

INVESTMENT UPDATE

FOCUS ON PRIVATE CREDIT

Barely a day goes by without a headline about the private credit asset class, ranging from its rapid growth to liquidity pressures and concerns about the impact on broader financial markets. Yet many investors remain unclear on what private credit actually is, how it evolved, who originates these loans, and who ultimately provides the capital. Given the growing attention on the investment category, we thought it was worthwhile to provide a clear framework for understanding its structure, its role in the financial system, and how to interpret the current noise.

PRIVATE CREDIT OVERVIEW

At its core, private credit refers to non-bank lending conducted outside the public bond markets. These loans are negotiated privately between lenders and borrowers and often feature flexible structures, customized documentation, and financing terms tailored to specific borrower needs. They also often include collateral protection and covenant packages to better protect lenders. Because these investments are generally not easily traded, investor capital is typically committed for long periods of time. In exchange for this reduced liquidity and elevated underwriting complexity, private credit tends to offer yields that are higher than those available in public markets.

For investors, the appeal of private credit lies in its potential for high current income and diversification. For borrowers, the benefits include speed, flexibility, and bespoke financing solutions that are often unavailable through traditional lending channels.

Private credit encompasses a broad range of subcategories, each serving different borrower profiles and investor objectives, with the vast majority of the approximately \$40 trillion market being investment grade. The roughly \$38 trillion investment grade segment includes direct corporate lending to investment grade issuers, privately issued residential and commercial mortgage backed loans, bank syndicated loans, asset-based loans, and infrastructure loans. These securities have similar attributes of like-rated public securities, including a low risk of default and strong capacity to meet debt service obligations.

Much of the recent scrutiny has focused on the remaining, generally non-investment grade, portion of the market—specifically the approximately \$1.7 trillion direct lending segment. In this segment, loans are extended primarily to non-rated or below-investment-grade middle-market companies, often private equity-backed, to finance acquisitions, expansion initiatives, recapitalizations, or ongoing operations. Despite being relatively small, the direct lending segment is among the most complex from a risk perspective. Borrowers are typically more highly levered, and while loans are often secured and covenant-protected, investor concerns have increased around weakening credit quality, underwriting discipline, and valuation transparency.

PRIVATE CREDIT EVOLUTION

To better understand these concerns, it helps to review private credit's evolution and today's key lenders and investors.

Private credit plays an important role in the global financial ecosystem. While private lending in various forms has existed for decades, its scale has expanded dramatically over the last ten years from approximately \$500 billion in 2015 to roughly \$1.7 trillion in direct lending today.

A major catalyst for this growth was the Global Financial Crisis (GFC) of 2008, which exposed vulnerabilities across traditional banking channels following the collapse of the housing market. In response, Congress passed the Dodd-Frank Act which materially increased the amount of capital banks are required to hold against various asset classes, particularly loans. As such, banks pulled back from certain forms of lending, including residential mortgages and corporate loans. Yet the economy's need for capital persisted, and non-bank lenders stepped in to fill the gap. That dislocation laid the groundwork

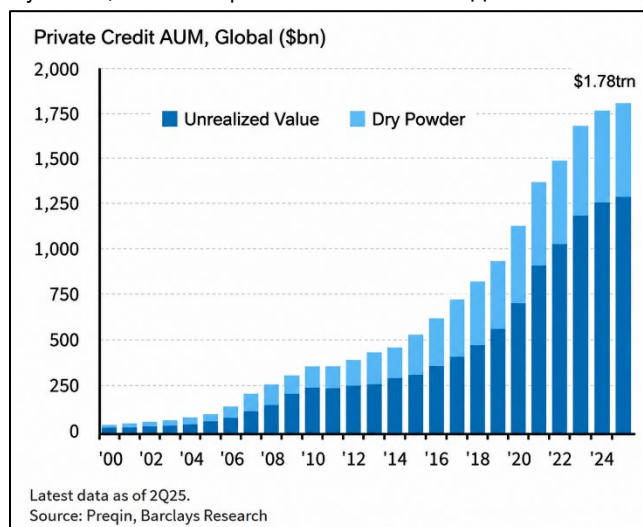
for the rapid expansion of what is now broadly referred to as private credit.

PRIVATE CREDIT LENDERS

So, who are these lenders? They are primarily non-bank financial institutions (NBFIs). This broad category includes asset managers, business development companies (BDCs), insurance companies, private equity firms, hedge funds, and online lenders. These institutions originate loans and assemble portfolios that are then sold, syndicated, or financed across a broad investor base, facilitating both lending and investment activity outside the traditional regulated banking system.

An important dynamic, however, is that traditional banks often provide financing to the NBFIs themselves, including in direct lending strategies. In fact, lending to NBFIs has been one of the fastest-growing loan categories for banks since the GFC. According to the FDIC, bank exposure to NBFIs has grown at a compound annual growth rate of nearly 22% over the last 10 years, approximately three times the growth rate of the next-fastest-growing loan segment.

Among non-bank lenders, BDCs have become especially important providers of private capital and therefore have drawn increased investor attention. BDCs were established by Congress in 1980 to promote capital formation for private businesses and are regulated under the Investment Company Act of 1940. They are permitted to use leverage to enhance returns but must operate within defined regulatory constraints. Specifically, BDCs are generally required to maintain debt-to-equity below 2x, and operating with leverage above 1x requires adherence to additional governance and asset coverage rules. By law, BDCs must distribute at least 90% of taxable income to shareholders, which is why many offer attractive dividend yields.





PRIVATE CREDIT INVESTORS

Investors typically access private credit through dedicated funds managed by specialized alternative asset managers. Historically, the investor base has been overwhelmingly institutional—insurance companies, pension plans, endowments, and sovereign pools of capital. The long duration nature of their liabilities aligns naturally with the long-dated, less liquid nature of private assets. More recently, however, retail participation has expanded considerably, as wealth managers increasingly allocate to private credit in search of higher income and improved portfolio returns. JPMorgan estimates that retail investors own as much as \$400B of the \$1.7T direct lending class. This shift has introduced a new set of concerns, as retail investors may not fully appreciate the liquidity constraints embedded in these vehicles.

PRIVATE CREDIT RISKS

While many of the private credit lenders and vehicles are subject to regulations including SEC oversight, the underlying investment portfolios can still be opaque, and the assets themselves remain inherently illiquid. Much of the concern surrounding private credit today focuses on the potential for deteriorating borrower fundamentals, stale valuations, looser underwriting standards, investor redemption risk, and the possible disruptive effects of AI on software-heavy borrower bases. However, making accurate assessments of these risks is challenging given the limited transparency and the lack of liquidity in secondary markets.

Recent press coverage has highlighted multiple instances in which investors have faced delays or restrictions on redemptions from private credit vehicles. In some cases, BDCs and related structures have imposed gates, limiting withdrawals. In others, sponsors or affiliated partners have provided temporary liquidity support, while some funds have been forced to sell assets at suboptimal prices to meet redemption demands.

In addition to the impact of illiquidity, several bankruptcies over the last few quarters have also caused turbulence. The most impactful of these include the high profile First Brands and Tricolor bankruptcies. They initially raised concerns about underlying credit quality; however, in both cases the losses were driven by fraud as the companies double-pledged collateral, emphasizing the importance of collateral monitoring.

That's not to say the coast is clear with regard to credit quality. Certain sectors are facing greater scrutiny due to lender concentrations and concerns about the durability of underlying business models. In particular, investors and lenders are growing increasingly uncomfortable with loans to software companies given that AI automation tools may reduce demand for some software services. Additionally, an increase in PIK (payment-in-kind) in lieu of cash interest payments indicates a worsening of credit quality. Construction of portfolios that includes diversification of borrowers by industry and geography, along with strict monitoring of loan covenants and collateral, and continuously reviewing exposures and correlations, will be paramount to the success of the asset class.

These developments reinforce the importance of careful due diligence—not only on the asset class itself and the underlying loans, but also on manager underwriting discipline, liquidity management practices, and the manager's long-term track record.

RECENT MARKET DEVELOPMENTS IN PRIVATE CREDIT

Market conditions within private credit became more challenging late last year and into early '26. Private credit lenders pulled back on originations due to weaker investor demand and rising redemption activity. To compensate for higher perceived risk and potential increases in loan losses, these lenders also increased borrowing costs. In Q1'26, private lenders reported a 14% decline in loan originations while banks reported an almost equivalent increase. This shift reflects the impact of tighter lending standards in private credit but also the impact of deregulation and easing capital requirements for banks, allowing banks to re-enter the market with more competitive rates.

IMPACT ON PUBLIC FIXED INCOME MARKET

How does all of this impact the public investment grade fixed income markets? Directly, the impact is minimal as publicly-traded BDC index-eligible debt totals about \$60 billion, which equates to less than 1% of the \$7.7 trillion IG Corporate Index and about 0.25% of the \$31 trillion US Aggregate Index. Indirect exposure to non-IG private credit by way of bank and insurance company debt is also quite small, although accurately identifying exposure can be challenging. In aggregate, insurance industry allocations to high yield securities, including private letter ratings, bank syndicated CLOs, middle market CLOs and ABS, are each estimated at less than 1% of investment portfolios. US bank exposure to NBFIs loans has increased meaningfully over the past decade, rising to just over 11% of total loans at year-end 2025 from only 4% at year-end 2015. However, this figure includes all lending exposure to NBFIs. Loans to business intermediaries account for less than one-quarter of that total exposure, representing only 2.8% of total bank loans.

Regardless, investors, rating agencies and regulators continue to keep their eye on private credit concentrations within bank and insurance portfolios. Given the interconnectedness of these entities, regulators have increased scrutiny on private credit to better understand hidden risks and linkages. Importantly, at the end of March '26, Fed Chair Powell said he did not see a risk of contagion in private credit markets that could result in a broader systemic event.

BOTTOM LINE

Private credit remains an important and evolving component of the global financial system. While portions of the market continue to offer attractive financing solutions and income potential, recent developments have reinforced the importance of liquidity awareness, disciplined underwriting, valuation transparency, and careful manager selection. Given the limited transparency, constrained secondary market liquidity, and relatively short track record of many direct lending strategies through a full credit cycle, we continue to favor publicly traded fixed income markets. We believe public markets offer meaningful advantages through daily liquidity, transparent pricing, broad diversification, and the flexibility to adjust portfolio positioning as market conditions evolve.

AGINCOURT NEWS

We're excited to welcome Vanessa Hampton, who joined Agincourt this month as a Director on our Client Service and Marketing team. She brings 20 years of experience in the financial services industry, most recently serving as an Institutional Client Strategist with Sterling Capital Management.