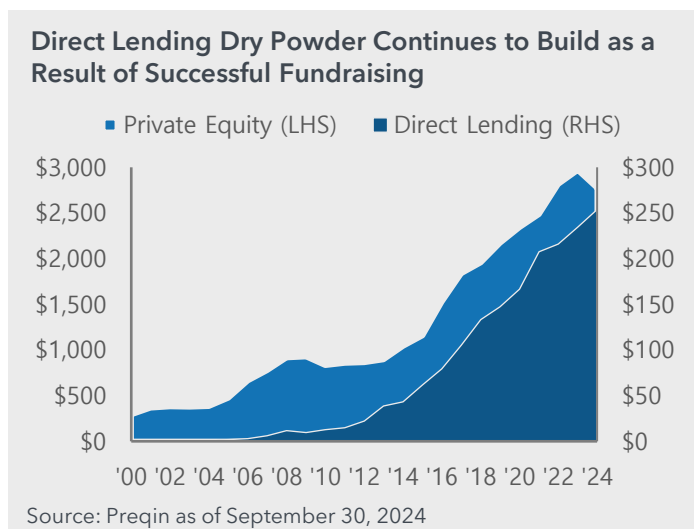
In recent years, "dry powder," or unallocated capital that is ready to deploy, has increased dramatically as shown in Exhibit 1, leading to a structural shift in the financing landscape for leveraged buyouts ("LBOs"). With substantial capital at their disposal, lenders at the larger end of the middle market are now competing with banks to deploy capital into large deals as illustrated in Exhibit 2. The result of this increased competition is looser terms as lenders seek to compete with the broadly syndicated loan ("BSL") market.

In the first of our three-part series examining how direct lending terms and structures are evolving today, we explore the importance of robust loan protections, especially in the current market environment.

## Key Investment Practices Drive Outcomes

TPG Twin Brook has various practices that we believe allow us to implement active portfolio management, mitigate risk, and drive positive economic outcomes. These practices include 1) transaction leadership, 2) disciplined revolver and covenant utilization, and 3) deployment of a dedicated and experienced in house workout team.

**Exhibit 1: Dry Powder (USD \$B)**



## I. Transaction Leadership

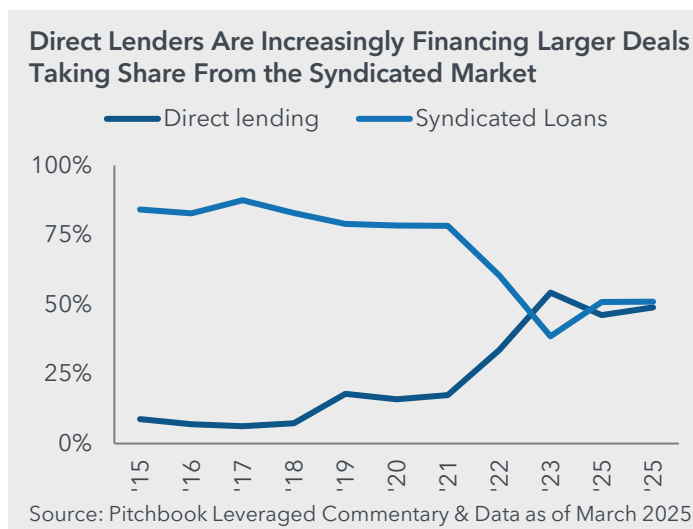
The role a lender holds in the bank group determines the lender's access to information and influence on the terms within the credit agreement. Larger deal sizes typically correlate with larger bank groups, which can dilute a lender's ability to determine loan protections.

In contrast to the upper mid-market (\$50+ million of EBITDA), terms have remained resilient in the lower mid-market (<\$25 million of EBITDA), where the competitive landscape is dominated by fewer established direct lenders with less bank competition. All else equal, smaller bank groups allow lenders to construct solutions and drive outcomes and recovery rates, given the potential for competing priorities in larger bank groups.

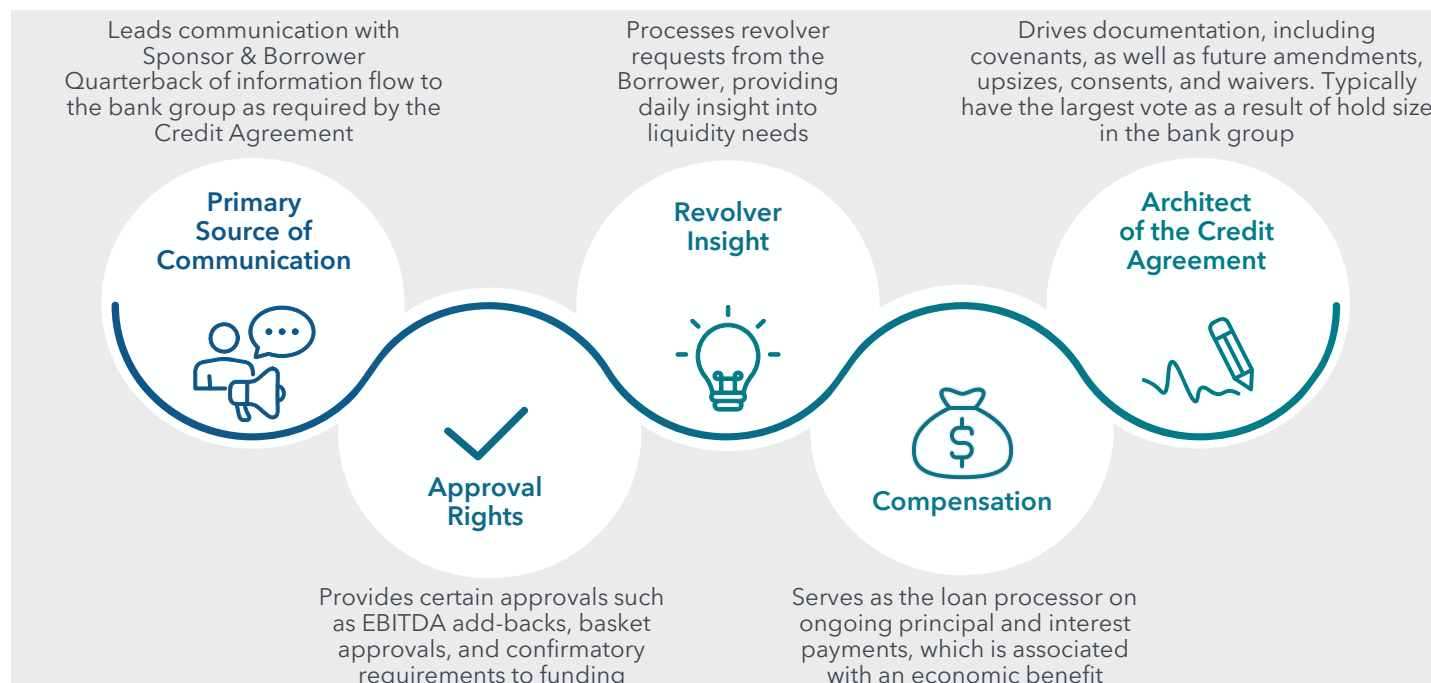
"Administrative Agent" is the most important title in the bank group, detailed in Exhibit 3, and only one lender is chosen to fill this role. The chosen lender is afforded access to the borrower and sponsor, certain rights that may materially impact outcomes, and the ability to define key items such as covenants, cash flows, and EBITDA add-backs. As a result of an established reputation and track record, TPG Twin Brook is the Administrative Agent on 96% of loans within its portfolio and a lead lender on nearly 100%.<sup>(2)</sup> According to Pitchbook, TPG Twin Brook was the most active lender during 2024 for "Select" or lead roles for both buyouts and add-ons.

We believe how you lend matters just as much as who you lend to. As direct lending competition intensifies, the ability to lead a transaction will be a key differentiator.

**Exhibit 2: \$1B+ Buyouts by Financing Type**



### Exhibit 3: Benefits of the Administrative Agent Role



#### Most Active Lenders in US Buyouts, Select Roles

1	<b>TPG Twin Brook</b>	<b>52</b>
2	BMO Financial Group	47
2	Churchill	47
4	Antares Capital	40
4	Ares	40
6	Golub Capital	37
7	The Goldman Sachs Group	31
8	Audax Private Debt	26
9	KKR Credit	24
10	UBS	22
10	MidCap Financial	22

#### Most Active Lenders in US Add-ons, Select Roles

1	<b>TPG Twin Brook</b>	<b>58</b>
2	Antares Capital	55
2	Churchill	54
4	BMO Financial Group	42
4	Ares	38
6	Golub Capital	34
7	Monroe Capital	29
8	KKR Credit	28
9	The Goldman Sachs Group	23
10	MidCap Financial	22
10	Mitsubishi Financial Group	22

## 2. Revolvers and Covenants

Issuing and retaining a revolving line of credit is often reserved for the Administrative Agent. It is operationally intensive, and therefore, for the majority of direct lenders, not often feasible. When instituted, however, a revolving line of credit gives near-term insight into borrower activity, as opposed to quarterly insight via a term loan. Unusual revolver activity is typically a leading indicator of stress and allows lenders to implement preventive maintenance prior to covenant default. At TPG Twin Brook, 100% of our loans include a retained revolver, a key aspect of our active portfolio management approach.

Covenants have become a highly discussed topic amongst investors, particularly amid the rising prevalence of liability management exercises ("LME"). The myth that "good borrowers don't need covenants" has led to an increase in covenant-lite deals, especially in the large market - deal sizes above \$500 million - where processes are more competitive and 90% of loans lack covenants as illustrated in Exhibit 4. The upper mid-market has quickly followed suit, with approximately 80% of loans lacking covenants.<sup>(3)</sup> S&P notes that while maintenance covenants are still "the standard" in the private credit market, their effectiveness has deteriorated due to generous leverage limits, which in turn limit a lender's ability to act on early signs of stress. Of note, lower mid-market deals offer more conservative leverage of 4.0x debt-to-EBITDA versus 5.2x for the larger market.<sup>(4)</sup>

#### TO PUT THIS INTO CONTEXT:

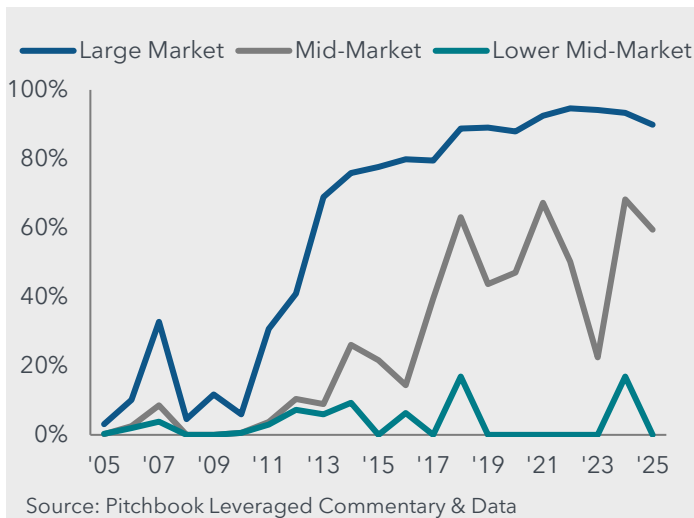
Revolver usage spiked in March 2020. **80% of portfolio companies were utilizing their revolver with an average drawn balance of 60%** - versus a historical average of 50% and 25%, respectively. The following quarter, covenant defaults spiked and normalized within a few quarters. As a result, lenders who retain the revolver in addition to the term loan, may have meaningful foresight into potential covenant defaults, versus lenders who are waiting for quarterly covenant compliance tests, or worse if covenants are “loose” or nonexistent.

Note: TPG Twin Brook did not experience a spike in payment defaults as a result, highlighting the importance of implanting solutions early in the process.

In the lower mid-market, multiple covenants remain prevalent, representing 35% of deals as shown in Exhibit 5. For comparison, as many as 55% of upper mid-market loans are “covenant-loose” with very wide covenants that will not be violated unless there is meaningful stress and deterioration, lessening the likelihood that the lender and sponsor will be able to implement a successful recovery plan. Non-existent or loose covenants lead to lower recovery rates, in the magnitude of 11% as measured by S&P.

Meaningful covenants allow TPG Twin Brook to engage with sponsors and borrowers at a time when enterprise value exists, allowing stakeholders an opportunity to

**Exhibit 4: % of Covenant-Lite Loan Volume<sup>(5)</sup>**



implement solutions and avoid further stress, which could lead to a payment default or worse.

TPG Twin Brook requires covenants on 100% of deals, not because we don't have conviction in our borrower's financial position, but rather because covenants are a vital part of our active portfolio management process. When a covenant default occurs, we are likely already implementing an improvement plan with the sponsor, borrower, and additional resources as needed, typically including sponsor equity support.

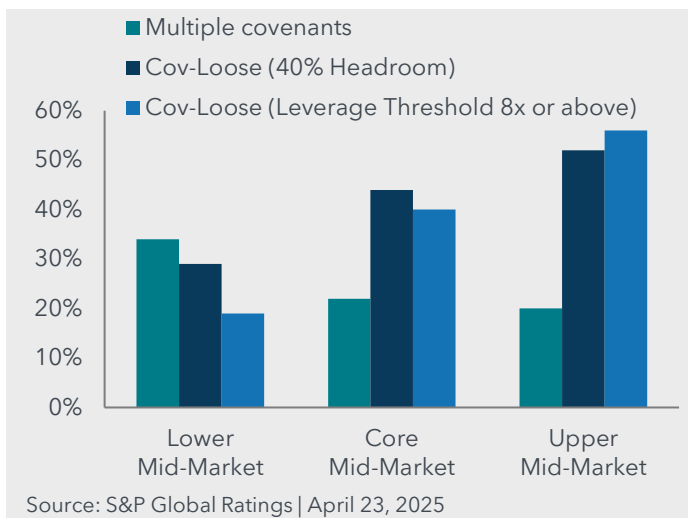
Through covenants and revolving credit lines enabled by a lead lender role, capable lenders in the lower mid-market can continue to influence outcomes to a degree that has become increasingly challenging further up market.

### 3. Dedicated Workout Team

In order to effectively navigate complex scenarios, mitigate losses and drive recoveries, we believe a lender must have a dedicated and experienced in house workout team. Workout teams are less prevalent amongst direct lenders, and even more so in the lower mid-market, with lenders often outsourcing this service to investment banks. Yet, these teams provide critical support to quickly resolve or prevent potential issues.

TPG Twin Brook stands out with a dedicated five-person team focused on this effort. When portfolio companies face challenges or are added to our “watch list,” specialized workout professionals are assigned to support the deal team, sponsor, and portfolio company, offering dedicated expertise to implement improvement plans effectively.

**Exhibit 5: Loosening of Covenants in Private Credit**



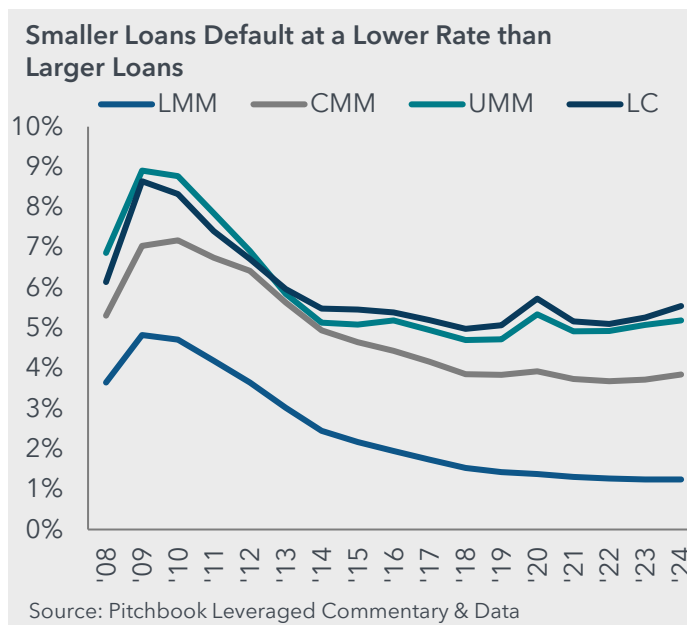


TPG Twin Brook and its network of selected sponsors have access to a network of experienced resources that may be utilized for workout scenarios. Improvement plans vary, with multiple potential paths to recovery, including:

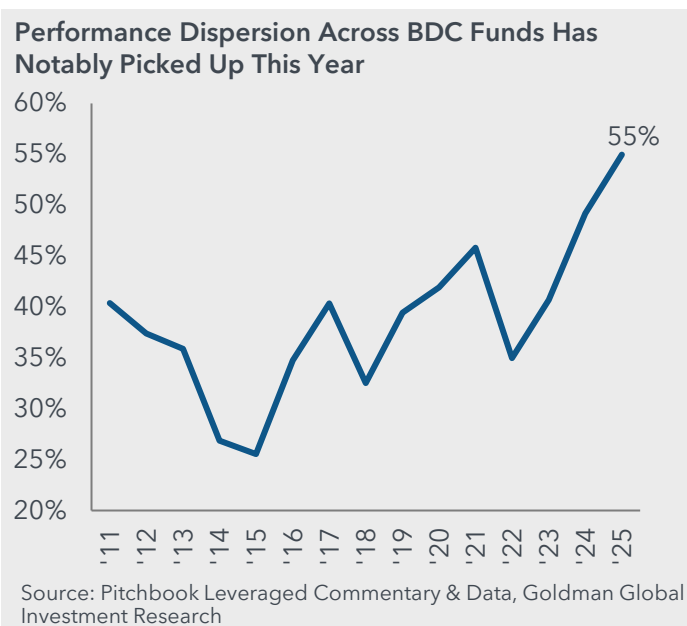
- 1 Engage an Operating Consultant:**  
Typically utilized if underperformance is sustained, despite covenant compliance. Operating consultants are viewed favorably as an expert resource in the given field. TPG Twin Brook has a deep bench of partners with a proven track record.
- 2 Engage an Operating Partner or Board Member:**  
Operating partners and board members generally focus on business strategy and aid the management team with execution. TPG Twin Brook may appoint an independent director to the board as part of an amendment negotiation.
- 3 Exercise a Right or Remedy within the Credit Agreement:**  
Although typically a last resort, the credit agreement includes remedies such as (i) charging default rate interest, (ii) restricting access to the remaining / undrawn revolver commitment, (iii) executing rights to withdraw cash from a borrower's bank accounts covered by DACAs (Deposit Account Control Agreements), (iv) foreclosing on / selling the collateral, and (v) voting the pledged equity.

As a result of smaller bank groups, the potential for active loan management, and tighter credit documentation, smaller loans are expected to experience fewer payment defaults, as shown in Exhibit 6, and therefore, higher recovery rates. Actual recovery rates will depend on a manager's ability to influence outcomes, driven by their role in the bank group, credit documentation and underwriting philosophy, as well as workout capabilities and experience.

**Exhibit 6: Cumulative Default Curves by Tranche Size<sup>(6)</sup>**



**Exhibit 7: Annual Total Return Differential: Top vs Bottom Decile BDC**



## Conclusion

The private debt landscape has been dynamic over the past several years - from macro-events, such as rising base rates, inflation, regulatory shifts and tariffs, to structural market shifts such as a material market expansion driven by fundraising success and companies' preference for private financing. Manager dispersion is beginning to materialize, as shown in Exhibit 7, and may be exacerbated by the loosening of terms. The "winners" will be managers who have established sound investment practices, been prudent and disciplined in underwriting and loan structuring, and built experienced workout capabilities to capture stable cash income, mitigate losses and drive recoveries.

## Endnotes

1. KBRA Direct Lending Deals Private Deal Analysis as of June 30, 2025. Sources include the BDC market, Solve, Direct Lending Funds, and Preqin.
2. Lead Lender is defined as Administrative Agent or Co-Lead Arranger. TPG Twin Brook is a lead lender on 99% of deals as of June 30, 2025.
3. S&P Global Ratings as of December 2024. Systemic Risk: Private Credit's Characteristics Can Both Exacerbate And Mitigate Challenges Amid Market Evolution.
4. KBRA DLD Research; Private LBOs: Leverage by EBITDA as of June 30, 2025. Lower Middle Market defined as EBITDA of <\$20 million, and the larger market above \$20 million of EBITDA.
5. Pitchbook Leveraged Commentary & Data as of July 30, 2025. Represents percentage of covenant lite leveraged loan volume for the Large Market (deal sizes greater than \$500 million), the Mid-Market (all middle market deal sizes) and the Lower Mid-Market (middle market deal sizes of \$200 million or less).
6. Pitchbook Leveraged Commentary & Data Cumulative Default Rates for Leveraged Loans. Lower Middle Market ("LMM") Defined as loan sizes of \$100 million and below. Core Middle Market ("CMM") defined as loan sizes of \$100 million to \$249 million. Upper Middle Market ("UMM") defined as loan sizes of \$250 million to \$499 million. Large Cap ("LC") defined as loan sizes of \$500 million or greater.

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