Private Credit - Growth Drivers and Interactions with the Corporate Bond Market

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Private Debt Opportunity as Banks Retreat from Middle-Market Lending

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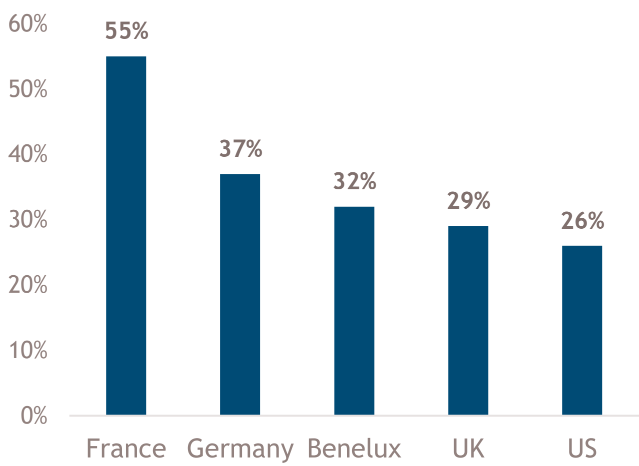
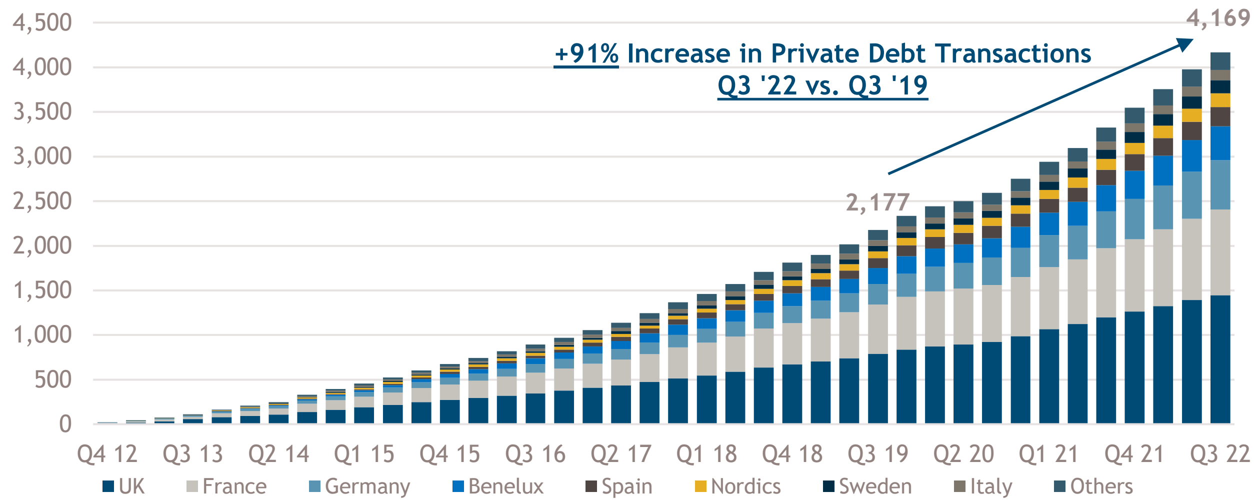
The number of private debt transactions in Europe grew by 91% between 2019-22

Weight of Bank Lending by Geography[1]



Cumulative Number of Private Debt Deals Across Jurisdictions[2]



Weight of Bank Lending in Europe is Converging to US Levels…

- Banks' retreat from Middle-Market lending continues to create significant opportunities for direct lenders.

…Leaving room for significant growth in the Private Debt Market in Europe

- Different levels of Private Debt penetration across jurisdictions favors continued growth in the Private Debt Market for the foreseeable future
- Less penetrated jurisdictions experienced 7.5-10.0x number of transactions in 2022 vs. 2015, whereas more advanced jurisdictions such as the UK, France and Germany grew by 4.5-6.0x

(1) European Bank Lending Share based on Houlihan Lokey MidCap Monitor 2021 (issued in Q1 2022). Data for US based on Preqin, as of July 7, 2022. (2) Private Debt Deals based on Deloitte Alternative Lender Deal Tracker – Autumn 2022.

Illiquidity Premium and Low Volatility vs. Public Markets

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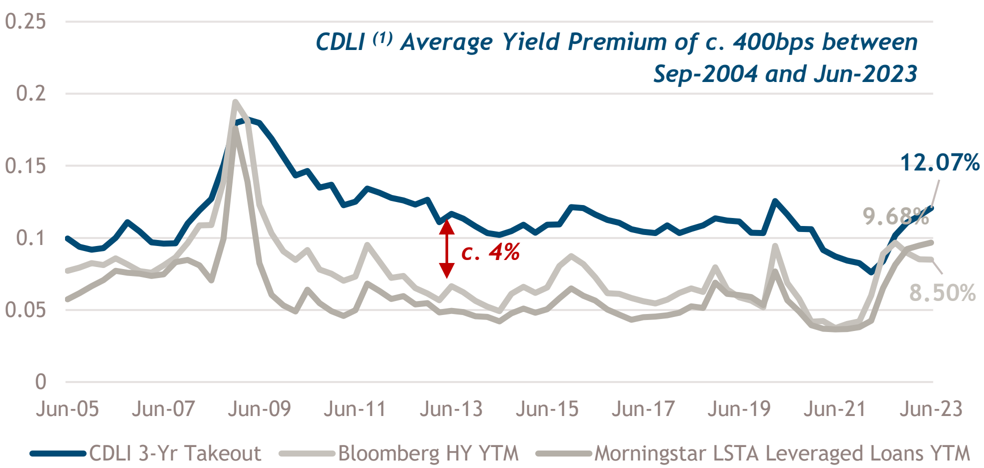
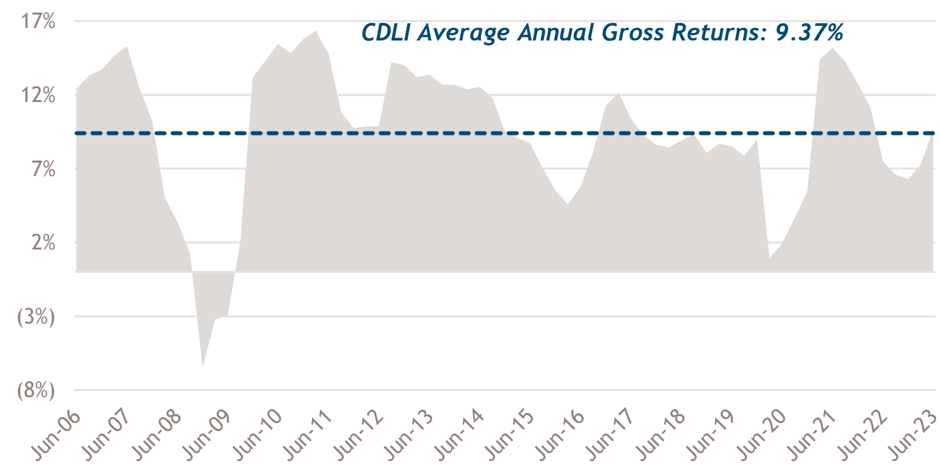
Since 2004, Private Debt has offered on average c. 4% illiquidity premium, limited volatility and 9.4% average return

The Cliffwater Direct Lending Index is used as a proxy for Global Private Debt as it provides publicly available data

Yield Comparison – Private Debt vs. HY and Leveraged Loans, 2005-2023



Cliffwater Direct Lending Index[1] Performance (LTM), 2006-2023



Private Debt Offers c. 4% Illiquidity Premium vs. Public Markets

- Despite temporary dislocations (2008 and 2022), Gross yields for direct lending have averaged c. 4 percentage points above traded high yield bonds and Leveraged Loan Indexes over the last 19 years.

Reduced Volatility, with just 3 Quarters of negative returns since 2005

- Direct Lending has shown a robust track record through the cycle, with average gross returns of c. 9.4%

Past performance is not indicative of current or future results.

Source: Cliffwater Direct Lending Index (CDLI) data as per Cliffwater 2023 Q2 Report on U.S. Direct Lending as of June 30, 2023. Data is updated on annual basis. Please see index definitions at the end of this presentation. Index performance is for illustrative purposes only. You cannot invest directly in the index. Muzinich views and opinions not to be construed as investment advice.

Drivers and Corporate Bond Market Interaction

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Growth Drivers

Borrowers

- Desire for customized funding solutions and no need for public disclosure of proprietary and confidential information

Investors

- 28% investors currently invested in private debt vs. 63% in private equity[1]
- Estimated average target private debt allocation just over 6% of total assets vs. 15% in private equity
- Offers significant yield pick-up versus high yield bonds and leveraged loans
- Newish ELTIF structures allow retail investors to access the asset class

Structural Changes in Public Markets

- Growth in public market deal sizes (due to asset price inflation and need for liquidity) has broadened opportunity set for private debt funds which need not worry about liquidity mismatch
- Growth of 'barriers to entry' in public markets for smaller borrowers

Bank Lending Regulation

- Changes in bank regulation contributed to banks' retreat from corporate lending, especially for companies with gross debt/EBITDA above 4x (European Central Bank's supervisory expectation on bank leveraged lending)

1. Source Prequin, as of March 2024. Muzinich views and opinions for illustrative purposes only.

Discussion Points

1. Impact on the broader credit market
The private credit market is impacting the functioning of the public debt markets. Amend and extend restructuring are a new feature in the public debt market. The Asset Management Industry does not fall under the Basel Banking Definition of Default.
How might the public market further change in response to growth in private debt?

2. Diverging Leverage
Current bank regulation has put a lid on lending to highly levered companies in the banking sector but has not stifled unregulated risk taking across private credit funds. More than 90% of private debt deals had a leverage of >5x, more than 40% had a leverage of >6x in 2023. PIK and Toggle (pay-when-you-can) option offered to borrowers might create ‘zombie’ companies.
How much of a concern is the level of leverage in private debt markets?

3. Diverging ability to fund refinancing and restructurings
On top of the Basel Banking Regulation, the ECB has issued the Calendar Provisioning Regulation under which Non-Performing Exposure must progressively be written off against Tier 1 capital. This rule is EU specific and encourages banks to fire sale. This regulation does not apply in Asset Management and in Non-Bank Lending.
Against this backdrop will private debt continue to grow at the expense of public debt issuance?

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