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Private Credit Market Update

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access OPPORTUNITY

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Private credit: key takeaways

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> Private credit market overview
  - Global private credit fundraising trends
  - Private credit growth relative to other financing markets

> Impact of inflation on the credit market
  - Impact of inflation and rising rates on deal activity
  - Performance of the asset class during inflationary/rising interest rate environments
  - Enhanced focus on three key industries during inflationary periods
  - Historical loss ratio for credit during turbulent periods

> Key considerations for investors and managers in private credit
  - Returning to basics

Private Credit Market Overview

Private markets have experienced double digit growth over the last 5 years

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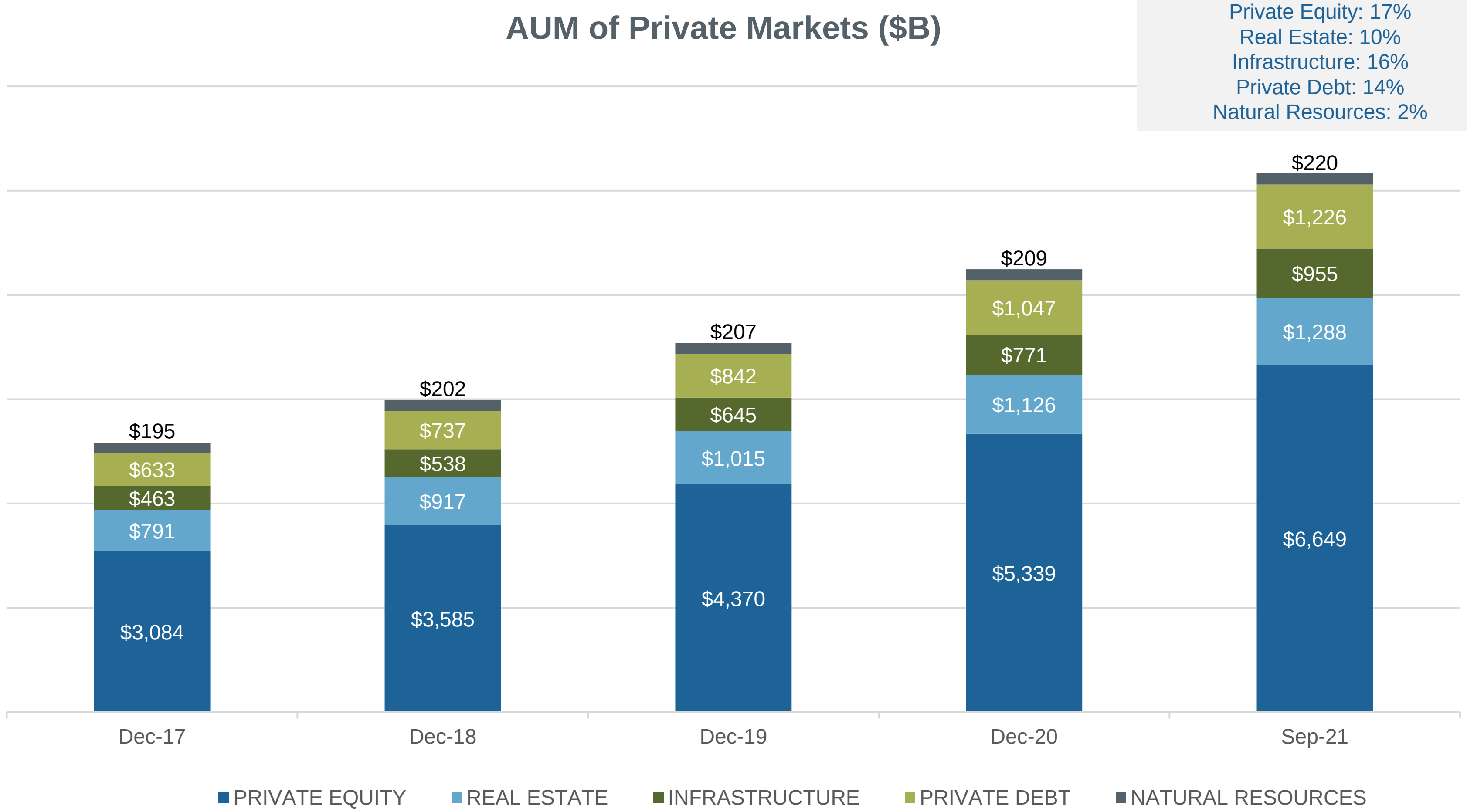
The private credit market is estimated to be \$1.2-\$1.6 trillion in size and continues to grow

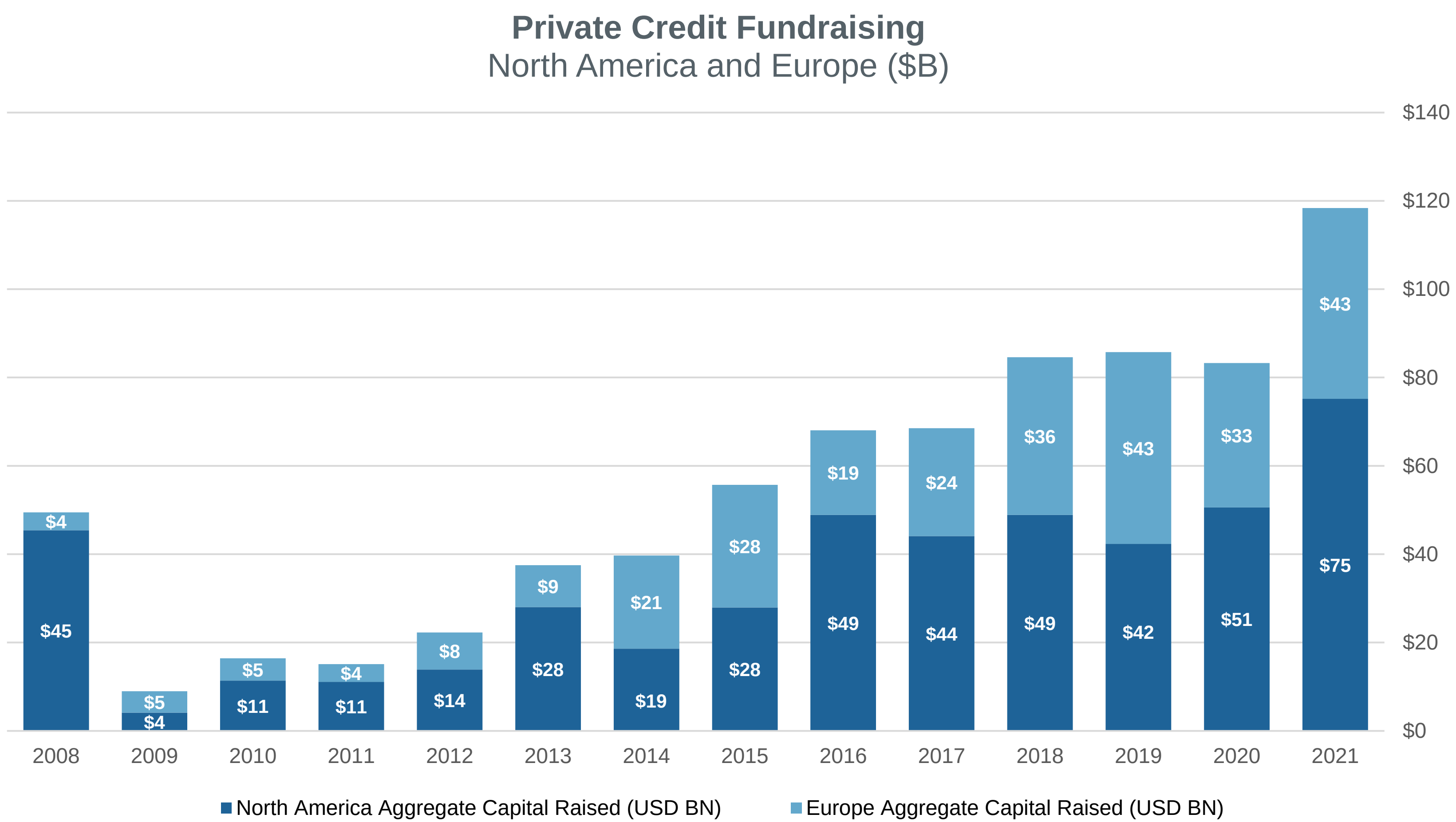
CAGR since 2017
Private Equity: 17%
Real Estate: 10%
Infrastructure: 16%
Private Debt: 14%
Natural Resources: 2%



Source: Preqin

Global private credit fundraising set a record in 2021

The average fund size in both the US and Europe crossed $1B for the first time



Source: Preqin. Private Credit includes all Direct Lending and Mezzanine Funds. As of December 31, 2021

Dry powder of private equity funds remains 4x that of private credit paving the way for future demand

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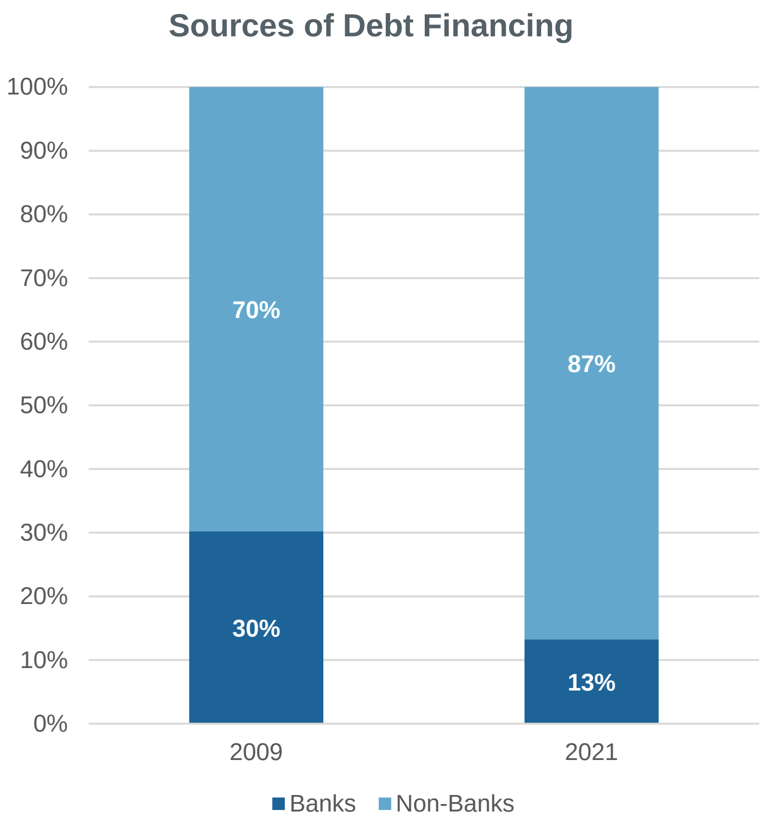
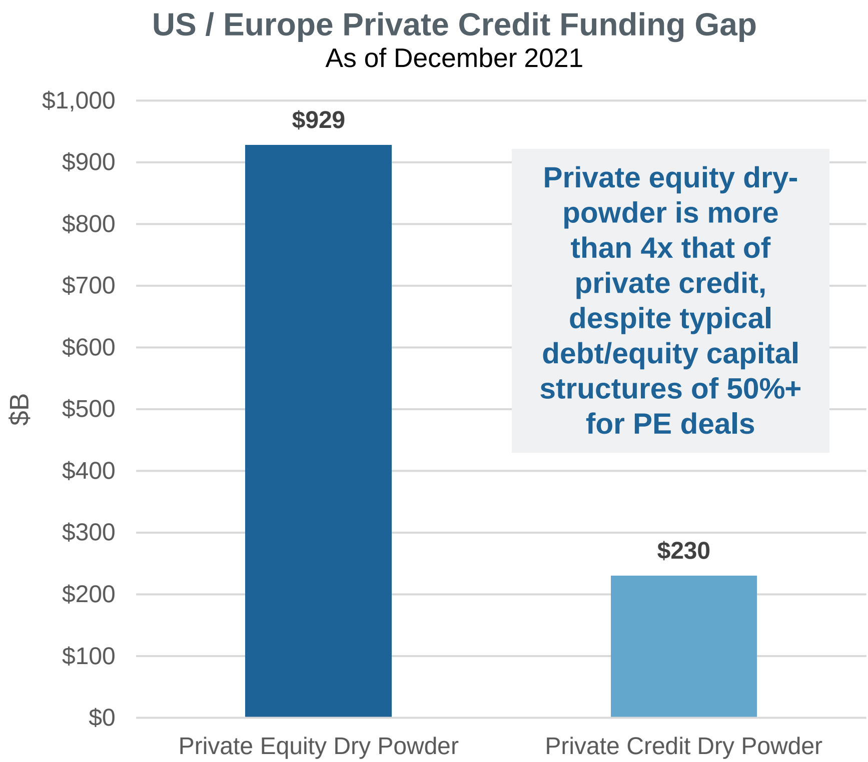
Private credit growth has been driven by share-gains from banks and increased private equity activity. Despite the rapid growth, current dry-powder suggests a significant funding gap remains.

Non-Bank lenders continue to provide the majority of financing supply for middle market lending globally



Increased demand for Private Equity financing to support buyouts



Source: S&P LCD Quarterly Q4 2021, PitchBook, as of December 31, 2021. Funding gap assumes a 50/50 split between debt and equity financing.

Private Credit has grown 3x as fast as the other financing sources for private equity managers

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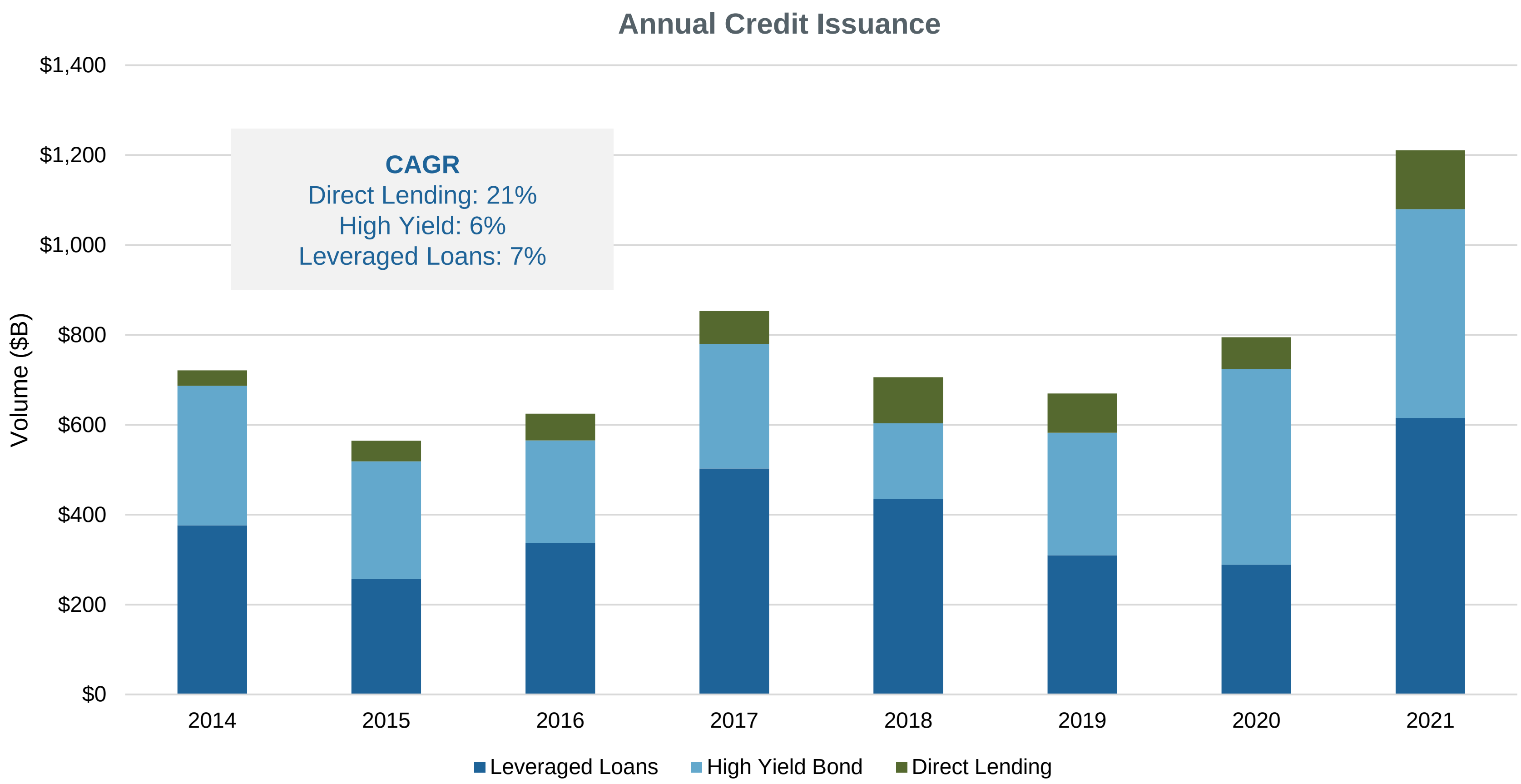
Direct lending has grown faster than comparable credit asset classes, validating its acceptance by the market as a preferred form of credit financing



Source: S&P LCD, Refinitiv. As of December 31, 2021.

Speed, scale and flexibility are the key drives of the growth for direct lenders

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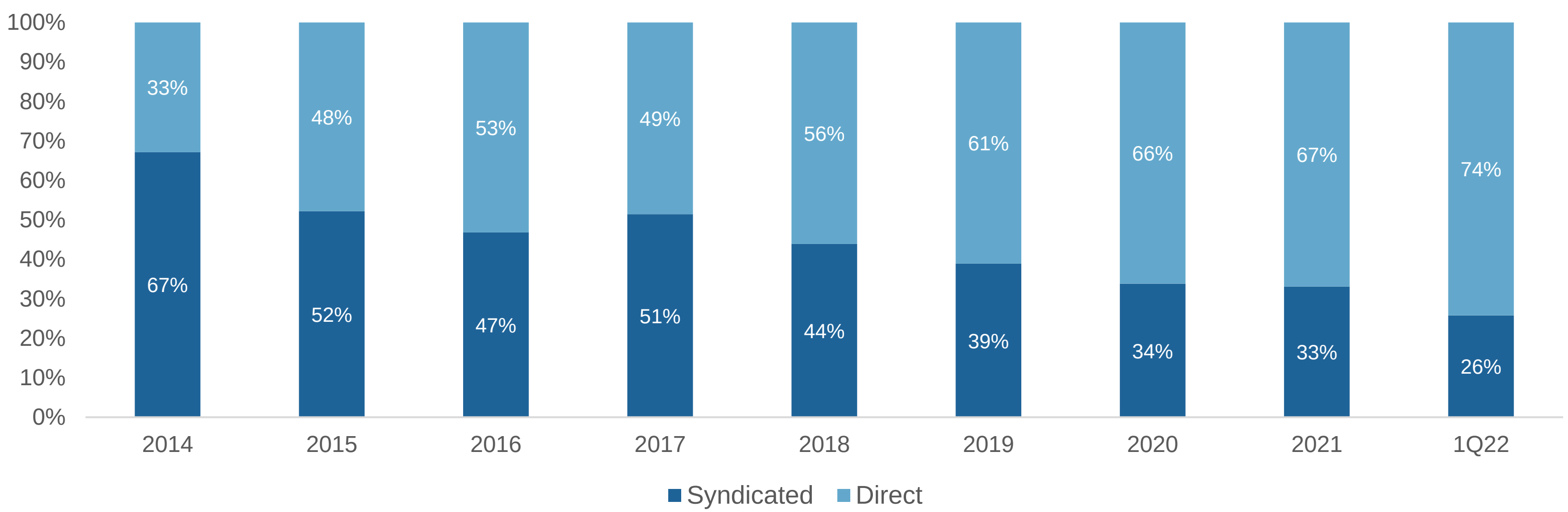
Direct lenders continue to take market share from the syndicated loan market; expanding the opportunity set for private credit providers

Benefits for Investors	Benefits for Issuers / PE Owners
> Less volatile than public markets	> Certainty and speed of execution
> Resilience across market cycles	> Privacy and less public disclosure
> Better outcomes in a workout; higher recovery rates	> Expanding hold sizes ($3B+)
> Illiquidity premium	> Fewer counterparties

Annual MM Sponsored Loan Volume ($B)



Source: Refinitiv LPC 1Q 22 Private Deals Analysis

Large $1B financings + are creating an even larger market for direct lenders

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The number of $1B+ unitranche loans increased substantially in 2021

- 20 **$1B+ unitranche loans** issued it 2021 vs 4 in 2020
- Two **$3B+** unitranche loans issues in the second half of 2021
- “Megatranche” loans accounted for nearly **$40B** of total 2021 unitranche volume

Five Recent Large Unitranche Investments

Issuer	Size	Lenders
The Ardonagh Group	$2.4B	HPS, CDPQ, KKR
Calypso Technology	$2.3B	Owl Rock
Galway Insurance	$3.4B	Antares, Ares, Golub, KKR, HPS
Inovalon Holdings	$2.8B	Blackstone
Stamps.com	$6.6B	Ares, Blackstone, PSP, Thoma Bravo

Source: Direct Lending Deals Weekly as of January 7, 2022, KKR “Regime Change Enhancing the Traditional Portfolio”

Impact of inflation on the private credit market

Inflation and market volatility have impacted the total deal volume in the market

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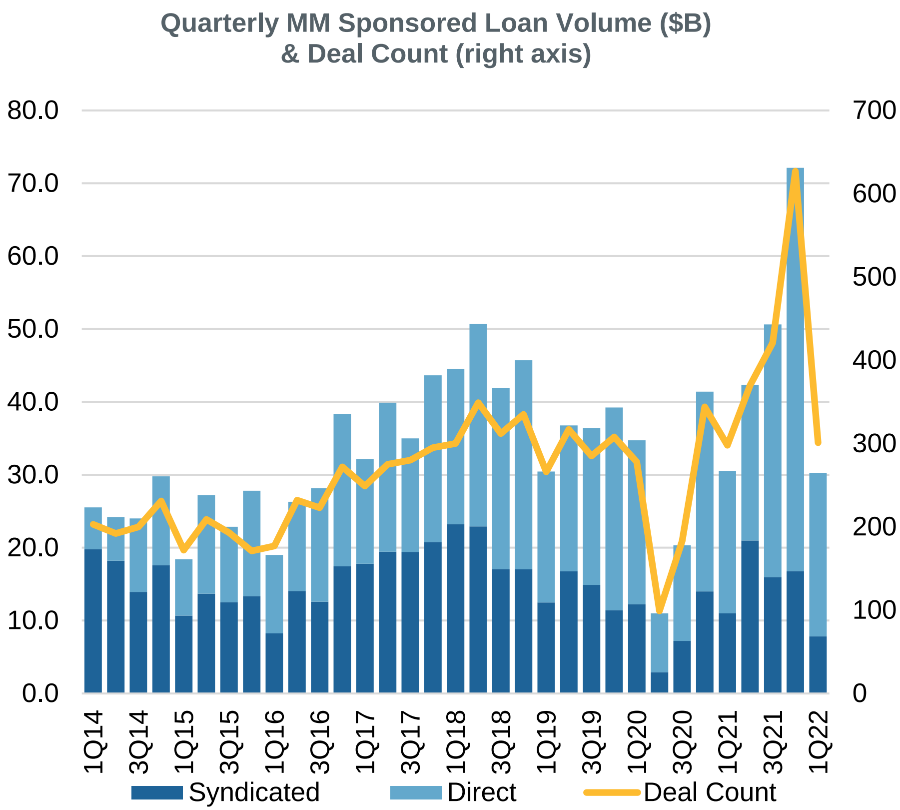
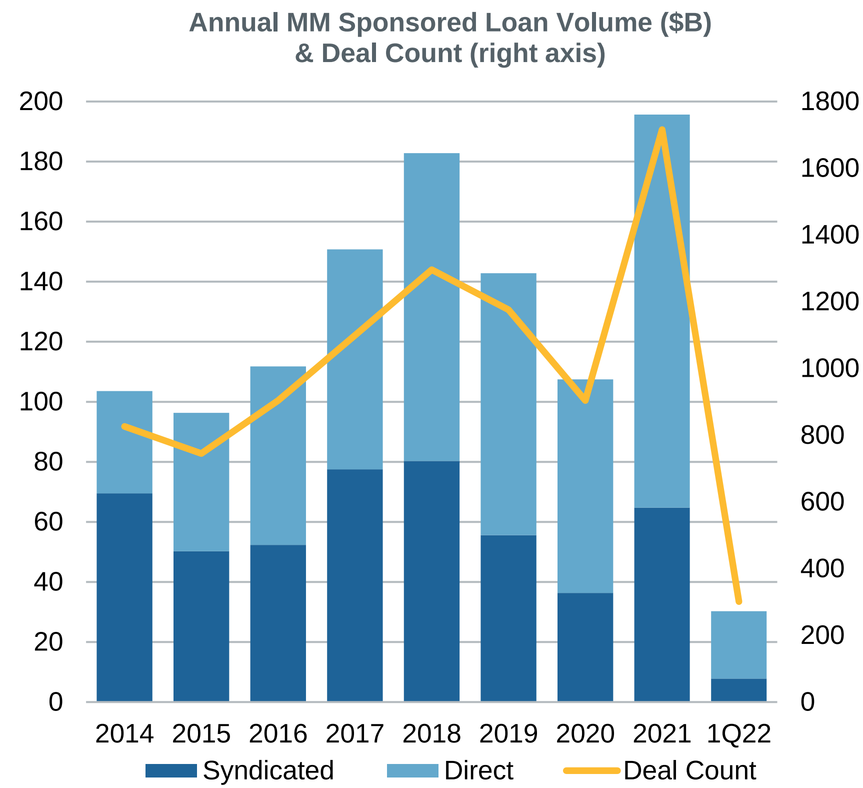
Total sponsored issuance (syndicated and direct) dropped 58% from 4Q21 but was on par with 1Q21. Syndicated volume dropped 29% from 1Q21, while direct lending increased 15%.





Direct lending market share has increased every year since 2014 except for 2017

Source: Refinitiv 4Q21 Sponsored MM Private/Club Analysis

Private credit benefits from floating rate instruments while loan to values are still at all-time lows

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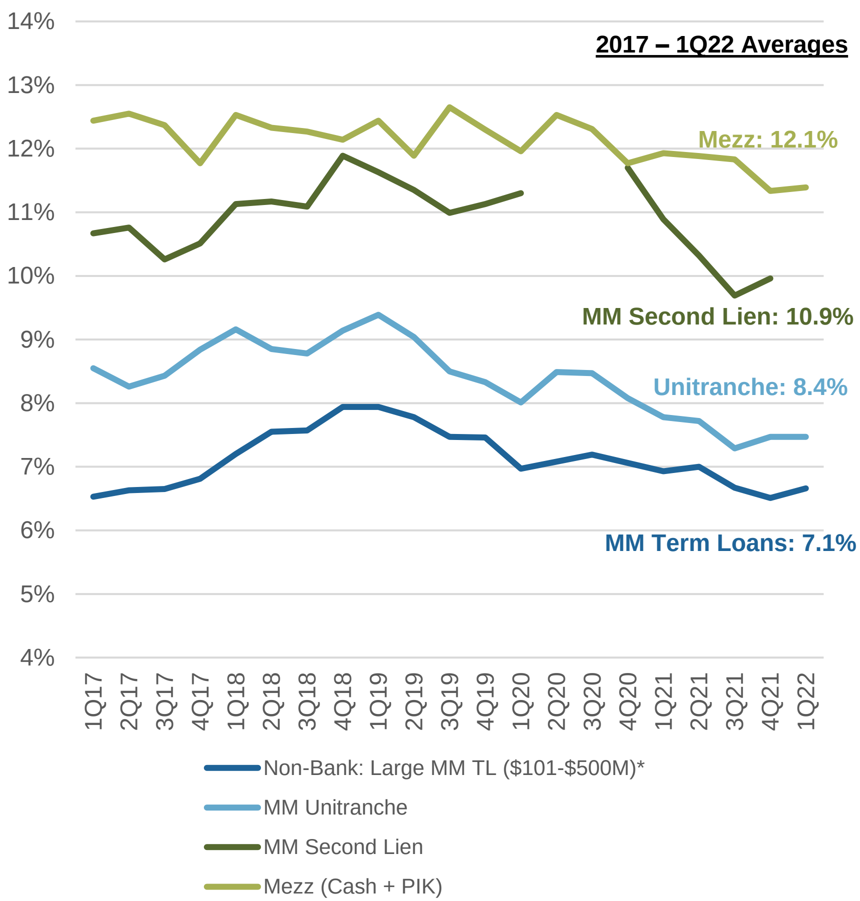
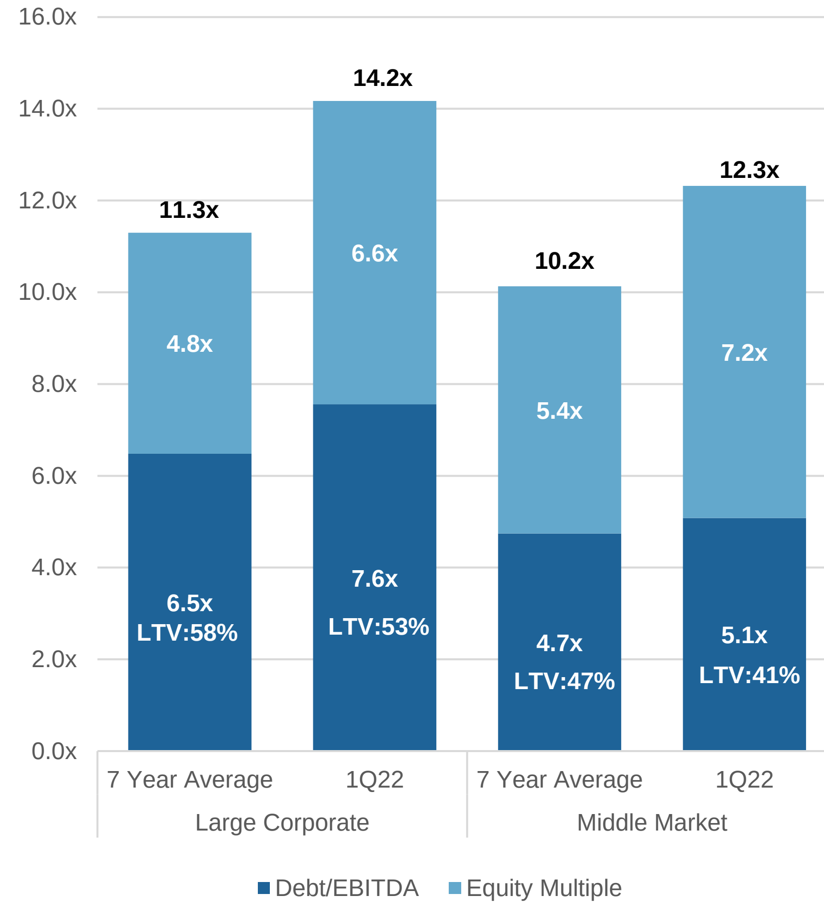
Private credit yields have remained consistent given floating rate nature while loan to value's have decreased given rising asset prices in the private markets

Quarterly middle market yields



Purchase Price Multiple for LBO Deals



Source: Refinitiv LPC 1Q22 Private Deals Analysis.

Private credit returns during inflationary periods has outperformed that of US bonds

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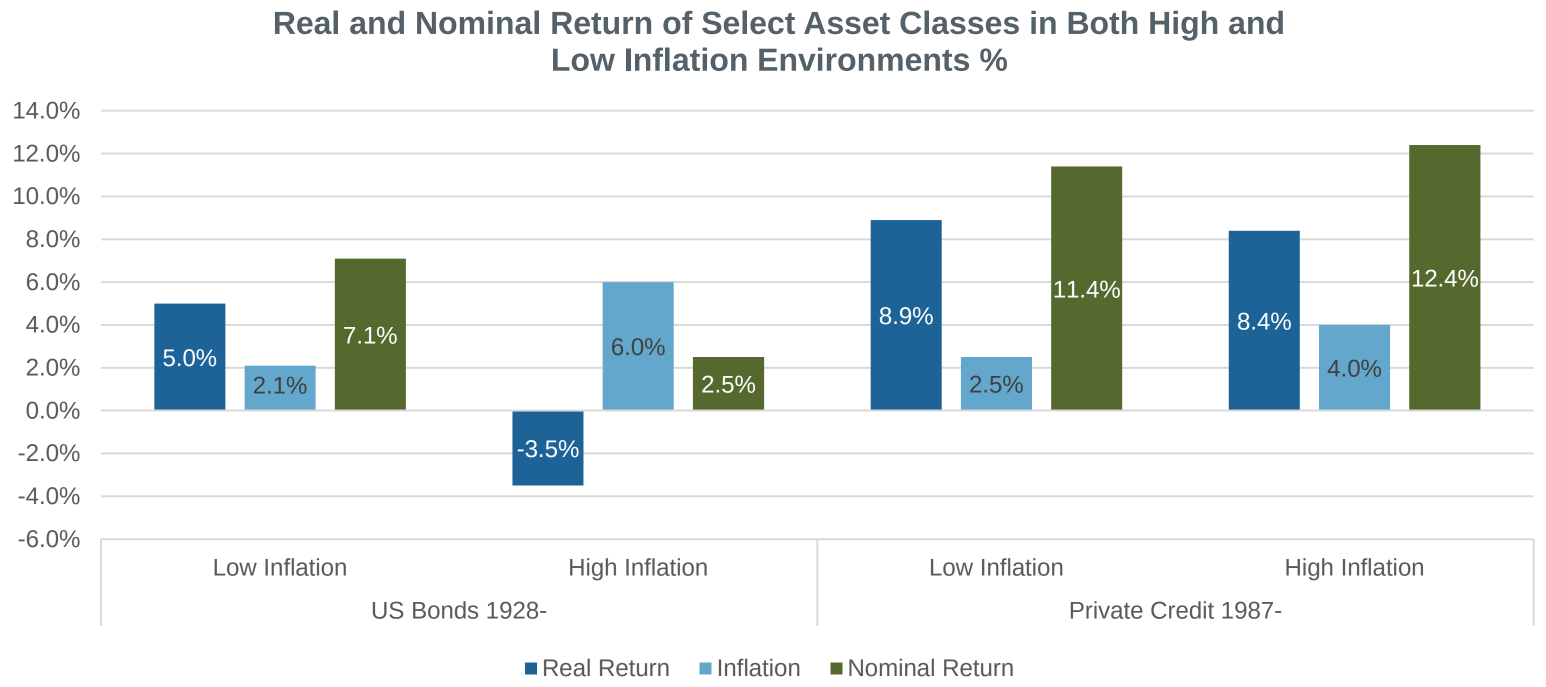
US Bonds yielded negative real returns in inflationary environments, while private credit has shown higher resiliency (on a shorter time frame)



Source: KKR “Regime Change Enhancing the Traditional Portfolio”.
Using annual total returns from 1928 to 2021 for US Bonds and from 1987 to 2021 for Private Credit. Real returns calculated as [(1+nominal return)/(1+Y/y Inflation) -1]. Inflation component of the asset class return calculated as the difference between nominal and real return over the given time period. Private Credit modeled using the Burgiss Private Credit All Index. Bonds modeled using a mix of 50% US T.Bond and 50% Baa Corp Bond annual returns, computed historically by Professor Damodaran (NYU Stern).

The correlation of private credit has a negative correlation to US Bond index

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Asset classes with lower dependence on growth and superior inflation properties could act as "risk off" beneficiaries. Private credit has fixed income qualities but the least correlation to US Bonds.

From 06/30/76 to 12/31/21	US Public Equities	US Bond Aggregate	Real Estate (NPI)	Infra-structure (Burgiss)	Private Debt (Burgiss)
US Public Equities	1.00	0.11	0.15	0.50	0.74
US Bond Aggregate	0.11	1.00	-0.11	-0.06	-0.23
Real Estate (NPI)	0.15	-0.11	1.00	0.48	0.26
Infrastructure (Burgiss)	0.50	-0.06	0.48	1.00	0.67
Private Debt (Burgiss)	0.74	-0.23	0.26	0.67	1.00

Sources: KKR "Regime Change Enhancing the Traditional Portfolio".

Portfolio returns and volatility modeled using annual total returns from 1928 to 2021 for the S&P500, from 1978 to 2021 for Real Estate, from 2004 to 2021 for Infrastructure, from 1928 to 2021 for Bonds, and from 1987 to 2021 for Private Credit. Assumes continuous rebalancing of the portfolios. US equities modeled using the S&P500 Index. Bonds modeled using a mix of 50% US T.Bond and 50% Baa Corp Bond annual returns, computed historically by Professor Damodaran (NYU Stern). Real Estate modeled using the NCREIF Property Levered Index. Private Infrastructure modeled using the Burgiss Infrastructure Index. Private Credit modeled using the Burgiss Private Credit All Index.

Resilience of private debt through crises relative to other fixed income asset classes

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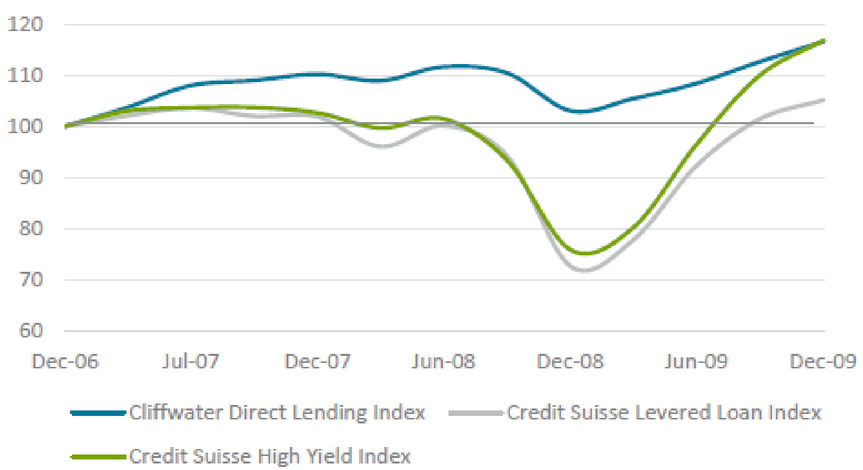
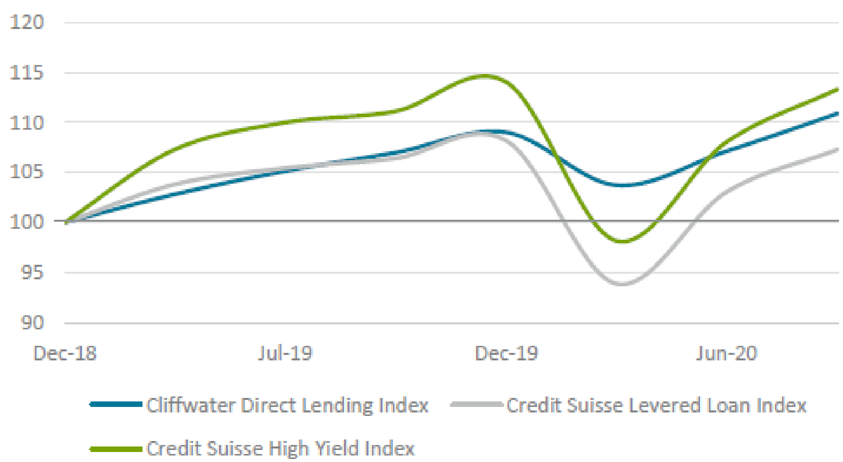
Direct lending has exhibited low volatility in both the GFC and COVID environments

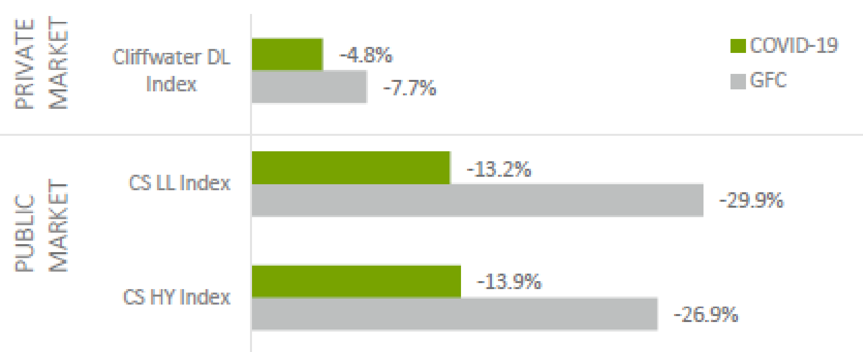
GFC Performance



COVID Performance



Peak to Trough Declines



Source: Cliffwater as of Q4 2020.
Syndicated loans data is based on the Credit Suisse Leveraged Loan Index; High yield bonds data is based on Credit Suisse High Yield Index; Direct Lending data is based on Cliffwater Direct Lending Index

Industry selection is a key pillar to risk mitigation

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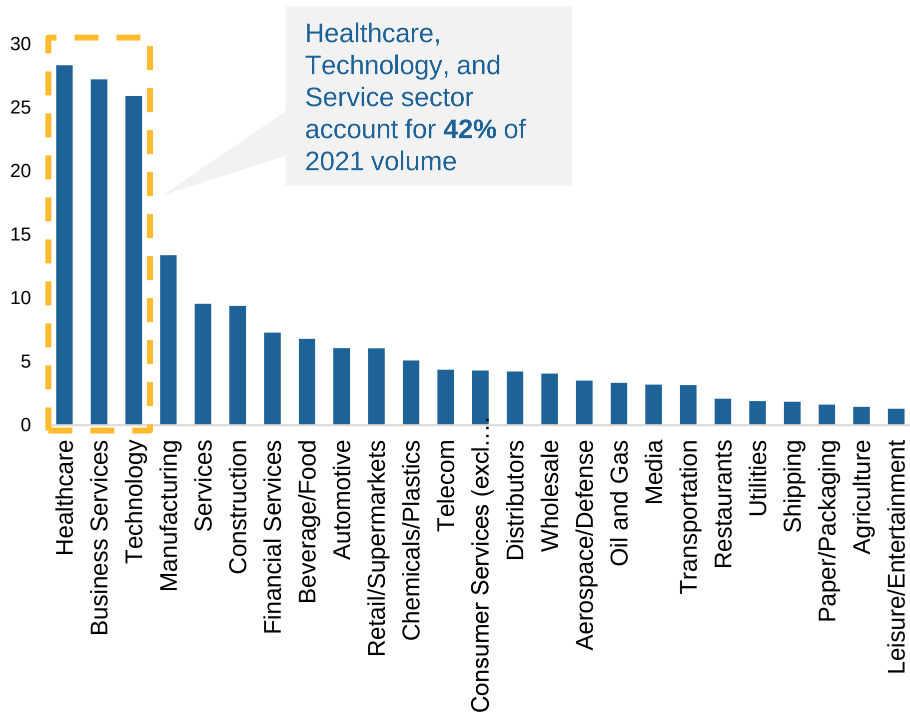
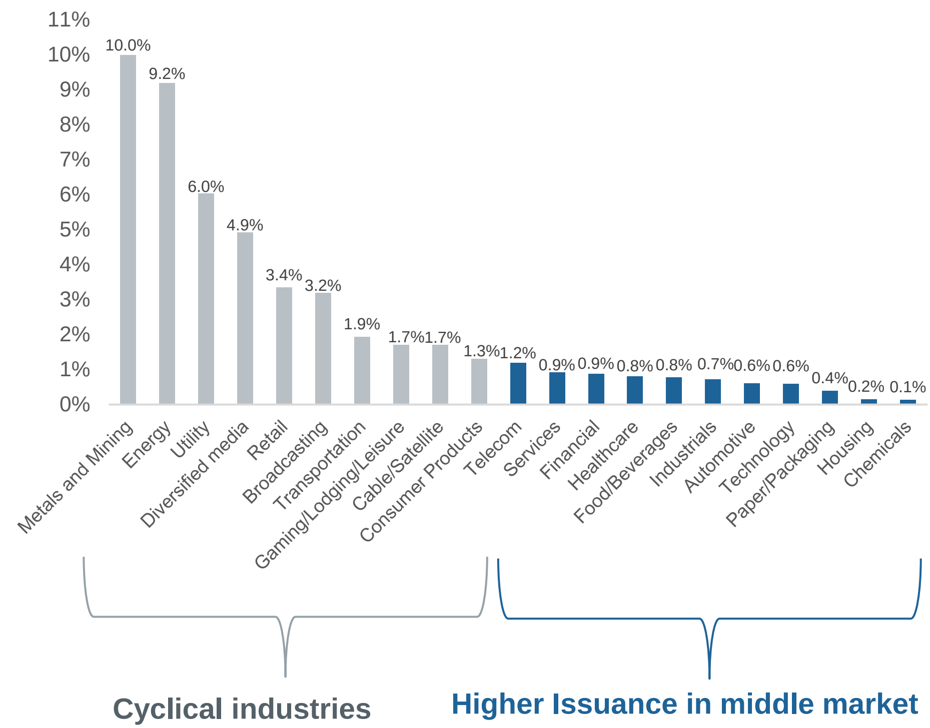
- Private credit is heavily weighted towards healthcare and technology and services which are defensive, non-cyclical industries with attractive attributes (market stability, revenue visibility, and cash flow)
- Little to no exposure to the industries that have had the highest historical default rates in the leveraged loan market
- Minimize exposure to deep cyclicals, energy, commodities, retail, restaurants, utilities, etc.

2021 Middle Market Loan Volume by Industry ($B)



JPM Leveraged Loan Monitor
Avg default rate by Industry Last 10 years



Source: Refinitiv's Q421 Private Deals Analysis & JP Morgan Leveraged Loan Monitor

Middle-market loans offer downside protection and recovery rates compared to other asset classes

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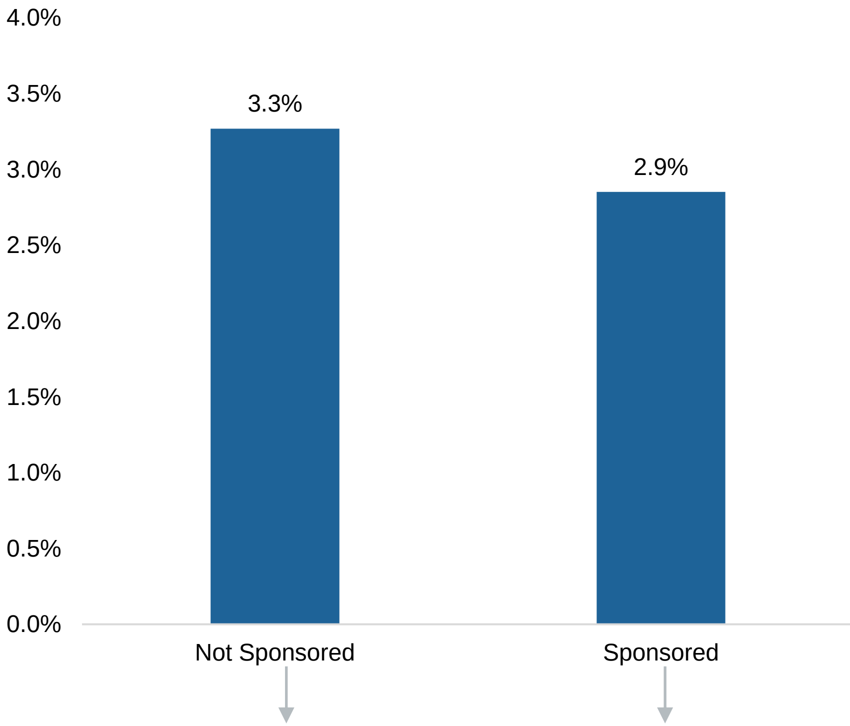
Sponsored deals exhibited much lower default rates than unsponsored during the GFC

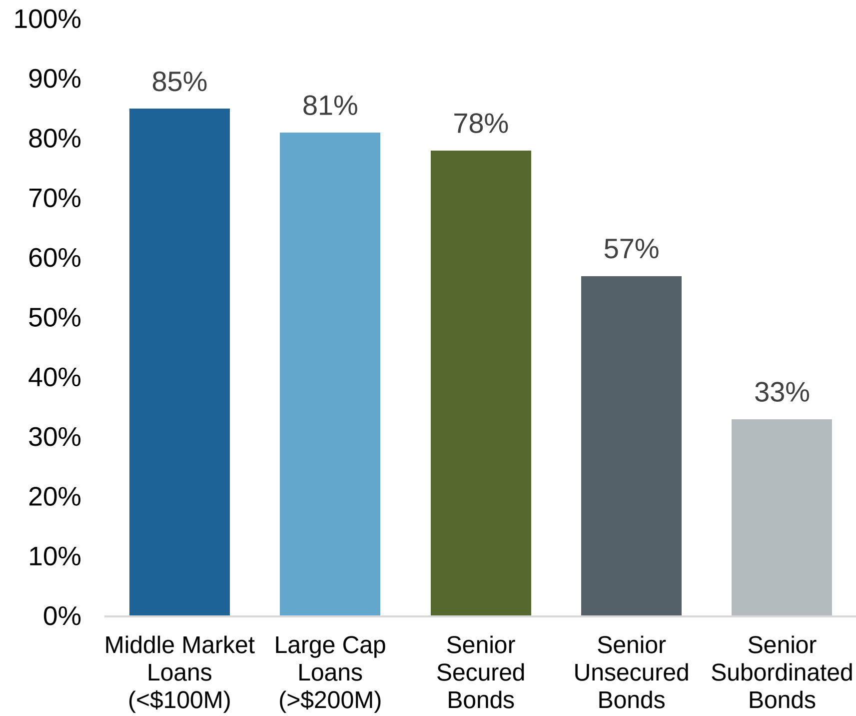
Average Lagging Twelve-Month Default Rates by Principal Amount (Q4 1998 – Q1 2022)*



Peak During GFC: 16.3%*

Peak During GFC: 7.5%*

Historical Average Recovery Rates by Asset Class



* Source: S&P LCD (Q1 2022). Based on loans in the S&P/LSTA Leveraged Loan Index. Peak during GFC data represents maximum default rates during 2008-2010 time period.

** Source: Pension Consulting Alliance (March 2018). Based on S&P Credit Pro data. Past performance is not a reliable indicator of future results.

How GPs and LPs are approaching the market

Key considerations in today's market

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It is critical for Private Credit manager's to be focused on:

1. **The industries they are investing in**
2. **The sponsors they are completing transactions with**
3. **The companies they are underwriting**
4. **The relative value of each investment opportunity**

Industry Selection

Emphasize **non-cyclicals** in business services and consumer segments

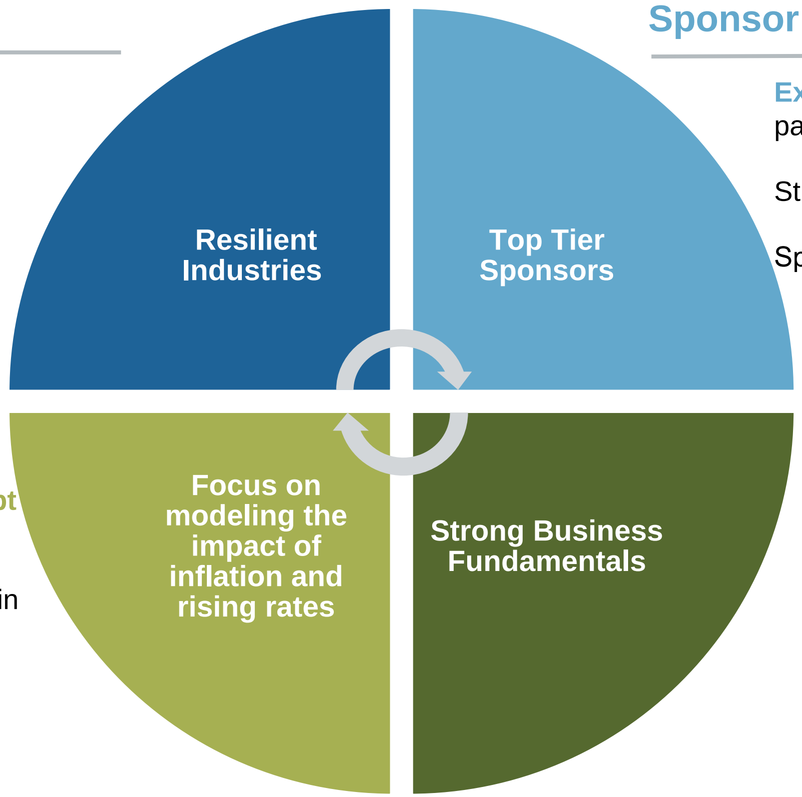
Minimize deep cyclicals, **energy, commodities, retail, restaurants, etc.**

Sponsor Profile

Experience through multiple cycles in particular industry or business model

Strong **track record**

Sponsor's **follow-on** investment capacity



Credit Underwriting

Focus on ability to **service future debt payments**

Model **interest coverage** and **FCCR** in rising rate environment

Assess Relative Value

Ability to **price** the most attractive **risk adjusted returns** at various parts of the capital stack

Source: HarbourVest.

Case studies: underwriting focus in uncertain markets

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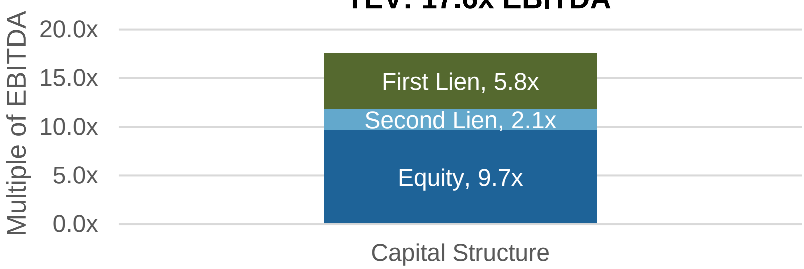
Company Description	Software Provider
Securities	Second Lien
Coupon / OID	7.25% / 98.5

TEV: 17.6x EBITDA



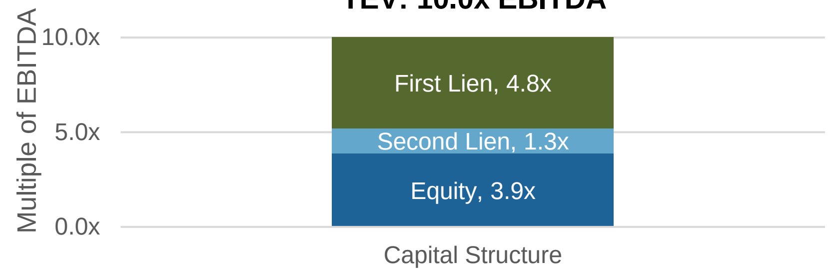
Underwriting Considerations

- Recurring revenue
- Diversified customer base
- Positive industry tailwinds
- Attractive relative value
- Calibrated asset with strong GP ownership

- Competitive differentiation
- M&A execution & integration

Company Description	Distributor of safety products
Securities	First Lien / Second Lien
Coupon / OID	4.25% / 8.25% 99% / 98%

TEV: 10.0x EBITDA



Underwriting Considerations

- Brand equity
- Low cost, high cost of failure products
- Stable demand drivers
- Strong free cash flow generation

- Commodity risk
- Cyclicality
- Concentrated distributor base
- M&A execution & integration

Provided for illustrative purposes only. Represents two case studies in Q1 2022 with similar financing structures (1L/2L), and alongside top-tier sponsors

Outlook for private credit in 2022

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2022

PRIVATE CREDIT HAS STRONG DRIVERS OF DEMAND

> Steady growth of private markets
> Significant amount of PE dry powder (4x that of Private Credit)
> Direct Lending is gaining share based on scale, flexibility and execution

INFLATION IS IMPACTING PRIVATE CREDIT

> Deal activity has been reduced
> Floating rate instruments in private credit are enhancing absolute and real return
> Private credit has outperformed many asset classes during high inflationary periods

PRIVATE CREDIT REMAINS ATTRACTIVE

> Performance of the private credit has been resilient during past cycles
> Investable universe and market opportunity increasing in key industries
> The middle market provides key downside protection

THE CURRENT MARKET CONDITIONS CAN BE NAVIGATED

> Selectivity to construct portfolios of high-quality borrowers hedges against inflationary pressure
> Key credit underwriting and sourcing capabilities will be tested

As of January 1, 2022

ADDITIONAL IMPORTANT INFORMATION

Additional important information

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