Private Credit in Your Plans

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Agenda

- What is private credit?
- Growth of private credit
- Role in your portfolio
- Manager assessment/selection
- Investment vehicle considerations

What Is Private Credit?

- Private Credit (also referred to as Private Debt) is generally defined as lending by non-bank financial institutions (e.g., asset managers, institutional investors) to entities (small, mid or large) in the private markets
 - Involves the negotiation of terms and conditions to meet the specific needs and objectives of the borrower and lender
 - Investors receive regular interest payments and repayment of the loan at the end of the loan term
 - To compensate for illiquidity, private credit offers higher yields than traditional fixed income
 - Lenders will hold these loans until maturity or a refinancing event

What Is Private Credit?

- Inception of the asset class dates back to the 1980s
 - Insurance companies served as direct lenders to companies with strong historical borrowing standards
- Popularity increased after the 2008 Global Financial Crisis
 - Banks risk appetite significantly reduced
 - Capital requirements and risk assessment standards increased by regulators
 - Market becomes more accepting of non-bank sources of capital

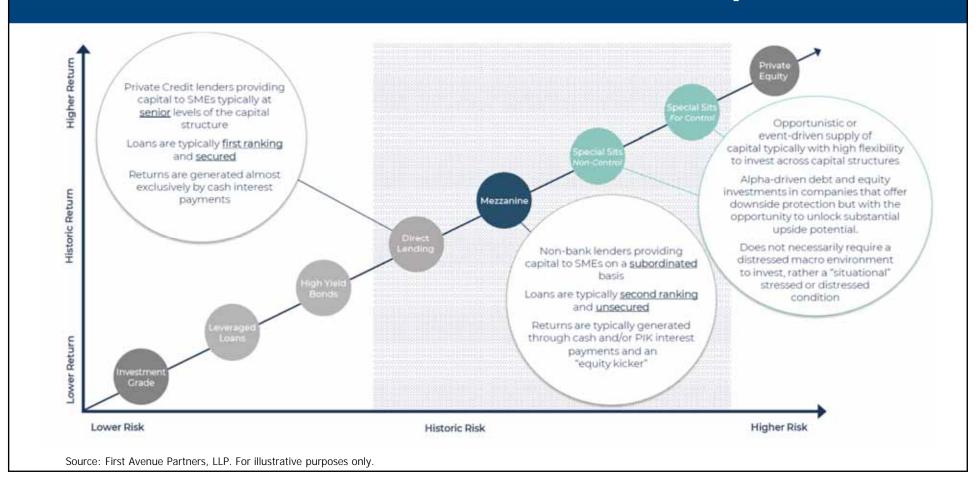
Types of Private Credit

- <u>Direct Lending</u>—Loans directly to middle-market companies, often used for buyouts or refinancings
- <u>Mezzanine Debt</u>—Subordinated debt with equity-like characteristics
- <u>Distressed Debt</u>—Investments in companies that are financially troubled or in default
- <u>Venture Debt</u>—Loans to early-stage, high-growth companies
- <u>Special Situations</u>—Loans are extended to take advantage of a particular event or situation
- <u>Other</u>—Opportunistic credit funds, asset-based lending, real estate debt, infrastructure debt, etc.

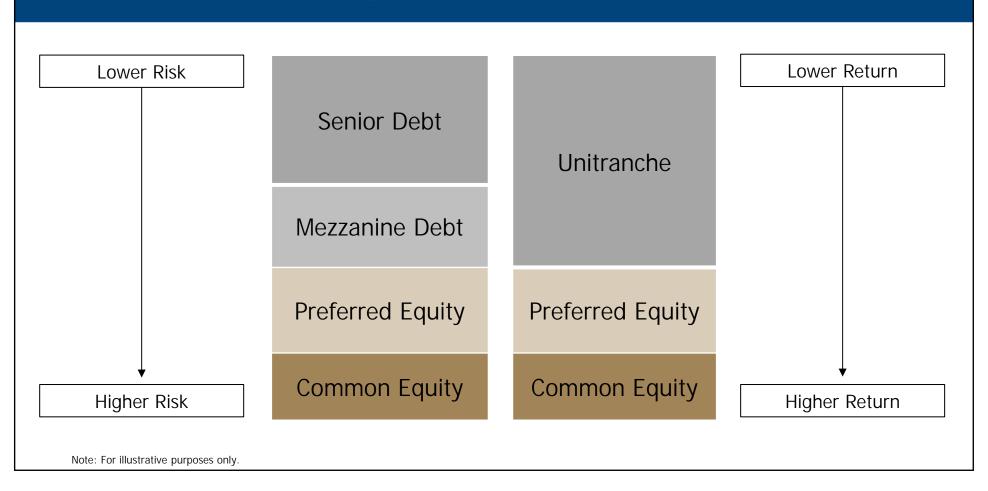
Private Credit vs. Traditional Fixed Income

	Traditional Fixed Income	Private Credit	
Market	Publicly Syndicated and Sold	Privately Originated and Held	
Traded	Yes	No	
Coupon Payments	Yes	Yes	
Coupon Structure	Typically, Fixed Rate	Typically, Floating Rate	
Credit Rating	Rated	Not Rated	
Liquidity	Liquid	Illiquid	
Valuations	Frequent	Infrequent	

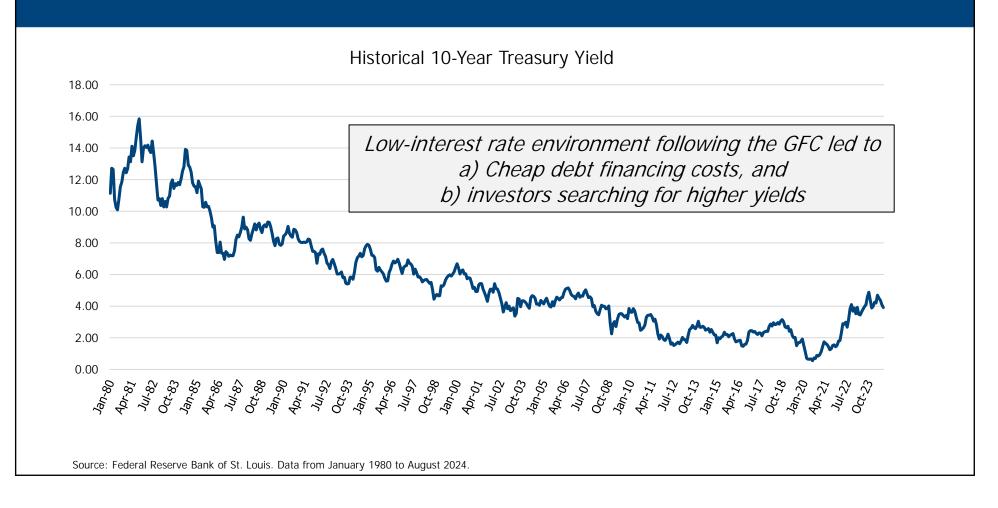
Private Credit—Risk vs. Return Spectrum



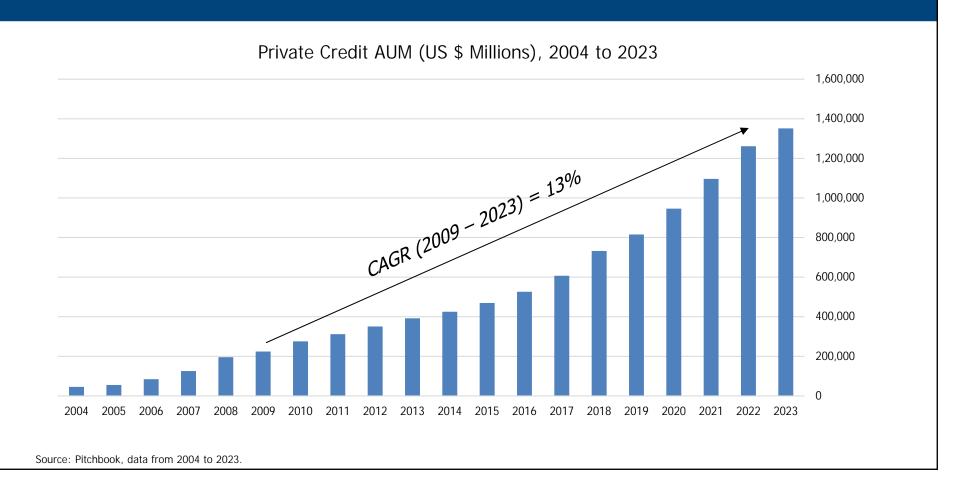
Illustrative Corporate Structure



Growth of Private Credit

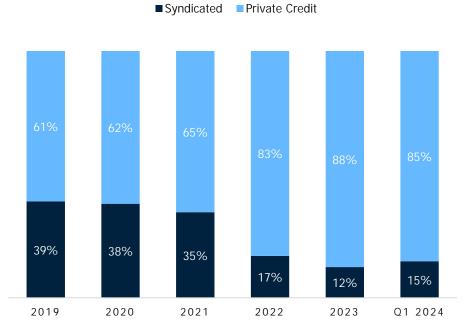


Growth of Private Credit



Growth of Private Credit

PERCENTAGE OF LBO FINANCED IN PRIVATE CREDIT VS BSL* MARKET

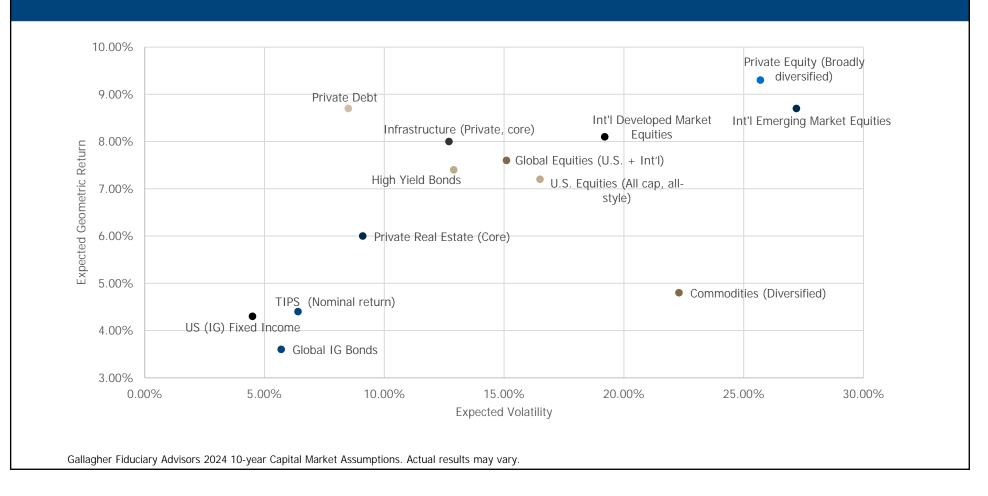


Why do private companies choose to work with private credit managers vs. public alternatives?

- Long-term partners and capital providers
- Speed of execution
- Certainty
- Complexity
- Confidentiality

Source: Hamilton Lane, Gallagher Fiduciary Advisors. *BSL = Broadly Syndicated Loan

10-Year Capital Market Assumptions



Role in Your Portfolio

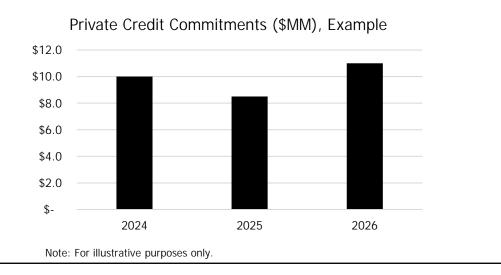
Asset Class	Portfolio 1	Portfolio 2	Portfolio 3
Global Equity	60%	60%	45%
Global Fixed Income	40%	30%	25%
Private Real Estate			5%
Private Equity			10%
Private Credit		10%	10%
Infrastructure			5%
Expected Return	6.2%	6.7%	7.2%
Expected Volatility	9.9%	10.0%	10.2%
Risk/Return	0.63	0.68	0.70

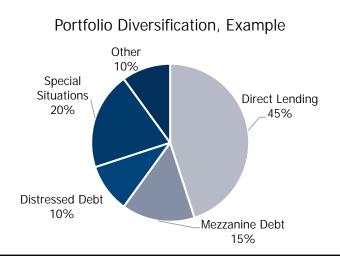
- It is important to recognize that alternative investments have additional risks that do not necessarily appear in asset allocation modeling
- Sizing the allocations to private market investments will depend on risk tolerance and liquidity needs
- Private Credit may offer diversification benefits and enhance the income component (i.e., return) of your portfolio

For illustrative purposes only. Actual results may vary. Expected return and volatility based on Gallagher Fiduciary Advisors' 10-year capital market assumptions.

Role in Your Portfolio

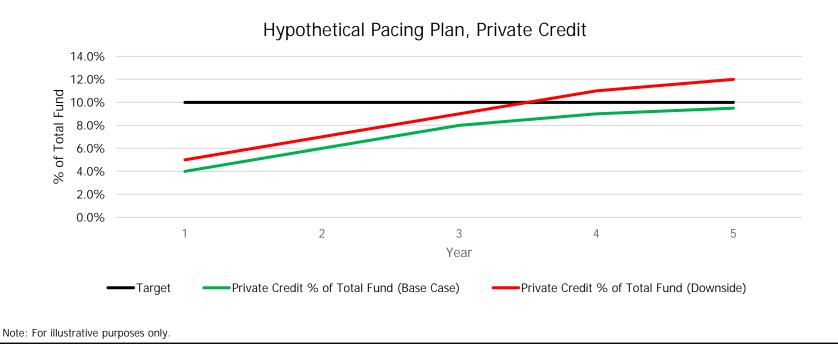
- After the strategic asset allocation has been established, it is important to develop a pacing plan to attain the desired portfolio target and composition
- Unlike public markets, deployment of a private credit portfolio is not immediate and may take several years





Role in Your Portfolio

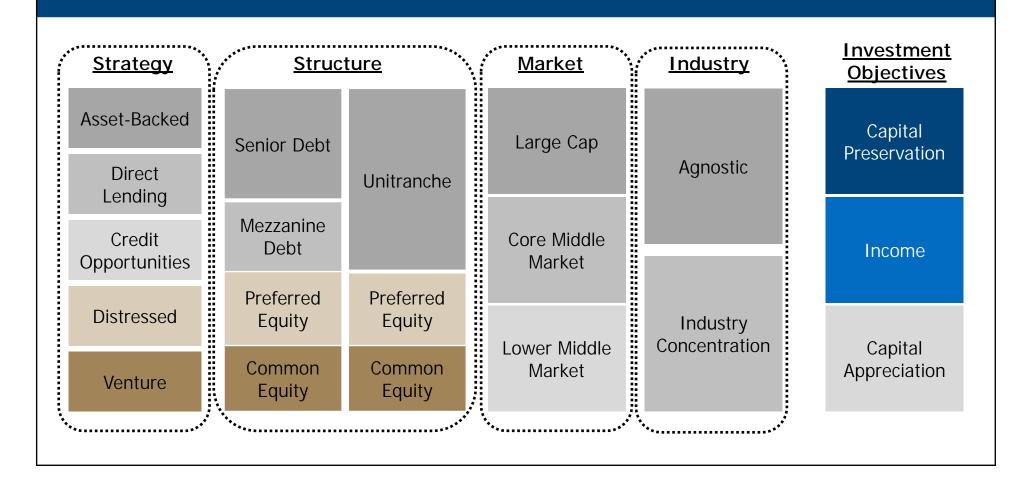
- The pacing plan helps drive the decision in terms of the amount to allocate and timing
- Note that the pacing plan is based on assumptions, actual results will most likely vary.
 It is important to "stress" your assumptions given the illiquidity of the asset class.



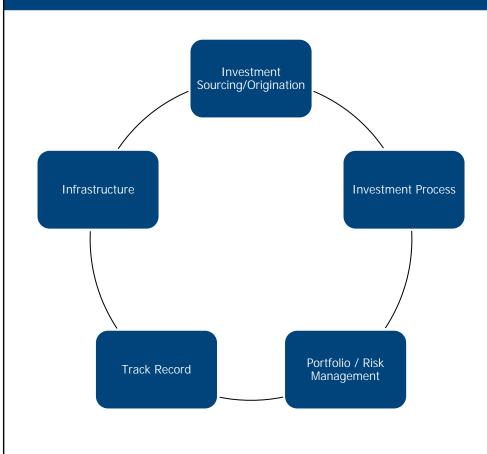
Manager Assessment/Selection

- Market/structure focus
- Capabilities
- Investment vehicle considerations

Market/Structure Focus



Capabilities—What to Look For



- <u>Sourcing</u>: Differentiated origination allows for stead deployment and selectivity in investment decisions and diversification in portfolio construction
- <u>Investment Process</u>: Proven, repeatable process yielding consistent performance
- Portfolio/Risk Management: Reporting frequency, valuations, workout capabilities, etc.
- <u>Track Record:</u> Tenure and consistency
- <u>Infrastructure</u>: Resources to support the investment team and investor relations

Investment Vehicle Considerations

- There has been a proliferation of fund structures to address diverging investor needs
- Institutional fundraising focus in Private Credit shifting away from traditional closed-end, draw-down structures to evergreen structures
 - Semi-permanent capital well suited for strategy and asset class
 - Liquidity features introduced (although somewhat limited)
- Investors should consider several factors when investigating vehicle options, including but not limited to:
 - Drawdown schedules/deployment
 - Expense/fee load
 - Liquidity needs/liquidity mechanics (if offered)
 - Tax (less relevant to public pension investors)

Key Takeaways

- Private credit has grown in popularity
 - Expanding investment opportunity
 - Compelling risk/return characteristics
- Strategic allocation
 - Diversification, low volatility, predictable income
- Private credit is multi-faceted
 - Understand the strategy and risk profile
- Manager and vehicle selection are important
 - Investment cadence/J-Curve
 - Performance

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