

Market Commentary

The rise of private credit in corporate lending

As private credit builds momentum, lenders manage heightened complexity with technology.

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PE firms looking to raise debt capital can go to one, two or three parties and get deals done quickly and with a lot of certainty."

Jack Holby

Director, Vista Equity Partners

With a current market value of \$3 trillion, projected to reach \$5 trillion by 2029*, private credit is playing an increasingly prominent role in the corporate lending space. As lenders grow their private credit portfolios, they're navigating opportunities and challenges related to servicing, technology and more.

* Source: www.morganstanley.com/insights/articles/private-credit-outlook-considerations



About the author

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Craig is a business leader and versatile strategy executive with over 25 years' experience in Financial Services and Fintech, having worked at State Street, Fidelity, ORIX Capital, Markit and OakNorth. Most significantly, Craig spent over 15 years building & growing the Wall Street Office (WSO) franchise. At WSO his roles ranged from product management, business development and GTM, P&L owner, to product strategy & client relationship management of multiple WSO businesses. He incubated the WSO data business, ran the WSO software business & drove WSO strategy globally. During his time at Markit, he was a member of the leadership team, helping to expand buy-side products with an emphasis in leveraged loans and private credit. Craig holds a bachelor's degree in finance & investments from Babson College & an MBA from the Tepper School of Business at Carnegie Mellon University. He lives outside Dallas with his wife Julie and two boys, Reilly and Reid. When not driving new business, Craig enjoys spending time with family, reading and golfing.



Rapid growth in recent years

The growth of private credit is the outcome of converging trends over the past 20 years. Regulatory changes following the 2008 financial crisis drove an increase in demand for loans from non-bank financial institutions (NBFIs). In addition, the rise of private equity (PE) firms has contributed to the uptick in private credit transactions, as the terms and tenor offered by private credit tend to align with PE sponsors' needs and preferences. LSTA CEO Sean Griffin describes a dynamic of "appropriate and healthy tension" between the syndicated and private credit markets, ultimately creating a more beneficial overall lending ecosystem for borrowers.

During and after the COVID-19 pandemic, interest in private credit grew among institutional investors. Insurance capital flowed into private credit transactions, and with the advent of new fund structures, retail investors followed. Recently, an executive order from the White House directed the SEC to allow participants in defined contribution plans, such as 401(k) plans, to invest in alternative assets including private credit.

No longer the purview of niche market players, private credit has truly gone mainstream.

Every bank on Wall Street either has a private credit arm, is investing in it directly from their balance sheet, or is partnering with a buy-side firm, very bank on Wall Street either has a private credit arm, is investing in it directly from their balance sheet, or is partnering with a buy-side firm.

As the volume of private credit loans increases, the nature of deals is evolving. A decade ago, most private credit loans were bilateral. Today, club executions among a small group of direct lenders are increasingly common.

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With the sheer velocity in the sponsor private credit market, time to turnaround can make the difference between leading a transaction or not being in it at all."

Jack Holby
Director, Vista Equity Partners

Bespoke loans to meet individual borrower needs

The value proposition for private credit in the corporate lending ecosystem is that it offers borrowers ease and certainty of execution, as well as highly customizable deal terms to suit individual borrowers' specific needs and preferences.

Where the syndicated loan market may be more competitive on pricing, it may not provide PE sponsors and other borrowers with the flexibility and creativity that private loans can offer. Private lenders are often willing to structure bespoke solutions such as economic triggers on a non-pro rata instrument, payment-in-kind (PIK) instruments, delayed funding components, and other financial covenants tailored to highly specific situations.

Enhanced flexibility helps meet private credit borrowers' particular needs and circumstances where a one-size-fits-all approach does not; however, when every deal (and as a result, every credit agreement) is unique, it creates operational challenges for lenders.

Servicing complexity leads to challenges at scale

Highly flexible loan terms are a key differentiator for private credit, but servicing bespoke private loans is a complex task. Whether lenders handle servicing and syndication themselves or outsource them to a third-party provider, there is a need for specialized expertise in the mechanics and systems required to service these loans effectively, which often translates to hiring additional servicing staff. Lenders in the private credit arena also need access to a sophisticated servicing platform with the capabilities required to manage private credit loans throughout the loan lifecycle.

At the same time, the corporate lending industry is making a concerted effort to reduce manual processes and leverage technology to drive efficiency and scale. Where private credit is concerned, it's more difficult to train systems and automate processes on non-standardized data. Private credit lenders looking to expand their private credit portfolios often face difficulties in scaling upward due to the variation in credit agreements and the lack of standardization in the space.

"That's the 'golden goose' question: How do you efficiently scale this without also scaling up your servicing staff?" says Robert Weil, SVP, Head of U.S. Loan Agency for Wilmington Trust, N.A.

Tapping into the potential of AI

In addition to the challenge of servicing loans, private credit providers need to be able to recall and synthesize high volumes of specific information, a use case that lends itself to the application of AI. A private credit institution may be monitoring hundreds of deals in its portfolio, responding to investor requests, and competing for new business.

Rather than relying on a handful of individuals with a knack for recalling minute details over decades of deals, private credit providers are now leveraging AI tools trained to synthesize and digest this data at scale. AI can enable underwriters and analysts to amplify their own skills and meet the demands of this fast-paced market. Additionally, AI tools can be used in the mid- and back-offices to recall and access information for reporting purposes.

As AI technology continues to evolve, lenders are exploring other use cases to support the growth of private credit transactions, such as using generative AI models to train staff on loan servicing software platforms.

AI tools also have the potential to streamline the deal onboarding process via models trained to interpret sections of a credit agreement and systematically input the information needed to build the facilities, deal and pricing ratios, which an experienced professional could then review and approve.

What's next for private credit

Looking ahead, the private credit space is positioned for continued growth, with the secondary market for private credit loans still nascent. As lenders capitalize on growth opportunities in the space, leveraging AI and other technology advances to boost capacity and efficiency will be vital to thriving in this quickly evolving landscape.





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