HAYNES BOONE

PRIVATE CREDIT CONNECTIONS

From The Insider's View

Scott Li, a Partner at CRG, shares his thoughts on recent deal flow and how CRG has been able to establish a track record of successfully investing in the healthcare industry for more than two decades.

Scott Li

Company & Title: *CRG - Partner*
Education: *AB in Economics from Princeton University and MBA from the Wharton School at the University of Pennsylvania*
Current City: *New York City*
Fun Fact: *My favorite sports trivia is mid 1980s New York Yankees*

How has deal flow been through the first half of 2024 and what are your projections for the rest of the year? In your view, what are the key drivers of that deal flow?

Deal flow has been strong in 2024. We've already closed four new investments this year. Unlike in 2023, when many investment opportunities were actually "zombies" as we call them (companies with little growth, limited resources, an older equity syndicate and no clear exit plan), 2024 has brought us far more compelling opportunities for deployment. We expect this trend to continue as more of the zombie companies restructure, merge, or go under, while the best ones rise to the top.

The primary driver of our deal flow is the development of our pipeline. As CRG has gained more experience and name recognition in the healthcare industry, we've been able to track more companies over a longer time period before investing. Currently, the average company in our pipeline has been tracked for approximately three years and this has allowed us to differentiate between industry trends and company performance. We've also built a robust network within the healthcare space, leading to a considerable amount of proprietary deal flow. Building this network and reputation has allowed us to source investments with little to no competition. With a focus on real, sustainable growth, we have the ability to strategically partner with borrowers and work with them if they miss a target or need more flexible terms.

A great example of this is OrthAlign, an investment we made at the end of 2023. The CEO, Eric Timko, was also the founder of Blue Belt Technologies, a prior CRG investment, and he and CRG stayed in touch after a successful exit from the company in 2015. Two years later, he became the Chairman of the Board for OrthAlign. Our team started preliminary discussions about partnering again, but OrthAlign wasn't in need of growth capital yet. We kept in touch with Eric over the years, and mid-last year, he approached us about doing serious diligence on OrthAlign as they were reviewing financing options. Within three months, we completed our diligence and provided a $50 million loan to the company.

What can CRG and other firms do to standout as competition increases in the private credit market?

At CRG, we aim to stand out in two key ways – with our deal structure and with our expertise. It's no secret that we focus exclusively on healthcare and that we have no plan to expand into other areas. Despite healthcare accounting for almost 20% of the US GDP, we

believe many pockets of the industry are still underserved. Additionally, healthcare is a highly specialized market and you can't be a tourist. While many firms have healthcare exposure, there is no substitute for managers that focus solely on healthcare given the need for product-specific knowledge and the vast array of opportunities.

How do you think firms can best manage the challenge of deciding whether to allocate limited resources to deploying committed capital versus managing existing portfolios?

We are a small team and time is our most valuable asset. If every company in our portfolio was performing at or above expectations, managing the portfolio would be easy. That's not always the case in practice (although we are getting closer). We firmly believe the best way to prevent a time-consuming workout process on an underperforming investment is to not make the investment in the first place. We believe that taking a proactive approach in both due diligence and company management allows us to spend as much time as possible on sourcing investments while also ensuring the best possible outcomes for our existing investments.

With respect to monitoring, we believe that it is vital to remain actively engaged with portfolio companies on an ongoing basis. As a general practice, we have the members of the diligence team for a new investment become the monitoring team after a deal is completed, and it is expected

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that they will own this investment throughout its lifecycle. Having the same team manage an investment through the entire lifecycle enables our team to gain valuable insights and experience at every stage. By actively monitoring and adjusting their investments over time, our team develops a deep understanding of various market dynamics, risk factors, and opportunities. This approach not only strengthens our team's ability to deal with unexpected hurdles, but also fosters trust and confidence between our team and our portfolio companies.

On the sourcing and diligence side, these processes are far more time-consuming. We conduct our diligence more like a PE firm in terms of the depth and modelling that we do internally. This also fits into our ideology of being a true partner to portfolio companies. We want to understand their growth trajectory and ability to repay our loan, but we also want to get to know their management team, understand their segment of the healthcare market, and assess how CRG can be a value add to the company outside of just providing capital. These things take time and energy and, in our view, limit the amount of time and energy spent on monitoring down the line.

About CRG

Founded in 2003, CRG invests in healthcare companies to meet their growth capital needs. The firm primarily uses senior secured term loans to provide capital to portfolio companies and, in certain cases, supplements these debt investments with equity exposure in various forms. The firm targets investments that it believes will generate consistent absolute returns in diverse market conditions, offer attractive current cash yields, and have strong downside protection. CRG seeks to capitalize on its deep industry knowledge to invest across all areas of the healthcare industry, including biopharma, medical devices, tools, diagnostics, pharmaceuticals, and services, with all investments achieving one or more of CRG's tenets of improving patient lives, reducing healthcare costs, and expanding access to care.

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