

Holdco PIKs take spotlight in challenging private credit market

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Against a difficult backdrop of a challenging economy and stringent documents, sponsors are now expanding their use of available tools, with payment-in-kind (PIK) instruments gaining traction in Europe, and preferred equity solutions being deployed in the US.

One Rock's acquisition of [Constantia Flexibles](#) from Wendel provides a case in point, with the financing for that deal strongly contested between private credit and the broadly syndicated market. Former owner Wendel had put the Vienna-based flexible packaging firm up for sale earlier this year, through advisors Evercore and Marlborough Partners.

While HPS Investment Partners offered a €1.5 billion debt deal with a PIK or preferred equity element likely to be included in the private package, banks are understood to have offered a roughly €1.4 billion underwritten financing in term debt, plus undrawns of €250 million.

As leverage is decreasing, the use of Holdco PIK financings is increasing, allowing businesses to get 1x or 1.5x turns of leverage on top of their existing Opco debt and avoid pressuring their cash flow. "In 2021 it was not uncommon to see leverage exceed 6x for many businesses and that has now come down, at which point PIK becomes really useful," says Aymen Mahmoud, partner at McDermott Will & Emery.

"Issuers are increasingly looking for Holdco PIK or preferred equity alongside unitranche to maximise leverage and reduce the interest cost burden on the company," said Floris Hovingh, managing director at Perella Weinberg Partners.

Similar to the increase of amend-and-extend activity in the loan realm, the hiking of rates can make repayments difficult for some, though with PIK financings it is possible to circumvent the immediate repayments.

"If there is an overlevered debt structure it is often easier to find a solution with the incumbent lenders rather than finding new junior capital providers to reduce Opco leverage, as they will require a significant premium to inherit problems created by others," Hovingh said.

“For companies that need and can sustain that extra leverage with an excellent credit story, it is worth using the expensive debt instrument, as it remains cheaper than equity,” Mahmoud notes.