



**Private Credit
under fire:
why the headlines
tell only half the story**

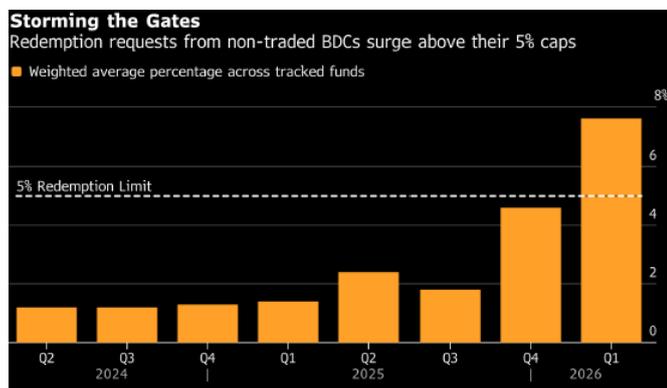
Source: iStockphoto.com/sankai

Redemptions, gates, defaults, AI fears, valuations, the noise around direct lending has never been louder. But a closer look at the data tells a more nuanced story.

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If you have followed financial news over the past few weeks, you would be forgiven for thinking private credit is in crisis. BlackRock capped withdrawals from its \$26 billion HPS Corporate Lending Fund after investors demanded nearly double the 5% limit. Blackstone allowed a record 7.9% redemption from BCRED, backstopped by \$400mn of internal capital. Blue Owl halted redemptions from OBDC II and sold \$1.4bn of loans. Cliffwater faced requests reaching 14% of shares, the list goes on and on and is expected to continue in the coming days.



Source: Bloomberg

The headlines are real, the anxiety understandable. But the narrative that private credit as an asset class is broken deserves scrutiny. What we are witnessing is not a credit crisis. It is a stress test of the distribution model, and a correction that will ultimately separate disciplined managers from the rest.

1. The liquidity paradox: a distribution problem, not an asset problem

The core tension is structural. Private credit loans are illiquid by design. Yet the industry's biggest growth story has been packaging these assets into non-traded BDCs in the US, UCI Part II SICAVs and ELTIFs in Europe, offering quarterly redemptions typically capped at 5% of NAV. In addition, most of these funds have a soft-lock feature putting emphasis on the longer time horizon of a direct lending investment (a penalty that the investor should pay if he decides to redeem before and agreed period, usually 12 to 18 months). Finally, the quarterly liquidity is always subject to an approval (optional).

As the FT's Robert Armstrong put it, there is no such thing as an investment product being a little bit liquid. At some point in every cycle, investors will want more than the structure can give, and when told "no," their demands only increase.

This is exactly what is happening now. Redemption requests from non-traded BDCs surged past the 5% quarterly threshold in Q1 2026 in many funds.

We hear saying that there is an "illiquidity mismatch" in these direct lending funds, but is that simple? Goldman Sachs's Vivek Bantwal called withdrawal limits "features and not bugs." Apollo's John Zito said BlackRock's gating decision was exactly right, noting these products exist to match fund liquidity to the natural liquidity of assets. In other words, the liquidity in these products is a liquidity option.

Private credit evergreen funds are long-term capital allocation vehicles with limited, conditional liquidity features, they are not money market funds. Therefore, how the liquidity terms are communicated to clients is of utmost importance. Was it the industry that failed to communicate the true nature of these products, or were investors so captivated by the returns that they heard only what they wanted to hear? Most likely, the answer is complicated and should be analysed on a case-by-case basis.

2. Shadow defaults and PIK: more noise than signal

One of the most prominent narratives has been the rise of the "shadow" default rate, an umbrella term lumping together PIK interest payments, maturity extensions, covenant waivers, and other amendments. While these can signal borrower stress, they are not defaults. They are tools private lenders use to stabilise businesses and avoid costly bankruptcy proceedings.

StepStone Group's February 2026 paper provides helpful data here. As of December 2025, the shadow default rate for middle-market loans had declined to around 4.5% from a top at 5.72% in Q4 2023. During the same period, the default rate slightly increased. This must be put in context of an unusually low default post Covid environment, where government support program artificially pushed default rates lower.

Middle Market Default Rate



Source: Stepstone, S&P Global, as of December 2025

PIK provisions have also drawn significant attention, but the picture is more granular. According to S&P Global data, PIK toggles are overwhelmingly concentrated among larger issuers: 44% of borrowers with over \$1 billion in debt have PIK optionality, compared to just 3% below \$350mn. This should be observed in greater context: larger companies can choose to finance through the broadly syndicated loan or high-yield bond markets, where documentation standards are typically more permissive. To remain competitive and justify the higher spreads that direct lending commands, private lenders have increasingly offered targeted flexibility, including PIK toggles, as a way to bridge the gap between what borrowers can get in public markets and what private capital demands in return.

Not all PIK is created equal. A PIK toggle negotiated at origination, so-called “good PIK”, is a pricing feature: the borrower secured flexibility upfront, the lender accepted it knowingly in exchange for a wider spread, and it may never be exercised. A PIK imposed through a loan amendment after the borrower can no longer service cash interest, “bad PIK”, is a workout concession that increases total debt, defers cash recovery, and typically signals deteriorating fundamentals. The distinction matters enormously when assessing portfolio risk, but it is almost absent from the headlines.

That said, the bear case deserves a hearing. Pimco’s Christian Stracke called the current environment a “crisis of really bad underwriting.” Partners Group’s Steffen Meister warned defaults could double, particularly where lenders are exposed to AI-driven disruption. While AI-related fears have added urgency to the sell-off, UBS projected a worst-case 15% default rate for software-exposed portfolios, a forecast Ares CEO Mike Arougheti publicly called “irresponsible”. The reality is that AI disruption will happen but will take time, and senior secured positions with sub-50% LTVs provide meaningful cushion. These are legitimate concerns. But they describe normalisation from exceptionally low post-Covid levels, not systemic distress, and many high-profile defaults involve large-cap syndicated loan borrowers or asset-based structures outside the scope of traditional middle-market direct lending.

3. Valuations: imperfect by design

Valuation becomes very important when you give investors a liquidity option. The valuation debate has arguably generated the most heat. Glendon Capital Management publicly questioned Blue Owl’s loan marks, alleging funds had underreported losses. Bloomberg detailed how Apollo and FS KKR valued the same Medallia loan at 77 and 91 cents on the dollar respectively, a 14-point gap that has become a poster child for mark-to-model scepticism. In addition, we have seen loans going from 100% to 0% which strongly question the validity of the initial 100% mark.

These are valid criticisms, and the industry must address them with more transparency. But the data does not support the conclusion that private credit valuations are systematically inflated. StepStone’s analysis of historical BDC data shows that during periods of financial stress,

cumulative markdowns have consistently exceeded realised losses by roughly 1.7 to 2.5 times. In other words, private credit managers have historically been too conservative in their markdowns, not too generous. Is this time different?

The recent sale of Blue Owl OBDC II seems to indicate a mixed picture: it sold \$1.4bn of its portfolio at 99.7 cents which represented roughly 30% of investor capital. This seem to indicate that at least for this part of the portfolio the marks were not disconnected to an actual transaction price. Only the future will tell how the remaining part of the portfolio (deemed riskier) will perform.

As Lincoln’s Ron Kahn noted, marks on performing loans are tightly clustered, divergence emerges only when borrower performance deteriorates and lenders reach different conclusions about recovery.

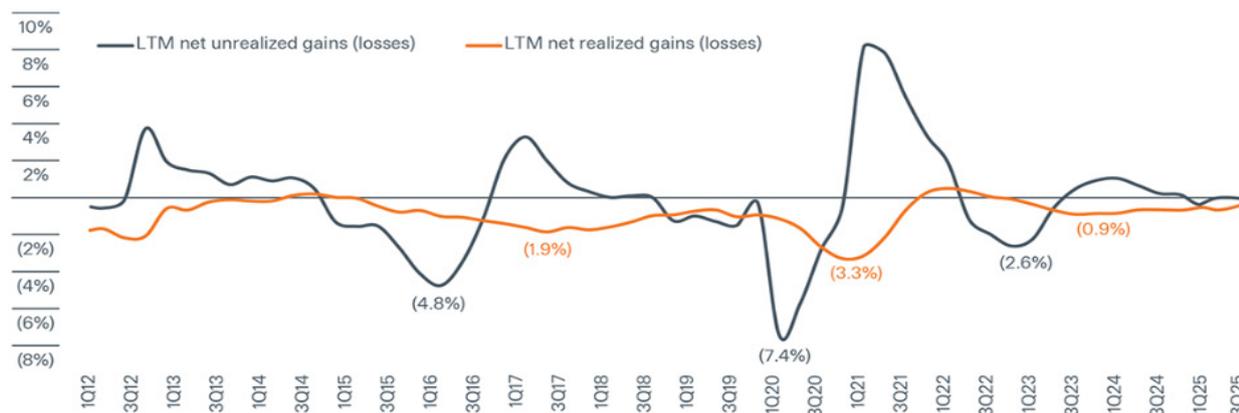
A loan that is marked from 100 to 0 poses other questions as it looks more like a failure of process rather than a failure of credit (unless a case of fraud appears): why weren’t the marks adjusted progressively? Was it avoiding triggering redemption anxiety? Or was it genuine analytical disagreement about recovery?

4. Private equity interconnection

Private credit is now a \$1.8tr market, deeply intertwined with private equity, which relies on direct lenders to finance leveraged buyouts, refinancings, and add-on acquisitions.

I have heard many commentators describe recent events as the beginning of the end for private credit. But even in a negative scenario coupled with a deteriorating macro environment, the systemic importance of the asset class means there is a high probability that the industry will not collapse as a whole. There is too much capital, too many institutional commitments, and too much structural reliance from private equity sponsors for the asset class to unwind. In addition, more private companies are remaining private for longer, also a strong argument for Private Credit. What can and likely will happen is that weaker managers, those with concentrated portfolios, more aggressive marks, or poor underwriting discipline, will be forced to consolidate or exit. For the survivors, the current events will be an opportunity: thinned competition, wider spreads, and more disciplined deal flow.

BDCS LTM realised and unrealised losses



Source: Stepstone, Cliffwater, as of September 2025

Indeed, spread widening in periods of stress is precisely the mechanism through which disciplined lenders get rewarded. Managers with dry powder can deploy into a market where borrowers have fewer alternatives and lenders can demand better terms, tighter documentation, and wider spreads. The best vintages in private credit have historically been assembled during periods of dislocation, not during the competitive frenzy that preceded them.

This dynamic also exposes an underappreciated structural weakness of evergreen fund: when investing in an evergreen structure, you delegate part of the vintage diversification to the fundraising team of the fund. Unlike closed-ended vehicles, which draw on committed capital regardless of market sentiment, and where the LP can decide how to allocate between vintages, evergreen funds are highly dependent on ongoing subscriptions to deploy into new deals. In a year like this one, where gates are being activated and net inflows are turning negative, evergreen funds may find themselves capital-constrained at precisely the moment the opportunity set is most attractive. Closed-ended funds from the same manager, by contrast, can continue to call and deploy committed capital into a dislocated market. The important question this raises is: will we see a meaningful performance gap emerge between evergreen and closed-ended vehicles of the same GP over the coming vintages?

5. What public markets are telling us

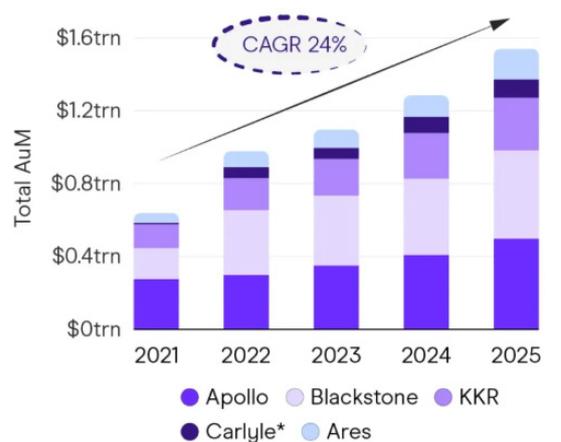
Multiple listed BDCs are trading at or near all-time lows, at steep discounts to reported net asset values. The weakness extends across the sector, but the repricing has not been uniform. Discounts vary significantly from one vehicle to the next, driven by a combination of factors: perceived portfolio quality, sector concentration (software exposure in particular has drawn scrutiny) the proportion of equity and payment-in-kind positions, the mix between pure senior direct lending and broadly syndicated or publicly traded loans, dividend sustainability, and simple liquidity. The BDC universe is far more heterogeneous than the label suggests, and markets are pricing these vehicles accordingly, with discounts ranging from modest to severe depending on how investors assess these overlapping risk dimensions. Technical factors, retail flows, index inclusion, yield-chasing dynamics, further amplify the divergence.



Source: Bloomberg

Blackstone, the world's largest alternative asset manager, is down roughly 30% from its November 2024 highs. It recently touched its lowest level since late 2023, as concerns around private credit redemptions and the evergreen model weighed on sentiment. Private asset manager stocks were priced for years of compounding fee growth, driven by the expansion of private credit into the wealth channel. That narrative, which underpinned much of the sector's re-rating in 2023–24, now appears to be on pause.

Five largest listed private credit managers, perpetual capital AuM



Source: With Intelligence

None of this is to say public markets are wrong. They may be correctly discounting a deterioration in credit quality that private marks have yet to acknowledge. What we can say is that the signal from listed markets deserves serious attention but should be read for what it is: a reflection of liquidity, positioning, and sentiment, not a real-time audit of underlying portfolio health.

6. Looking ahead: a stress test, not a death sentence

If there is a single takeaway for investors, it is this: dispersion across managers is widening, therefore manager selection is now even more important.

The private credit industry is going through its first real test of its evergreen structures. If the fire does not grow too big, which remains our base case, the outcome will be constructive: weaker players will be eliminated, and the industry will emerge with higher standards. The rapid growth of the past five years attracted new entrants, some of which were asset gatherers drawn by high fees rather than firms with genuine underwriting expertise. That distinction is now being laid bare.

The liquidity mismatches, shadow defaults, valuation debates, and gate decisions headlines will continue, and that is a positive for the industry. Greater transparency into portfolios and valuations is likely to become the new normal. In addition, we may even see fee compression as

investors demand gets weaker. Private credit has become too important an asset class to disappear, and it will come out of the current fire stronger.

The headlines will persist. But for investors with the discipline to look through the noise, select the right managers, the right structures, protections, and maintain a long-term horizon, private credit remains a compelling proposition in fixed income today.

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