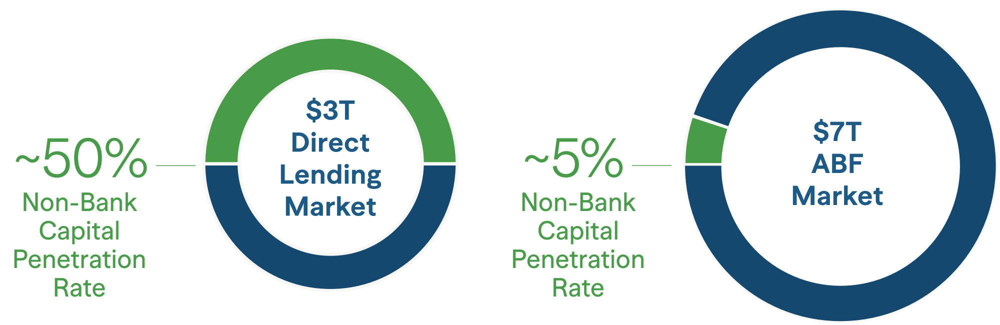
Inside Private Credit: Comparing Direct Lending and Asset-Backed Finance

Private credit is evolving, and investors have more ways than ever to access it. As banks continue to retrench and traditional financing channels become more constrained, private credit has become a core allocation for investors seeking income, risk mitigation and diversification.

Within private credit, direct lending and asset-backed finance (ABF) stand out as two distinct—and complementary—approaches. While both aim to deliver attractive risk-adjusted returns, they differ meaningfully in borrowers' sources of repayment and risk drivers. Understanding these differences can help investors build more resilient portfolios across market cycles.

Feature	Direct Lending	Asset-Backed Finance
Primary Borrower	Corporations (often sponsor-backed businesses)	Originators/originator-owned SPVs, asset owners
Source of Repayment	Cash flow from business operations	Cash flows generated by underlying assets
Collateral	Primarily senior secured on company assets	Explicitly secured by financial or real assets
Risk Focus	Balance sheet, business model and existing debt (leverage)	Asset quality, structure, and cash flow predictability
De-Risking Assets	Refinancing exit or enterprise value growth	Contractual cash flows
Structural Protection	Subject to bankruptcy process	Enhanced protections/ non-recourse SPVs
Self-Amortizing	No	Yes
Underwriting	Tailored corporate cash flow	Specialized asset expertise
Market Competition	Medium	Low
Yield Potential[1]	Low to mid teens	Low to mid teens
Typical Return Profile	May offer lower spread potential and is more sensitive to macroeconomic environment	May offer higher spread potential and is less sensitive to macroeconomic environment

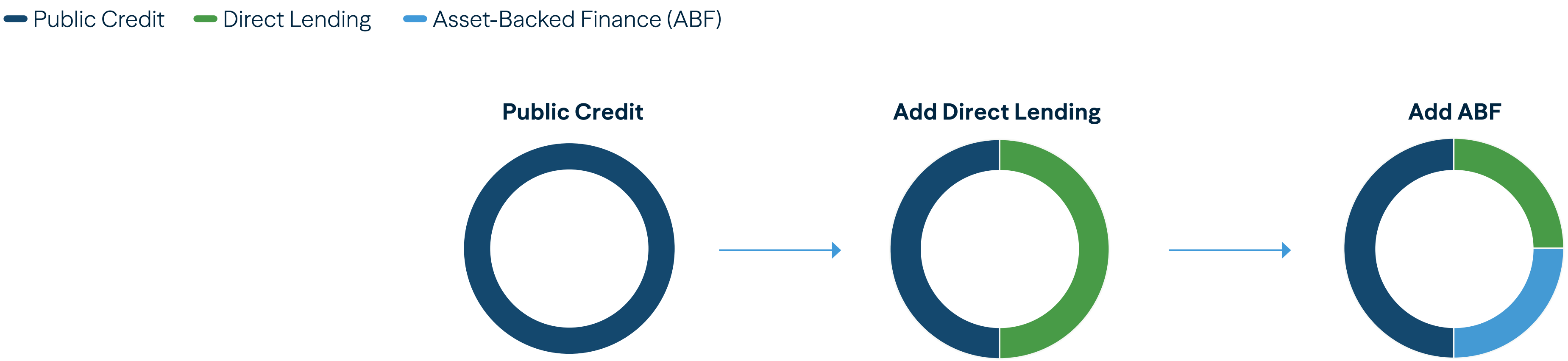


1. The yield potential is an objective based on current market conditions and is not a guarantee of future performance. Refer to endnote.

Actual returns and yields may fall outside these ranges due to market conditions, security selection, and other factors. Alternative investments are subject to a variety of risks and limitations, including, but not limited to, illiquidity, lack of transparency, complex structures, and the potential for significant loss of principal. These investments may not be suitable for all investors, and there is no guarantee that diversification, enhanced income, or risk-mitigation objectives will be achieved. Investors should carefully consider these risks before investing.

Source: Cliffwater, Brookfield.

A "modern" credit allocation includes "all of the above"



	Public Credit Portfolio	Public + Direct Lending	Public + Direct Lending + ABF
Gross Yield	6.06%	6.58%	7.10%
Gross Spread	195 bps	262 bps	318 bps
Expected Credit Loss	0.57%	0.47%	0.40%
Average Credit Rating	BB+	BB+	BB+

Past performance does not guarantee future results. Past performance shown for illustrative purposes only and does not predict or depict the future performance of any investment. Indexes are unmanaged and cannot be purchased directly by investors. The metrics shown are hypothetical and intended for illustrative purposes only. They do not represent actual or projected investment results and should not be relied upon as predictions of future performance. "Public Credit" is based on an illustrative portfolio comprising a 70% allocation to the ICE BofA U.S. Corporate Index and a 30% allocation to the ICE BofA US High Yield Index. "Public + Direct Lending" represents an illustrative portfolio comprising a 35% allocation to the ICE BofA U.S. Corporate Index, a 15% allocation to the ICE BofA U.S. High Yield Index, a 35% allocation to Private Investment-Grade Corporates and a 15% allocation to Direct Lending based on representative spreads and yields. "Public + Direct Lending + ABF" represents an illustrative portfolio comprising a 35% allocation to the ICE BofA U.S. Corporate Index, a 15% allocation to the ICE BofA U.S. High Yield Index, a 17.5% allocation to Private Investment-Grade Corporates, a 7.5% allocation to Direct Lending, a 17.5% allocation to Investment-Grade Asset-Based Finance and a 7.5% allocation to Sub-Investment-Grade Asset-Based Finance based on representative spreads and yields. As of April 30, 2025. The chart compares select credit allocation strategies but omits several material factors that may significantly impact investment decisions. Differences in liquidity constraints, management fees, tax treatment and risk considerations are not fully reflected and should be carefully evaluated before investing.

Endnote

1. Actual returns and yields may fall outside these ranges due to market conditions, security selection, and other factors. A long-term investment approach with 5+ year horizons may result in holding positions through periods of underperformance, which could negatively impact overall returns. While low-turnover strategies generally aim to reduce transaction costs and tax impacts, there may be circumstances where higher turnover is necessary, potentially increasing costs and tax consequences. Past performance is not indicative of future results, and all investment strategies involve a risk of loss.

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The ICE BofA U.S. High Yield Index tracks the performance of U.S. dollar-denominated, below-investment-grade (IG) corporate debt publicly issued in the major domestic markets.

Private Credit Risks

Alternative investments are complex, speculative investment vehicles and are not suitable for all investors. An investment in an alternative investment entails a high degree of risk, and no assurance can be given that any alternative investment fund's investment objectives will be achieved or that investors will receive a return of their capital.

All investing involves risk. The value of an investment will fluctuate over time, and an investor may gain or lose money, or the entire investment. Past performance is no guarantee of future results.

As an asset class, private credit comprises a large variety of different debt instruments. While each has its own risk and return profile, private credit assets generally have increased risk of default, due to their typical opportunistic focus on companies with limited funding options, in comparison with their public equivalents.

Because private credit usually involves lending to below-investment-grade or non-rated issuers, yield on private credit assets is increased in return for taking on increased risk.

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