

Crowded Market in Private Credit? Enter the Large, Public Alternative Managers

We see evidence of crowding specifically in the large market space among publicly traded alternative managers. These multi-asset alternative firms have had a clear impact on the private credit landscape by raising significant amounts of capital with an investment focus away from core middle market borrowers (\$20–100 million EBITDA); instead, they focus almost exclusively on large market borrowers (\$100+ million EBITDA). This should be no surprise. These firms were purpose-built to “go big” in order to rapidly grow their assets under management (and fee-based earnings) for public shareholders. The result is...a crowded market...but mostly in the large market space. While large market deals may be episodically attractive, we believe there’s an advantage in selective deal sourcing across the entire middle market universe.

Crowded Market?

Many investors ask whether the private credit market has gotten more crowded: We say it depends where you look.

The broad “core” of the middle market direct lending asset class (representing borrowers with average weighted EBITDA of \$20-100 million) has, by and large, retained its contours and characteristics over time. However, at the outer edge of the asset class, we’ve witnessed a kind of selective hypertrophy, focused almost exclusively in the “upper middle” or large market. This outsized growth is due to the recent entry of a rather small number of super-sized funds, managed typically by publicly traded alternative managers.

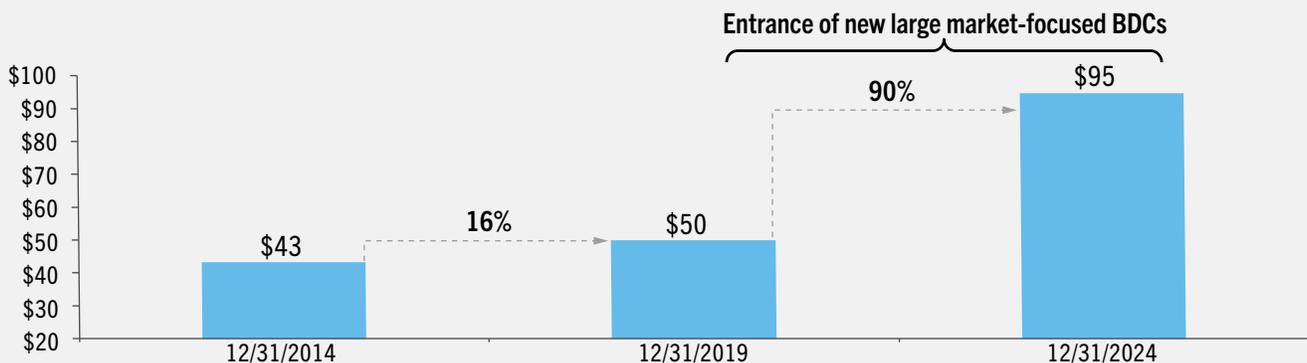
Signs of this bulge bracket intrusion in middle market lending are clear when looking, over time, at the average weighted EBITDA of borrowers across the direct lending market.

From 2014 through 2019, during a period of robust investor interest and asset growth in the middle market space (thanks in part to modest yields available from traditional fixed income during this time), the average direct lending borrower EBITDA edged up only modestly, rising 16% from \$43 million to \$50 million. But as several new publicly traded alternative managers entered the space, beginning around 2020, the borrower profile shifted significantly: Average EBITDA increased 90%, from \$50 million to \$95 million (see Exhibit 1).

Exhibit 1

A Sudden Shift: Enter Large Public Alternative Managers

Weighted Average Borrower EBITDA in Direct Lending (\$ in millions)



Source: Lincoln International and Golub Capital internal analysis. Borrower EBITDA represents the average EBITDA for all securities in the Lincoln Senior Debt Index. The Lincoln Senior Debt Index is a quarterly index that tracks the fair market value of 1,600 middle market direct lending credit investments every quarter across approximately 175+ fund clients in the United States and in Europe. The reflected data is as of December 31, 2024.

Is Double Trouble?

This large market approach by just a handful of business development companies (BDCs) had a tectonic impact on the middle market space in terms of growth, creating a kind of parallel universe in the asset class. This is evident in the sheer size and speed of asset growth among BDCs.

Over the first 20 years of this century, the middle market direct lending asset category, as measured by the BDC universe (comprising both publicly traded and non-traded BDCs), grew to \$126 billion in total assets—to be clear, that includes assets raised cumulatively over 20 years. But in just the last four years, six newly launched non-traded BDCs have raised a larger amount of capital (\$141 billion) all on their own. In just four

years, and attributable to just six newly launched funds, the private credit BDC space has more than doubled in size (see Exhibit 2).

Raising this amount of capital in such a short period is a significant achievement, but there's little secret in how it was done: These newcomer BDCs are getting big by buying big. They were able to achieve enormous scale over such a short period of time by targeting only the largest of private borrowers, lending to companies with an average EBITDA of \$241 million.

But beyond their commitment to large market borrowers, these new BDC entrants share several other characteristics.

Exhibit 2

Does Double Mean Bubble? Large Market BDCs Make Their Mark

20+ Years of Total BDC AUM Raised¹
(Ending 12/31/20)

4 Years of AUM Raised by Six Large Market BDCs²
(Ending 12/31/24)



Large market-focused BDCs have raised an enormous amount of capital in a short period, more than doubling the total assets under management (AUM) raised by the entire BDC sector over a 20-year period.

1. Source: Total BDC capital raised used total AUM from Cliffwater's Direct Lending Index. Based on market data as of December 31, 2024.

2. Source: Stanger Market Pulse, BDC monthly fact sheets, company presentations, SEC filings and Golub Capital internal analysis. BDC cohort consists of six largest private BDCs that report a weighted average EBITDA. Based on market data as of December 31, 2024.

The Big Must Get Bigger

The BDCs that have helped drive this asset class shift to higher EBITDA companies share similar characteristics:

- They are all large. The law of large numbers tells us that for larger asset management firms to grow, they need higher flows and larger investment sizes. To “move the needle” at these firms, they are required to gather more investor assets and seek out larger investments.
- They are almost all multi-asset managers, with distinct businesses in private equity, private credit, real estate, infrastructure, hedge funds and other verticals. This inculcates a natural competition across the businesses to deliver on the growth goals of the firm and its investors.

- They all tend to be publicly traded. This means that every quarter, their shareholders and analysts are watching to see progress; there’s one measure that matters above all, and shareholders continue to demand quarter-over-quarter growth in fee-generating AUM.

At the end of the day, these funds are obliged to “go big” when it comes to both asset gathering and, relatedly, the size of their individual deals. So, when public alternative asset managers advertise the particular virtues of large market lending, the truth of the claim should be assessed: They have little choice but to target these types of investments.

Style Drift Narrows the Public/Private Divide

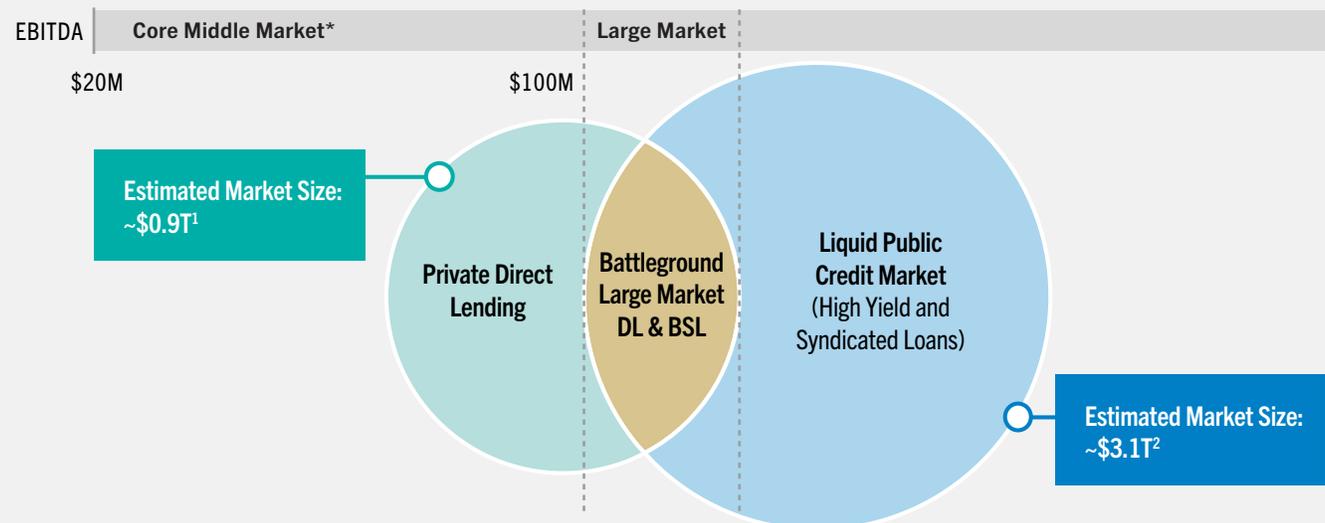
But away from debatable marketing assertions, is there any broader concern associated with this type of growth occurring in the traditional direct lending market? These large market private credit lenders are creeping into public credit territory, competing with broadly syndicated loans and high yield and clouding some important distinctions between public and private credit.

The large market BDCs occupy a form of “gray zone” between the less liquid private middle market and more liquid public

credit markets. We believe these are two distinct asset categories, each with unique characteristics, attracting different types of investors with varying costs of capital. For example, broadly syndicated loans (BSLs) typically have lower rates, fewer covenant protections and higher leverage compared to private middle market loans. Competing in this gray zone can result in a blending or blurring of terms between the BSL market and private direct lending (see Exhibit 3).

Exhibit 3

Blurring the Lines: Large Market BDCs Tilt Toward Public BSLs Public vs. Private Lending Spectrum and the Battle Within



1. Source: Private middle market direct lending represents total direct lending assets under management of \$594 billion from Preqin’s database plus \$325 billion of public BDCs and perpetually private BDCs from Cliffwater’s Direct Lending Index. The data is as of September 30, 2024.

2. Source: Syndicated loan market of \$1.4 trillion represents par amount of total U.S. loans in Morningstar’s LSTA U.S. Leveraged Loan Index. Sourced from Pitchbook LCD’s “U.S. Loan Stats Weekly Trend” report as of November 15, 2024. High yield market \$1.7 trillion represents total outstanding from S&P U.S. High Yield Corporate Bond Index. Sourced from Pitchbook LCD’s “Interactive High-Yield” Report as of October 31, 2024.

*Note: This presentation defines the core middle market generally as borrowers with \$20-100 million of EBITDA and the large market segment generally as borrowers with over \$100 million of EBITDA.

Seek a Wider Funnel

To be clear, we do not seek to apply value judgments to any segment of the market or to argue that “large is bad” or “it’s better in the middle.” Both approaches may deliver differentiated results for investors relative to their public credit peers. But their virtues are neither monolithic nor unchanging. In other words, the relative attractiveness of large market or traditional core middle market lending opportunities will vary over time, just like any other investment.

At times, investing in large market deals may look appealing. But we do not believe large market lending is best all the time, especially when the liquid credit markets are functioning well.

Instead, we believe a higher value proposition lies in being able to lend across the entire direct lending size spectrum—from lower middle to core middle and beyond.

But that requires a lot of resources, a good deal of experience, incumbencies across the sponsor and middle market company landscape and other strengths that we, in particular, have spent years developing. The important point is not to be beholden to any one segment of the market simply due to the external requirement for rapid and continuous growth. That would limit the opportunity set and reduce the diversification inherent in the broad middle market direct lending universe.

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