

FUND NEWS

# Private Credit: Popular, Complex, and NOT Where We're Taking Risk Today

Nedgroup Investments **21 October 2025** 8 min read

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From the Fixed-Income desk

The Nedgroup Global Strategic Bond Fund has material constraints hard coded into its prospectus. Several of those are designed to restrict the type of assets the fund managers can buy. Unrated, poorly researched, lower quality securities are generally excluded. Such limits can be of benefit in times of stress.

## Comments on private credit

Private credit has ballooned into a \$2trn asset class (depending on where you draw the line on the definition of 'private credit'). Looking more broadly, Non-banking Financial Institutions (NBFI) such as Private Credit vehicles, have seen their share of the corporate lending increase rapidly to over 10% of total loans in the US - filling the gap from the banks who have cut back on corporate lending

post GFC. The industry rightly deserves increased attention off the back of concerns related to lending standards, with First Brands and more recently two US regional banks. These issues are idiosyncratic and the Banks that have reported earnings thus far (including the regional banks) have reiterated that there is no need for concern across their business models and have on the whole seen improving credit quality. Despite this, the likes of JPM and Morgan Stanley are unlikely to be the location of the next 'cockroach' and focus should on the NBFI given its rapid growth in such a short space of time.

### **Warning...**

We have warned on private credit for a while now, highlighting its illiquid nature and relative opacity in relation to the underlying assets, and stressing that this asset class has not been tested through a default cycle. We are not alone as the IMF, the Boston Fed and Moody's have all stated that private credit is increasingly posing a systemic risk. Defenders of private credit highlight the low leverage, seniority of lending, and low non-accrual rates as reasons for the asset class to hold up. But we would be keen to understand how the asset class reacts with a pickup in default rates or increased market stress.

We know any increase in defaults would not be isolated to the private credit market but exposure to certain sectors such as software and technology is greater than in the public debt markets so it is plausible that private markets see a higher proportion of beta adjusted defaults. To add to this the recovery rates are not fully understood, debt is typically senior, but default rates have been masked as lenders are able to renegotiate clauses or implement Payment-in-kind ("PIK") structures that do not get classified as defaults. The lack of mark to market accounting of the underlying assets adds to the uncertainty but there will come a point when financial and legal engineering will not be able to mask the true value in the capital structure.

Secondly, the interconnectivity of the industry is not fully understood. For example, the extent to which private credit has been funding the 2021 vintage private equity backed companies that have struggled through the rate environment. Additionally, Business Development Companies (BDCs) are now big issuers of IG corporate bonds (see below). We know that Apollo for example is one of the biggest buyer of these bonds and suspect an individual institution's full exposure to the asset class across direct loans, private credit funds, GP

stakes, private equity and corporate bonds is likely understated but primarily, not understood.

Finally, the key concern for a credit investor is whether they will be repaid principal and interest. Retail investors now have access to private markets and one prominent UK retail site has warned investors they may never see their money again. Sure, investors can gain an illiquidity premium but is a 10% return with no visibility on recovery or when your money can be redeemed adequate compensation? BDCs point to their quarterly redemptions (technically a tender since they do not have to redeem your share), as a way to smooth stress but in a liquidity event leveraged participants who are unable to redeem stakes in BDCs could result in stress spreading to more liquid asset classes. Blackstone's listed BDC 'BCRED', limits redemptions to 5% a quarter and has cash to cover a quarter of redemptions, with 10% of its assets in liquid loans and then the portfolio providing a yield around 10% so there is liquidity there. This could change quickly but the focus would mainly be on the investor base and what happens when they are unable to redeem.

### **Our strategy: Nedgroup Investments Global Strategic Bond Fund**

The Nedgroup Investments Global Strategic Bond Fund strategy remains focused on the core part of the credit markets and we do not touch CCCs let alone anything 'private' so we can stay well clear of direct exposure. We believe in credit through the cycle but stress this refers to the public asset class only. It is worth highlighting though that BDC bonds now account for 3% of the US financials credit index which is not negligible and does warrant attention. The attraction for an IG credit investor would be the excess carry offered from the BDC bonds, which are BBB- rated and price towards BB. Over the last 2 years they have generated excess returns against the financials index but ultimately at the expense of increased volatility. At roughly 1.8x the beta of the US financials index, the bonds would materially underperform in a sell off. BCRED's bonds have widened 25 basis points as sentiment has weighed on private credit over the last two weeks and we can expect further underperformance when more 'cockroaches' are uncovered.

In terms of direct portfolio implications this is a sector we can avoid, elsewhere we are underweight insurers given their outsized exposure to private market.

The volatility in October and potential for a more systemic event has reaffirmed our preference for the core parts of the fixed income market.

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