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Increased Interest in Direct Private Placements

Direct private placements of bonds under Section 4(a)(2) of the United States Securities Act can provide a flexible method of raising capital and act as a strong complement or alternative to traditional offerings of bonds, whether public or under Rule 144A and Regulation S. While bond offerings and bank financings each customarily have advantages and disadvantages as part of a company's capital mix, directly-placed bonds can often present a bespoke solution for certain transactions.

For example, traditional bond financings often permit longer maturities than bank financings and fixed rates versus floating rate financing, while bank financings generally allow a more flexible amendment and waiver process involving a smaller group of lenders. Directly-placed bonds can permit a longer maturity, typical of bonds, but also allow for direct communication between the issuer and the smaller bondholder group when an amendment or waiver becomes necessary. As such, directly-placed bonds can also provide more narrowly-tailored covenant packages typical of bank financings when close covenant monitoring is warranted, or for particular collateral and issuer types not yet priced in the public or Rule 144A markets.

Volume in the Section 4(a)(2) private placement sector has traditionally been driven by insurance company demand for exposure to particular asset classes, and we are seeing increased issuance and interest in the sector in our practice.

LONG TERM RELATIONSHIPS WITH A LIMITED SYNDICATE

Direct placements are typically offered to small groups of "club" investors with a "buy-and-hold" investment strategy. This facilitates meaningful, long-term relationships among issuers and investors and may help insulate investors from price fluctuations typical in registered and Rule 144A markets caused by more active secondary trading. At the same time, a smaller syndicate and more stringent trading restrictions will generally limit secondary market liquidity for bondholders.

MORE TARGETED DISCLOSURE

Direct placements under Section 4(a)(2) typically involve more targeted disclosure than public or Rule 144A transactions. Direct placement of bonds facilitates information flow directly from the issuer to bondholder to an investor in response to their direct due diligence as part of the investor's investment decision. Ongoing reporting is typically delineated in a negotiated note purchase agreement, allowing for disclosure to a smaller population of investors and prospective investors, which can be useful for "early stage" issuers not ready for a full public- or Rule 144A-style disclosure package. This more limited disclosure group can help enhance privacy and confidentiality for smaller issuers or others with sensitive business information. That said, such flexibility often comes with closer monitoring of the credit on a periodic basis by the investor group—more like a traditional bank syndicate dynamic.

RATINGS

Investors in directly-placed bonds often do not require a public rating from a nationally recognized statistical rating organization. That said, such a lack of an external rating may lead investors to seek a tighter covenant package. Certain issuers may be willing to live with a stricter covenant package in exchange for potential time and cost savings as well as increased privacy and confidentiality resulting from avoiding the ratings process.

It should be noted that if the debt is held by an insurance company, a private credit designation by the Securities Valuation Office of the National Association of Insurance Commissioners will typically be required.

ISSUER INVOLVEMENT

Direct placements may offer a more limited burden on the issuer's management resources as compared to a full public- or Rule 144A-marketed bond offering because of more targeted disclosure requirements, potentially shorter transaction timelines and a more directed due diligence process, partly due to the absence of public ratings.

INCREASED INTEREST IN DIRECT PLACEMENTS

While direct placements of bonds will generally involve smaller offerings than public- or Rule 144A-marketed bonds, we are seeing increasing interest from both issuers and investors in the direct placement market. Certain needs of an issuer are sometimes better understood and accommodated by direct placement investors who have particular familiarity with the issuer's business or asset class. As a general rule, direct placement investors negotiate covenant protections that are on a par with or often stricter than those seen in public- or Rule 144A-marketed bonds, but issuers benefit from a smaller set of investors to consult when dealing with matters of compliance and interpretation, and a more direct point of contact when an amendment is needed. The lack of a requirement to structure direct placements as "one-size-fits-all" tends to benefit certain issuers as well as motivated investors, who are often willing to conduct the necessary diligence to understand unique deal features that may not be otherwise permitted and/or reasonably priced by the broader market.

ABOUT KING & SPALDING

Celebrating more than 130 years of service, King & Spalding is an international law firm that represents a broad array of clients, including half of the Fortune Global 100, with 1,100 lawyers in 20 offices in the United States, Europe, the Middle East and Asia. The firm has handled matters in over 160 countries on six continents and is consistently recognized for the results it obtains, uncompromising commitment to quality, and dedication to understanding the business and culture of its clients.

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